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Editorial

On 9 April 2024, the International Accounting Standards Board (IASB) issued IFRS 18, *Presentation and Disclosure in Financial Statements*. IFRS 18 supersedes IAS 1, *Presentation of Financial Statements* with effect from accounting periods beginning on or after 1 January 2027. Under current IFRS Accounting Standards, companies use different formats to present their results, making it difficult for investors to compare financial performance across companies. IFRS 18 promotes a more structured income statement and introduces a newly defined 'operating profit' subtotal and a requirement for all income and expenses to be allocated between three new distinct categories based on a company's main business activities. IFRS 18 will affect companies across all industries that prepare financial statements under IFRS Accounting Standards. Companies will be able to tell their story better through their financial statements, with the help of IFRS 18. Investors will also benefit from greater consistency of presentation in the income and cash flow statements, and more disaggregated information. This edition of Accounting and Auditing Update (AAU) discusses the new standard IFRS 18 and aims to provide an overview of the key requirements of IFRS 18.

With increasing focus on climate threat, Governments around the globe have made commitments to limit global warming and reach net zero carbon emissions by 2050 (or earlier). Carbon markets are crucial in meeting these commitments as they allow governments and organisations to efficiently regulate emissions and emission reduction limits. Under the Paris Agreement, India has set ambitious targets to reduce the intensity of carbon emissions by 45 per cent. Aligned with this vision, the country has developed a comprehensive strategy to achieve net-zero emissions by 2070, emphasising environmentally friendly practices. Considering these commitments, Carbon Credit Trading Scheme, 2023 (CCTS 2023) was notified by the Government of India in June 2023 under the Energy Conservation Act, 2001, to develop the country's first-ever domestic carbon market. The notification emphasises the essential structure and the responsibilities of various stakeholders in the establishment and operation of the Indian Carbon Market (ICM). Additionally, in October 2023, the Green Credit Rules, 2023 were notified, by the Ministry of Environment, Forest and Climate Change (MoEFCC). These rules aim to initiate a Green Credit program that utilises a competitive market-based approach to encourage voluntary environmental actions by stakeholders. The Green Credit program is designed to supplement the Carbon Credit Trading Scheme, issued under the Energy Conservation (Amendment) Act, 2022. This publication carries an article on this topic, which aims to provide an overview of the recent developments around the carbon credit and green credit markets.

As is the case each month, we have also included a regular round-up of some recent regulatory updates in India and internationally.

Sai Venkateshwaran
Partner - Assurance
KPMG in India

Ruchi Rastogi
Partner - Assurance
KPMG in India

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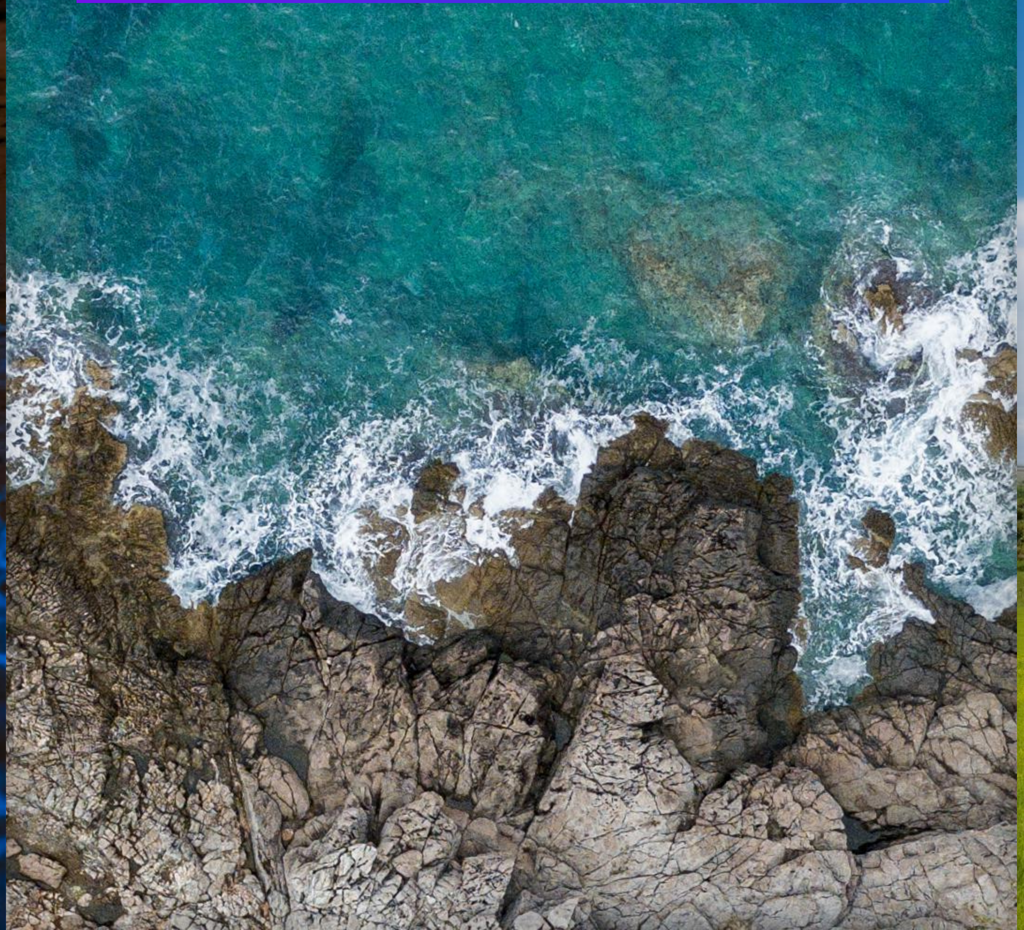
CHAPTER 1

IFRS 18, *Presentation and Disclosure in Financial Statements*

CHAPTER 2

Development of Carbon Credit and Green Credit



CHAPTER 3

Regulatory updates

CHAPTER 1

IFRS 18, *Presentation and Disclosure in Financial Statements*

This article aims to:

Provide an overview of the IFRS 18.

Introduction

On 9 April 2024 the International Accounting Standards Board (IASB) issued IFRS 18 *Presentation and Disclosure in Financial Statements*. IFRS 18 replaces IAS 1 *Presentation of Financial Statements* with effect from accounting periods beginning on or after 1 January 2027. The requirements in IAS 1 that are unchanged have been transferred to IFRS 18 and other Standards. Companies will be required to apply the new requirements in interim financial statements in the initial year of application, and to restate comparative information for the prior year ('apply IFRS 18 retrospectively') in accordance with IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*.

The objective of IFRS 18 is to improve communication of financial information in the financial statements, particularly the statement of profit or loss.

Essentially, companies' net profit will not change. What will change is how they present their results on the face of the income statement and disclose information in the notes to the financial statements.

Investors wanted comparable subtotals and more disaggregation of information to better understand a company's performance and enable greater comparability between companies. IASB noted that while some companies present an "operating profit or loss" subtotal today, it is calculated differently, and this diversity made it challenging for investors to compare across companies. In response to investors' calls for more relevant, transparent and comparable information IFRS 18 have been introduced.

IFRS 18 will affect companies across all industries that prepare financial statements under IFRS Accounting Standards.

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Overview of IFRS 18

Some of the key changes brought in by IFRS 18 are introduction of three categories of income and expenses, two income statement subtotals and one single note on management performance measures. These, combined with enhanced disaggregation guidance, will set the stage for better and more consistent information for users – and will affect all companies.

IFRS 18 affects the complete set of financial statements, including:

Primary financial statements

- **statement of financial position** (balance sheet)
- **statement of profit or loss** (income statement)
- **statement presenting comprehensive income**
- **statement of changes in equity**
- **statement of cash flows** (cash flow statement)
- **and the notes to the financial statements**

Legend:

Major changes | Some changes | Minimal changes

Requirements on grouping of information will affect the complete set of financial statements.

(Source: Project Summary of IFRS 18 issued by IASB, April 2024)

Major impact on the Statement of Profit or Loss (income statement)

IFRS 18 have introduced subtotals in the statement of profit or loss where a company will classify income and expenses into **operating**, **investing** and **financing** categories plus **income taxes** and **discontinued operations**; and will present two new defined subtotals:

a. Operating profit and

b. Profit before financing and income taxes in the statement of profit or loss.

The standard further requires companies to analyse the operating profit either by nature, by function or using mixed presentation. If any operating expenses are presented by function or using mixed presentation, then new disclosures will apply.

This information is likely to provide investors a breakup of operating profit and profit before investing and financing activities where operating profit is used as a comparable measure of financial performance and a starting point for forecasting future cash flows.

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How will the income statement look now?

Income statement
Companies without specified main business activities

Operating*	Revenue	X
	Operating expenses (analysed by nature, function or both as appropriate)	(X)
	Operating profit	**X**
Investing*	**Share of profit or loss of equity-accounted investees**	X
	Income from other investments	X
	Interest income from cash and cash equivalents	X
	Profit or loss before financing and income tax*	**X**
Financing*	Interest expense on borrowings and lease liabilities	(X)
	Interest expense on pension liabilities	(X)
	Profit before tax	**X**
	Income tax	(X)
	Profit for the year	**X**

* The operating, investing and financing categories are not aligned with those for the cash flow statement.

* Companies providing financing to customers as a main business activity (e.g. banks) typically do not present this subtotal.

(Source: How companies communicate financial performance is changing, KPMG IFRG Limited's publication, April 2024)

Major impact in the notes to financial statements

a. MPMs to be disclosed in the notes to financial statements.

Non-GAAP measures that are a subtotal of income and expenses i.e. Management-defined Performance Measures ("MPM") (other than those listed by IFRS 18 or specifically required by IFRS Accounting Standards) which are used in public communications outside financial statements and are used to communicate to investors management's view of an aspect of the financial performance of the company as a whole will be reported now as a part of noted in the financial statements and subject to audit.

Companies often use these MPMs to explain their financial performance because it allows them to tell their own story and provides investors with useful insight into a company's performance.

IFRS 18 now requires the companies to identify and disclose these MPMs in the financial statements. For each MPM presented, companies will need to explain in a single note to the financial statements why the measure provides useful information, how it is calculated and reconcile it to an amount determined under IFRS Accounting Standards including tax and non - controlling interest effects for each reconciling item.

Making certain non-GAAP measures part of audited financial statements will bring more credibility to management's key performance indicators.

Some of the examples of MPMs are "adjusted profit", "adjusted operating profit" or "Adjusted earnings before interest, tax, depreciation and amortisation".

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b. Enhanced requirements for grouping (aggregation and disaggregation) of information

IFRS 18 sets out requirements to help companies determine whether information about items should be in the primary financial statements or in the notes and provides principles for determining the level of detail needed for the information. Under more aggregated information the companies in its primary financial statements will be required to provide **'useful structured summary'** of the company's assets liabilities, equity, income, expense and cash flows. Under more disaggregated information the companies in its notes will be required to provide 'additional **material** information'.

IFRS 18 also includes requirements for the presentation of operating expenses in the statement of profit or loss, disclosure of specified expenses by nature. Companies are discouraged from labelling items as 'other' and will now be required to disclose more information if they continue to do so.

There are certain clarifications provided in the standard with regard to:

- **Operating Category**

  The standard states that the operating category is a default category and will include all income and expenses arising from a company's operations, regardless of whether they are volatile or unusual in some way. It will also include, but will not be limited to, income and expenses from a company's main business activities which means that income and expenses from other business activities, such as income and expenses from additional activities, will also be classified in the operating category if those income and expenses do not meet the requirements to be classified in any of the other categories.

- **Investing Category**

  This will include income and expenses from assets that generate returns separately from a company's business activities—for example, a company might collect rentals from an investment property or dividends from shares in other companies and; income and expenses from cash and cash equivalents and investments in associates and joint ventures—for example, a company might earn its share of profits from an associate.

- **Financing Category**

  This will include income and expenses on liabilities such as bank loans and bonds (liabilities arising from pure financing transactions); and interest expenses on any other liability, for example, lease and pension liabilities. Therefore, the financing category includes interest expenses on all liabilities.

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- **Classification of foreign exchange differences**

  Foreign exchange differences are classified in the same category of the statement of profit or loss as the income and expenses from the items that gave rise to the foreign exchange differences. For example, foreign exchange differences on bank loans are classified in the financing category.

- **Nature of business that may impact in the classification**

  Some companies invest in assets or provide financing to customers as a main business activity—for example, banks and insurers. Income and expenses that would otherwise be classified in the investing or financing categories by most companies would form part of the operating result for such companies. IFRS 18 therefore requires these income and expenses to be classified in the operating category.

Changes introduced to other IFRS Standards

IFRS 18 has also introduced changes to other IFRS Accounting Standards, the most important include:

IAS 7, *Statement of Cash Flows*

- Operating Profit will be the starting point for the indirect method
- The option for classifying interest and dividend cash flows as operating activities has been eliminated[1].

IAS 34, *Interim Financial reporting*

IAS 34 was amended to require companies to disclose information about MPMs in interim financial statements. Some of the other changes (including those about subtotals) also apply to condensed financial statements in interim reports.

1. Classifying interest and dividends will differ for companies with specified main business

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Our Comments

IFRS 18 marks a step towards more connected reporting. It will significantly update the requirements for presentation and disclosures in the financial statements, with a particular focus on improving the reporting of financial performance.

The major impact will extend to statement of profit or loss and notes to financial statements with some minor changes to statement of cash flows and balance sheet.

Statement of profit or loss

- All Companies will need to carefully assess which income and expenses belong in each category. Classification will vary depending on whether a company has specified main business activities.
- Companies with multiple main business activities that include specified main business activities may find it onerous to classify income and expense in the income statement.
- Presentation by function and mixed presentation of operating expenses would represent a significant change to Ind AS 1. This is because Ind AS 1 currently mandates presentation of income and expenses by nature only in the statement of profit and loss.

Notes to financial statements

- Certain 'non-GAAP' measures that meet the definition of MPMs will now be reported in the financial statements and subject to audit. As a result, companies may need to decide to revisit the purpose and relevance of existing 'non-GAAP' measures communicated outside of the financial statements.
- The reconciliation under MPMs may involve additional effort. For instance, a company may need to develop an appropriate method to calculate income tax effect for each reconciling item in the note.

Next Steps

The new standard is effective from 1 January 2027 and applies retrospectively. It is also available for early adoption.

The companies will also have to carefully assess and evaluate the impact of requirements of the new standard in its financial statements and need to plan in advance and invest time as the standard will apply retrospectively. In addition to the presentation and disclosures changes due to IFRS 18, companies will also have to assess their strategy to explain the impact of change to their stakeholders such as investors and analysts. Additionally, this would also require changes to systems and processes including, IT systems, internal controls, etc.

Ind AS is converged to IFRS and IFRS 18 would be adopted in due course. The changes brought in by IFRS 18 would also need to be incorporated in the Schedule III to the Companies Act, 2013.

Certain amendments have also been made in other standards like IAS 7, IAS 33 and IAS 34 to align with the requirements of IFRS 18 which the companies will have to monitor and track the impact in its financial statements.

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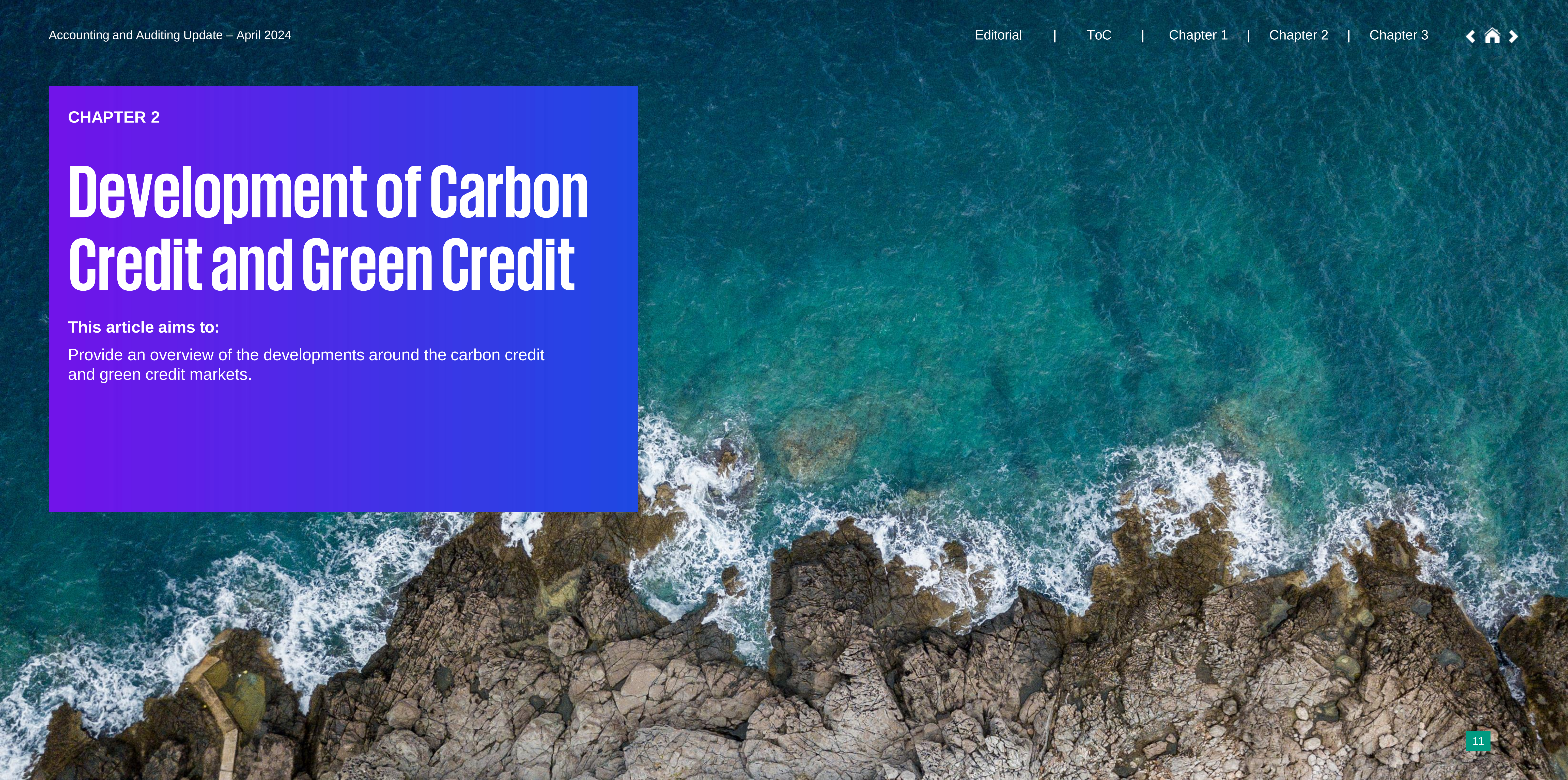


CHAPTER 2

Development of Carbon Credit and Green Credit

This article aims to:

Provide an overview of the developments around the carbon credit and green credit markets.

Introduction

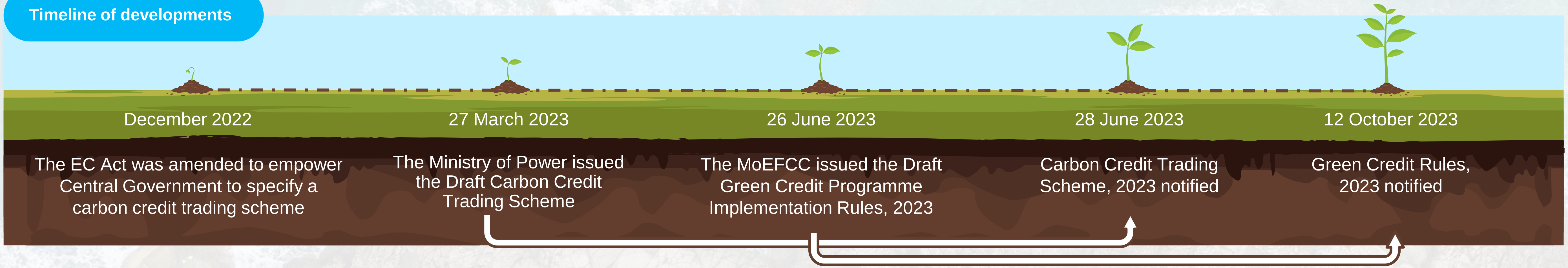
With climate change becoming a reality, governments of many countries have taken the responsibility of managing their carbon footprint in order to reduce the impact of climatic change or breakdown. The Paris Agreement adopted by 196 nations, including India, at the UN Climate Change Conference (COP21), is an international treaty to combat climate change. The participating countries are required to submit their Nationally Determined Contributions (NDCs) which provide the action plan of each country to reduce their Greenhouse Gas (GHG) emissions to achieve the goals of the Paris Agreement. The carbon credit market is one of the key solutions that is being adopted globally.

India is committed to reducing its carbon emissions intensity by 45 per cent by 2030 as per the Paris Agreement. Further, India has made commitments to limit global warming and has announced net-zero targets by 2070. Net-zero refers to reduction of GHG emissions to as close to zero, as much as possible, and offsetting the remaining emissions. Net-zero commitments typically include all value chain emissions as defined in the GHG Protocol. Carbon markets play a significant role to achieve such net zero commitments.

Against this backdrop, on 26 December 2022, the Ministry of Power issued amendments to the Energy Conservation Act, 2001 (EC Act). The EC Act establishes a regulatory framework for energy efficiency and its conservation. The amendments issued in 2022 to insert new provisions relating to carbon credit, emphasising decarbonization through a domestic carbon-trading scheme. To facilitate the achievement of India's enhanced NDC targets, the government has initiated the development of the 'Indian Carbon Market' (ICM) which will mobilise new mitigation opportunities through demand for emission reduction credits by private and public sector entities.

In this regard, in June 2023, the Central Government of India notified the Carbon Credit Trading Scheme (CCTS). Subsequently, in October 2023, the Ministry of Environment, Forest and Climate Change (MoEFCC) further notified the Green Credit Rules (the Rules).

Timeline of developments



(Source: KPMG in India's analysis read with Notification no. 26 issued on 20 December 2022 issued by Ministry of Law and Justice, notification no. S.O. 2825 issued by Ministry of Power on 28 June 2023 and notification no. S.O. 4458 (E). dated 12 October 2023 issued by the Ministry of Environment, Forest and Climate Change)

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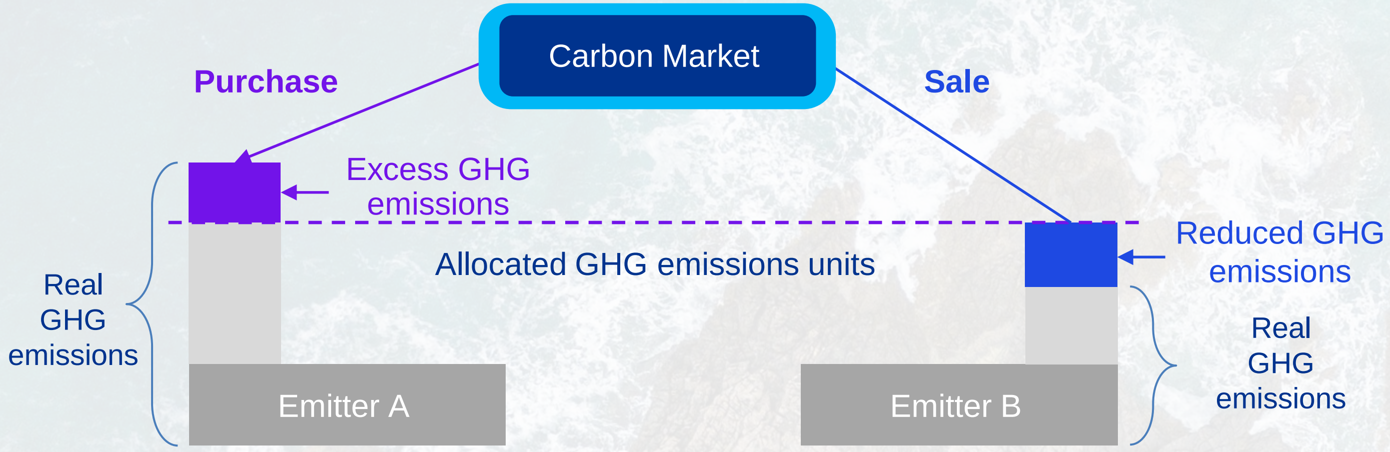
How does the carbon market work?

Every industry is permitted to emit certain amount of carbon dioxide or other GHG in the atmosphere. Carbon markets incentivise entities for reducing or removing GHGs within the prescribed limits, by issuing Carbon Credit Certificates (CCC).

On the other hand, if an entity exceeds the GHG emission threshold, it is required to purchase carbon credits from the organisation that has been issued with the CCC in order to offset its excess emissions. These CCC are transferable or tradeable instruments. Companies can purchase carbon credits to achieve net emissions targets or meet regulatory requirements. The entities may face penalties by the government for not meeting the regulatory requirements.



(Source: KPMG in India's analysis, 2023)

1. The Scheme defines obligated entities as 'registered entities' that are notified under the compliance mechanism of the Scheme and given a target for emission reduction. The non-obligated entities as 'registered entities' that can either generate or purchase the carbon credit certificates on voluntary basis. As per EC Act, a registered entity means any entity, including designated consumers, registered for carbon credit trading scheme.

Carbon Credit Trading Scheme (CCTS)

The CCTS is a strategic government initiative to establish and operationalise the domestic carbon market in India. The CCTS lays out the roles of various stakeholders for the functioning of the carbon market. It includes formation of the National Steering Committee as the governing board, the Bureau of Energy Efficiency as the administrator of the carbon market, trading of carbon credit certificates, the registry, the trading administrator, formation of Technical Committees, offset mechanism, etc.

The National Steering Committee for Indian Carbon Market (NSCICM) would help establish the Indian carbon market; by suggesting rules, regulations, developing the framework for voluntary carbon credit trading, and establishing trading criteria for carbon credits.

Carbon Credits

As per CCTS, carbon credit means a value assigned to a reduction, removal, or avoidance of GHG emissions achieved and is equivalent to one ton of carbon dioxide (tCO_2e). The CCTS requires obligated entity[1] to comply with the GHG emission norms in accordance with the targets as notified by the Central Government.

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Compliance mechanism under CCTS

CCTS has been notified in June 2023 and to operationalise CCTS, the Bureau of Energy Efficiency (the bureau), Ministry of Power and the Ministry of Environment, Forest and Climate Change (MoEFCC) issued a draft compliance mechanism. The draft compliance mechanism outline steps for obligated entities to ensure compliance with the CCTS scheme. Following are the key components of the draft mechanism:

i. GHG emission intensity trajectory and targets

The government would decide on the sectors and obligated entities that need to record and maintain GHG emissions data. It would then notify the GHG Emission intensity targets in terms of tons of carbon dioxide equivalent (tCO_2e) per unit of equivalent product, which must be met annually over a three-year trajectory period. The obligated entities who fail to achieve the emission targets can purchase the CCC to meet the emission targets.

GHG emission intensity reduction trajectory for relevant sectors will be based on the following -

- Nationally Determined Contributions
- Potential for usage of non-fossil fuels and decarbonisation in the sector
- Technology and cost of implementations

GHG emission intensity reduction targets for relevant sectors will be based on the following -

- The GHG emission intensity reduction trajectory for that sector
- Average rate of reduction in GHG emission intensity for that sector determined based on the historical data

ii. Monitoring and reporting process

- In order to achieve the GHG emissions targets set, the obligated entities are required to put in place a transparent and credible monitoring plan to monitor and report their GHG emissions.
- The monitoring plan would be submitted to the Bureau with prescribed timelines covering details such as activities being monitored, sampling procedure, written procedure, etc.
- All the activities undertaken by the obligated entity under this procedure should be scrutinised by the accredited carbon verifier for the purpose of preparation of verification report and verify compliance with respect to GHG emissions norms as notified by the MoEFCC.

iii. Other components

- ***Verification and performance assessment:*** The compliance mechanism provides that the performance of the obligated entities in achieving the GHG emission intensity targets would be verified and assessed in the prescribed manner.
- ***Issuance of Carbon Credit Certificates:*** The obligating entities on achieving the set targets will be issued carbon credit certificates by the Bureau.
- ***Trading of Carbon Credit Certificates:*** After the issuance of the carbon credit certificates, it can be traded in the Indian Carbon Market (ICM) as per the prescribed procedures.
- ***Banking of Carbon Credit Certificates:*** At the end of every compliance cycle, the balance CCC can be banked for utilisation in the next compliance cycles. The obligated entity also has the option of selling the banked CCC that was issued to it in the ICM in the next compliance cycles. However, the banked CCC that were purchased from the ICM can be used only in the compliance cycles in which it was purchased.

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Green credit rules

In October 2023, the MoEFCC introduced the Green Credit Rules (the rules) or the Green Credit Programme (GCP) which include activities for environmental preservation and protection that go beyond greenhouse gas emissions reduction or removal. The Rules define 'green credit' as a single unit of an incentive provided for a specified activity, delivering a positive impact on the environment.

The Green Credit market is independent of the CCTS framework, expanding the scope for climate action. The governance framework under these rules is supported by inter-ministerial Steering Committee and the Indian Council of Forestry Research and Education (ICFRE) as the administrator, who are responsible for program implementation, management, monitoring and operation.

List of activities notified under the Green Credit Rules

- Tree Plantation
- Water Management
- Sustainable Agriculture
- Waste Management
- Air pollution reduction
- Mangrove conservation & restoration
- Ecomark label development
- Sustainable building & infrastructure

(Source: KPMG in India's analysis, 2023 read with the Ministry of Environment, Forest and Climate Change notification dated 12 October 2023)

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The Green Credit system incentivises positive environmental actions by individuals, organisations, and industries, extending beyond greenhouse gas emissions and encourages improvements in air and water quality, waste reduction or management, etc. Similar to the carbon market structure, the programme allows entities to claim credits for actions positively impacting the environment and trade these for financial benefits also.

The rules outline detailed process for obtaining green credits. The Central Government would constitute a Steering Committee and technical committee to monitor and assist implementation of the Green Credit programme.

In this regard, on 22 February 2024, the MoEFCC notified the methodology for calculation of green credit in respect of tree plantation. Additionally, a draft methodology for water harvesting has also been issued in October 2023.

Some of the key points covered in the notified tree plantation methodology and draft methodology for water harvesting are as follows:

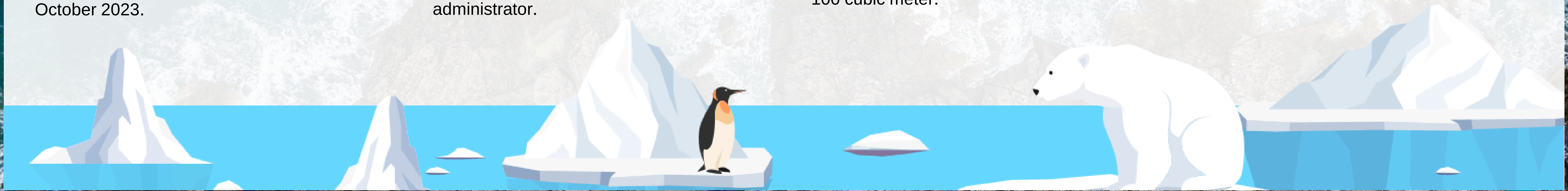
Tree plantation methodology

- The Forest Department of every State and Union territory is responsible to identify degraded land parcels, which should be made available for tree plantation and for green credit generation under the said notification. The land parcels identified should be sized five hectares or above and be free from all encumbrances.
- Any person or entity desirous of undertaking tree plantation is required to apply to the administrator who will assign a land parcel to the applicant.
- The applicant is required to submit a proposal for undertaking tree plantation for generation of green credit to the administrator.
- The green credit should be calculated at the rate of one green credit per tree grown through the tree plantation on such land parcel, subject to minimum density of 1100 trees per hectare, based on the local silvi-climatic and soil conditions, on the certification of completion of tree plantation provided by the concerned Forest Department.

Draft water harvesting methodology

- All persons and entities including individuals/Follow-on Public Offerings (FPOs)/Cooperatives/Forest Management Committees/Sustainable Agricultural Enterprises/Self Help Groups (SHGs)/Eco-development committee/Urban and rural local bodies are eligible for registration under the water harvesting scheme.
- The green credit should be calculated at the rate of 75 green credits per 100 cubic meter.
- Physical verification is carried out for projects upto 1000 cubic meter by the existing government machinery such as (Revenue, Municipal, Forest, Agriculture and Irrigation Department) and for projects of 1000 cubic meter and above by third party verifiers designated under Green Credit Rules, 2023.
- Any water harvesting project covered under any existing/new laws, as amended will also get registered under the Green Credit Rules, 2023 and can trade/generate the green credits generated as mandated under these laws/regulations.

The methodology and procedure for calculation of generating green credit for each of the balance environment activities mentioned above and the trading platform are yet to be developed and pending notification by the Government of India.



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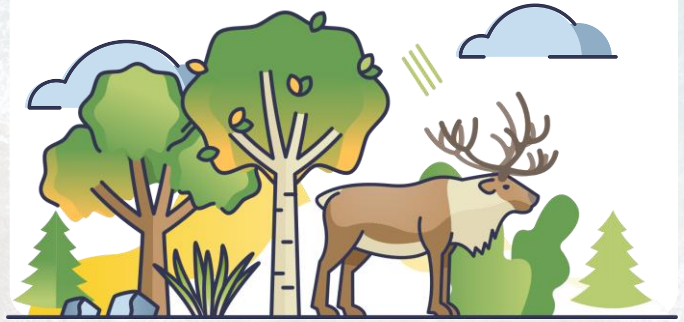
Key considerations relating to carbon credit market and green credit programme

With the CCTS framework already in place, the green credit programme is expected to encourage an incentive-based approach to achieve a low emission future. Even though green credit programme encompasses registration, calculation and issuance of green credits, final guidelines around them are yet to be notified by the government. Following are some additional points of consideration related to carbon credit market and green credit rules:

- The notified carbon credit scheme does not provide clarity regarding the timeline for operationalising the carbon market and which section of the market applies it first. The concept of carbon credit is not new and is currently regulated by Perform, Achieve and Trade (PAT) scheme by government. PAT is a mechanism designed to achieve the required energy efficiency in energy intensive sectors, with an associated market-based mechanism to enhance the cost effectiveness through certification of excess energy saving which can be traded. The scheme and draft compliance mechanism do not provide clarity that whether all the existing entities under the PAT scheme to get transferred to the carbon credit market.
- One of the crucial points for the effectiveness of the carbon market is the carbon price discovery. The price should be balanced to encourage participation and incentivise emission reduction. There is a need for robust price discovery methodology across sectors along with regular intervention to avoid over supply or over demand of credits.
- Currently, the carbon certificates are being traded under the voluntary international markets by the Indian stakeholders. With the new domestic carbon market now in place, clarity is required on the functioning of global carbon credit certificates parallelly with the domestic carbon credit certificates.
- The green credit programme is a new initiative by the government of India and currently, there is no existing market for green credit leading to lack of awareness around it. Since the main purpose of this initiative is to boost voluntary environmental activities, the government should take steps to develop awareness programs as part of this initiative. Such steps would help increase participation across various sectors and boost environmental conservation efforts by corporate entities.

The bottom line

Carbon markets have a significant role to play in achieving GHG targets and net zero commitments by enabling governments and organisations to effectively manage emissions and emission reduction limits. This is an emerging area and regulatory focus on carbon markets has been increasing. The carbon credit trading scheme and green credit programme are two groundbreaking steps taken by Indian government against climate change. The corporates in India should track the regulatory announcements in this area.



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CHAPTER 3

Regulatory updates

Clarifications related to investment in AIFs

In order to address certain regulatory concerns relating to investments by Regulated Entities (REs) in Alternative Investment Funds (AIFs), on 19 December 2023[1], the Reserve Bank of India (RBI) had issued a circular providing a set of instructions for investment in AIFs by REs (the ‘Circular’). Subsequently, to address the practical concerns raised by the industry related to the implementation of the Circular, on 27 March 2024, RBI issued certain clarifications with respect to the existing requirements as mentioned below:

I. **Downstream investments:** REs were instructed to not make investments in any scheme of AIFs which has downstream investments either directly or indirectly in a debtor company of the RE. It has now been clarified that downstream investments should exclude investments in equity shares of the debtor company of the RE but include all other investments, including investment in hybrid instruments.

II. **Provision requirement:** In case of a downstream investment by the AIF, the RE is required to liquidate its investment in the scheme within 30 days from the date of such investment. If the REs fail to liquidate the investment within the prescribed timeline, they should make 100 per cent provision on such investments. It has been clarified that provisioning is required only to the extent of investment by the RE in the AIF scheme which is further invested by the AIF in the debtor company, and not on the entire investment of the RE in the AIF scheme.

III. **Investment in subordinated units of AIF scheme:** Investment by REs in the subordinated units of any AIF scheme with a ‘priority distribution model’[2] shall be subject to full deduction from RE’s capital funds. It has been clarified that this would apply only in cases where the AIF does not have any downstream investment in a debtor company of the RE.

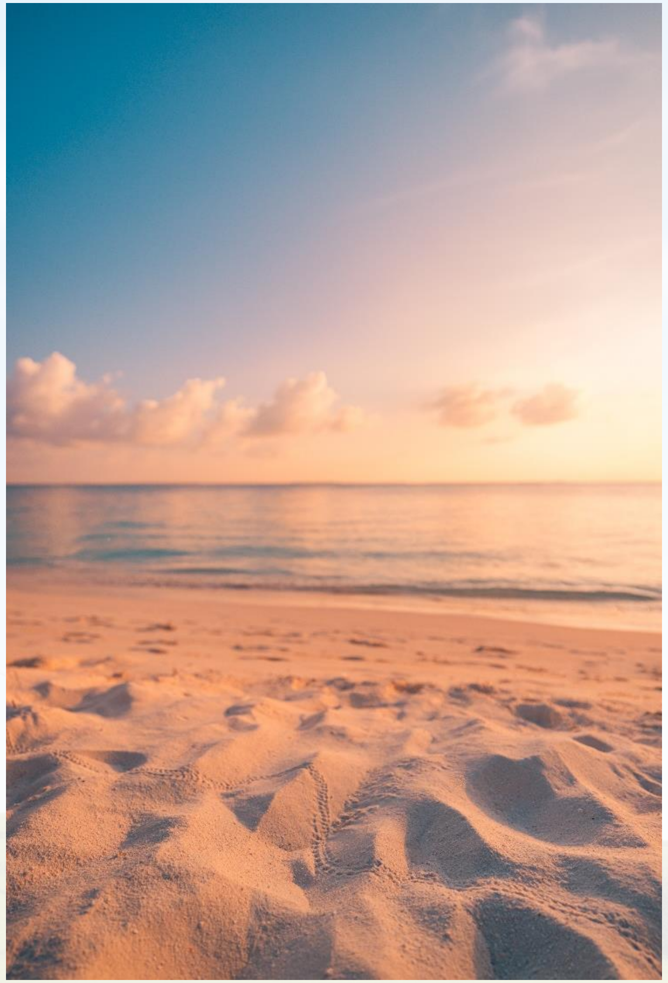
If the RE has investment in subordinated units of an AIF scheme, which also has downstream exposure to the debtor company the RE should comply with paragraph 2 of the Circular issued by RBI (i.e point i and ii above).

Further, with respect to priority distribution model requirements, it has been clarified that:

- The deduction should take place equally from both Tier-1 and Tier-2 capital.
- Reference to investment in subordinated units of AIF Scheme includes all forms of subordinated exposures, including investment in the nature of sponsor units.

IV. **Exclusion:** Investments by REs in AIFs through intermediaries such as fund of funds or mutual funds are not included in the scope of the Circular.

(Source: RBI circular no. RBI/2023-24/140 dated 27 March 2024)



1. RBI circular no. RBI/2023-24/90 dated 19 December 2023
2. ‘Priority distribution model’ shall have the same meaning as specified in the SEBI circular SEBI/HO/AFD-1/PoD/P/CIR/2022/157 dated November 23, 2022‘Priority distribution model’ shall have the same meaning as specified in the SEBI circular SEBI/HO/AFD-1/PoD/P/CIR/2022/157 dated November 23, 2022

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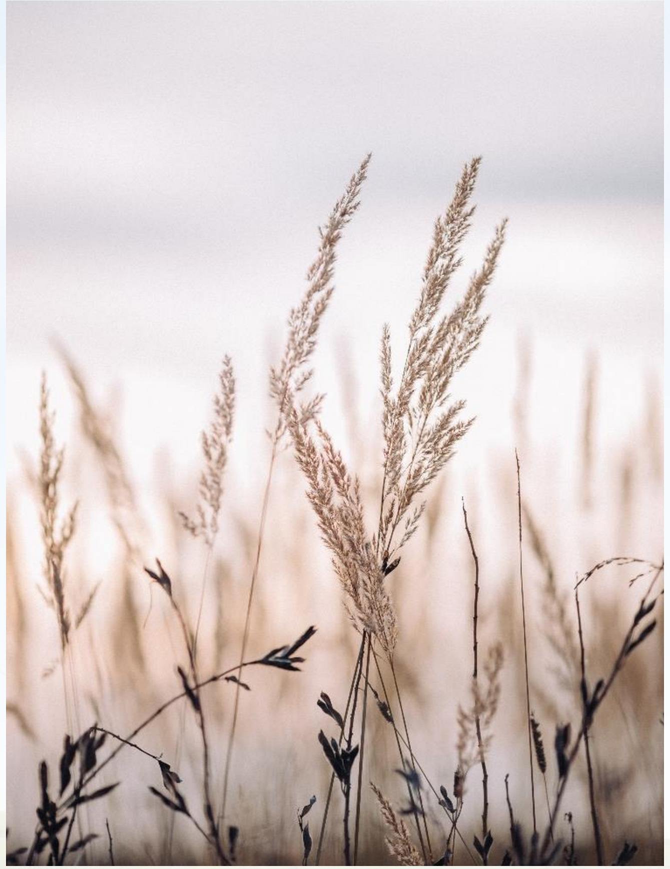
Stringent corporate governance framework for insurers

Previously, the Insurance Regulatory and Development Authority of India (IRDAI) had issued a set of guidelines that laid down the corporate governance practices for Indian insurers in addition to the requirements set out in the Insurance Act, 1938, IRDAI Act, 1999 and various other rules and regulations issued under the above laws.

On 20 March 2024, IRDAI notified the IRDAI (Corporate Governance for Insurers) Regulations, 2024 (Corporate Governance Regulations) which replaces the extant guidelines relating to corporate governance practices[3]. Some of the key points of the regulations pertain to the following:

Board of Directors

- The board of every insurer should have competent and qualified individuals as directors, with qualifications and experience that are commensurate with scale, nature, complexity of business and size of the insurer.
- Insurers are required to ensure independence of the Board from the management as well as the promoters and maintain independence of control functions including compliance, risk, audit, actuarial and secretarial function.
- The Board should be responsible for formulating the overall strategy and direction to the insurer and ensure that appropriate systems and procedures for risk management and internal controls are in place.
- The Board can delegate its responsibilities and authority to various committees[4] of the Board, but such delegation does not absolve the Board from its primary responsibilities.
- The Board should put in place adequate systems, policies and procedures to address potential conflicts of interest and *inter alia* ensure compliance with the provisions of the Companies Act, 2013.
- The Board is required to formulate a policy on related party transactions and review it annually.
- Appropriate measures should be taken by the board towards identification and nurturing of individuals for taking up directorship and KMP positions of the insurer.



3. Circular titled Guidelines for Corporate Governance for Insurers in India dated 18 May 2016
4. The Board shall constitute the following committees, who shall perform such roles and responsibilities as may be specified by the Competent Authority:
    - Committees as mandated by the Companies Act
    - Risk Management Committee
    - Policyholder Protection, Grievance Redressal and Claims Monitoring Committee
    - (PPGR&CM Committee)
    - Investment Committee
    - With Profits Committee

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Key Management Persons (KMPs)

- KMPs should be appointed by the Board on recommendation of the Nomination and Remuneration Committee. Every insurer is required to appoint Managing Director/ Chief Executive Officer or Whole-time Director(s), by whatever name called in accordance with the provisions of Section 34A of the Insurance Act, 1938.
- The minimum fixed tenure of the Chief Compliance Officer (CCO) should not be less than three years.
- The board should fill vacant KMP positions on priority to ensure it does not remain vacant for a continuous period of 180 days.
- Insurers should formulate and adopt a comprehensive board approved remuneration policy in accordance with the framework specified by the Competent Authority[5] for Chairperson of the Board, Non-Executive Directors and KMPs.

Appointment of statutory auditors

- Insurers should appoint joint statutory auditors with no conflict of interest in their appointment.
- The appointment should be based on the recommendation of the Audit Committee, subject to the shareholders' approval at the general meeting of insurer.

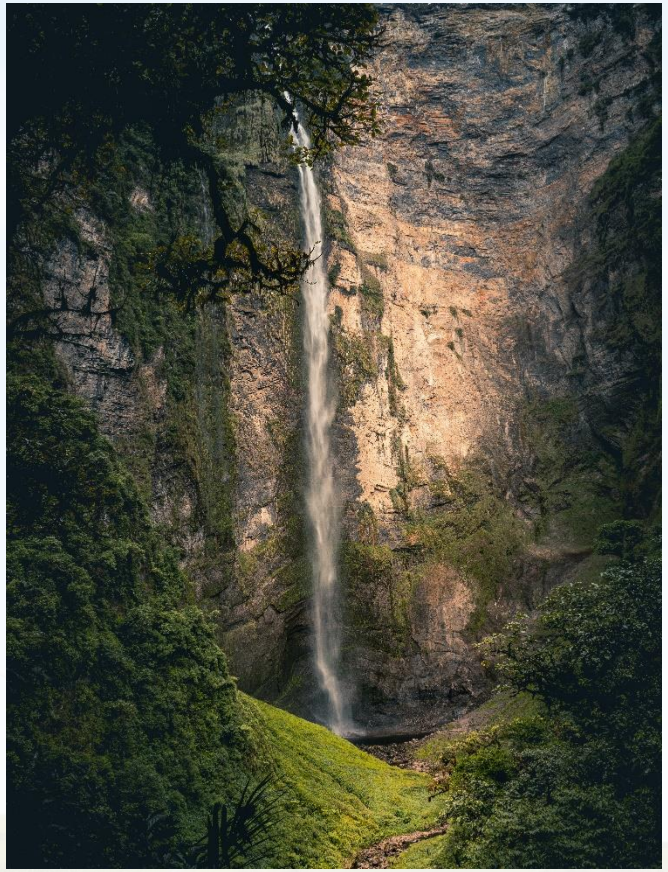
Disclosure and reporting requirements

- The CCO should be the designated compliance officer for submitting returns, reports and applications for approvals to the authority[6] and ensuring compliance with the Corporate Governance Regulations.
- The status of compliance with the Corporate Governance Regulations is required to be filed on an annual basis within the time and format specified by the competent authority.
- Insurers are required to make disclosures[7] in such a manner and format as required by the competent authority.

Environment, Social and Governance (ESG)

- Insurers are required to put in place a board approved ESG framework which should be annually reviewed by the board.
- The board is required to establish a comprehensive climate risk management framework based on the size, nature and complexity of operations.

(Source: IRDAI notification no. IRDAI/Reg/7/201/2024 dated 20 March 2024)



5. "**Competent Authority**"
   i. means Chairperson or
   ii. such whole-time member or committee of the whole-time members or such officer(s) of the Authority, as may be determined by the Chairperson.
6. "**Authority**" means the Insurance Regulatory and Development Authority of India established under sub-section (1) of Section 3 of the Insurance Regulatory and Development Authority Act, 1999
7. All insurers shall make necessary disclosures about the composition of its Board, meetings of Board & its Committees, details of attendance of meetings by directors and members of Committees, details of remuneration paid, if any, to all directors including Independent Directors, etc.

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ICAI has issued an education material on Ind AS 12, *Income Taxes*

Ind AS 12 provides a structured framework for recognising and measuring income taxes, ensuring that financial statements accurately reflect an entity's tax obligations and the associated impacts on its financial performance and position.

On 13 March 2024, the Institute of Chartered Accountants of India (ICAI) has issued an educational material on Ind AS 12 which provides summary of the standard and discusses fundamental concepts related to exploring the nuances of deferred tax assets and liabilities. Additionally, it includes Frequently Asked Questions (FAQs) to address certain practical issues along with guidance that covers accounting for the interest and penalties related to income taxes, difference between current tax and deferred tax, accounting and presentation of taxes that are scoped out of Ind AS 12, etc.

(Source: ICAI announcement dated 13 March 2024)

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First Notes

The Reserve Bank of India amends the classification and valuation norms for investments held by banks

Banks are currently required to follow the Master Direction - Classification, Valuation and Operation of Investment Portfolio of Commercial Banks (Directions), 2021 (2021 regulations) for the classification and valuation of their investment portfolio. With significant developments in the global standards on classification, measurement and valuation of investments (i.e. IFRS), the linkages with the capital adequacy framework as well as progress in the domestic financial markets, there was a need to review and update the 2021 regulations.

Accordingly, on 12 September 2023, the Reserve Bank of India (RBI) issued revised regulatory guidelines on investment classification and valuation - the Master Directions - Classification, Valuation and Operations of Investment Portfolio of Commercial Banks (Directions), 2023 (2023 guidelines).

This issue of the First Notes provides an overview of the of the key changes in the 2023 guidelines and how these changes conform with Ind AS (which are largely aligned with IFRS).

To access the First Notes, please click here

Voices on Reporting - Webinar

On 5 April 2024, KPMG in India held the Voices on Reporting webinar to discuss the key financial reporting and regulatory matters which are expected to be relevant for the stakeholders for the quarter ended 31 March 2024.

In the session, some of the key updates discussed are as follows:

- Recent climate-related regulatory updates
- Key updates from Securities and Exchange Board of India's (SEBI) recent board meeting
- Year-end reminders
- Other regulatory updates

To access the webinar, please click here

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KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011 Phone: +91 22 3989 6000, Fax: +91 22 3983 6000.

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