Newsletter

Sharp View

December 2021

December 21

December – the winter month is celebrated across the globe for Christmas and followed by the New Year eve. As India waits to enter into the new year shortly, the stakeholders have their eyes set on the upcoming crypto currency bill, expected to be tabled by the Government in the winter session of the Parliament.

There was much deliberation during the year, whether and when the crypto currency regulation would be enacted. However, considering the speculative nature, risks and the anonymity involved in the crypto currencies, RBI is of the view that crypto currencies, even if regulated, will pose very serious concerns from a macro economic and financial stability point of view. The Government is seeking to ban all the private crypto currencies and instead create a facilitative framework for the creation of the official Central Bank Digital Currency (CBDC). The Government however intends to tax the crypto currency gains in the upcoming Budget 2022.

Till the time, the things are clear, we wait and watch to see the final outcome of the bill.

Assurance

1. Schedule III – Disclosure on loans and advances given to / received by the company

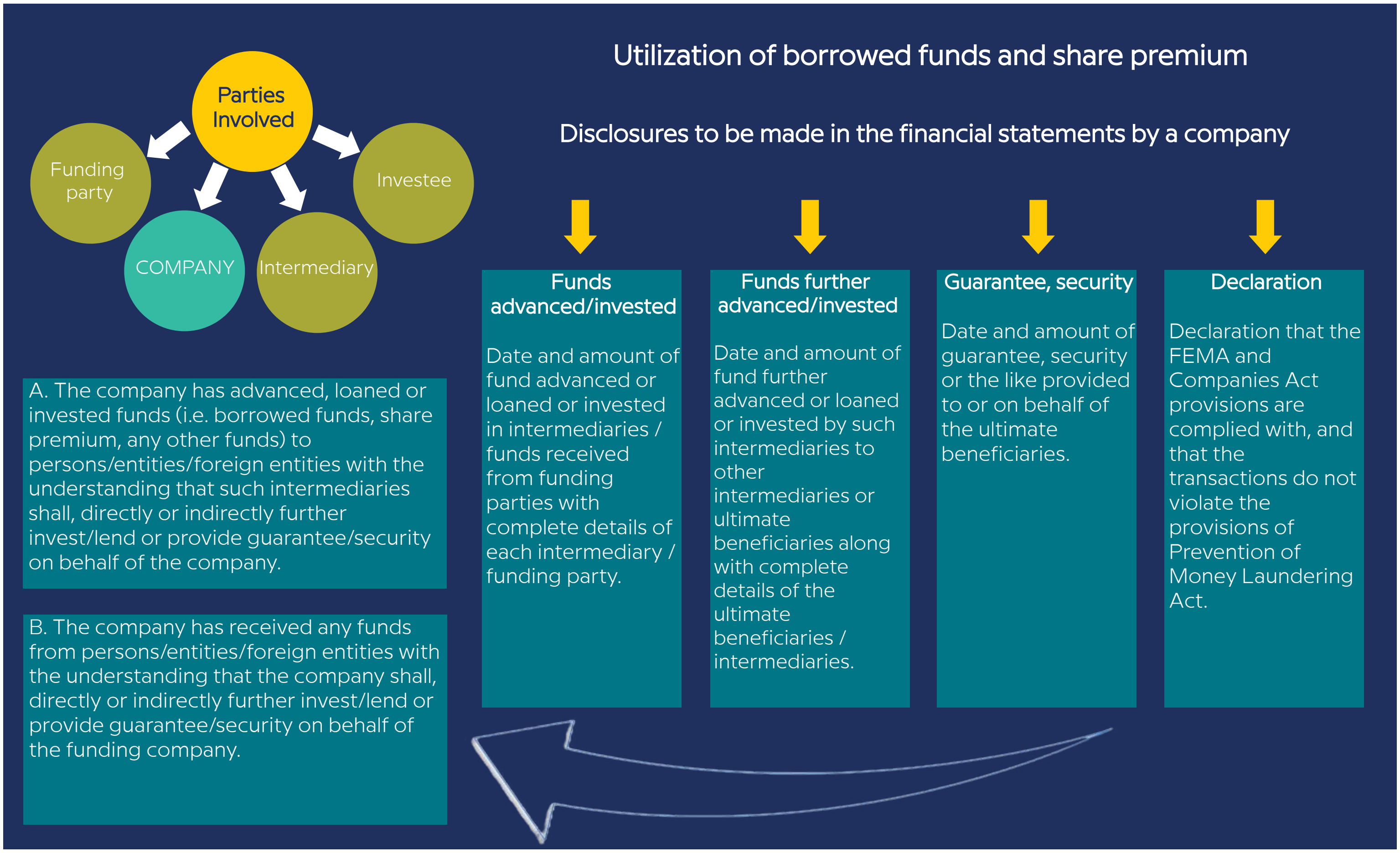
Schedule III reporting requires a company to disclose the particulars of loans, advances either given to or taken from any persons / entities / foreign companies. Disclosure of indirect receipts and transfers of funds routed through intermediaries are also mandatory. It is expected that the new reporting requirement for the companies keeps a check on money laundering activities and disclosure of intermediaries who act as pass-through entities in such transactions. Ms. Lalithashree from Chennai office has briefed the readers on the same.

2. SEBI (Listing Obligations and Disclosure Requirements) (Sixth Amendment) Regulations, 2021

Recently, SEBI has widened the term' related party' and 'related party transactions' through the SEBI(LODR) Regulations. Coming financial years will require the listed entities to obtain prior approvals of the audit committee & shareholders for the related party transactions as well as appropriate disclosures to SEBI. The increased compliance and governance aspects of the regulations are captured by Mr. Arjun M K (Bangalore office) and Mr. Varun Choraria (Chennai office).

Assurance | Schedule III – Disclosure on loans and advances given to / received by the company

Schedule III to the Companies Act, 2013 issued by the Ministry of Corporate Affairs (MCA) vide notification dated 24 March 2021 mandates the disclosure of certain particulars where a company makes advances, loans to, or invests funds with any persons/entities/foreign companies. Similar disclosures are to be made where the company receives the funds directly or indirectly through intermediaries.



- For disclosure of utilisation of funds (mentioned in A above), the ultimate beneficiary is the company.
- For the disclosure of receipt of funds (mentioned in B above), the ultimate beneficiary is the funding party (in case of a single layer) and the ultimate funding party (in case of multiple layers.)

The prime objectives of this additional reporting requirement are to give an early red signal of the possibilities of money laundering and to have a closer vigilance upon intermediaries and entities involved. The movement of money within India and abroad through a chain of entities is monitored and can be cross matched with the records of the company and the intermediary.

This mandated disclosure by the management of the companies would pave the way for the auditors to establish an audit trail of transactions and the parties involved. The auditors would be required to perform additional procedures, substantiating the disclosures made are accurate and free from misrepresentation. External confirmation from all the parties involved, verification of bank statements, perusal of legitimacy of the fund received and further lent, review of legal agreements of such transactions if any, and verification of rightfulness of the guarantees and securities provided by the ultimate beneficiary would aid auditors in collating audit evidence for such transactions.

Group companies and special purpose vehicles in the group may improve the governance process as the running account balances maintained between group companies may fall into this amendment and will warrant disclosures if the amounts remain outstanding at the end of the financial year. Settling such current account balances periodically can be one of the ways to ensure that such balances are not treated as loans and advances in view of schedule III disclosures and CARO reporting.

Conclusion

The new reporting requirement enables the regulators to track the movement of funds routed through intermediaries / pass-through entities with an intention to conceal the identity of the ultimate beneficiary, both in India and abroad. The details required to be disclosed include the name, registered address, any government identification number (e.g., PAN, SSN, CIN, etc.) and relationship with the company making the disclosure.

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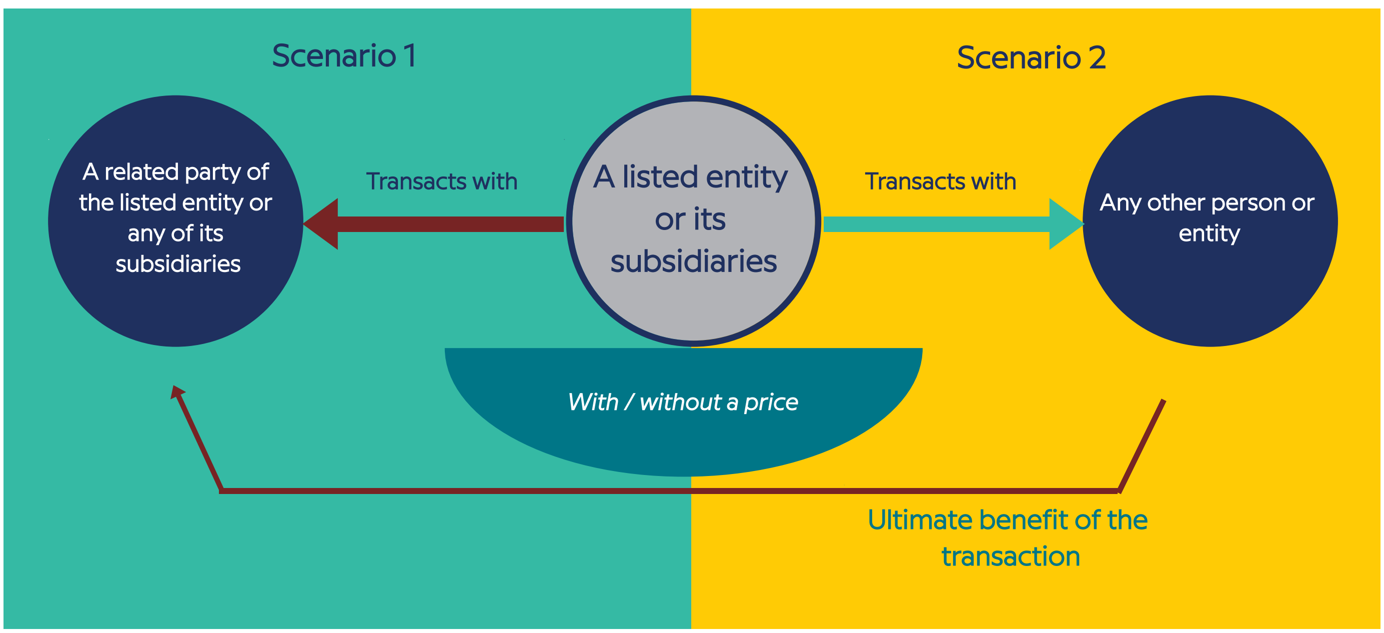
Assurance | SEBI (Listing Obligations and Disclosure Requirements) (Sixth Amendment) Regulations, 2021

SEBI has recently amended its Listing Obligations and Disclosure Requirements Regulations, viz. SEBI (LODR) regulations, enhancing the scope and reporting of the term 'related party' and 'related party transactions' (RPT). The effective date is 1 April 2022 unless otherwise specified.

1. Related party: The term related party is widened to cover
   a. Any person or an entity forming part of the promoter group OR
   b. Any person holding equity shares of 20% and more in the listed entity (directly or through a beneficial interest basis). From 1 April 2023, 10% or more equity holding will apply (in point b. above).

Conditions a. and b. are independent of each other and satisfying any one of them is sufficient to be termed 'related party.' A person without any equity shareholding but belonging to the promoter group will qualify as a related party. Similarly, only equity shareholding (and not preference shareholding) will qualify in determining related party existence.

2. Related party transaction (RPT):



Exclusions from RPT:

i. Issue of specified securities on a preferential basis to related parties. (Subject to compliance with SEBI (ICDR) Regulations, 2018.
ii. Corporate actions (which are uniformly applicable/offered to all shareholders in proportion to their shareholding) like payment of dividend, subdivision or consolidation of securities, issuance of securities by way of a rights issue or a bonus issue and buy-back of securities which are offered by listed companies to all shareholders uniformly.
iii. Where Bank/NBFC accepts fixed deposits from related parties at terms offered to all, provided disclosure of the same along with RPT is intimated to stock exchange every 6 months.

3. Materiality of RPT: An RPT will be considered to be material, if such transaction individually or with earlier RPTs taken together exceeds lower of the following:

- INR 1,000 crore OR
- 10% of the annual consolidated turnover of the listed entity as per the last audited financial statements.

**W.e.f. 1 April 2023, the above limit of 10% will apply to the subsidiary's standalone annual turnover (as per the last audited financial statements.)*

4. Approval of audit committee and shareholders for RPT and material modifications thereto

RPT - Responsibility of the Listed entity's 'Management' and the 'Audit Committee'

Subsidiary of the Listed Entity

1. Local management/BOD to compile and provide a list of related party & the RPTs proposed to be entered

2. Keep a track of the RPTs (past & future) and provide the same to the listed entity

Audit Committee (AC) of the Listed Entity

1. Obtain complete list of related parties (listed entity level and subsidiary level)

2. Define RPT and material modifications thereto. Disclose it as a part of 'Materiality Policy.' (Mandatory from 1 January 2022)

3. Review the SEBI (LODR) requirements for prior approval of RPT. (Click to read the relevant circular)

3. Corroborate RPT information + Seek additional RPT information (at subsidiary level)

4. Communicate the information to listed entity

1. Provide the details to AC (including subsidiary level details)

2. Communicate the Materiality Policy to the management

5. RPTs approved and communicated to the management

Management of the Listed Entity

1. Identify all the RPT (own and subsidiary level), past trends and RPT proposed to be entered during the FY
2. Closely monitor shareholding pattern and management composition changes for determining a 'Related Party'
3. Identify the related parties and RPT on the value and % of turnover criteria (i.e. lower of INR 1,000 crores and the specified percentage Note)
4. Justification of the proposed RPT to the AC

RPT approved by AC

Listed entity's shareholders' approval

Required, if the RPT is matrial

(Click here to view relevant circular)

Not Required

If RPT entered into by the listed subsidiary having paid up equity capital upto INR 10 crore and net worth upto INR 25 crore as on the last day of the previous FY and to whom the corporate governance provisions of the LODR do not apply.
Prior approval of of the audit committee of the listed subsidiary shall suffice.

Note:

Year	If the individual/cumulative value of transaction during the FY > 10% of:
FY 2022-23	the annual consolidated turnover of the listed entity, as per the last audited financial statements.
FY 2023-24 onwards	the annual standalone turnover of the subsidiary, as per the last audited financial statements.

In case of RPT between two unlisted subsidiaries of a listed subsidiary, the prior shareholders' approval of the listed subsidiary will suffice.

5. RPT disclosure to stock exchanges

- The listed entity shall submit to the stock exchanges disclosures of RPT in the format as specified by SEBI & publish the same on its website as below:
  - Upto 1 April 2023: 15 days from the date of publication of its standalone and consolidated financial results for each half year.
  - W.e.f. 1 April 2023: Simultaneously along with the standalone and consolidated financial results.
  - A high value debt-listed entity shall submit its RPT disclosures along with the standalone financial results for each half year.

The format of the reporting requirements is recently notified by SEBI in *Annex*.

- **Annual Report disclosures (Schedule V):** The listed entity which has listed its non-convertible securities shall make disclosures in compliance with the AS on "Related Party Disclosures.'

- **'Other disclosures' in Corporate Governance Report:** Disclosure by listed entity and its subsidiaries of 'Loans and advances in the nature of loans to firms/companies in which directors are interested by name and amount.' (Not applicable to listed banks.)

6. Certain deletions from the erstwhile regulations

- Review of statement of significant related party transactions (as defined by the audit committee).- Sch. II Part C Para b, point no. 2
- The clause pertaining to 'voting rights of related parties.' – Reg 23(7)

Conclusion

SEBI has widened the scope of related parties, RPT and the term materiality. Approval of the audit committee for all RPT and material modifications will increase quantum of information to be placed before AC and the vigilance on the RPT. SEBI has enhanced the reporting requirements by bringing debt-listed entities within its ambit and certain consequential disclosures to include subsidiaries. The new regulations will bring in good corporate governance and enhance the degree of assurance for the stakeholders.

Click here for notification

GRC

Managerial remuneration under the Companies Act, 2013

Managerial remuneration is compensation paid to the company's directors and key managerial personnel. The Companies Act regulates managerial remuneration provisions wherein every company must comply with the limits/conditions specified therein. Ms. Aditi Jain (Baroda office) throws light on the complex provisions of this topic.

A Company established under the Companies Act, 2013 (the Act) shall ensure smooth functioning of its business, good corporate governance and protection of the interest of its stakeholders. This needs directors and managers to administer its functions, and hence, they are entitled to remuneration in lieu of the services rendered by them, incentivising the work to increase motivation and build morale.

Simply put, managerial remuneration is paid to managerial personnel, including managing director (MD), whole-time director (WTD), and manager.

I. Managerial remuneration – statutory provisions

As per section 197 of the Act, the overall remuneration paid by a public company to its directors, including MD, WTD, and its manager in relation to the financial year (FY) shall not exceed 11% of the company's net profits.

Section 198 specifies the manner of calculating the net profits for this purpose.

A company in general meeting may authorise the payment of remuneration exceeding 11% of its net profits, subject to the provisions of Schedule V of the Act.

- **Tabular depiction of managerial remuneration payable by a public company**

Particulars of managerial remuneration payable to MD/WTD/Manager	Limits of remuneration for a particular FY	Remarks / Exceptions
MD/WTD/Manager	<=11% of the net profits for that FY	Remuneration over 11% can be allowed only if the articles of association permit or by a special resolution in a general meeting.
One managerial personnel (MD/WTD/Manager)	<=5% of the net profits for that FY	Excess payment above the specified percentage needs a special resolution to that effect.
More than one managerial personnel (MD/WTD/Manager)	<=10% of the net profits for that FY for all such personnel taken together	
Directors (other than MD/WTD)	1% of the net profits	If there is MD/WTD/Manager
	3% of the net profits	If there is no MD/WTD/Manager

- **Sitting fees:** Sitting fees of the directors are distinct from managerial remuneration. Hence, the percentage mentioned above will be exclusive of any fees/sitting fees paid to its directors.
    - The sitting fee per director per board/committee meeting (as decided by the BoD) shall not exceed INR 1,00,000.
    - The sitting fees payable to independent directors and women directors shall not be less than those payable to other directors.

- **Remuneration in any other capacity:** The above remuneration shall include 'remuneration payable to the director in any other capacity' (subject to certain exceptions, e.g., rendering of such other services in a professional capacity, which is justified by the nomination and remuneration committee.)

- **Refund of excess remuneration:** If a director receives remuneration in excess of the above-specified limits, or without the necessary approvals of the company, he/she shall refund such excess sum to the company within maximum 2 years and, until refunded, hold it in the trust for the company.

II. Managerial remuneration in case of loss or inadequacy of profits

As per Part II of Schedule V of the Act, where in any financial year in case the company has no profits, or its profits are inadequate, it may pay remuneration to the managerial person or other director not exceeding the limits under Condition (A) and (B) given below:

1. Condition A

(1)		(2)	(3)
Sr. No	Where the effective capital (in rupees) is	Limit of yearly remuneration payable shall not exceed (in Rupees) in case of a managerial person	Limit of yearly remuneration payable shall not exceed (in rupees) in case of other director
(i)	Negative or less than 5 crore.	60 lakh	12 lakh
(ii)	5 crore and above but less than 100 crore.	84 lakh	17 lakh
(iii)	100 crore and above but less than 250 crore.	120 lakh	24 lakh
(iv)	250 crore and above.	120 lakh plus 0.01% of the effective capital in excess of INR 250 crore	24 lakh plus 0.01% of the effective capital in excess of INR 250 crore

Note:- Effective capital is the aggregate of paid-up share capital, the amount in share premium account, reserves and surplus, long-term loans and deposits repayable after one year as reduced by the aggregate of any investments, accumulated losses and preliminary expenses not written off.

Remuneration over the above limits may be paid by passing a special resolution in the general meeting.

2. Condition B

In the case of a managerial person or other director who is functioning in a professional capacity, remuneration as per item (A) may be paid-

- if such managerial person or other director is not having any interest, directly/indirectly, in the capital of the company or its holding company or any of its subsidiaries
- not having any direct or indirect interest or is not related to the directors or promoters of the company/its holding company/any of its subsidiaries at any time during the last two years before or after the date of appointment
- possesses graduate-level qualifications with expertise and specialised knowledge in the field in which the company operates.

Conclusion

Directors of a company hold a fiduciary position; hence must be paid remuneration as prescribed under the Act. Obtaining Central Government's approval is a time-consuming process, and therefore doing away with it by the Companies (Amendment) Act, 2017 and replacing it with the requirement of a special resolution indeed provides relief to the companies. The overall remuneration should be within the limits specified by the Act. Other provisions regarding sitting fees, fees to independent directors, and payments to directors in an additional capacity ensure that the remuneration is commensurate with the benefits derived by the company and its stakeholders.

Consulting

Energy conservation through Energy Audit – A Review

Energy is the resource of the past, present and future. The growth of an economy is closely linked with its energy consumption. Mr. Akshay Aware (Baroda office) presents valuable insight on Energy Audit & the related terms as well as the way forward in effective energy management.

Abstract: Energy is the driving force for the economy of any country. It is highly essential to ensure the smooth progress of the industry and the transport sector of a nation. However, the ever-increasing depletion of conventional fossil fuel sources and increase in environmental hazards due to pollution arising from fuel-burning necessitates the conservation of energy. An energy audit is a systematic approach to achieve energy conservation. It also technically and economically evaluates the benefits achieved for industry through energy conservation. In the present article, a significant review of energy audits is presented. Such a review will be beneficial for further studies in this area.

I. Introduction

The growth of an economy is closely related to its energy consumption growth. It is recognized that the non-availability of energy is a serious obstacle to economic growth. Energy is the ability to do work, and work takes place in the transfer of energy from one form to another. In practical terms, energy is what we use to manipulate the world around us, whether by exciting our muscles, using electricity, or using mechanical devices such as automobiles. Energy comes in different forms - heat (thermal), light (radiant), mechanical, electrical, chemical, and nuclear energy. Energy is one of the principal inputs for the economic development of any country. In the case of developing countries, the energy sector assumes significance due to ever-increasing energy needs requiring considerable investments to meet them. The per capita energy consumption is low for India compared to developed countries but is likely to grow with economic growth. Energy intensity is measured as energy consumption per unit of GDP. Energy intensity indicates the development stage of a country. Compared to the U.S., Japan and the world average, India's energy intensity is low.

The usage of energy resources in the industry leads to environmental damages by polluting the atmosphere. A few of examples of air pollution are sulphur dioxide (SO2), nitrous oxide (NOX), carbon monoxide (CO) emissions from boilers and furnaces, chloro-fluro carbons (CFC) emissions from refrigerant use, etc. In chemical and fertilizers industries, toxic gases are released. Cement plants and power plants spew out particulate matter. Typical inputs, outputs, and emissions for a typical industrial process are shown in Figure 1.

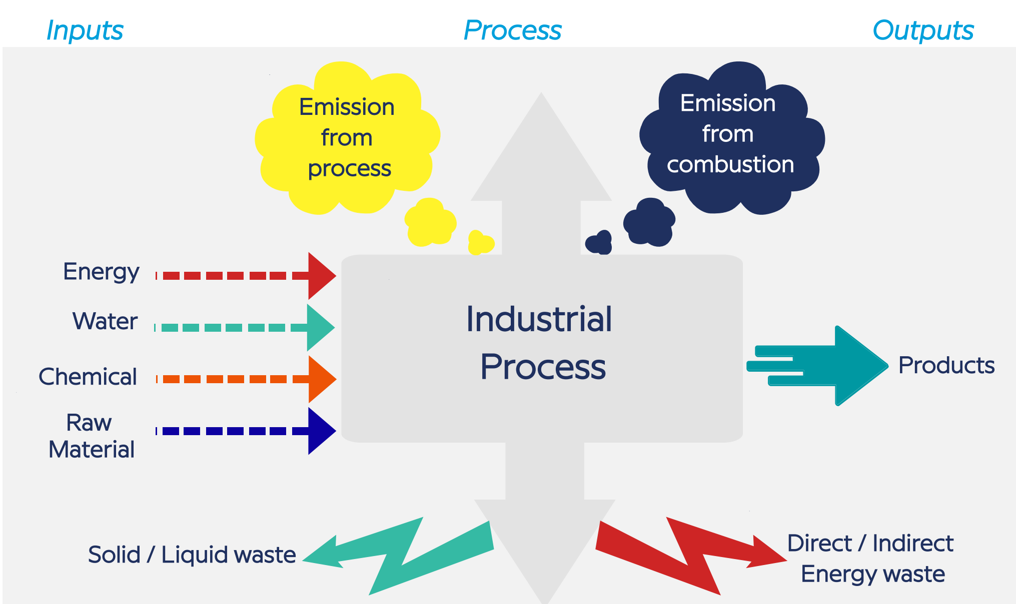


Figure 1. Input & Output of Process

In both developed and rapidly industrializing countries, the major historic air pollution problem has typically been high levels of smoke and SO2 arising from the combustion of sulphur containing fossil fuels such as coal for domestic and industrial purposes.

II. Energy Dependency/Efficiency

Energy efficiency for a nation is to reduce its dependency on imported energy sources for its economic growth. India will continue to experience an energy supply shortfall throughout the recent shortage period of coal. This gap has widened since 1985 when the country became a net importer of coal. Imports of oil and coal have been increasing every year. The dependence on energy imports is projected to increase in the future. The import of gas and LNG (liquefied natural gas) are likely to increase in the coming years. This energy import dependence implies vulnerability to external price shocks and supply fluctuations, which threaten the country's energy security. Increasing dependence on oil imports means reliance on imports from the Middle East, a region susceptible to disturbances and consequent disruptions of oil supplies. This calls for diversification of sources of oil imports. The need to deal with oil price fluctuations also necessitates measures to be taken to reduce the economy's oil dependence, possibly through fiscal measures to reduce demand and by developing alternatives to oil, such as natural gas and renewable energy. Some of the strategies that can be used to meet future challenges to their energy security are:

A. **Diversification of energy supply sources:** Energy diversification means introducing different energy sources like Renewable, Thermal, Hydro into the energy generation mix and increasing the share of energy generated from each source to avoid a sole dependence on a single energy resource.
B. **Demand restraint:** Control on energy demand which means demand side management.
C. **Development of renewable energy sources:** Renewable energy means energy from a source that is not depleted when used, such as wind or solar power.
D. **Energy efficiency:** Energy efficiency means using less amount of energy to perform the same task or operation by adopting new technology and eliminating energy waste.
E. **Sustainable development:** Sustainable development goal focuses on developing and expanding renewable energy resources like sun, wind, hydropower, liquid and solid biofuels, biogas etc., using them judiciously without compromising the need of the present and future generations.

Although all these options are feasible, their implementation will take time. Out of all these options, the simplest and the most easily attainable is reducing demand through persistent energy conservation efforts.

III. Energy Conservation and its Importance

Coal and other fossil fuels, which have taken three million years to form, are likely to deplete soon. In the last two hundred years, we have consumed 60% of all resources. For sustainable development, we need to adopt energy efficiency measures. Today, 85% of primary energy comes from non-renewable and fossil sources (coal, oil, etc.). These reserves continually diminish with increasing consumption and will not exist for future generations (see Figure 2).

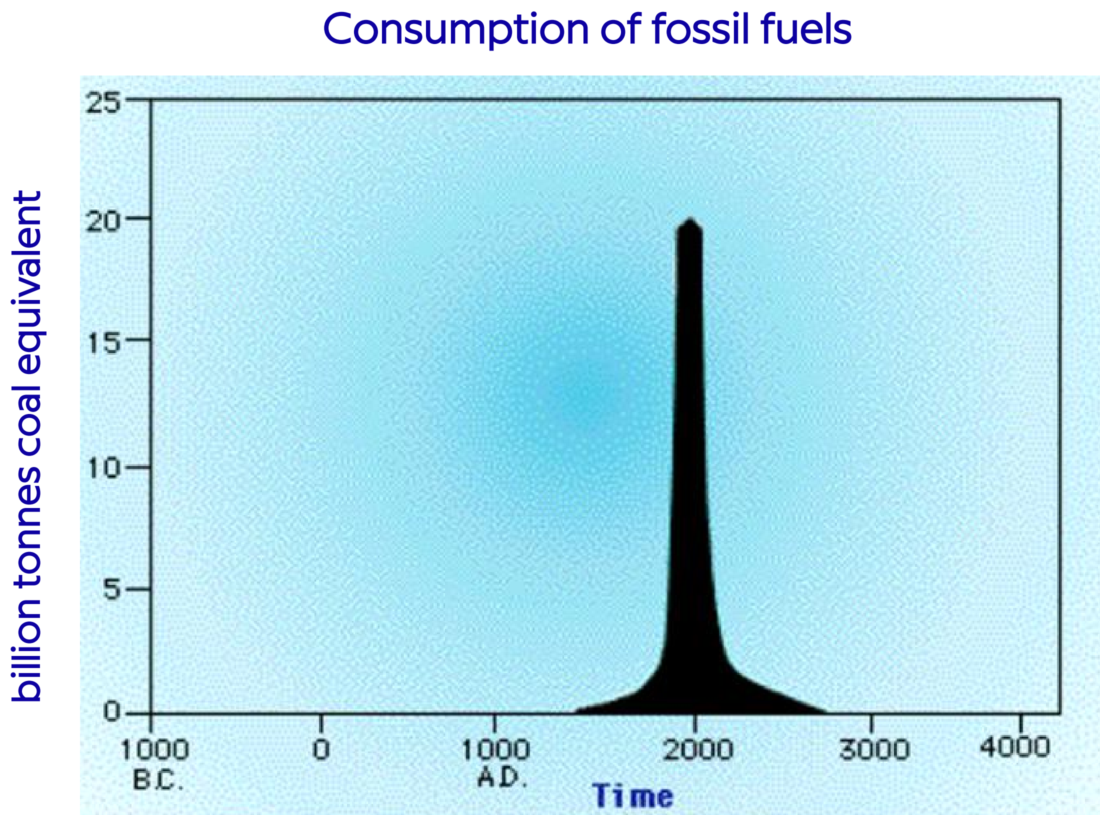


Figure 2. Consumption of trend of fossil fuels by human being

IV. Energy Conservation and Energy Efficiency

Energy Conservation and Energy Efficiency are distinct but related concepts. Energy conservation is achieved when growth in energy consumption is reduced, measured in physical terms. Energy conservation can, therefore, be the result of several processes or developments, such as productivity increase or technological progress. On the other hand, energy efficiency is achieved when energy intensity in a specific product, process or area of production or consumption is reduced without affecting output, consumption or comfort levels. Promotion of energy efficiency will contribute to energy conservation and is therefore an integral part of energy conservation promotional policies.

V. Definition & Objectives of Energy Management

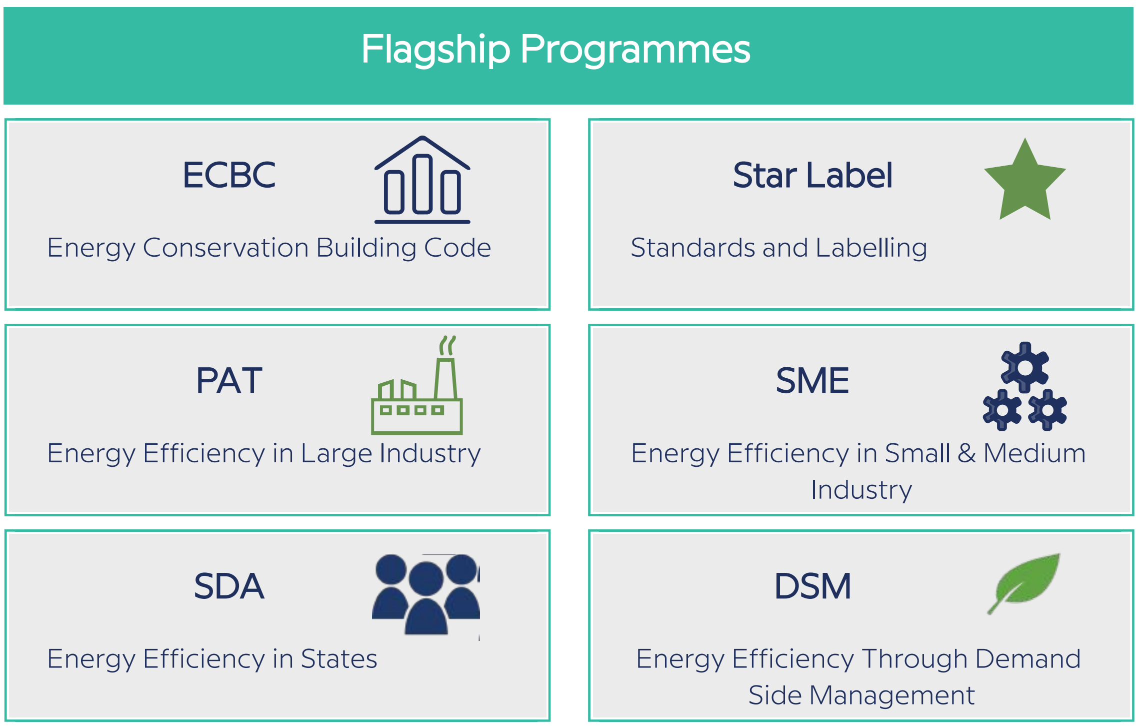
The fundamental goal of energy management is to produce goods and provide services with the least cost and environmental effect. The objective of energy management is to achieve and maintain optimum energy procurement and utilization throughout the organization and:

- To minimize energy costs/waste without affecting production & quality
- To minimize environmental effects.

Energy audit is the key to a systematic approach for decision-making in the area of energy management. It attempts to balance the total energy inputs with its use and serves to identify all the energy streams in a facility. It quantifies energy usage according to its discrete functions. Industrial energy audit is an effective tool in defining and pursuing a comprehensive energy management programme. In the present project, we have focused our attention on the methodology and results of previous work carried out in the domain of energy audit.

VI. The Way Forward

Flagship Programmes by Bureau of Energy Efficiency (Ministry of Power, GOI)



- **ECBC:** ECBC 2017 (Energy Conservation Building Code) was launched by Hon'ble Minister (IC) for Coal, Mines, NRE and Power on 19 June, 2017 and is applicable for large commercial buildings with a connected load of 100 kW and above or 120 kVA and above. ECBC focuses on building envelope, mechanical systems and equipment including heating, ventilating, and air conditioning (HVAC) system, interior and exterior lighting systems, electrical system and renewable energy, and also takes into account the five climates zones (Hot Dry, Warm Humid, Temperate, Composite and Cold) present in India.

- **Star Label:** **The Standards & Labelling Programme** is one of the major thrust areas of Bureau of Energy Efficiency. A key objective of this scheme is to provide the consumer an informed choice about the energy-saving and thereby the cost-saving potential of the relevant marketed product. The scheme targets the display of energy performance labels on high-energy end-use equipment & appliances and lays down minimum energy performance standards.

- **PAT: Perform, Achieve and Trade (PAT)** scheme is a flagship programme of Bureau of Energy Efficiency under the National Mission for Enhanced Energy Efficiency (NMEEE). NMEEE is one of the eight national missions under the National Action Plan on Climate Change (NAPCC) launched by the Government of India in the year 2008.

- **SME:** With climate change, a transition towards an energy-efficient economy is highly imperative for the manufacturing sector, including micro, small and medium enterprises (MSMEs), which account for a large part of the world's consumption of resources.

- **SDA:** In exercise of the powers conferred by section 15(d) of the Energy Conservation (EC) Act 2001, all the State Governments / UT administrations have designated an agency as State Designated Agency (SDA) to coordinate, regulate and enforce the provisions of this Act within the State, either by assigning additional responsibilities to one of the existing departments of the State Government or by establishing a dedicated stand-alone SDA for energy efficiency.

- **DSM:** Demand Side Management (DSM) has been traditionally recognized as one of the major interventions to achieve reduction in energy demands while ensuring continuous development.

VII. Case Studies

Following are some examples of energy audit saving potential at industries carried out by our firm.

Sr. No	Observations
1.	Possible savings by improving the power factor which results approx. INR 50 Lakh per annum.
2.	Potential to install Variable Frequency Drive (VFD) at chiller secondary pumps leads to save 25% energy with existing energy consumption.
3.	Replacement of old reciprocating compressor with new single one energy efficient screw compressor - leads to save 30% of energy.
4.	Possible to recover waste heat from boiler exhaust fuel gases by installing economizer - leads to save boiler fuel and improve efficiency.
5.	Potential energy saving at electrical motors by switching to IE-4 Class which is premium efficiency motor over general standards motors - leads to save 3 % to 8 % of energy.

References: Guide books on Energy Audit by Bureau of Energy Efficiency.

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