CHAPTER 3

Regulatory updates

Updates relating to social stock exchange

The Finance Minister, in her budget speech for FY 2019-20 had proposed to initiate steps towards creating a Social Stock Exchange (SSE), under the regulatory ambit of the Securities and Exchange Board of India (SEBI).

Accordingly, SEBI constituted a Working Group (WG) and Technical Group (TG) in September 2019 and 2020, respectively to provide recommendations relating to establishment of the SSE and to provide guidance on the matters relating to the scope of work, eligibility criteria and regulation of social auditors. This was followed by a release of regulatory framework for SSE by SEBI in February 2022. Based on the recommendations of the WG and the TG, and from the stakeholders, SEBI through its notification dated 25 July 2022, issued amendments to SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations) to insert a new chapter X-A on the SSE.

Corresponding amendments have been made to SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and SEBI (Alternative Investment Funds) Regulations, 2012.

Key points relating to SSE

- **Social Enterprise:** A social enterprise (i.e either a Not for Profit Organisation (NPO) or a for profit social enterprise that meets the eligibility criteria specified in the new chapter X-A) shall be eligible to raise funds from an SSE provided such a social enterprise engages in a social activity that is listed by the regulator (there are 16 broad categories). An SSE would be a separate segment of a recognised stock exchange having nationwide trading terminals permitted to register NPO and/or list the securities issued by an NPO in accordance with provisions of these regulations.
- **Applicability:** The provisions of the chapter X-A are applicable to:
  a. NPO seeking to only get registered with an SSE
  b. NPO seeking to get registered and raise funds through an SSE
  c. For profit social enterprise seeking to be identified as an SE.
- **Eligibility conditions for being identified as a social enterprise:** In order to be recognised as a social enterprise, an NPO or for profit social enterprise would need to establish social intent as their primary goals by demonstrating their focus towards the eligible social objectives and satisfy the prescribed conditions.

The notification also prescribes the manner and procedures in which funds can be raised by a social enterprise and the ineligibility with respect to the same.

Social audit standards

With regard to the aforementioned amendments to the SEBI ICDR Regulations, the Sustainability Reporting Standards Board (SRSB) of the Institute of Chartered Accounts of India (ICAI), on 5 August 2022, has released an Exposure Draft (ED) on the Compendium of Social Audit Standards (SAS). The following aspects are covered in the ED:

i. **Draft preface:** As per the ED, the SAS shall be mandatorily applied whenever an independent social audit of a social enterprise is carried out. The SASs may also have application, as appropriate, to other related functions of social auditors.

ii. **Draft framework:** The framework in the ED defines and describes the elements and objectives of a social audit performed by an social auditor. It also provides a frame of reference for:
   a. Social auditors when performing social audits i.e., social impact assessment of a project/programme executed by the social enterprises.
   b. The responsible party, the engaging party, if any, and other stakeholders who are the intended users of a social audit report.

iii. **Draft SASs on 16 thematic areas:** The SASs contain essential procedures and related guidance/criteria for the performance of each of the area-specific social audit engagements based on the 16 categories of social activities as specified by SEBI. The respective SASs may be referred for the area specific social indicators. The list of the draft SAS are as follows:

- **SAS 100:** Eradicating hunger, poverty, malnutrition and inequality
- **SAS 200:** Promoting health care (including mental health) and sanitation; and making available safe drinking water
- **SAS 300:** Promoting education, employability and livelihoods
- **SAS 400:** Promoting gender equality, empowerment of Women and LGBTQIA+ communities
- **SAS 500:** Ensuring environmental sustainability, addressing climate change including mitigation and adaptation, forest and wildlife conservation
- **SAS 600:** Protection of national heritage, art and culture
- **SAS 700:** Training to promote rural sports, nationally recognised sports, Paralympic sports and Olympic sports
- **SAS 800:** Supporting incubators of social enterprises
- **SAS 900:** Supporting other platforms that strengthen the non-profit ecosystem in fundraising and capacity building
- **SAS 1000:** Promoting livelihoods for rural and urban poor including enhancing income of small and marginal farmers and workers in the non-farm sector
- **SAS 1100:** Slum area development, affordable housing, and other interventions to build sustainable and resilient cities
- **SAS 1200:** Disaster management, including relief, rehabilitation and reconstruction activities
- **SAS 1300:** Promotion of financial inclusion
- **SAS 1400:** Facilitating access to land and property assets for disadvantaged communities
- **SAS 1500:** Bridging the digital divide in internet and mobile phone access, addressing issues of misinformation and data protection
- **SAS 1600:** Promoting welfare of migrants and displaced persons.

The last date to provide comments was upto 29 August 2022.

(Source: SEBI notification no. SEBI/LAD-NRO/GN/2022/90 dated 5 July 2022 and Exposure Draft of Compendium of Social Audit Standards issue by ICAI on 5 August 2022)

SEBI amended the definition of an 'associate' under mutual fund regulations

SEBI (Mutual Funds) Regulations, 1996 are regulations that govern mutual funds and provide the rules to buy and sell of mutual funds in India.

The regulations define an 'associate' as a person:

i. Who directly or indirectly, by himself, or in combination with relatives, exercises control over the asset management company or the trustee (or the sponsor), as the case may be, or

ii. In respect of whom the asset management company or the trustee (or the sponsor), directly or indirectly, by itself, or in combination with other persons exercises a control, or

iii. Whose director (except an independent director), officer or employee is a director, officer or employee of the asset management company;

On 3 August 2022, SEBI amended the definition of an 'associate' to include a proviso to the definition. As per the amendment the definition of an associate would not be applicable to such sponsors, which invest in various companies on behalf of the beneficiaries of insurance policies or such other schemes as may be specified by SEBI from time to time.

This amendment is applicable from 3 September 2022.

Consequent to the above amendment, SEBI has issued a circular on 25 August 2022, to provide that the Asset Management Companies (AMCs) investing in securities of entities are excluded from the revised definition of 'associate'. Additionally, such AMCs are required to provide the scheme wise disclosure of investments including International Securities Identification Numbers (ISIN) wise value of investment and value as percentage of Assets Under Management (AUM) of scheme. The specified disclosure should be made on the websites of respective AMCs and on the website of Association of Mutual Funds in India (AMFI) within one month from the close of each quarter.

(Source: SEBI notification SEBI/LAD-NRO/GN/2022/92 dated 3 August 2022 and SEBI circular SEBI/HO/IMD/DOF2/P/CIR/2022/111 dated 25 August 2022)

Amendment in the Companies (Accounts) Rules, 2014 relating to availability of books of account and other relevant books and papers

The Ministry of Corporate Affairs (MCA) through its notification dated 5 August 2022 has amended the certain provisions of Rule 3 of the Companies (Accounts) Rules, 2014 relating to availability of books of account and other relevant books and papers maintained in electronic mode. The amendments are as follows:

- Rule 3(1) relating to maintaining the books of account and other relevant books and papers in electronic mode has been amended. The amended provision provides that such books of account and other relevant books and papers should be accessible in India, **at all times.**
- Rule 3(5) of the Accounts Rules provides that there should be a proper system for storage, retrieval, display or printout of the electronic records. The provision relating to maintenance of backups has been amended. The amendment provides that the back-up of the books of account and other books and papers of the company maintained in an electronic mode, including at a place outside India, if any, shall be kept in servers physically located in India **on a daily basis** earlier it was required to be maintained on periodic basis.
- Rule 3(6) relating disclosure in case of service provider has been amended. The amendments requires an additional disclosure by the company to the Registrar of Companies (ROC) the name and address of the person in control of the books of account and other books and papers in India, where the service provider is located outside India.

  Therefore, the revised requirements to be disclosed to the ROC on an annual basis at the time of filing of financial statement are:

  a. the name of the service provider

  b. the internet protocol address of service provider

  c. the location of the service provider (wherever applicable)

  d. where the books of account and other books and papers are maintained on cloud, such address as provided by the service provider

  e. details of where the service provider is located outside India, the name and address of the person in control of the books of account and other books and papers in India.

  (Emphasis added to highlight the changes)

(Source: MCA notification G.S.R. 624(E), Companies (Accounts) Fourth Amendment Rules, 2022 dated 5 August 2022)

ICAI released revised Guidance Note on Tax Audit for AY 2022-23

Section 44AB of the Income-tax Act, 1961 (IT Act) contains provisions pertaining to the tax audit. A tax audit is an examination of a taxpayer's books of account and other relevant records. Basis the examination, an audit report in Form No. 3CA/3CB and particulars in Form No. 3CD is required to be issued by the practicing chartered accountants.

The Direct Tax Committee of the ICAI has issued a revised Guidance Note on Tax Audit under Section 44AB of the IT Act. This guidance note is for the audits to be conducted for Assessment Year (AY) 2022-23. The guidance note is revised to incorporate changes in provisions of law and new clauses included in the particulars to be furnished in the Form No. 3CD since the last edition. The revised guidance note incorporates all the changes in the desired clauses which have taken place due to amendments to the IT Act, 1961 as well as judicial pronouncements, circulars etc.

(Source: Revised Guidance Note on Tax Audit under section 44AB of the Income-tax Act, 1961 issued by ICAI dated 19 August 2022)

Reporting going concern matters in the auditor's report

The Going Concern Task Force of the International Auditing and Assurance Standards Board (IAASB) has issued a Frequently Asked Questions (FAQs) publication in August 2022 to address some of the common questions involving the use of and the interrelationship of material uncertainty related to going concern and Key Audit Matters (KAM) sections, and Emphasis of Matter paragraphs (EOM), in the auditor's report prepared in accordance with International Standards on Auditing (ISAs).

Key considerations addressed in the publication include:

i. Purpose, applicability and inter-relationship of the material uncertainty related to going concern, KAM and EOM in the auditor's report

ii. Implications of material uncertainty related to going concern, KAM and EOM on the auditor's opinion and the auditor's report

iii. Situations where no material uncertainty related to going concern exists, can going concern matters be communicated as a KAM or EOM in the auditor's report.

(Source: FAQs issued by IAASB on 1 August 2022)

Implementation guide released for identifying and assessing the risk of material misstatements in an audit of financial statements

In December 2019, IAASB has issued the revised ISA 315, *Identifying and Assessing the Risks of Material Misstatement* to include a robust and consistent risk identification and assessment. The revised standard is effective for periods beginning on or after 15 December 2021.

In light of the revised standard and considering that it became appliable, on 27 July 2022, IAASB released the First-Time Implementation Guide for ISA 315 (Revised 2019) which highlights and focusses on the substantial changes made in revised standard.

The objective of this First-Time Implementation Guide is to help understand and apply the changes in ISA 315 (Revised 2019). Additionally, IAASB highlighted that the contents of this publication do not amend or override ISA 315 (Revised 2019).

(Source – IAASB Press Release/News Alert dated 27 July 2022)

IAASB proposes narrow scope amendments to operationalise changes to the IESBA code that enhance transparency about independence

In April 2022, the International Ethics Standards Board for Accountants (IESBA) approved the revisions to the definition of a listed entity and a public interest entity to the International Code of Ethics for Professional Accountants (including International Independence Standards) (the Code). The revisions include an expanded definition of a 'Public interest Entity (PIE)' in the Code by specifying a broader list of public interest entity categories, including a new category a 'publicly traded entity' to replace the category 'listed entity'.

The revisions also introduce a transparency requirement for firms to publicly disclose the application of independence requirements for PIEs where they have done so. The aforementioned pronouncement would be applicable for audits of financial statements for periods beginning on or after 15 December 2024.

Considering the updates from IESBA, in July 2022, the International Auditing and Assurance Standards Board (IAASB) proposed narrow scope amendments to ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, and ISA 260 (Revised), *Communication with Those Charged with Governance* to support the operationalisation of IESBA's transparency requirement.

Key proposals include:

i. **Statement of independence:** The IAASB has proposed two possible approaches in ISA 700 (Revised) relating to auditor's statement on independence:

   a. A conditional requirement that applies only when the relevant ethical requirements require public disclosure that differential independence requirements for audits of financial statements of certain entities were applied. If the condition is met, then the auditor is required to indicate in the auditor's report that the relevant ethical requirements for independence for those entities were applied, or

   b. A non-conditional requirement that would apply in all circumstances when differential independence requirements for audits of financial statements of certain entities were applied, even if the relevant ethical requirements do not require the auditor to publicly disclose that such differential independence requirements were applied.

ii. **Communication with Those Charged with Governance:** A new application material has been proposed to ISA 260 (Revised) in line with the proposed requirements for ISA 700 (Revised).

iii. **Amendment to ISRE 2400:** Paragraph 86(j) of ISRE 2400 (Revised) *Engagements to Review Historical Financial Statements,* requires a practitioner's report to include a reference to the practitioner's obligation under this ISRE to comply with relevant ethical requirements. The practitioner is not required to provide a statement similar to the requirement in paragraph 28(c) of ISA 700 (Revised), which requires an auditor to identify the jurisdiction of origin of the relevant ethical requirements or refer to the IESBA Code. IAASB is seeking stakeholder views to whether to amend ISRE 2400 in a manner which is consistent with proposed amendments to ISA 700 (Revised) wherein a conditional requirement could be introduced in ISRE 2400 (Revised), together with application material and illustrations as necessary.

iv. **Proposed effective date:** The effective date for application of the proposed amendments to ISA 700 (Revised) and ISA 260 (Revised) has been proposed to be applicable for audits of financial statements for periods beginning on or after 15 December 2024 in line with the effective date for application of revisions made to IESBA Code.

The period to provide comments on the exposure draft is upto 4 October 2022.

(Source: IAASB announcement dated 6 July 2022)