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Foreword

Many companies undertake supplier financing arrangements as a means to improve working capital position. Reverse factoring is a common form of supply chain financing involving three parties: an entity that purchases a good or service, a supplier providing those goods or services and a financial institution. The arrangement typically allows the supplier to be paid by the financial institution at a date earlier than the entity pays the financial institution. The terms of reverse factoring arrangements vary depending on the agreement between the entity, its suppliers and the financial institution. Therefore, depending upon the terms of reverse factoring arrangements, presentation in the balance sheet and presentation in statement of cash flows may also change. Also with increasing prominence of reverse factoring arrangements as source of financing, expectations of users of financial statements with respect to more detailed and transparent disclosures of such arrangements have also increased many folds. Currently there is no explicit guidance in Ind AS or IFRS on presentation of reverse factoring arrangements in the financial statements. However, in near future International Accounting Standards Board (IASB) would be issuing guidance on this topic. This edition of Accounting and Auditing Updated (AAU) aims to provide key considerations for presentation of reverse factoring arrangement in the balance sheet, statement of cash flows and notes to the financial statements.

All companies are facing climate-related risks and opportunities. Some are affected more than others. As the impact of climate change intensifies, investors and regulators are increasingly seeking greater transparency of climate-related information in financial statements. Considering growing implications of climate risk and lack of sufficient disclosure of climate-related information in financial statements, the regulators around the globe such as Securities Exchange Commission (SEC), the European Union (EU) and the International Sustainability Standards Board (ISSB) are working on developing the disclosure requirements relating to climate risk. The proposed standards and guidelines would support companies in providing information about their exposure to climate-related risks and opportunities. In India, Securities and Exchange Board of India has issued Business Responsibility and Sustainability Reporting (BRSR) which requires reporting on environment aspects. Considering the growing emphasis on climate related disclosure and reliability of information, our article on this topic aims to provide an overview of climate related risks and its disclosures.

There have been various regulatory developments in India and internationally during the month. Recently, the Ministry of Corporate Affairs (MCA) issued the Companies (Indian Accounting Standards) Amendment Rules, 2023 to notify certain amendments to Ind AS. These amendments are effective from 1 April 2023. Additionally, IASB has issued an exposure draft to propose amendments to the classification and measurement requirements in IFRS 9, *Financial Instruments* and IFRS 7, *Financial Instrument: Disclosure* in response to feedback received from a Post-Implementation Review (PIR) of the classification and measurement requirements in IFRS 9. Further, the Reserve Bank of India (RBI) issued a framework for acceptance of green deposits. Our regulatory updates article covers these and other important regulatory developments.

We would be delighted to receive feedback/suggestions from you on the topics we should cover in the forthcoming editions of AAU.

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CHAPTER 1

Reverse factoring arrangement – presentation in the financial statements

This article aims to:

- Provide key considerations for presentation of reverse factoring arrangement in the balance sheet, statement of cash flows and notes to the financial statements.

Introduction

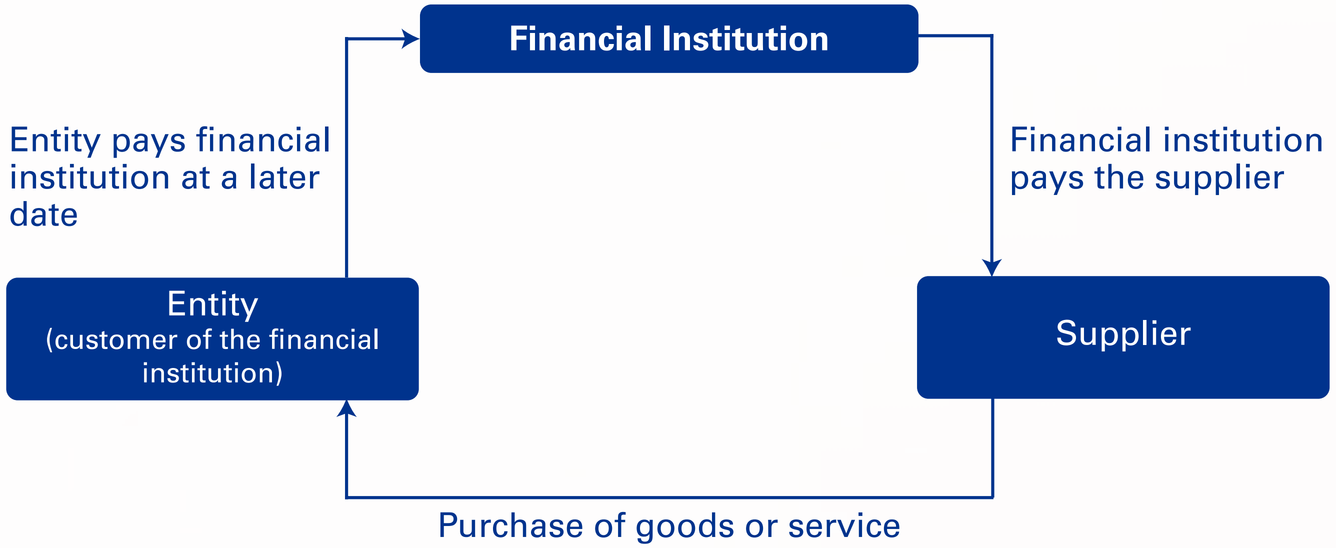
Reverse factoring is a common form of supply chain financing involving three parties: an entity that purchases a good or service, a supplier providing those goods or services and a financial institution. The arrangement typically allows the supplier to be paid by the financial institution at a date earlier than the entity pays the financial institution.

In a traditional factoring arrangement, a supplier of goods or services obtains cash from a bank or other financial institution (i.e. the factor) against receivables due from its customers.

In contrast, reverse factoring is initiated by the customer of the financial institution (in this case, the purchase of goods or services) and the financial institution (factor).

A reverse factoring arrangement may provide liquidity to the entity (i.e. customer of the financial institution) if it allows deferral of payment to the factor beyond the original maturity of the supplier's invoice or if the arrangement enables the entity to negotiate extended payment terms with its supplier. Depending on the terms of the arrangement, and similar to traditional factoring, the reverse factoring arrangement may also provide to the supplier:

- Liquidity by enabling it to receive cash before the invoice due date and
- Access to funding at a lower interest rate based on the customer's credit rating.



(Source: KPMG in India analysis, 2023)

Similarly, the reverse factoring arrangement may allow the customer to take advantage of an early payment discount offered by the supplier. The reverse factoring arrangement may also allow the supplier and the customer to make administrative savings through more streamlined collection and payment procedures.

The terms of reverse factoring arrangements vary depending on the agreement between the entity, its suppliers and the financial institution. Therefore, depending upon the terms of reverse factoring arrangements, presentation in the balance sheet and statement of cash flows may also change. Further, due to the impact on the financial statements, it is also important to appropriately provide disclosures in relation to reverse factoring arrangement in the financial statements.

There is no specific guidance in the Ind AS/IFRS on presentation of reverse factoring arrangements in the financial statements. In this regard, the IFRS Interpretations Committee[1] (IFRIC) discussed the presentation of liabilities that are part of reverse factoring arrangements in the balance sheet and presentation in the statement of cash flows under IFRS. The Committee published its agenda decision in December 2020 that provided guidance/explanatory information on presentation of liabilities that are part of a reverse factoring arrangement in the balance sheet, presentation in the statement of cash flows and disclosures in notes to the financial statements.

A common scenario of a reverse factoring arrangement

Company ABC is in the business of manufacturing and selling product X. The company enters into a reverse factoring arrangement with a bank as per which:

- Company will upload the supplier invoice on due date on bank's platform;
- The bank will give quote for the invoice financing for 60/90/180 days at interest rate specified in offer;
- On acceptance by the company, the amount will be paid to supplier on due date by the bank on behalf of company; and
- Company would pay to the bank at a later date (60/90/180 days) along with the interest.

1. The IFRS Interpretations Committee (Interpretations Committee) is the interpretative body of the International Accounting Standards Board (IASB). The Interpretations Committee works with the IASB in supporting the consistent application of IFRS Accounting Standards. The Interpretations Committee responds to questions about the application of the Accounting Standards and does other work at the request of the IASB. Agenda decisions often include explanatory materials to help entities in applying IFRS Standards.

Presentation in the balance sheet

Under Indian Accounting Standards (Ind AS), Ind *AS 1, Presentation of Financial Statements* specifies how an entity is required to present its liabilities in the balance sheet.

Further, the Schedule III to the Companies Act, 2013 lays down the framework for preparation of financial statements which is sub-divided into three divisions. Division-II to the Schedule III is applicable for the Companies which prepare their financial statements in accordance with Ind AS.

Ind AS 1 and Schedule III to the Companies Act, 2013 (Division-II) requires separate presentation of trade payables and borrowings on the balance sheet. Further, Ind AS 1 state that an entity shall present additional line items, headings and subtotals in the balance sheet when such presentation is relevant to an understanding of the entity's financial position.

Hence, under Ind AS, it is important to determine whether to present liabilities that are part of a reverse factoring arrangement:

- Within trade payables;
- Within borrowings; or
- As a separate line item in balance sheet.

Consistent with IFRIC agenda decision, an entity presents such liabilities as part of 'trade payables' when those liabilities have a similar nature and function to trade payables, i.e. when those liabilities are part of the working capital used in the entity's normal operating cycle and are in respect of the amounts due on account of goods purchased or services received in the normal course of business.

An important aspect to be noted in this respect is that reverse factoring arrangement, in some cases, may result in the derecognition of the original trade payable and the recognition of a new financial liability and in other cases, there may not be de-recognition - would depend on whether there is legal release or whether there is substantial modification. However, consistent with IFRIC agenda decision discussed above, regardless of whether the original trade payable is derecognised, presentation of amounts related to reverse factoring arrangements needs to be done as per Ind AS 1, i.e. new financial liability owed to financial institution could still be presented as 'trade payables'.

Following are examples of features that may indicate that the nature or function of the amounts due is sufficiently different from a trade payable:

- The principal business purpose of the reverse factoring arrangement is to provide funding to the customer, rather than to provide funding to the supplier or to facilitate efficient payment processing
- The factor is a bank or similar financial institution and
- The arrangement:
  - Significantly extends payment terms beyond the normal terms agreed with other suppliers
  - Adds a requirement for the customer to pay interest or to pay interest at a higher rate
  - Requires additional collateral or a guarantee or
  - Changes the terms defining default and cancellation

Presentation in the statement of cash flows

Consistent with IFRIC agenda decision, in relation to presentation in the statement of cash flows, judgement needs to be first applied to assess whether a single cash outflow or multiple cash flows occur for the entity. This assessment is based on the specific facts and circumstances and the entity may consider whether the factor in substance acts on behalf of the entity in the reverse factoring arrangement.

Single cash outflow

- Payment to the supplier by the factor is a non-cash transaction that requires disclosure as per of Ind AS 7, *Statement of Cash Flows.*
- A single cash outflow for cash payments made to the factor is presented as operating or financing cash outflow. An entity applies judgement in determining whether to classify payments made to the factor as an operating or financing cash outflow, giving consideration to the primary principle that cash flows are classified according to the nature of the activity to which they relate, taking into account the specific facts and circumstances.

  For example, an entity needs to consider if the principal business purpose of the reverse factoring arrangement is to provide funding to the supplier or to facilitate efficient payment processing, and whether the reverse factoring arrangement significantly extends payment terms beyond the normal terms agreed with other suppliers.

Multiple cash flows

Gross cash flows are presented - i.e. financing cash inflows and operating cash outflows when the factor makes a payment to the supplier in respect of the purchase of goods or services made by the entity, together with a financing cash outflow for settlement of amounts due to the factor.

Key disclosures in notes to the financial statements

Given the impact on the financial statements, it is important to appropriately provide disclosures in relation to reverse factoring arrangement in the financial statements. Some of the key disclosures would include:

- Disclosure of significant accounting policies as per Ind AS 1
- Disclosure of significant judgements made in the process of applying the accounting policies and that have the most significant effect on the amounts recognised in the financial statements as per Ind AS 1
- Qualitative disclosures about the entity's exposure to liquidity risk as per Ind AS 107, *Financial Instruments: Disclosures*
- Quantitative information relating to liquidity risk, including concentrations of it as per Ind AS 107
- Where cash flows for related liabilities are classified as financing activities, disclosures that enable users to evaluate changes in liabilities arising from financing activities as per Ind AS 7.

Future developments

In November 2021, IASB published an Exposure Draft *Supplier Finance Arrangements - Proposed amendments to IAS 7 and IFRS 7* in response to users' calls for additional information about such arrangements in financial statements. The proposals did not address the classification or presentation of the related liabilities and cash flows. Rather, the proposals complement the IFRS Interpretations Committee's agenda decision Supply Chain Financing Arrangements - Reverse Factoring published in December 2020.

The proposals require entities to disclose information about their supplier finance arrangements that enables users of financial statements to assess the effects of those arrangements on the entity's liabilities and cash flows. The proposals would introduce a new disclosure objective in IAS 7 and specific disclosure requirements in IAS 7 and IFRS 7, including the following:

- The terms and conditions of each supplier finance arrangement (including, for example, extended payment terms and security or guarantees provided)
- For each supplier finance arrangement, at the beginning and the end of the reporting period:
  a. The carrying amount of financial liabilities recognised in the entity's statement of financial position that are part of the arrangement and the line item(s) in which those financial liabilities are presented
  b. The carrying amount of financial liabilities that are part of the arrangement for which suppliers have already received payment from the finance providers and
  c. The range of payment due dates (e.g. 30 to 40 days after the invoice date) of financial liabilities that are part of the arrangement
- At the beginning and the end of the reporting period, the range of payment due dates of trade payables that are not part of a supplier finance arrangement and
- Additional information about supplier finance arrangements necessary to meet the disclosure objective.

The amendments are expected to be issued in May 2023 and the IASB tentatively decided to require an entity to apply the amendments for annual reporting periods beginning on or after 1 January 2024.

Key points for consideration

Each reverse factoring arrangement must be assessed separately, taking into account the contractual terms and conditions. Entities need to carefully consider the principal business purpose of the reverse factoring arrangement, other terms and conditions of the arrangement, and apply judgement in determining the presentation in the balance sheet and statement of cash flows.

Entities should also carefully consider the disclosures that will be necessary to explain the nature of the reverse factoring arrangement, impact of the arrangement and the judgements made.

Source: KPMG IFRG Limited's publication Insights into IFRS, 19th edition, October 2022.

CHAPTER 2

Climate related disclosures

This article aims to:

- Provide an overview of climate related risks and its disclosures.

Background

Over the recent years, there has been an increased focus on the importance of Environmental, Social and Governance (ESG) factors. As climate-related risk is a dominant factor of ESG, companies and other stakeholders are increasingly interested because of its potential effect on companies' business models, cash flows, financial position and financial performance. On account of the growing implications of climate risk for the preparation of financial statements and lack of sufficient disclosure of climate-related information in financial statements, regulators and standard setting bodies such as Securities Exchange Commission (SEC), the European Union (EU) and the International Sustainability Standards Board (ISSB) would be issuing climate related disclosure requirements to increase transparency and clarity.

Further, it is important to note that in March 2023, the International Accounting Standards Board (IASB) initiated a project to explore - whether and how a company's financial statements can provide better information about climate-related risks. The project is a result of feedback received from stakeholders stating climate related risks may not be appropriately disclosed in the financial statements and that there is a need for better qualitative and quantitative information about the effect of climate-related risks on the carrying amounts of assets and liabilities reported in the financial statements.

Regulatory developments

The regulators around the globe are working on developing the disclosure requirements relating to climate risk. Following are some of the developments by standard setters relating to climate risk:

- **ISSB:** The ISSB has been formed to develop IFRS Sustainability Disclosure Standards that will result in a high-quality and comprehensive global baseline sustainability disclosures. In March 2022. ISSB had proposed global baselines standards for sustainability disclosures-which include two standards IFRS S1 and IFRS S2. IFRS S1 provides general requirements for disclosure of sustainability-related financial information and IFRS S2 delas with climate-related disclosures. The standards are expected to be finalised by June 2023 and applicable for periods beginning on or after 1 January 2024.
- **European Financial Reporting Advisory Group (EFRAG):** In November 2022, the European Union adopted a Corporate Sustainability Reporting Directive (CSRD), which introduces more detailed climate related and other ESG reporting requirements including assurance for many entities. The entities subject to the CSRD will have to report according to European Sustainability Reporting Standards (ESRS).

  The EFRAG has developed 12 draft European Sustainability Reporting Standards (ESRSs) providing detailed disclosure requirements based on CSRD by the European Commission. The draft ESRSs consist of ESG topics including climate change[1]. The ESRSs are expected to be finalised by June 2023 and applicable for periods beginning on or after 1 January 2024 .
- **SEC:** The SEC proposed climate rule[2] in March 2022 based on the Task Force on Climate-related Financial Disclosures (TCFD) framework and the Greenhouse Gas (GHG) Protocol. The proposed rules are expansive and intend to provide more consistent, comparable and decision-useful information to enable investors and stakeholders to evaluate the impact of climate-related matters. The final rules are expected to be issued in near future.
- **Business Responsibility and Sustainability Reporting (BRSR) mandated by SEBI:** The Securities Exchange Board of India (SEBI) mandated the BRSR disclosures for top 1,000 listed companies[3] from Financial Year (FY) 2022-23 onwards. One of the important disclosures under the BRSR relates to an entity's material responsible business conduct and sustainability issues pertaining to environmental, social matters that present a risk or an opportunity to an entity's business, rationale for identifying the same, approach to adapt or mitigate the risk along with its financial implications. These disclosures would include risk arising from climate change such as impact on operations, employees, etc.

Further, in March 2023 SEBI has approved to introduce 'BRSR Core' which consist of limited set of Key Performance Indicators (KPIs) under each E, S and G attributes/areas. The BRSR Core would include attributes such as change in GHG footprint, change in water footprint, environmental footprint, waste management etc.

The SEBI has also provided that reasonable assurance would be applicable on BRSR Core in the following manner:

a. Top 150 listed entities (by market capitalisation) from FY 2023-24 and

b. Gradually, applicability will be extended to the top 1,000 listed entities by FY 2026-27

In relation to assurance of sustainability information, the Institute of Chartered Accountants of India (ICAI) has developed Standard on Assurance Engagement (SAE) 3410, *Assurance Engagement on Greenhouse Gas Statements* and Standard on Sustainability Assurance Engagements (SSAE) 3000, *Assurance Engagements on Sustainability Information* to be applicable for assurance reports covering periods ending 31 March 2024 and voluntary for 31 March 2023.

1. The standard, ESRS E1, *Climate change* provides the disclosure requirements on the impact of climate change, mitigation efforts, the plans and capacity of the undertaking to adapt its strategy business model and other such climate change related disclosures.
2. The SEC proposes rules to enhance and standardise climate-related disclosures for investors.
3. As per market capitalisation as on 31 March of previous year

About climate risk

The TCFD categories climate risk as follows:

Physical risk	Transition risk
• Effects of climate risk on the physical environment • Examples: Floods, hurricanes, wildfires, drought, rising temperatures and sea levels, weather pattern changes.	• Risks arising from transition to a lower-carbon economy • Examples: Changing customer behaviour, availability of capital, stigmatisation of industries, stranded assets.

About TCFD: The TCFD was established by Financial Stability Board (FSB) with an aim to develop recommendations on the types of information that companies should disclose to support investors, lenders, and insurance underwriters in appropriately assessing and pricing risks related to climate change. The TCFD recommendations are structured around the four thematic areas representing core elements of how organisations operate: governance, strategy, risk management, and metrics and targets. The four thematic areas are supported by recommended disclosures that build out the framework with information aimed at helping investors understand how companies assess climate related risks and opportunities.

Although the effects of climate risks are relevant to all entities, certain industries are more susceptible by their nature. TCFD has identified the following high-risk industries:

Finance	Energy	Transportation	Material and buildings	Agriculture, food, forestry products
▪ Banks ▪ Insurance companies ▪ Asset owners ▪ Asset managers	▪ Oil and gas ▪ Coal ▪ Electric utilities	▪ Air freight ▪ Passenger air ▪ Maritime ▪ Rail ▪ Trucking ▪ Automobiles, components	▪ Materials, mining ▪ Chemicals ▪ Construction materials ▪ Capital goods ▪ Real estate	▪ Beverages ▪ Agriculture ▪ Packaged foods, meats ▪ Paper, forest products

Source: KPMG US Handbook, Climate risk in the financial statements, February 2023

However, it is important to note that the list of industry stated is only an indicator of risk but the nature and extent of risk to which an entity is exposed depends on numerous factors such as its business model, assets, geographical locations, services provided and supply chains.

Further, the climate related risks should be assessed in terms of business risks and opportunities such as changes to the viability of certain business activities, changes to market demand, changes to supply chain continuity etc.

Disclosure of climate related risks in the financial statements

In current times, all companies face climate-related risks and opportunities, but some are affected more than others. Therefore, investors and regulators are increasingly seeking greater transparency of climate-related information in financial statements. However, the disclosure of the impact of climate-related matters in the financial statements depends on specific facts and circumstances including the nature and extent of those impacts on the company, however, certain stakeholders have expressed concerns regarding an information gap with respect to disclosure of climate-related risks such as:

- A lack of evidence that material climate-related risks are reflected in the financial statements.
- A lack of transparency regarding climate-related assumptions and judgements made in preparing the financial statements.

What information is relevant to stakeholders?

Through the disclosure, a user wants to understand how climate risk impacts the entity and its environment including the business model, strategy and the assumptions and judgements used to make estimates. Therefore, it is important to understand how management presents its assessment of the impacts of climate-related risk. Following are some of the key factors that management should consider while disclosing its impact assessments are:

- **Business model and governance:** If the management has identified an emerging climate-related reporting risk which has an impact on its business model and governance of the organisation, then the same should be disclosed.
- **Risk, strategy, progress and viability:** Consider providing comprehensive disclosure on sustainability matters, particularly with respect to climate, to provide stakeholders information about how the climate-related risks and opportunities impact the entity, and the entity's strategy to respond, because it could affect their assessments of the entity's long-term prospects.
- **Materiality:** Considering materiality carefully will be a key issue in addressing user expectations. Materiality involves both quantitative and qualitative considerations. Further, even if the information is not material in amount, it may be material in nature thereby requiring disclosure of the same.
  - For some companies – e.g. those in higher-risk industries – the impacts may be quantitatively material.
  - For others with no significant quantitative impact in the current reporting period, management may need to provide an explanation because this could be qualitatively material to users.
  - For those that have not yet fully assessed the potential future impact on the financial statements, this fact may be qualitatively material and so an explanation may be needed.
- **Key judgements and estimates:** Many companies face uncertainty when considering the impacts of climate-related risks in recognising and measuring assets and liabilities. Investors and regulators expect robust disclosures of the most significant assumptions, estimates and judgements made in preparing the financial statements to understand whether and how they are affected by climate-related matters. While making disclosures, management should consider the specific disclosure requirements in Ind AS/IFRS standards as well as the overarching requirements of IAS 1/Ind AS 1[4] i.e. disclosure of information that is relevant to an understanding of the financial statements but is not specifically required by IFRS/Ind AS Standards or presented elsewhere in the financial statements.
- **Connectivity between financial statements disclosure and climate-related information:** There should be connectivity between non-financial reporting and financial reporting. The management should ensure consistency in the assumptions used in relevant areas of the company's financial statements and also, they are in sync with the climate-related risks discussed elsewhere in the annual report. It is pertinent to note that in case of changes in key assumptions related to climate-related risk, certain changes would not be expected to result in material adjustments in the measurement of assets and liabilities in the next financial year, but the chance of material adjustments in the longer term may be significant. In these circumstances, and given the expectations of investors, companies may need to consider disclosing key assumptions related to climate-related risk even though the risk of material adjustments in the next financial year may be considered to be low.
- **Other note disclosures:** Climate-related risks having financial consequences would impact the recognition and measurement of assets and liabilities. Therefore, climate-related risks may impact financial statements through, for example concentrations of risk and/or provisions and contingent liabilities. The company may want to consider other note on disclosure of contingent liabilities and financial instrument risks arising from climate-related factors.

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4. TInd AS 1, *Presentation of Financial Statements* deals with the overall requirements for the presentation of financial statements, guidelines for their structure and minimum requirements for their content. Further IAS 1/Ind AS 1 requires specific disclosures on key judgements and estimates made by management in preparing the financial statements.

The following section provides certain specific examples of potential impacts of climate related risk on the financial statements:

- **Asset useful life:** Life of the asset may be affected by commitments and strategies that affect the future operation of the business model. For example, commitments to operate the business on a carbon neutral basis or changes to the business model to respond to changing customer needs.
- **Impairment:** The longer-term assumption of 'business as usual' in impairment testing models may be affected by expectations of changes related to climate-related issues.
- **Provisions and contingent liabilities:** Obligations may arise from legal requirements, specific commitments or past practice to remedy environmental damage. Provisions for longer-term contracts may be required if they become loss-making as a result of increased direct costs, including those triggered by climate-related factors.
- **Expected credit losses:** Actual or expected adverse changes in the regulatory, economic or technological environment of borrowers could result in a significant change in their ability to meet debt obligations.

Additionally, it is important to note that, the European Securities and Markets Authority (ESMA) in its recent enforcement decisions published in March 2023 also highlighted that companies should provide more information in relation to climate-related matters in the notes to the financial statements as required by the principles of IAS 1.

Next steps

Unlike financial reporting where companies have robust systems in place to capture and report necessary data, reporting around ESG parameters is still developing, however it is developing at fast pace. The proposed standards and guidelines would support companies in providing information about their exposure to climate-related risks and opportunities. Assurance on sustainability information (including climate related matters) is also gaining importance as independent assurance helps in building trust, robustness and comparability of sustainability information. In this regard, regulators around the world are working towards bringing reforms in the sustainability assurance space. Therefore, companies should stay abreast of sustainability related developments and start accessing the disclosure requirements related to ESG and climate risk.

Source:

- KPMG US Handbook, Climate risk in the financial statements, February 2023
- The Center for Audit Quality (CAQ) publication, The Role of the Auditor in Climate-Related Information, March 2023
- KPMG IFRG Limited publication "Have you disclosed the impacts of climate-related matters clearly", January 2022 edition.

CHAPTER 3

Regulatory updates

Amendments to Ind AS

The Ministry of Corporate Affairs (MCA), through a notification dated 31 March 2023, issued the Companies (Indian Accounting Standards) Amendment Rules, 2023 to notify certain amendments to Ind AS. These amendments are effective from 1 April 2023.

Source: MCA notification no. G.S.R. 242(E). dated 31 March 2023

The key amendments are with respect to:

Ind AS	Amendment notified
Ind AS 1, *Presentation of Financial Statements*	• Companies are now required to disclose material accounting policies instead of significant accounting policies. • Accounting policy information considered together with other information, is material when it can reasonably be expected to influence decisions of primary users of general-purpose financial statements. • Accounting policy information that relates to immaterial transactions, other events or conditions need not be disclosed. Accounting policy information may be material because of the nature of the related transactions, other events or conditions, even if the amounts are immaterial. However, not all accounting policy information relating to material transactions, other events or conditions is itself material.
Ind AS 8, *Accounting policies, Change in Accounting Estimates and Errors*	• The definition of 'change in account estimate' has been replaced by the definition of an 'accounting estimate'. As per the amendment, accounting estimates are monetary amounts in the financial statements that are subject to measurement uncertainty. • The amendment states that a company develops an accounting estimate to achieve the objective set out by an accounting policy. • As per the amendment, measurement techniques and inputs are used to develop an accounting estimate. Measurement techniques include estimation techniques and valuation techniques.
Ind AS 12, *Income Taxes*	The amendment has narrowed the scope of the Initial Recognition Exemption (IRE) for deferred tax liability and asset. As per the amendment, a deferred tax liability or asset is not required to be recognised from: a. Initial recognition of goodwill or b. Initial recognition of an asset or liability arising in a transaction which: I. Is not a business combination II. At the time of the transaction, affects neither accounting profit nor taxable profit (tax loss); and **III. At the time of the transaction, does not give rise to equal taxable and deductible temporary differences** *(emphasis added to highlight the change)*
Other consequential amendments	• On account of the amendment to Ind AS 1 consequential amendment have been made in Ind AS 107, Financial Instrument Disclosures and Ind AS 34, Interim Financial Reporting • On account of the amendment to Ind AS 12, consequential amendments have been made in Ind AS 101, First-time Adoption of Indian Accounting Standards

SEBI issues circular for Large Corporates (LCs) meeting financing needs from debt market

On 31 March 2023, the Securities Exchange Board of India (SEBI) issued a circular to extend the period of compliance stipulated in the NCS Operational Circular[1] for LCs meeting their financing needs through issuance of debt securities in debt markets.

As per a circular issued on 31 March 2023, LCs are required to raise minimum 25 per cent of their incremental borrowings in a financial year through issuance of debt securities which has to be met over a contiguous block of **three years** *(earlier two years)* from Financial Year (FY) 2021-22 onwards.

Source: SEBI circular no. SEBI/HO/DDHS/DDHS-RACPOD1/P/CIR/2023/049 dated 31 March 2023)

RBI issues framework for acceptance of green deposits

Green finance has been gaining importance in India. It has been observed that some Regulated Entities (REs) are offering green deposits for financing green activities and projects.

In this regard, the Reserve Bank of India (RBI) issued a framework for acceptance of green deposits on 11 April 2023. The framework aims to encourage REs to offer green deposits to customers, protect interest of the depositors, aid customers to achieve their sustainability agenda, address greenwashing concerns and assist in increasing the flow of credit to green activities/ projects.

The framework would be applicable to the following REs with effect from 1 June 2023:

a. Scheduled commercial banks including small finance banks (excluding regional rural banks, local area banks and payments banks) and

b. All deposit taking Non-Banking Financial Companies (NBFCs) registered with RBI[2].

The framework provides guidance with respect to:

- Denomination, interest rates and tenor of deposits
- Policy on issuance of green deposits
- Financing framework for effective allocation of green deposits
- Allocation and use of proceeds raised from green deposits
- Requirements on independent third-party verification/assurance with respect to the allocation of funds raised through green deposits
- Reporting and disclosure requirements.

Source: RBI notification no. RBI/2023-24/14 DOR. SFG.REC.10/30.01.021/2023-24 dated 11 April 2023

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1. Operational Circular for issue and listing of Non-Convertible Securities (NCS), Securitised Debt Instruments (SDI), Security Receipts (SR), Municipal Debt Securities and Commercial Paper (CP) dated 10 August, 2021 and amended from time to time

2. Register under Section 45IA(5) of the RBI Act, 1934, including Housing Finance Companies (HFCs) registered under Section 29A of the National Housing Bank Act, 1987

NFRA issues circular on measurement of revenue and trade receivables

On 29 March 2023, the National Financial Reporting Authority (NFRA) issued a circular to highlight non-compliances in the areas of recognition and measurement of revenue and initial measurement of corresponding trade receivables.

The key takeaways from the circular are as follows:

- **Revenue from contracts with customers - recognition and measurement**

  As per Ind AS 115, *Revenue from Contracts with Customers,* transaction price should be recognised as revenue, and it should exclude estimates of variable consideration that is allocated to the performance obligation.

  NFRA circular highlighted that many companies, in their significant accounting policies, have incorrectly stated that the revenue is recognised and measured at fair value of the consideration received or receivable leading to non-compliance with the requirements of Ind AS 115. It is pertinent to note that the transaction price defined in Ind AS 115 is different from 'fair value' defined in Ind AS 32, *Financial Instruments: Presentation.* Under Ind AS 115, the application of fair value is relevant only in a limited set of situations for example where a customer promises consideration in a form other than cash, an entity shall measure the non-cash consideration at fair value.

- **Trade receivables – initial measurement**

  As per Ind AS 109, *Financial Instruments*, trade receivables are financial assets which are initially measured at their transaction price (as defined in Ind AS 115) unless they contain a significant financing component determined in accordance with Ind AS 115.

  NFRA circular highlighted that many companies in their accounting policy are erroneously stating that the trade receivables are initially recognised (or measured) at fair value, which is contrary to the requirements of Ind AS 109. Further, there have also been instances of inconsistency between the accounting policy for initial measurement of trade receivables and the accounting policy for measurement of corresponding revenue leading to misleading and confusing information to the users of the financial statements. This has resulted in a non-compliance with requirements of the standards.

Source: NFRA circular no. NF-25011/1/2023-O/o Secy-NFRA dated 29 March 2023

ICAI has issued technical guide on disclosure and reporting of Key Performance Indicators (KPIs) in offer documents

As per the provisions of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations) an issuer company is required to disclose Key Performance Indicators (KPIs) in the offer document under heading 'Basis for Issue Price' in case of an Initial Public Offer (IPO). KPIs are numerical measures of the issuer company's historical financial or operational performance and financial or operational positions which provide valuable insight of the entity's business. KPIs are required to be approved by the audit committee of the issuer company.

Further, they should be certified by professionals (statutory auditors or chartered accountants or firm of chartered accountants or cost accountants). In this regard, the Institute of Chartered Accountants of India (ICAI) has issued a Technical Guide (the guide) on disclosure and reporting of KPIs in the offer documents.

The guide provides guidance on KPIs that can be disclosed based on different industry, the role and responsibility of bankers, issuer company and practitioners, detailed guidance to practitioners on various aspects of reporting requirements relating to KPIs including illustrative format of the report on KPIs. Additionally, the guide also provides guidance to issuer companies for disclosing KPIs in offer documents as per the requirements of ICDR Regulations.

Source: ICAI announcement 6 April 2023

ICAI issues exposure draft on transfer of capital reserve

As per the requirements under certain Ind AS, capital reserve is required to be created towards unrealised profits arising from certain transactions or other events. However, currently there is no specific guidance on subsequent transfer of such capital reserve to retained earnings or other free reserve. Therefore, in order to provide appropriate guidance on this matter, ICAI has issued an exposure draft on 'Guidance Note on Transfer of Capital Reserve'.

The draft guidance note lays down the principles for transfer of capital reserve to free reserve/ retained earnings, including the timing when such transfer can be made. However, it does not deal with whether the amount so transferred can be utilised for payment of dividend, issue of bonus shares, or any other purpose.

The key considerations from the exposure draft are as follows:

- Any reserve created as per the requirements of the Companies Act, 2013 or other applicable law cannot be transferred to other reserve except as per the requirements of the applicable law.
- For capital reserves created as per the requirements of Ind AS or erstwhile Accounting Standards (AS), the amount can be transferred to retained earnings or other free reserves when the following two conditions are met:
  a. The company has realised the underlying amount.
  b. The amount has become available for distribution under the law.
- The amount may be transferred either proportionately each year or at end on sale of the asset.
- Specific disclosures are required to be provided in the year of transfer.
- The guidance note would come into effect in respect of capital reserve appearing in the books of accounts retrospectively.

The period to provide comments on the exposure draft ended on 20 April 2023.

Source: ICAI announcement dated 21 March 2023

IASB proposes narrow-scope amendments to classification and measurement requirements for financial instruments

On 21 March 2023, the International Accounting Standards Board (IASB) has issued an exposure draft to propose amendments to the classification and measurement requirements in IFRS 9, *Financial Instruments* and IFRS 7, *Financial Instrument:* Disclosure in response to feedback received from a Post-Implementation
Review (PIR) of the classification and measurement requirements in IFRS 9. IFRS 9 specifies how a company should classify and measure financial assets and financial liabilities.

The key proposal are as follows:

- **Classifying financial assets with an ESG-linked feature:** The proposed amendments clarify how a company would assess the Solely Payments of Principal and Interest (SPPI) condition for the contractual cash flows arising from a financial asset with contingent features. The proposals provide clarification on how to classify financial assets with an ESG-linked feature. Further, the proposal addresses all contingent features and not just ESG-linked features. The proposals also include additional disclosures for all financial assets and financial liabilities that have particular types of contingent cash flows and are not measured at fair value through profit or loss.
- **Classifying Contractually Linked Instruments (CLI):** In order to address concerns regarding application of SPPI requirements to CLIs, the proposal aims to clarify their key characteristics and how they differ from financial assets with non-recourse features. The proposals also provide factors a company could consider when assessing the cash flows underlying a financial asset with non-recourse features (the 'look through' test).
- **Disclosures on investments in equity instruments:** Additional disclosures are proposed for equity instruments that are measured at fair value and whose gains or losses are presented in other comprehensive income (FVOCI). IASB is not proposing any change to the measurement requirements for investments in equity instruments.
- **Settlement of liabilities through electronic payment systems:** With respect to settlement of a financial asset and financial liability via electronic cash transfers, the IASB's proposal clarifies that a company would generally recognise and derecognise financial assets or financial liabilities on their settlement date

  Further, the IASB is proposing an exception that would apply only for financial liabilities. As per the proposal, a company would be allowed derecognise a financial liability that will be settled with cash using an electronic payment system before the settlement date if and only if the company has initiated the payment instruction and:

  a. The company has no ability to withdraw, stop or cancel the payment instruction

  b. The company has no practical ability to access the cash to be used for settlement as a result of the payment instruction and

  c. The settlement risk associated with electronic payment system is insignificant.

The comments on the above proposal can be provided till 19 July 2023.

Source: IASB news dated 21 March 2023, KPMG IFRG article on 'Addressing financial asset classification issues' issued on 23 March 2023 and KPMG IFRG article on 'Addressing financial asset classification issues' issued on 23 March 2023

FASB provides guidance on application of leases to arrangements between entities under common control

During the Post-Implementation Review (PIR) of Topic 842, *Leases*, certain concerns were highlighted to the Financial Accounting Standards Board (FASB) with respect to application of Topic 842 to related party arrangements between entities under common control. Considering this, FASB issued an Accounting Standard Update (ASU) on 27 March 2023.

The ASU provides private companies and not-for-profit organisations that are not conduit bond obligors with a practical expedient to use the written terms and conditions of a common control arrangement to determine whether a lease exists and, if so, the classification of and accounting for that lease. Further, the ASU also requires all entities (that is including public companies) to amortise leasehold improvements associated with common control leases over the useful life to the common control group.

(Source: FASB news and media advisory issued on 27 March 2023)

FASB issues ASU to improve accounting for investments in tax credit structures

On 29 March 2023, FASB issued an ASU with aim to improve the accounting and disclosures for investments in tax credit structures.

Reporting entities were previously permitted to apply the proportional amortisation method only to qualifying tax equity investments in Low-Income Housing Tax Credit (LIHTC) structures. However, stakeholders provided feedback to FASB to extend the application of the proportional amortisation method to qualifying tax equity investments that generate tax credits through other programs.

The ASU allows reporting entities to elect to account for qualifying tax equity investments using the proportional amortisation method, regardless of the program giving rise to the related income tax credits.

(Source: FASB news and media advisory issued on 29 March 2023)

Technology related revisions to the international code of ethics for professional accountants

On 11 April 2023, the International Ethics Standards Board for Accountants (IESBA) issued revisions to the International Code of Ethics for Professional Accountants (including International Independence Standards) (the Code) in order to increase the Code's robustness and expand its relevance considering the rapid technological advancements and accelerated digitalisation.

Key takeaways from the revision are:

- To strengthen the Code in guiding the mindset and behaviour of professional accountants when they use technology.
- Provides enhanced guidance for the digital age in relation to the fundamental principles of confidentiality, and professional competence and due care, as well as in dealing with circumstances of complexity.
- Strengthens and clarifies the International Independence Standards (IIS) by addressing the circumstances in which firms and network firms may or may not provide a technology-related non-assurance service to an audit or assurance client.

The revisions to the IIS and other revisions to the ethics provisions of the Code will be effective for audits and reviews of financial statements for periods beginning on or after 15 December 2024.

(Source: IESBA news dated 11 April 2023)

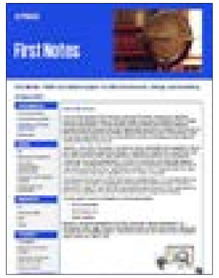
New sustainability reporting guidance issued by COSO

On 30 March 2023, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) issued supplemental guidance, 'Achieving Effective Internal Control Over Sustainability Reporting' for organisations to achieve effective Internal Control over Sustainability Reporting (ICSR) based on globally recognised COSO Internal Control-Integrated Framework (ICIF).

The supplemental guidance includes several key themes as organisations and practitioners begin or continue their journeys towards establishing and maintaining an effective system of internal control over financial and sustainable business information. The guidance is based on COSO's 2013 framework for evaluating and improving internal control systems over all types of business information used for external reporting and enterprise decision-making.

(Source: COSO news dated 30 March 2023 and IFAC article on 'How COSO's New Sustainability Reporting Guidance Provides Opportunities for the Profession' dated 12 April 2023)

First Notes



SEBI consultation paper on ESG disclosures, ratings and investing

There has been a growing emphasis towards the significant economic and financial impact of Environmental, Social and Governance (ESG) related risks and opportunities, ESG investing is becoming increasingly popular among the investors and other stakeholders. This has also led to an increase in the number of ESG funds being launched and related rating products being used. Considering the relevance of ESG information to stakeholders, it is important that such information is complete, comparable and relevant to the extent possible. In order to address this, SEBI constituted the ESG Advisory Committee to recommend regulatory framework for ESG disclosures, ratings and investing.

Based on the recommendations of the ESG Advisory Committee and other internal deliberations, on 20 February 2023, SEBI issued a 'Consultation Paper on ESG disclosures, ratings and investing'. Subsequently, on 22 February 2023, SEBI issued a consultation paper to propose a regulatory framework for ERPs.

In this issue of the First Notes, we aim to provide an overview of key proposals of the consultation papers issued by SEBI relating to regulatory framework of ESG disclosures by listed entities, ESG ratings in securities market (including regulatory framework for ERPs) and ESG investing by mutual funds.

To access the First Note, please **click here.**

Key financial reporting updates for the quarter ended 31 March 2023

In this session of the Voices on Reporting webinar, we have discussed following key updates:

- Implementation of audit trail
- Key SEBI updates
-Other key regulatory updates and year-end reminders.

For presentation and recording, please **click here.**

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