Assurance Gazette

December 2021

NANGIA & CO LLP
CHARTERED ACCOUNTANTS

www.nangia.com

Foreword

India is undoubtedly one of the world's most vibrant capital markets with a combined push by Government and private sector due to which the capital market has witnessed a significant rise in investor participation thus necessitating the concerned authorities to safeguard the interest of investors and enabling them to take more informed and diligent Investing decisions.

To ensure the above said objectives are attained, the Government with the Regulators assure the translucent and fair financial reporting.

We have highlighted the attempts by the regulatory Bodies - Security Exchange Board of India and Ministry of Corporate Affairs vide its recent guidelines to enhance the transparency credibility and accountability of Listed entities through disclosure requirements in respect of related party transactions (RPT’s) in the format specified by the Board from time to time, adjacently the amendments in the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules intended to curtail compliances for investors to claim refunds regulated under the aforesaid, respectively.

We attempt to accentuate the dilemmatic classification of Investment Property as PPE or an Investment? In financial statements, In view of the Accounting Standard 13 “Accounting for Investments” and Accounting Standard 10 Property, Plant and Equipment.

We aim to provide an overview of the these endeavours in a simplified manner along with highlighting key changes and implications in order to assist you with your financial reporting and audits. We believe that our publication will be beneficial to you enabling adherence to compliances and ensuring better corporate governance.

We also take this opportunity to wish you all a Merry Christmas & A Happy New Year!!!

Table of Contents	Page No.

SEBI Prescribes RPT Information for Audit Committee Consideration

Vide notification dated 9th November, SEBI amended Regulation 23 of the SEBI (Listing obligations and Disclosure requirements) by mandating listed entities to submit to the stock exchanges disclosure of related party transactions (RPT's) in the format specified by the Board from time to time.

Further to above notification, SEBI vide circular No SEBI/HO/ CFD/ CMD1/ CIR/ P/ 2021/ 662 dated November 22, 2021 issued in exercise of powers conferred under Section 11(1) of the Securities and Exchange Board of India Act 1992 read with Regulation 101 of the LODR has now decided to prescribe the information to be placed before the audit committee and shareholders for consideration of proposed RPTs.

Circular requirements

- Information to be reviewed by the Audit Committee for approval of RPT's

  SEBI had provided guidelines on the information which needs to be submitted to audit committee for their review and approval of proposed RPT. As per the guidelines provided, Company will have to disclose

- the material terms, type and particulars of the proposed transaction along with the name of the related party and its relation to the entity or its subsidiary.

- tenure of the transaction, value of proposed transaction

- percentage of the listed entity consolidated turnover for immediately preceding financial year that represent the proposed transaction value.

- In case the proposed transaction relates to loans, inter- corporate deposits and advances or investments made or given by listed entity or subsidiary then disclosure will be required for the following:

  o Source of funds in connection with transaction

  o Where financial indebtedness is incurred to make or give inter-corporate loans & deposits, advances or investments in such case nature of indebtedness, cost of funds and tenure

  o Applicable terms including covenants, tenure, interest rate, repayment schedule, whether secured or non-secured, if secured then nature of security.

  o Purpose for which the funds will be utilized by the ultimate beneficiary of such funds pursuant to the RPT.

- Justification as to why the RPT is in the interest of the listed entity

- A copy of the valuation or other external party report, if any such report has been relied upon

- Percentage of the counter party's annual consolidated turnover that is represented by the value of the proposed RPT on a voluntary basis.

- Any other information that may be relevant

- The audit Committee is also mandated to review the status of long-term (more than one year) or recurring RPT's on an annual basis.

- Information to be provided to shareholders for consideration of RPT's

  Information to be presented to shareholders, a notice being sent to shareholders seeking approval on proposed RPT shall be in addition to the requirements of Companies Act 2013 and will include:

  - Summary of information provided by management to Audit committee

  - Justification for why the transaction is in the interest of listed entity

  - Where the transaction relates to any loans, advances, inter-corporate deposits or investments made or given by listed entity or its subsidiary, details as included in report to audit committee.

  - Any other information that may be relevant

    As per the notification, justification as to why RPT is in the interest of listed entity along with a copy of valuation or external other party report will be made available to the shareholders through the registered email address.

    RPT disclosure to stock exchange by the listed entity shall be every six months in the format provided.

Nangia's Take

SEBI's RPT disclosure for listed companies is expected to undergo a change after this amendment which is made effective from 1st April 2022. SEBI's move of enforcing governance over RPT transactions through these frameworks seems like a measure to fill the gap. These steps are majorly inspired by the need for more transparency and promptness of information. The amendments bring about a paradigm shift in the RPT regime, and once again places RPT regulation at the forefront of India's battle for good governance.

Amendments to the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules, 2016

The Ministry of Corporate Affairs (MCA) has issued the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Second Amendment Rules, 2021 vide circular dated the 9th November, 2021.

IEPF Authority (IEPFA) was set up for the administration of the IEPF fund. IEPFA promotes investor protection and facilitates refunds to the rightful claimants the dividend, unclaimed shares and other amounts transferred. IEPFA works under the administrative control of the ministry.

As per the Companies Act, it is mandatory for the business to transfer to IEPF all the dues to shareholders which remains unpaid or unclaimed for seven years. Shareholders/ Investors can seek a refund of the same from IEPF.

MCA has taken the relevant steps to make the process of refund easier for shareholders. The funds transferred to IEPF includes unclaimed dividend, matured deposits, matured debentures, application money due for refund, or interest on it and redemption proceeds of preference shares.

The MCA has made it less cumbersome for investors to claim refunds of such funds that companies have transferred to the Investor Education and Protection Fund (IEPF).

The relaxations include replacing the requirement of notarization of documents with self-attestation.

Relaxations in terms of requirements of affidavits and surety has also been provided. The amendment has reduced the compliance burden related to filing of supporting documents such as Will/Decree/Succession certificate/ Letter of administration etc. to effect the transmission of securities held in physical / DEMAT mode. Further, the threshold value of the securities per issuer company, who are required to do such filings, is increased from Rs. 2 lakhs to Rs 5 Lakhs.

In case of loss of securities held in physical mode, self-attested copy of FIR / Police complaint containing the information of security holder, holding details, folio number and distinctive numbers of the share certificates shall be submitted as proof.

Nangia's Take

The new regime works strongly towards ease of doing business and creating a trust-based model for faster turnaround time. Such moves help in building faith and confidence among the investors thereby creating a positive and healthy environment. Government should continuously work towards identifying such areas of difficulties and should take relevant measures to overcome the same.

Investment Property: A PPE or an Investment?

As per paragraph 3.4 of AS 13 “Accounting for Investments”, an investment property is an investment in land or buildings that are not intended to be occupied substantially for use by, or in the operations of, the investing enterprise. Such property, in essence, could be purchased with intentions to hold as an investment or be let out to earn rentals.

Ordinarily, investment property would meet the definition of *‘property, plant and equipment’ (PPE) and be accounted for in accordance with AS 10 Property, Plant and Equipment. However, a specific standard, AS 13 Accounting for Investments*, was developed which also accounts for this specific type of asset in addition to investments having high liquidity potential.

Investment property is often a significant balance in the statement of financial position of property investors. Making one or a number of common errors in relation to this standard could therefore have a material impact on profit or loss.

There are numerous ways in which preparers can get the classification of investment properties wrong. This month we focus on few common errors.

Error 1: Investment property is not PPE

Investment properties usually comprise a building or piece of land rented to tenants over a long period (more than one year). As such, they would meet the definition of PPE to be accounted for under AS 10 if the separate standard on investment property did not exist.

Property, plant and equipment are tangible items that:

- are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

- are expected to be used during more than one period.

Investment property is property (land or a building - or part of a building - or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

- use in the production or supply of goods or services or for administrative purposes; or

- sale in the ordinary course of business.

The major defects observed in industry accounting practices adopted are: -

- For Investment property held for rentals or capital appreciation, the same shall be specifically disclosed below Tangible Fixed Assets on the face of Balance Sheet.

- For Investment properties put to sale in case of real estate and construction companies, the same shall be classified as Inventories and be dealt according to AS 2 Inventories.

- For Investment property held for sale, the same shall be dealt under AS 24.

Error 2: Investment properties must be land or buildings

In Error 1 above, we noted that the definition of PPE includes tangible items held for 'rental to others' and that investment property is 'land or a building - or a part of a building - or both'.

The deliberate inclusion of the words 'held for rental to others' in the definition of PPE indicates the intention that some assets held for rental are not investment property. This includes 'owner occupied property', Classifying assets as PPE or investment property is relatively simple in some situations, such as for a car hire vehicle which is clearly not land or buildings and cannot fall within the scope of AS 13.

Error 3: Land is Investment Property if you haven't decided what you want to do with it

Property companies often purchase blocks of land, either to sell as subdivided parcels of land, or for development as apartments, homes or offices. Such properties are classified as 'inventories' under IAS 2 Inventories because the entity will sell them in the ordinary course of business.

Sometimes property companies may acquire a parcel of land without knowing exactly what they intend to do with it. Possibilities include:

- Developing and then selling in the ordinary course of business as inventory (IAS 2)

- Use as owner-occupied land (AS 10), or

- Renting out and holding for capital appreciation (AS 13).

Error 4: Temporarily leased properties are not always investment properties

Despite the definition of 'investment property' specifically including property held to earn rentals, if the intention from the outset is to sell a property in the ordinary course of business, the fact that it is being rented out while the property is being marketed does not automatically mean that it is an investment property.

Large properties may take a long period of time to sell, and renting them out in the short-term is merely a means of reducing cash outflows from rates and taxes, etc. Also, tenanted commercial properties may achieve a higher selling price than untenanted properties. These types of properties should be classified as inventories.

If the entity measures investment property at fair value, automatically classifying such properties as investment property rather than inventories could result in profit on sale of the property being recognized prematurely in profit or loss.

We also wish to highlight that immovable properties classified as investment property are also subject to depreciation similar to property plant and equipment.

Nangia's Take

Through this article, we have tried to highlight the most common errors in investment property accounting. Despite the fact that IGAAP recommends valuation of Investment property at Cost and valuation of PPE too at cost, an erroneous classification of these types of assets in financial statements can reduce the effectiveness of faithful representation in financial reporting. Ideally, these assets should separately be disclosed on the face of balance sheet and not merged with PPE.

Meet our Experts

Vikas Gupta
Partner
vikas.gupta@nangia.com

Prateek Agrawal
Partner
prateek.agarwal@nangia.com

Vikram Pratap Singh
Partner
vikram.pratap@nangia.com

Jaspreet Singh Bedi
Partner
jaspreet.bedi@nangia.com

NOIDA
(Delhi NCR - Corporate Office) A-109, Sector 136, Noida - 201304
T: +91 120 259 8000

DELHI
(Registered Office)
B-27, Soami Nagar,
New Delhi-110017, India
T: +91 120 2598000

GURUGRAM
812-814, Tower B, Emaar Digital Greens Sector 61, Gurugram, Haryana, 122102
T: +0124-4301551/1552/1554

MUMBAI
11th Floor, B Wing, Peninsula Business Park, Ganpatrao Kadam Marg, Lower Parel, Mumbai 400013, India | T : +91 22 61737000

CHENNAI
Pestige Palladium Bayan, Level 5, 129-140, Greams Road, Thousand Lights, Chennai 600006
T: +91-44-40509200

BENGALURU
Prestige Obelisk, Level 4, No 3
Kasturba Road Bengaluru - 560 001
Karnataka, India
T: +91-80-2228-0999

PUNE
3rd Floor, Park Plaza, CTS 1085, Ganeshkhind Road, Next to Pune Central Mall, Shivajinagar, Pune - 411005

DEHRADUN
First Floor, “IDA” 46 E. C. Road,
Dehradun – 248001, Uttarakhand
T: +91 135 271 6300

www.nangia.com | query@nangia.com