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GAAP Reporter

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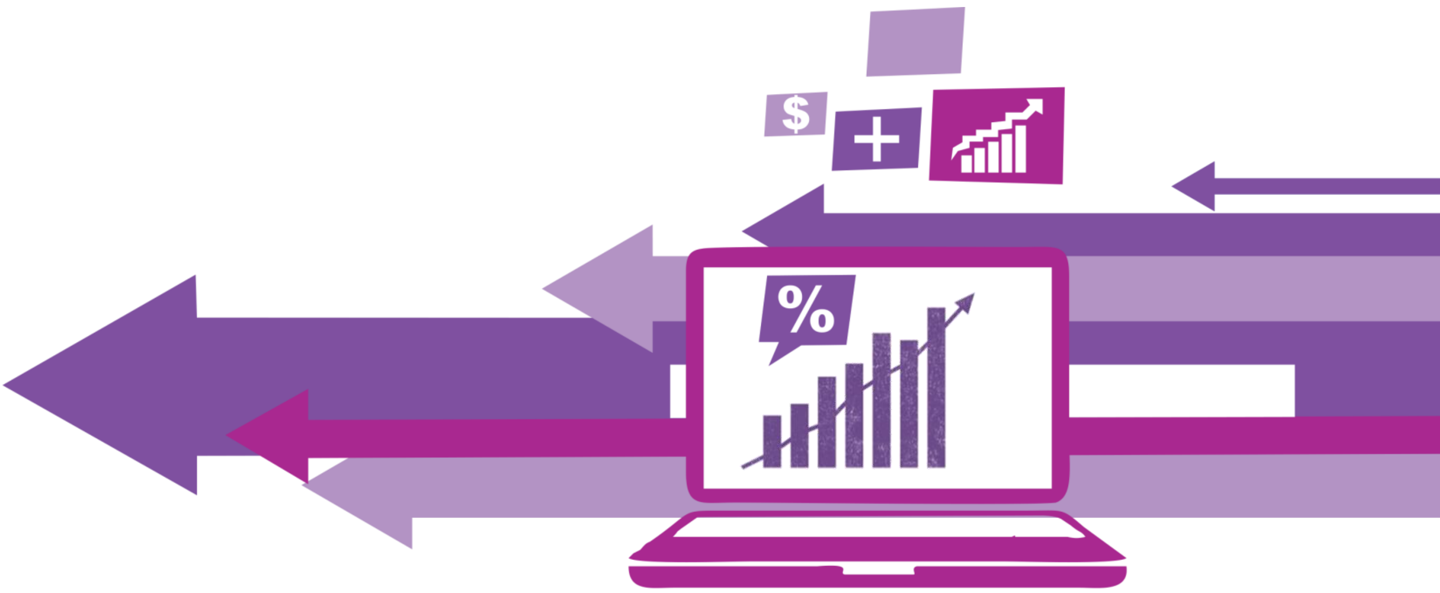
Year-end edition, 2014-15



Introduction

Dear reader,

Grant Thornton in India presents the year-end edition of 'GAAP Reporter', its quarterly bulletin that summarises significant accounting, auditing and related updates. This publication has been compiled to meet the needs of dynamic Indian businesses and focuses on key developments in India and across the globe. To access the source of information, you can click the hyperlink text in blue wherever applicable; for complete details, please refer the original pronouncements.

We would be pleased to receive your feedback. Please write to us at contact@in.gt.com with your comments, questions or suggestions.

This edition presents a round-up of the significant accounting, auditing and related updates from the year 2014-15 including key updates from the quarter ended March 2015. Following is the index of updates summarised below:

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India

Accounting updates

MCA notifies the Ind AS standards

The Ministry of Corporate Affairs (MCA), vide Companies (Indian Accounting Standards) Rules, 2015 has notified the Ind AS for companies other than insurance, banking, and non-banking finance companies.

The MCA notification provides for mandatory application of Ind AS as follows:

Phase 1, financial year 2016-17 onwards

For accounting periods beginning on or after 1 April 2016, with comparatives for the periods ending 31 March 2016, for the companies specified below:

a. companies with a net worth of Rs. 500 crore or more.
b. holdings, subsidiaries, joint ventures or associate companies of the companies covered above.

Phase 2, financial year 2017-18 onwards

For accounting periods beginning on or after 1 April 2017, with comparatives for the periods ending 31 March 2017, for the companies specified below not already covered above:

a. companies whose equity and/or debt securities are listed or are in the process of being listed on any stock exchange in India or outside India.
b. companies with net worth of Rs. 250 crore or more.
c. holdings, subsidiaries, joint ventures or associate companies of companies covered above.

The net worth shall be calculated in accordance with the stand-alone financial statements of the company as on 31 March 2014 or the first audited financial statements for accounting period which ends after that date. The companies meeting the specified thresholds for the first time at the end of an accounting year after 31 March 2014 shall apply Ind AS from the immediate next accounting year.

Companies listed on SME exchanges in India

Companies, whose securities are listed or in the process of listing on SME exchanges, shall not be required to adopt Ind AS. Such companies shall continue to comply with the existing accounting standards unless they choose otherwise.

Voluntary adoption

Companies not covered above shall continue to apply the existing accounting standards prescribed in the Annexure to the Companies (Accounting Standards) Rules, 2006.

All companies have the option to adopt Ind AS voluntarily for financial statements for accounting periods beginning on or after 1 April 2015, with the comparatives for the periods ending 31 March 2015. Once a company opts to report under Ind AS, it will be required to do this for all subsequent financial statements.

Click here for the MCA notification and the Ind AS standards.

Amendments to Schedule II of the Companies Act 2013

Useful lives and residual values different from Schedule II

The MCA, vide its notification dated 29 August 2014, has issued certain amendments to Schedule II of the Companies Act 2013.

As per the previous text of Schedule II, the useful life of an asset shall not be longer than the useful lives specified in Part C, and the residual value of an asset shall not be more than 5% of the original cost of the asset. Further, where a company adopts a different useful life or residual value, justification for the same is to be disclosed in its financial statements.

The amendment, in relation to the useful lives, replaces the word ‘longer’ with the word ‘different’ to suggest that the companies are permitted to adopt useful lives, either longer or shorter than those specified in Schedule II.

The amendment further adds a new requirement that the justification for adopting a different useful life or residual value must also be duly supported by a technical advice.

Separate useful lives of significant parts of an asset mandatory from 1 April 2015

The amendments provide that the requirement to determine the useful lives of significant parts of an asset separately shall be voluntary for the financial year, commencing on or after 1 April 2014 and mandatory for the financial years commencing on or after 1 April 2015.

Amendments to the transitional provisions

As per the previous text of Schedule II, on adopting the revised provisions of Companies Act 2013, where the remaining useful life of an asset is nil, the carrying amount of that asset, after retaining the residual value, shall be recognised in the opening balance of retained earnings. The amendment replaces the word ‘shall’ with the word ‘may’ to suggest that the companies can recognise the amount either in opening reserves or as a charge against the current profit or loss account.

Click here for the MCA notification.

Capitalisation of costs incurred during extended delay in commercial production for reasons beyond the developer's control

The MCA, vide its General Circular No. 35/2014 dated 27 August 2014, has clarified that costs incurred during the extended delay in commencement of commercial production after the plant is otherwise ready for use cannot be capitalised as such costs do not increase the worth of fixed assets.

The MCA circular also clarifies that in case one of the units of the project is ready for commercial production and is capable of being used while construction continues for other units, capitalisation should cease in relation to the completed unit once it is ready for commercial production.

The announcement comes in response to representations received by the Government seeking clarification in relation to the capitalisation of borrowing costs incurred during extended delay in commercial production for reasons beyond the developer's control.

Click here for the MCA circular.

Requirement for consolidated financial statements

The MCA has amended the Companies (Accounts) Rules, 2014 to provide that the requirement to prepare consolidated financial statements in accordance with Schedule III to the Companies Act 2013 shall not apply to an intermediate wholly-owned subsidiary, other than a wholly-owned subsidiary whose immediate parent is a company incorporated outside India. Further, companies which do not have any subsidiaries but only associate(s) and/or joint venture(s) are exempt from preparing consolidated financial statements for the financial year 2014-15.

Click here for the MCA notification.

The MCA has further amended the Companies (Accounts) Rules, 2014 to provide that the requirement to prepare consolidated financial statements in accordance with Schedule III to the Companies Act 2013 shall not apply to a company having subsidiary or subsidiaries incorporated outside India only for the financial year commencing on or after 1 April 2014.

Apparently, it seems that all companies with a foreign subsidiary are exempt from preparing consolidated financial statements for the financial year 2014-15. However, on a plain reading, it is not completely clear whether the exemption is available if a company has at least one foreign subsidiary along with Indian subsidiaries, or will be available if a company has only foreign subsidiaries but no Indian subsidiaries.

Click here for the MCA notification.

Schedule III to the Companies Act 2013 provides that a company while preparing the consolidated financial statements shall follow the same requirements applicable for preparing the standalone financial statements and make disclosures as per the applicable accounting standards.

The MCA has clarified that Schedule III read with the applicable accounting standards does not envisage that a company while preparing its consolidated financial statements merely repeats the disclosures made under stand-alone accounts being consolidated. In the consolidated financial statements, the company must provide all the disclosures relevant for consolidated financial statements only.

Click here for the MCA circular.

Exposure Draft of the Ind AS-compliant Schedule III to the Companies Act 2013

The ICAI has issued the exposure draft of Ind AS compliant Schedule III to the Companies Act 2013 for companies other than Non-Banking Finance Companies (NBFCs). Schedule III deals with the 'General instructions for preparation of balance sheet and statement of profit and loss of a company'. The exposure draft aims to align Schedule III with the requirements of Ind AS.

Click here for the ICAI exposure draft.

ICAI Guidance Note on *Accounting for Rate Regulated Activities (Second Edition)*

The ICAI has issued the second edition of the Guidance Note on *Accounting for Rate Regulated Activities*. The guidance note includes guidance consistent with the Ind AS 114, *Regulatory Deferral Accounts*, formulated corresponding to IFRS 14. Further, the guidance note also includes some illustrative examples for the effective and consistent application of the principles.

The guidance note is effective for accounting period beginning on or after 1 April 2015; early application is permitted.

Click here for the ICAI guidance note.

ICAI Exposure draft of *Guidance Note on Accounting for Derivative Contracts*

The ICAI has issued the exposure draft of Guidance Note on *Accounting for Derivative Contracts*. The objective of the guidance note is to provide guidance on recognition, measurement, presentation and disclosure for derivative contracts so as to bring uniformity in their accounting and presentation in the financial statements. The guidance note also provides accounting treatment for derivatives where the hedged item is covered under existing accounting standards.

The guidance note will also be applicable to entities carrying on the business of banking (including NBFCs) and insurance to the extent it does not in conflict with the requirements of the relevant regulations issued by Reserve Bank of India (RBI) and Insurance Regulatory and Development Authority (IRDA), respectively.

The Guidance Note comes into effect in respect of accounting periods beginning on or after 1 April 2015.

Click here for the ICAI exposure draft.

ICAI issues FAQs on provisions for CSR

The ICAI has issued guidance in the form of Frequently Asked Questions (FAQs) on the provisions of corporate social responsibility (CSR) under Section 135 of the Companies Act 2013. The FAQs, approved by the Corporate Laws and Corporate Governance Committee of the ICAI, provide additional useful guidance, especially for accounting and presentation of the CSR amounts in the financial statements of a company.

The FAQs clarify that if the CSR expenditure meets the definition of an asset, the same should be recognised on the balance sheet. However, once the cost of the asset has been considered as CSR expenditure, subsequently, depreciation, etc. shall not be considered as CSR expenditure to avoid double-counting.

The FAQs also clarify that if the CSR expenditure does not give rise to an asset, the company needs to determine whether the amounts incurred are part of its normal business activity or not. If the CSR expenditure is in fact incurred as part of the normal business activity (e.g. a FMCG company distributes its ready-to-eat products free of cost to people affected by flood), the same shall continue to be charged to the statement of profit and loss. However, if the CSR expenditure is not incurred as part of normal business activity (e.g. an IT company distributes ready-to-eat products free of cost to people affected by flood), the same shall be presented as an appropriation of profit.

The FAQs also clarify that all CSR expenditure that qualifies to be recognised as expense in the statement of profit and loss can be presented in a separate line item labelled as 'CSR expenditure'. Alternatively, the company can continue to present them according to their natural classification.

The FAQs also provide a few useful examples of expenditure that can be and that should not be considered as CSR expenditure

Click here for the ICAI document.

Auditing updates

MCA clarification on commencement of certain provisions of the Companies Act 2013

The MCA has clarified that the requirements of the Companies Act 2013 with respect to financial statements (including certain other documents required to be attached to the financial statements), the auditors' report and board's report shall be applicable only in respect of financial years commencing on or after 1 April 2014. Financial years that commenced before 1 April 2014 shall continue to be governed by the Companies Act, 1956.

Click here for the MCA circular.

The ICAI has reiterated and further clarified that the auditors' report of a company pertaining to any financial year that commenced before 1 April 2014, would be in accordance with the requirements of the Companies Act, 1956 even if that financial year ends after 1 April 2014. For example, where the financial year of a company is 1 January 2014 to 31 December 2014, the statutory auditors' report for that year would be in accordance with the requirements of the Companies Act, 1956.

Click here for the ICAI announcement.

Auditor reporting on internal financial controls

Section 143(3)(i) of the Companies Act 2013 requires the auditors of the companies to report whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls. The ICAI had clarified that the aforesaid provision would apply to the audits of the financial statements for the year beginning on or after 1 April 2014. As a corollary, the requirements of these sections and related Rules would not apply to audits of financial statements of the periods beginning before 1 April 2014, even if the audit is actually carried out and auditor's report is issued on or after 1 April 2014. These would continue to be done as per the requirements of the Companies Act 1956.

Click here for the ICAI announcement.

Subsequently, the MCA has amended the Companies (Audit and Auditors) Rules, 2014 by inserting Rule 10A to defer the applicability date of reporting by the auditors on the internal financial controls. The amendment provides that the aforesaid provision would apply for financial years commencing on or after 1 April 2015; however, the auditor may voluntarily report on these matters in the financial year commencing on or after 1 April 2014 and ending on or before 31 March 2015.

Click here for the MCA notification.

ICAI Guidance Note on *Audit of Internal Financial Controls over Financial Reporting*

In November 2014, the Auditing and Assurance Standards Board (AASB) of the ICAI had released the Guidance Note on *Audit of Internal Financial Controls over Financial Reporting*. However, subsequently, the ICAI has issued an announcement stating that the said guidance note is currently under revision and the revised version shall be uploaded in due course.

Click here for the ICAI announcement.

Clarification on auditor's responsibility under Companies Act 2013 on fraud reporting

The Council of ICAI has issued clarification for its members on auditor's responsibility under Section 143(12) of the Companies Act 2013 on fraud reporting.

The Council noted that Section 143(12) has come into force with respect to financial years beginning on or after 1 April 2014. The Council is thus of the view that the provisions of Section 143(12) of the Companies Act 2013 is applicable to the auditors appointed under the Companies Act 2013 to audit the financial statements for the year beginning on or after 1 April 2014. As a corollary, the requirements of these sections and related Rules would not apply to audits of financial statements of the periods beginning before 1 April 2014, even if the audit is actually carried out and auditor's report is issued on or after 1 April 2014.

Click here for the ICAI announcement.

The Council also considered if the auditor would be required to report pursuant to Section 143(12) while carrying out audits of financial statements for the interim periods, such as quarterly or half yearly audits. The Council is of the view that if such quarterly/ half yearly audits are not carried out pursuant to the requirements of the Companies Act but to meet the specific requirements of the auditee company, for example, to comply with the listing agreement requirements, the requirement of Section 143(12) prima facie would not be applicable to such audits. The Council is in the process of further communicating with the MCA in this regard.

Click here for the ICAI announcement.

ICAI Guidance Note on *Reporting on Fraud under Section 143(12) of the Companies Act 2013*

The AASB of the ICAI has issued the Guidance Note on Reporting on Fraud under Section 143(12) of the Companies Act 2013. The guidance note provides detailed guidance for the ICAI members to fulfil auditor's responsibility to comply with reporting requirements of the said section, such as materiality for the purpose of fraud reporting, reporting on frauds detected by management and other persons, reporting on frauds identified during an audit of consolidated financial statements, reporting on frauds relating to periods before Companies Act 2013 came into effect, etc.

Click here for the AASB announcement.

Illustrative formats of the auditor's report on the standalone financial statements under the Companies Act 2013

The ICAI has issued six illustrative formats of the auditor's report on the standalone financial statements under the Companies Act 2013, covering various situations. These include illustrative reports for both the scenarios, i.e. when reporting under Section 143(3)(i) regarding internal financial controls is required, and when it is not required.

The announcement specifies that these illustrative formats would be added to the respective Appendic*es of Standard on Auditing (SA) 700, Forming an Opinion and Reporting on Financial Statements*, and Standard on Auditing (SA) 705, *Modifications to the Opinion in the Independent Auditor's Report*, as issued by the ICAI.

The AASB is in consultation with the MCA with respect to issues pertaining to the independent auditor's report on consolidated financial statements under the Companies Act 2013. Accordingly, the illustrative format of the independent auditor's report on consolidated financial statements under the Companies Act 2013 will be issued in due course.

Click here for the AASB announcement.

Illustrative formats of the engagement letter for audit of financial statements under the Companies Act 2013

The ICAI has issued two illustrative formats for engagement letter for audit of financial statements under the Companies Act 2013 for both the scenarios, i.e. when reporting under Section 143(3)(i) is applicable, and when it is not applicable. These illustrative formats would be added to the Appendix 1 of Standard on Auditing (SA) 210, *Agreeing the Terms of Audit Engagements*, issued by ICAI.

Click here for the AASB announcement.

ICAI Guidance Note on *Audit of Banks (2015 edition)*

The AASB of the ICAI has issued the Guidance Note on Audit of Banks (2015 edition). The guidance note discusses various important aspects of the financial statements of a bank. Further, it also gives illustrative formats of an engagement letter and an auditor's report for a banking company, meeting the requirements of the Banking Regulation Act, 1949 as well as the Companies Act 2013. The Guidance Note has also recommended an updated audit programme for a branch of a banking company. Click here for the AASB announcement.

ICAI reiterates prohibition to undertake audit and accounting work together for the same entity

The ICAI had noticed that certain entities, while inviting tenders for services of chartered accountants for the assignment of statutory audit, are mentioning accounting and book keeping related works in the scope of work required to be performed by the auditor. The ICAI has advised its members, not to undertake such assignment since it violates the provisions of 'Code of Ethics' and 'Guidance Note on Independence of Auditors' for auditor of an entity to perform book keeping work for the entity. Further, the said prohibition in the case of companies is also mentioned in Section 144 of the Companies Act 2013.

Click here for the ICAI announcement.

Other updates

Amendments to Clause 49 of the Listing Agreement

The Securities Exchange Board of India (SEBI) has issued amendments to Clause 49 (revised Clause 49) of the Listing Agreement. These amendments follow the overhaul in the corporate governance norms under the Companies Act 2013, and aim to align the SEBI requirements with the provisions of the Companies Act 2013 and adopt best practices on corporate governance.

The revised Clause 49 is applicable to all listed companies with effect from 1 October 2014 except as specifically stated otherwise in the circular. The provisions regarding appointment of a woman director shall be applicable with effect from 1 April 2015.

For listed entities, which are not companies but body corporate, or are subject to regulations under other statutes (e.g. banks, financial institutions, insurance companies etc.), the revised Clause 49 shall apply only to the extent it does not violate the respective statutes and guidelines or directives issued by the relevant regulatory authorities. The revised Clause 49 is not applicable to Mutual Funds.

To implement the corporate governance framework effectively, the SEBI circular providing for the amendments also requires that the monitoring cell of the stock exchanges shall also monitor the compliance with the provisions of the revised Clause 49 on corporate governance for all listed companies. The monitoring cell shall ascertain the adequacy and accuracy of disclosures in the quarterly compliance reports received from the companies and shall submit a consolidated quarterly compliance report to SEBI.

Click here for the SEBI circular dated 17 April 2014.

Click here for the SEBI circular dated 15 September 2014.

SEBI (Share Based Employee Benefits) Regulations, 2014

The SEBI has issued the *SEBI (Share Based Employee Benefits) Regulations, 2014* which replace the *SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999*, effective 28 October 2014.

The Regulations apply to: (i) Employee Stock Option Schemes (ESOS); (ii) Employee Stock Purchase Schemes (ESPS); (iii) Stock Appreciation Rights (SARs); (iv) General Employee Benefits Schemes (GEBS); and (v) Retirement Benefit Schemes (RBS). Further, a company can implement schemes either directly; or through an irrevocable trust after obtaining the shareholders' approval through a special resolution.

The Regulations provide that share based schemes shall follow the requirements of the Guidance Note on *Accounting for Employee Share-based Payments* or Accounting Standards as may be prescribed by the ICAI from time to time, including the disclosure requirements. The Regulations also provide certain safeguards to improve the governance and transparency of the schemes and also address concerns regarding potential market abuse.

Listed companies having existing schemes to which these regulations apply are required to comply with them in their entirety within one year i.e. by 27 October 2015. Applicability of these provisions is subject to the following exceptions where a longer transition period of five years has been provided for:

- trusts holding shares beyond the permissible limits to bring down its holding in shares to such limits;
- trusts holding shares, for implementing GEBS and RBS, in order to bring down the trust's holding in shares within the permissible limits of 10% of the total assets of the trust;
- ensuring compliance with the requirement of maintaining adequate public shareholding for trusts holding shares of the company, in order to reclassify its shareholding from either the 'promoter' or 'public'.

Click here for the SEBI Regulation.

Amendments to definition of related party

The MCA, vide its order dated 9 July 2014, has amended the wordings in Section 2(76)(v) of the Companies Act 2013 and modified the definition of a 'related party' to provide that 'related party' in the context of a company means a public company in which a director or manager is a director [and] holds along with his relatives, more than 2% of its paid-up share capital. Previously, inadvertently, the word 'or holds' appeared in place of 'and holds', thus defeating the intention of the statute.

Click here for the MCA order.

Further, the MCA, vide its order dated 24 July 2014, has amended the wordings in Section 2(76)(iv) of the Companies Act 2013 and modified the definition of a 'related party' to provide that 'related party' in the context of a company means a private company in which a director or a manager [or his relative] is a member or director. Previously, difficulties arose in interpreting the said clause due to the absence of the word 'relative' resulting in a disharmonious interpretation of the said definition.

Click here for the MCA order.

Changes to thresholds triggering approval of related party transaction

The MCA, vide its notification dated 14 August 2014, has amended Rule 15(3) of the Companies (Meetings of Board and its Powers) Rules, 2014 to remove the threshold for paid-up share capital. The revised thresholds, effective 14 August 2014, are as follows:

Nature of related party transactions	Revised thresholds
Sale, purchase or supply of any goods or materials directly or through appointment of agents	Exceeding 10% of annual turnover or Rs 100 Cr. (whichever is lower)
Selling or otherwise disposing of, or buying, property of any kind directly or through appointment of agents	Exceeding 10% of net worth or Rs.100 Cr. (whichever is lower)
Leasing of property of any kind	Exceeding 10% of net worth or 10% of annual turnover or Rs 100 Cr. (whichever is lower)
Availing or rendering of any services directly or through appointment of agents	Exceeding 10 % of annual turnover or Rs. 50 Cr. (whichever is lower)
Appointment to any office or place of profit in the company, its subsidiary company or associate company	Monthly remuneration exceeding Rs. 2.5 lakhs
Remuneration for underwriting the subscription of any securities or derivative	Exceeding 1% of net worth

Click here for the MCA notification.

Clarifications on matters relating to related party transactions

The MCA, vide its General Circular No. 30/2014 dated 17 July 2014, has clarified that related party ineligible to vote on a special resolution to approve the contract or arrangement in terms of second proviso to Section 188(1) of the Companies Act 2013 shall be construed with reference only to the contract or arrangement for which the said special resolution is being passed. Thus, only the interested related parties would be required to abstain from voting on such special resolution. The circular further clarifies that the transactions arising out compromises, arrangements and amalgamations will not attract requirements of Section 188 of the Companies Act 2013. Further, contracts which were entered into by companies before the commencement of Section 188 of the Companies Act 2013 do not require fresh approval until the expiry of original term of such contracts; however any modifications to such contracts on or after 1 April 2014 would fall under the new requirements.

Click here for the MCA circular.

Clarificatory amendment to exclude independent director from related party

The MCA, vide its notification dated 17 July 2014, has made a clarificatory amendment to Companies (Specification of definitions details) Rules, 2014 to the effect that a director other than an independent director or key managerial personnel of the holding company or his relative with reference to a company shall be deemed to be a related party.

Click here for the MCA notification.

Clarification with regard to loans and advances to employees

The MCA, vide its circular dated 10 March 2015, has clarified that the loans and advances made by the companies to their employees, other than the managing or whole time directors (which is governed by Section 185) are not governed by the requirements of Section 186 of the Companies Act 2013 if such loans/advances to employees are in accordance with the conditions of service applicable to employees and are also in accordance with the remuneration policy, in cases where such policy is required to be formulated.

Click here for the MCA circular.

Clarifications on provisions for CSR

The MCA has issued clarifications with regard to provisions of Corporate Social Responsibility (CSR) under Section 135 of the Companies Act 2013. Key highlights of the circular include:

- the items listed under Schedule VII to be interpreted liberally so as to capture the essence of the subjects enumerated in that Schedule
- one-off events such as marathons/ awards/ charitable contribution/ advertisement/ sponsorships of TV programs etc. would not qualify as part of CSR expenditure
- expenses incurred by companies for the fulfillment of any Act/ Statute of regulations would not count as CSR expenditure
- 'Any financial year' referred under Sub-section (1) of Section 135 of the Companies Act 2013 read with Rule 3(2) of Companies CSR Rule, 2014, implies 'any of the three preceding financial years'
- expenditure incurred by Foreign Holding Company for CSR activities in India will qualify as CSR spend of the Indian subsidiary if, the CSR expenditures are routed through Indian subsidiaries

- contribution by a company to corpus of a Trust/ Society, etc. will be considered as CSR contribution of that company; provided, these Trust/ Society, etc. are created exclusively for this purpose

Click here for the MCA circular and here for subsequent amendment.

Amendments to provisions for CSR

The MCA, vide its notification dated 6 August 2014, has added a new item 'slum area development' as an eligible CSR activity in Schedule VII of the Companies Act 2013.

Click here for the MCA notification.

Further, the MCA, vide its notification dated 12 September 2014, has amended the Companies (Corporate Social Responsibility Policy) Rules, 2014 to provide that expenditure on administrative overheads can also be included within the 5% limit of total CSR expenditure which a company may spend for building CSR capacity of their own personnel as well as those of through external institution. Consequently, salaries paid to regular CSR staff and volunteers (in proportion to company's time spent on CSR) is not considered as CSR expenditure separately, but as part of administrative overheads within the 5% limit of total CSR expenditure.

Click here for the MCA notification.

Further, the MCA, vide its notification dated 19 January 2015, has issued the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2015.

The amendments provide that the CSR entity can be established only under Section 8 of the Companies Act 2013. The CSR entity can be established by the company, either singly or along with its holding or subsidiary or associate company, or along with any other company or holding or subsidiary or associate company of such other company, or otherwise.

Previously, a CSR entity could have been established under Section 8 and also otherwise, by the company or its holding or subsidiary or associate company.

Click here for the MCA notification.

Clarification on applicability of the Companies Act 2013 to issue of FCCBs

Chapter III of the Companies Act 2013 contains the provisions with respect to prospectus and allotment of securities by companies in India. The issue of Foreign Currency Convertible Bonds (FCCBs) and Foreign Currency Bonds (FCBs) is covered by the specific regulations issued by the Ministry of Finance and the RBI.

The MCA has clarified that unless otherwise provided in the said regulations, provisions of Chapter III shall not be applicable to issue of FCCBs and FCBs by Indian companies exclusively to person resident outside India.

Click here for the MCA circular.

Amendments to relax provisions on acceptance of deposits by companies

Section 74 of the Companies Act 2013 deals with requirements for repayment of deposits, etc., accepted before commencement of the Companies Act 2013.

The MCA has issued an amendment to make Sections 74(2) and 74(3) of the Companies Act 2013 effective from 6 June 2014.

Click here for the MCA notification.

Company (Acceptance of Deposits) Amendment Rules, 2014

The MCA, vide its notification dated 31 March 2015, has issued the Companies (Acceptance of Deposits) Amendment Rules, 2015. The amendments, amongst other things, provide that:

- unless otherwise required under the Companies Act 1956 or the Securities and Exchange Board of India Act, 1992, if a company received any amount by way of subscriptions to any shares, stock, bonds or debentures before 1 April 2014 (and disclosed in the balance sheet for the financial year ending on or before the 31 March 2014) against which the allotment is pending on the 31 March 2015, the company shall, by 1 June 2015, either return such amounts to the persons from whom these were received or allot shares, stock, bonds or debentures or comply with these rules
- if there is any amount received by a company before 1 April 2014 as a subscription for any shares, bonds or debentures, against which the allotment is pending and the same has been disclosed in the balance sheet for the year ending 31 March 2014, the company shall, by 1 June 2015, either allot such shares, bonds or debentures, or return the said amount.
- every eligible company shall obtain, at least once in a year, credit rating for deposits accepted by it
- the companies may accept deposits without deposit insurance contract till the 31 March 2016 or till the availability of a deposit insurance product, whichever is earlier

Click here for the MCA notification.

Clarification regarding applicability of deposit rules on amount received before 1 April 2014

MCA, vide its circular dated 30 March 2015, has clarified that amounts received prior to 1 April 2014 amounts received by private companies prior to 1 April 20l4 shall not be treated as 'deposits' under the Companies Act 2013 and Companies (Acceptance of Deposits) Rules, 2014, subject to the condition that relevant private company shall disclose, in the notes to its financial statement for the financial year commencing on or after l April 2014 the figure of such amounts and the accounting head in which such amounts have been shown in the financial statement. Any renewal or acceptance of fresh deposits on or after 1 April 2014 shall, however, be in accordance with the provisions of Companies Act 20 13.

Click here for the MCA circular.

Amendments related to meetings of board through video conferencing

The MCA, vide its notification dated 14 August 2014, has amended Companies (Meetings of Board and its Powers) Rules, 2014 to remove the requirement that provided that the scheduled venue for meetings conducted through video conferencing should be in India to suggest that the scheduled venue for such meetings can be at any place, even outside India.

The notification further amends the restriction on consideration of accounts of a company in audit committee meetings to refer consideration of financial statement including consolidated financial statement, if any, to be approved by the Board under section 134(1) of the Companies Act 2013.

Click here for the MCA notification.

Companies (Amendment) Bill, 2014

The MCA has issued the Companies (Amendment) Bill, 2014. The Bill has already been passed by Lok Sabha and waiting for next approvals to become the part of the legislation. Following are the key highlights of the Bill:

- Omitting the requirement for minimum paid up share capital by the companies for the purpose easing out the business operations in India
- Making the use of the common seal optional for authorisation of execution of documents
- Prescribing specific punishments for deposits accepted in contravention of the provisions of the Companies Act 2013
- Prohibiting public inspection of the Board resolutions filed in the Registry
- Including provision for writing off past losses/depreciation before declaring dividend for the year
- Rectifying the requirement with respect to transferring equity shares together with transferring the unclaimed/unpaid dividend to the Investor Education and Protection Fund

- Prescribing thresholds for fraud reporting to the Central Government and related disclosures in the Board's Report
- Exempting loans to wholly owned subsidiaries and guarantees/securities on loans taken from banks by subsidiaries from the requirements of Section 185 of the Companies Act 2013
- Introducing provision for omnibus approvals of audit committee for related party transactions on annual basis, similar to the listing agreement
- Replacing 'special resolution' with 'ordinary resolution' for approval of related party transactions by non-related shareholders
- Exempting the requirement of approval of non-related shareholders with respect to related party transactions between holding companies and wholly owned subsidiaries
- Bail restrictions to apply only for offence relating to fraud u/s 447 of the Companies Act 2013
- Process of winding up eased out; these cases to be heard by 2-member bench instead of a 3-member bench
- Lesser burden on the special courts; special courts to try only offences carrying imprisonment of two years or more

Click here for the copy of the Bill.

Companies (Removal of Difficulties) Order, 2015

The MCA, vide its Companies (Removal of Difficulties) Order, 2015 dated 13 February 2015, has amended the provisions of Companies Act 2013 to provide the following:

a. Amendment in the definition of small company: According to clause (85) of Section 2, a company may be treated as a 'small company' if it meets if its paid up share capital does not exceed Rs. 50 lakhs (or such other amount as may be prescribed) or its turnover as per the last statement of profit and loss does not exceed Rs. 2 crore. The MCA has amended this definition to replace the word 'or' with the word 'and'.

b. Amendment to Section 186: In the context of restrictions on a company to make investment through layers of investment companies, in clause (b) of sub-section (11) of Section 186, an exemption has been added for a banking company or an insurance company or a housing finance company making acquisition of securities in its ordinary course of business.

Click here for the copy of the MCA order.

FAQs on the Companies Act 2013

The Institute of Company Secretaries of India (ICSI) has published a handbook titled FAQs on the Companies Act 2013. The handbook is a compilation of the queries received by the

ICSI and their responses based on the interpretation of provisions, the rules and the clarifications, notifications and orders issued by the MCA.

Click here for the ICSI publication.

Revised regulatory framework for NBFCs

The RBI, pursuant to its review of the existing regulatory framework, has issued certain amendments to the regulatory framework for NBFCs. The amendments address the sector risks, the regulatory gaps and arbitrage arising from differential regulations, both within the NBFC sector and vis-à-vis other financial institutions, and harmonise and simplify the regulations to facilitate a smoother compliance and strengthen the governance standards. The amendments provide a revised framework for minimum net owned funds requirements, systemic significance, acceptance of deposits, prudential norms, amongst other requirements.

Click here for the RBI notification.

Final rules on Cost Records and Audit

The MCA had issued the final Companies (Cost Records and Audit) Rules, 2014. These rules, as amended, provide for the following aspects on the matter:

- specified class of companies
- prescribed turnover
- prescribed format of cost records
- procedure for appointment of cost auditor

These rules shall come into force on the date of publication in the Official Gazette.

Click here for the MCA notification and here for the amendments.

Cost Accounting Standard 22, *Manufacturing Cost*

The Institute of Cost Accountants of India has issued Cost Accounting Standard (CAS) 22, *Manufacturing Cost*, to bring standardisation and evenness in the principles and approaches of determining the manufacturing cost of excisable goods. The standard is intended to deal with the methodologies of classification, measurement and assignment for determination of the manufacturing cost of excisable goods. The standard also prescribes the rationale and manner for presentation and disclosure of these costs in the cost statements of the entities. The standard shall be effective from the period commencing on or after 1 April 2015.

Click here for the text of CAS 22.

Accounting updates

IFRS 15, *Revenue from Contracts with Customers*

The International Accounting Standards Board (IASB), in a joint project with Financial Accounting Standards Board (FASB), has issued a new standard, IFRS 15, *Revenue from Contracts with Customers*. Click here for the IASB announcement.

The joint standard is aimed at enhancing quality and increasing global comparability and is the culmination of a long ongoing project by the IASB and the FASB to overhaul the existing revenue recognition guidance and introduce a more principles-based approach.

Unlike the current guidance to recognise revenue on transfer of risk and rewards, the new guidance requires revenue recognition on transfer of control in goods and services to the customer. IFRS 15 requires the following five-step framework to be followed for revenue recognition:
1. identification of the contracts with the customer
2. identification of the performance obligations in the contract
3. determination of the transaction price
4. allocation of the transaction price to the performance obligations in the contract (as identified in step 2)
5. recognition of revenue when the entity satisfies a performance obligation

Further, IFRS 15 requires extensive disclosures including allocation of total revenue, information about performance obligations, changes in contract asset and liability and significant judgments and estimates.

IFRS 15 replaces the previous revenue standards viz. IAS 18, *Revenue*, and IAS 11, *Construction Contracts*, and the related interpretations viz. IFRIC 13, *Customer Loyalty Programmes*, IFRIC 15, *Agreements for the Construction of Real Estate*, IFRIC 18, *Transfers of Assets from Customers* and SIC 31, *Revenue—Barter Transactions Involving Advertising Services*.

IFRS 15 becomes effective for annual periods beginning on or after 1 January 2017; early adoption is permitted. IFRS 15 needs to be applied in full for the current period, including retrospective application to all contracts that are incomplete at the beginning of that period. In respect of prior periods, the transition guidance allows entities an option to either apply IFRS 15 in full to prior periods or to record a cumulative adjustment to the opening balance of equity as at the beginning of current reporting period.

Joint Transition Resource Group for Revenue Recognition

The IASB and the FASB have formed a Joint Transition Resource Group (TRG) for Revenue Recognition:

- to solicit, analyse, and discuss stakeholder issues arising from implementation of the new Standard;
- to inform the IASB and the FASB about those implementation issues, which will help the boards determine what, if any, action will be needed to address those issues; and
- to provide a forum for stakeholders to learn about the new standard from others involved with implementation

TRG will inform the IASB and the FASB about potential implementation issues that could arise when entities implement the new standard.

Click here to track the meetings of TRG. Click here to submit an issue to TRG.

IFRS 9, *Financial Instruments*

The IASB has published the complete final version of IFRS 9 *Financial Instruments*. The new standard revamps the guidance for accounting of financial instruments, and is a culmination of IASB's projects on measurement and classification, impairment and hedge accounting. IFRS 9 replaces IAS 39 *Financial Instruments: Recognition and Measurement*.

The IASB has completed IFRS 9 in phases. In the first phase, the IASB issued new classification and measurement model for financial assets in 2009 followed by accounting for financial liabilities and guidance on de-recognition of financial assets in 2010. In the second phase, the IASB issued new general hedge accounting guidance. Recently, the IASB completed the final phase of IFRS 9 to provide guidance for impairment of financial assets and made certain other amendments to the guidance previously issued in IFRS 9.

Expected loss impairment model

IFRS 9 introduces a new impairment model, under which expected credit losses are required to be recognised. Expected credit losses are to be measured based on reasonable and supportable historical, current and forecasted information. This is a significant change from the existing 'incurred' credit loss model of IAS 39. The new impairment guidance also adds extensive disclosure requirements to IFRS 7, *Financial Instruments: Disclosures*, on entity's credit risk management and its effects on, and methods and assumptions used for measuring expected credit loss.

Amendments to classification and measurement of financial assets

IFRS 9 adds a new classification, 'fair value through other comprehensive income' (FVTOCI). A debt instrument must have simple principal and interest cash flows and be held in a business model in which both holding and selling financial assets are integral to meeting management's objectives for classification as FVTOCI. The IASB has also introduced new guidance on assessment of the contractual cash flow characteristics in certain cases.

IFRS 9 becomes effective for annual periods beginning on or after 1 January 2018; early application is permitted.

Click here for the IASB announcement.

Equity method in separate financial statements

The IASB has published *Equity Method in Separate Financial Statements (Amendments to IAS 27)*. Under the amendments, in the standalone financial statements, an entity can apply the option to account for investments in subsidiaries, associates and joint ventures using the equity method, as provided in IAS 28 *Investments in Associates and Joint Ventures*.

The amendments would be effective for annual periods beginning on or after 1 January 2016; early application is permitted.

Click here for the IASB announcement.

Amendments to IAS 16 and IAS 38

The IASB has published amendments to IAS 16, *Property, Plant and Equipment* and IAS 38, *Intangible Assets* to clarify that the use of revenue-based methods is not appropriate to calculate the depreciation of an asset because generation of revenue would likely include factors other than the consumption of the economic benefits of the asset.

The IASB has also clarified that there is a rebuttable presumption that an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate. This presumption can be overcome only in the limited circumstances when the intangible asset is expressed as a measure of revenue or it can be demonstrated that revenue and the consumption of the economic benefits of the intangible asset are highly correlated.

The amendments become effective for annual periods beginning on or after 1 January 2016 and shall be applied prospectively; early adoption is permitted.

Click here for the IASB announcement.

Amendments to IFRS 10 and IAS 28

The IASB has published *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28)*. The amendments provide that in case of contribution of a business (whether it is housed in a subsidiary or not) to a joint venture or an associate, full gain or loss should be recognised. However, in case of contributions of assets that do not constitute a business, or a subsidiary that does not meet the definition of a business under IFRS 3 *Business Combinations*, recognition of gain/loss would only be to the extent of unrelated investors' interest in the associate or joint venture.

The amendments would be effective for annual periods beginning on or after 1 January 2016; early application is permitted.

Click here for the IASB announcement.

Amendments to IFRS 11

The IASB has published amendments to IFRS 11, *Joint Arrangements*, which provide guidance on accounting for acquisition of an interest in a joint operation that constitutes a business. The amendments require the acquirer of an interest in a joint operation in which the activity constitutes a business, as defined in IFRS 3, *Business Combinations*, to apply all of the principles on business combinations accounting in IFRS 3 and other IFRSs except for those principles that conflict with the guidance in IFRS 11. In addition, the acquirer shall disclose the information required by IFRS 3 and other IFRSs for business combinations.

The amendments become effective for annual periods beginning on or after 1 January 2016 and shall be applied prospectively; early adoption is permitted.

Click here for the IASB announcement.

Narrow-scope amendments to IAS 1

The IASB has issued 3 narrow scope amendments to IAS 1, *Presentation of Financial Statements*, as summarised follows:

a. **Materiality and aggregation:** The amendments provide that an entity shall not reduce the understandability of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions. Further, it is clarified that an entity need not provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material (even if it is specifically referred to by the standard).
b. **Information to be presented in statement of financial position and statement of other comprehensive income:** The amendments clarify that subtotals can be inserted in the financial statements, if such presentation is a better indicator of the performance, and is consistent from one period to the next. The amendments further provide that presentation of 'share of OCI arising from associates and joint ventures' will be made as a single line item in other comprehensive income, separately from the rest of OCI items.
c. **Notes:** The amendments clarify that an entity shall have flexibility to structure the notes in a manner that improves understandability and comparability of its financial statements. It further provides certain examples of systematic ordering and grouping of notes.

The amendments are effective for annual periods beginning on or after 1 January 2016; earlier adoption is permitted.

Click here for the IASB announcement.

Annual Improvements to IFRSs 2012–2014 Cycle

The IASB has issued the following amendments as part of its *Annual Improvements to IFRSs 2012–2014 Cycle*:

a. IAS 19, *Employee Benefits*: The amendments clarify that the high quality corporate bonds used to estimate the discount rate for post-employment benefit obligations should be denominated in the same currency as the liability. It further clarifies that the depth of the market for high quality corporate bonds should be assessed at the currency level and not the country.
b. IAS 34, *Interim Financial Reporting*: The amendments clarify the meaning of disclosure of information 'elsewhere in the interim financial report' and to require the inclusion of a cross-reference from the interim financial statements to the location of information.
c. IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*: The amendments provide that if an asset is reclassified from 'held for distribution' to 'held for sale', or vice versa, the guidance on accounting if an asset ceases to be considered as held for sale (or held for distribution), would not be applied. The asset would continue to be accounted for in the same manner as before under IFRS 5.
d. IFRS 7, *Financial Instruments: Disclosures*: The amendments provide that, with respect to servicing assets, the right to earn a service fee is generally considered as continuing involvement for the purpose of disclosure requirements. Further, it is clarified that the disclosure requirements on offsetting financial assets and liabilities is not specifically required for condensed financial statements.

The amendments are effective for annual periods beginning on or after 1 January 2016; earlier adoption is permitted.

Click here for the IASB announcement.

Auditing updates

IAASB issues new and revised auditor reporting standards

The International Auditing and Assurance Standards Board (IAASB) has issued new and revised auditor reporting standards. The overall objective of the IAASB's auditor reporting project has been to enhance the communicative value of the auditor's report in the public interest. The amendments are effective for audits of financial statements for periods ending on or after 15 December 2016. The significant highlights of the changes are as follows:

Mandatory for audits of financial statements of listed entities, voluntarily application allowed for entities other than listed entities

- new section to communicate key audit matters (KAM). KAM are those matters that, in the auditor's judgment, were of most significance in the audit of the current period financial statements
- disclosure of the name of the engagement partner

For all audits

- opinion section required to be presented first, followed by the Basis for Opinion section, unless law or regulation prescribe otherwise
- enhanced auditor reporting on going concern, including:
    - description of the respective responsibilities of management and the auditor for going concern
    - a separate section when a material uncertainty exists and is adequately disclosed, under the heading 'Material Uncertainty Related to Going Concern'
    - new requirement to challenge adequacy of disclosures for 'close calls' in view of the applicable financial reporting framework when events or conditions are identified that may cast significant doubt on an entity's ability to continue as a going concern
- affirmative statement about the auditor's independence and fulfillment of relevant ethical responsibilities, with disclosure of the jurisdiction of origin of those requirements or reference to the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants
- enhanced description of the auditor's responsibilities and key features of an audit. Certain components of the description of the auditor's responsibilities may be presented in an appendix to the auditor's report or, where law, regulation or national auditing standards expressly permit, by reference in the auditor's report to a website of an appropriate authority

Click here for the IAASB announcement.

Accounting updates

Amendments to guidance on discontinued operations

The FASB has issued Accounting Standards Update (ASU) 2014-08, *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*, to change the definition of discontinued operations. Under the new guidance, only disposals representing a strategic shift in operations that will have a major impact on operations and financial results will be presented as discontinued operations.

For all entities: The amendments become effective for annual financial statements with fiscal years beginning on or after 15 December 2014; early adoption is permitted but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance.

Click here for the ASU.

ASC 606, *Revenue from contracts with customer*

The FASB has issued ASU 2014-09, *Revenue from contracts with customer (Topic 606)*. The guidance issued by the FASB is substantially same as the guidance issued by the IASB in IFRS 15 (as discussed above) and is issued with the intention of improving the existing revenue recognition framework under US GAAP, which was considered to be overly rule-based and inconsistent in certain areas, by making a single principles-based model for all revenue transactions with customers. The ASU will replace almost all of the current revenue recognition guidance including industry-specific guidance.

For public business entities: The ASU becomes effective for annual periods beginning after 15 December 2016; early adoption is prohibited.

For all other entities: The ASU becomes effective for annual periods beginning after 15 December 2017; early adoption is prohibited.

Click here for the ASU.

Recently, the FASB has voted to propose a deferral of the effective date of the new revenue standard by one year, but to permit entities to adopt one year earlier if they choose (i.e., the original effective date). The FASB decided, based on its outreach to various stakeholders and the forthcoming exposure drafts, which amend the new revenue standard, that a deferral is necessary to provide adequate time to effectively implement the new revenue standard.

Guidance to improve financial reporting for development stage entities

The FASB has issued ASU 2014-10, *Elimination of Certain Financial Reporting Requirements, Including an Amendment to Variable Interest Entities Guidance in Topic 810, Consolidation*, to eliminate the additional disclosure requirements that existed for development stage entities. Current US GAAP required a development stage entity to present inception-to-date information about income statement line items, cash flows, and equity transactions.

For public business entities: The ASU becomes effective for the first annual period beginning after 15 December 2014, the presentation and disclosure requirements in Topic 915 will no longer be required. The revised consolidation standards are effective one year later, in annual periods beginning after 15 December 2015; early adoption is permitted.

For all other entities: The ASU becomes effective for the first annual period beginning after 15 December 2014, the presentation and disclosure requirements in Topic 915 will no longer be required. The revised consolidation standards are effective two years later, in annual periods beginning after 15 December 2016; early adoption is permitted.

Click here for the ASU.

Amendments to guidance on repurchase agreements

The FASB has issued ASU 2014-11, *Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures*, to change the accounting for repurchase-to-maturity transactions. The amendment requires such arrangements to be accounted for as secured borrowings, although earlier they could have met the criteria to be accounted for as sales. The disclosure requirements are also enhanced.

For public business entities: The ASU becomes effective for first interim or annual period beginning after 15 December 2014, but the disclosure for transactions accounted for as secured borrowings are required to be presented for annual periods beginning after 15 December 2014, and interim periods beginning after 15 March 2015; early adoption is prohibited.

For all other entities: The ASU becomes effective for annual periods beginning after 15 December 2014, and interim periods beginning after 15 December 2015; entities may elect to apply the requirements for interim periods beginning after 15 December 2014.

Click here for the ASU.

Guidance on share-based awards where a performance target could be achieved after the requisite service period

The FASB has issued ASU 2014-12, *Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*, to amend the guidance in ASC 718, *Compensation—Stock Compensation*. The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period should be treated as a performance condition, i.e. the employee would be eligible to vest in the award regardless of whether the employee is rendering service on the date the performance target is achieved. Compensation cost shall be recognised in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service already has been rendered.

For all entities: The ASU is effective for reporting periods (including interim periods) beginning after 15 December 2015; early adoption is permitted.

Click here for the ASU.

Disclosure of going concern issues

The FASB has issued ASU 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*. The ASU provides guidance for the entity to consider, while evaluating the entity's ability to continue as a going concern, and providing disclosures on the matter. The ASU requires management to evaluate based on relevant conditions and events that are known and reasonably knowable, at the date that the financial statements are issued. The ASU provides that substantial doubt about an entity's ability to continue as a going concern exists when relevant conditions and events, considered in the aggregate, indicate that it is probable that the entity will be unable to meet its obligations as they become due within one year after the date that the financial statements are issued. The ASU also provides the disclosure requirements.

For all entities: The ASU becomes effective from annual periods ending after 15 December 2016 and for interim periods and annual periods thereafter; early application is permitted.

Click here for the ASU

Additional guidance for determining the nature of host contract when performing embedded derivative analysis

The FASB has issued Accounting Standards Update (ASU) 2014-16, *Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity*, to provide guidance on how to evaluate the nature of the host contract of a hybrid financial instrument.

The ASU provides that an entity should determine the nature of the host contract by considering all stated and implied substantive terms and features of the hybrid financial instrument, weighing each term and feature on the basis of relevant facts and circumstances. Therefore the 'chameleon approach' (under which the embedded derivative that is being evaluated for separate accounting is removed before considering the features of the instrument) is disallowed.

Further, the existence or omission of any single term or feature, like redemption option held by the investor, does not necessarily determine the economic characteristics and risks of the host contract, and it should be weighed in with other terms and features.

For public business entities: The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after 15 December 2015.

For all other entities: The ASU is effective for fiscal years beginning after 15 December 2015, and interim periods within fiscal years beginning after 15 December 2016.

Early adoption is permitted for all entities.

Click here for the ASU.

Pushdown accounting made optional

The FASB has issued ASU 2014-17, *Pushdown Accounting*, to provide the acquired entity with an option to apply pushdown accounting in its separate financial statements upon occurrence of a business combination transaction where it is acquired.

An acquired entity may elect the option to apply pushdown accounting in the reporting period in which the change-in-control event occurs. If pushdown accounting is not applied in the reporting period in which the change-in-control event occurs, the entity will further have the option to elect to apply pushdown accounting in a subsequent reporting period to the acquired entity's most recent change-in-control event. Applying it in subsequent reporting period would be accounted for as a change in accounting principle.

The ASU is effective from 18 November 2014.

Further, the Securities and Exchange Commission (SEC) has also issued Staff Accounting Bulletin (SAB) 115 to remove SAB 5-J. SAB 5-J provided conditions for public companies on when push down accounting is required, when it is optional, and when it is not allowed. Thus, both, public and non-public entities, will apply the push-down accounting guidance in ASU 2014-17.

Click here for the ASU.

Accounting alternative to private companies with respect to intangibles recognised in business combination accounting

The FASB has issued ASU 2014-18, *Accounting for Identifiable Intangible Assets in a Business Combination*, to provide an alternative for non-public entities to separately recognising certain intangible assets at fair value under acquisition accounting in ASC Topic 805.

The amendment provides the option that the following assets may not be recognised separately from goodwill:

a. customer-related intangible assets unless they are capable of being sold or licensed independently from the other assets of the business, and
b. noncompetition agreements

As such, adopting such option would result in reduced financial reporting effort and cost. This option is provided to all entities, except for public business entities and not-for-profit entities.

It is further noted, that if such option is elected, the entity would also need to adopt the accounting alternative under ASU 2014-02, *Intangibles—Goodwill and Other (Topic 350): Accounting for Goodwill*, which would require the amortisation of goodwill over a period not more than 10 years. However, an entity that elects the accounting alternative in ASU 2014-02 is not required to adopt the amendments in ASU 2014-18.

For public business entities: Not applicable

For all other entities: The ASU becomes effective for fiscal years beginning after 15 December 2015.

Early adoption is permitted for all entities.

Click here for the ASU.

Eliminating the concept of extraordinary items

The FASB has issued ASU 2015-01, *Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items*, which eliminates the concept of extraordinary items. An entity will no longer:

- segregate an extraordinary item from the results of ordinary operations,
- separately present an extraordinary item on its income statement, net of tax, after income from continuing operations, or
- disclose income taxes and earnings-per-share data applicable to an extraordinary item.

However, entities are still required to separately disclose (in notes to accounts) material items that are unusual in nature or occur infrequently.

Currently, a transaction is required to be separately classified and presented in the income statement if the following two criteria are met:

a. Unusual nature: it possess a high degree of abnormality and is of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the entity
b. Infrequency of occurrence: it is of a type that would not reasonably be expected to recur in the foreseeable future

For all entities: The ASU is effective for annual periods beginning after December 15, 2015 and interim periods within those annual periods; early adoption is permitted. Entities have the option to apply the new guidance prospectively or retrospectively.

Click here for the ASU.

Amendments to guidance on consolidation

The FASB has issued ASU 2015-02, *Amendments to the Consolidation Analysis*, to simplify the guidance related to consolidation evaluation in several areas. Under the ASU, all reporting entities are within the scope of Subtopic 810-10, *Consolidation—Overall*, including limited partnerships and similar legal entities, unless a scope exception applies. The presumption that a general partner controls a limited partnership has been eliminated.

Further, fees paid to a decision maker are excluded from the evaluation of the economics criterion if the fees are both customary and commensurate with the level of effort required for the services provided. The amendments place more emphasis in the consolidation evaluation on other variable interests such as principal investment risk, guarantees of the value of the assets or liabilities of the variable interest entity (VIE), written put options on the assets of the VIE, or similar obligations, including some liquidity commitments or agreements (explicit or implicit). Further, the amendments in the ASU reduce the extent to which related party arrangements cause an entity to be considered a primary beneficiary.

As a result, entities would need to re-evaluate its consolidation conclusions for entities which are affected by the changes in the ASU.

For public business entities: The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after 15 December 2015.

For all other entities: The ASU is effective for fiscal years beginning after 15 December 2016, and interim periods within fiscal years beginning after 15 December 2017.

Early adoption is permitted for all entities, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period.

Click here for the ASU.

Auditing updates

PCAOB Auditing Standard No. 18, *Related Parties*

After public comment, the Public Company Accounting Oversight Board (PCAOB) has adopted the Auditing Standard No. 18, *Related Parties* and amendments to certain PCAOB auditing standards regarding significant unusual transactions; and other amendments to PCAOB auditing standards. Subject to the SEC's approval, Auditing Standard No. 18 will supersede the PCAOB's interim auditing standard, AU sec. 334, *Related Parties* and sec. 9334, *Related Parties: Auditing Interpretations of Section 334*, and will be effective for audits of financial statements for fiscal 2016 onwards.

The new standard requires specific audit procedures for the auditor's evaluation of a company's identification of, accounting for, and disclosure of transactions and relationships between a company and its related parties, and requires the auditors to communicate with the audit committee on their evaluation from the aforesaid audit procedures.

Click here for the PCAOB release.

AICPA amends the guidance for comfort letters

To address unintended changes to previous practice as a result of its Clarity Project, the Auditing Standards Board (ASB) of the American Institute of Certified Public Accountants (AICPA) has issued Statement on Auditing Standards (SAS) No. 129, *Amendment to Statement on Auditing Standards No. 122 Section 920, Letters for Underwriters and Certain Other Requesting Parties, as Amended* (AICPA, Professional Standards, AU-C sec. 920).

AU-C sec. 920 addresses the auditor's responsibilities when engaged to issue letters (commonly referred to as comfort letters) to requesting parties in connection with a non-issuer entity's financial statements included in a registration statement or other securities offerings.

Click here to download the summary.

AICPA issues interpretative guidance on going concern

The AICPA has issued AU-C Section 9570, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern: Auditing Interpretations of AU-C Section 570*, to provide interpretative guidance on going concern. This guidance follows issue of ASU 2014-15 by the FASB, and addresses practical difficulties in application of AU-C Section 570, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, that arose due to inconsistencies in definitions of certain terms in the accounting and auditing standards.

AU-C Section 9570 contains guidance on the following topics:

- Definition of 'substantial doubt about an entity's ability to continue as a going concern'
- Definition of 'reasonable period of time'
- Interim financial information
- Consideration of financial statements effects

Click here for AU-C Section 9570.

Fraud reporting by auditors

Section 143(12) of the Companies Act 2013 (2013 Act) provides, in part, that "…if an auditor of a company, in the course of the performance of his duties as auditor, has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the Central Government…".

The related rules provide that if the auditor has sufficient reason to believe so, the auditor shall first report the fraud to the board/ audit committee within a 45-day period, followed by a 15-day period for the board/ audit committee to respond. The auditor shall then report the fraud to the Central Govt. along with the response received from the board/ audit committee.

The rules also provide that the requirements equally apply to a cost auditor and a secretarial auditor during the performance of his duties under section 148 and section 204, respectively.

This is a new reporting responsibility for the auditors introduced by the 2013 Act, and especially due to lack of implementation guidance and practical experience in this regard, various queries and concerns were raised by the auditing profession, for example, how to interpret the phrase 'in the course of the performance of his duties as auditor', whether the concept of materiality needs to be considered, what is the extent of auditor's responsibility when the fraud may have already been identified by others, etc.

To address such queries, and provide the much needed guidance, the ICAI has issued the Guidance Note on '*Reporting on Fraud under Section 143(12) of the Companies Act, 2013'*. The guidance note confirms that the auditor's reporting responsibilities are only within the purview of performance of his duties as an auditor appointed under the provisions of the 2013 Act, and in no other capacity. Thus, the auditors of a company shall consider the requirements of the auditing standards (e.g. Standards on Auditing (SA) 240, *The Auditor's Responsibility related to Fraud in an Audit of Financial Statements*) in planning and performing his audit procedures in an audit of financial statements to address the risk of material misstatement due to fraud.

The guidance note also confirms that reporting under Section 143(12) is applicable only when the auditor has sufficient reason to believe and has knowledge that a fraud has occurred or is occurring i.e., when the auditor has evidence that a fraud exists. The guidance note recognises that an auditor may not be able detect all frauds, and illustrates that, for example, an auditor may not be able to detect if an employee is receiving pay-offs for favoring a specific vendor, which is a fraudulent act, since such pay-offs would not be recorded in the books of account of the company.

The auditor should continue to apply the concept of materiality in performing the audit in accordance with SA 320, *Materiality in Planning and Performing an Audit*. It is noteworthy that the Companies (Amendments) Bill, 2014 approved by the Lok Sabha includes an amendment to the provide that in case of a fraud involving lesser than a specified amount, the auditor shall report the matter to the Audit Committee or to the Board in other cases. Accordingly, only those frauds, where the amount exceeds the prescribed amount, shall be reported to the Central Government. The said amendments are pending for the approval of the Rajya Sabha and the Presidential assent.

The guidance note clarifies that if a fraud has already been identified by the management and such case is informed to the auditor, he will not be required to report the same under Section 143(12). However, the auditor should review the steps taken by the management/those charged with governance with respect to such instance of suspected offence involving fraud stated above, and if he is not satisfied with such steps, he should state the reasons for his dissatisfaction in writing and request the management/those charged with governance to perform additional procedures to enable the auditor to satisfy himself that the matter has been appropriately addressed.

Further, in respect of reporting on suspected offence involving frauds identified during a review/audit of interim financial statements, or during the course of other attest services and non-attest services, the guidance note provides that:

- if the amount involved will be material to the financial statements of the company prepared under the 2013 Act or
- if the auditor uses or intends to use the information that is obtained in the course of performing such attest or non-attest services when performing the audit under the 2013 Act

the matter may become reportable under Section 143(12). However, this would require exercise of professional judgement.

The guidance note asserts that in engagements to audit only the consolidated financial statements, the auditor of the parent company is not required to report on frauds under Section 143(12) if they are not being or have not been committed against the parent company by the officers or employees of the parent company. However, the auditor of the parent company shall be liable to report if:

a. he identifies such suspected offence involving fraud in the component 'in the course of the performance of his duties as an auditor' of the consolidated financial statements; or
b. he is directly informed of such a suspected offence involving fraud in the component by the component auditor and the management had not identified/is not aware of such suspected offence involving fraud in the component; or
c. a component that is not a company since the component auditors of such components are not covered under Section 143(12).

In case of joint audits, where a suspected offence involving fraud against the company by its officers or employees is identified/noted by one of the joint auditors, such joint auditor should communicate the same to the other joint auditor(s) to enable them to consider and evaluate if the same could exist in the areas/account balances audited by them and each of the joint auditor should individually comply with the requirements of the guidance note.

The guidance note establishes that in case of fraud relating to earlier years to which the Companies Act 1956 was applicable, reporting under Section 143(12) will arise only if the suspected offence involving fraud is identified by the auditor in the course of performance of his duties as an auditor during the financial years beginning on or after 1 April 2014, and to the extent that the same was not dealt with in the prior financial years either in the financial statements or in the audit report or in the Board's report under the Companies Act 1956.

The requirements for reporting by auditors under Section 143(12) would apply even if the fraud is required to be and/or has been reported under any other statute or to any other regulator. Further, in relation to illegal acts, if the auditor, in the course of performance of his duties as the auditor, comes across instances of corruption, bribery and money laundering and other intentional non-compliances with laws and regulations, the auditor would need to report the same under Section 143(12). The auditor should comply with the relevant auditing standards (e.g. SA 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*) when performing the audit to evaluate the impact to determine whether the same would have a material effect on the financial statements.

If a fraud is identified and reported u/s 143(12), the auditor will have to evaluate the implications of the matter reported in the financial statements, on his audit opinion on the financial statements, and on any other matter to be included in his report on the adequacy and operating effectiveness of the internal financial controls.

The guidance note also contains useful practice aids like, illustrative matters for engagement team discussion on fraud, illustrative checklist of inquiries with Board, Audit Committee, etc., illustrative format for reporting to the Board or the Audit Committee; illustrative management representation letter, etc.

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