I. Companies (Corporate Social Responsibility Policy) Amendment Rules, 2022

The Ministry of Corporate Affairs ('MCA') has recently issued **Companies (Corporate Social Responsibility Policy) Amendment Rules, 2022.** Some of the key changes are summarised as under:

1. It prescribes that the company having any amount in its Unspent Corporate Social Responsibility Account, has to continue to constitute a CSR Committee; and comply with the provisions contained in sub-section (2) to (6) of Section 135 of the Act irrespective of the fact that in subsequent years it is not covered under subsection (1) of section 135 of the Companies Act, 2013 ('the Act'). As per earlier provisions, company which ceased to be a company covered under subsection (1) of section 135 of the Act for three consecutive financial years was not required to constitute a CSR Committee; and comply with the other provisions of Section 135 of the Act till such time it meets the criteria again as specified in sub-section (1) of section 135 of the Act.

2. The company having an average CSR obligation of Rs. 10 crore or more in the three immediately preceding financial years is required to undertake impact assessment, through an independent agency in respect of specified projects. The impact assessment report is placed before the Board and is also annexed to the annual report on CSR.

   For such companies, earlier it was allowed to book the expenditure towards Corporate Social Responsibility for that financial year upto a lower of 5 % of the total CSR or Rs. 50 lakhs. As per the amendment, the said expenditure is now restricted to the higher of 2% of the total CSR or Rs. 50 lakhs.

II. Expert Advisory Committee Opinion:

1. Adoption of 'Net Book Value' method as one of the valuation techniques to measure the fair value of investments in equity instruments that do not have a quoted market price in an active market:

A. Background:

The Expert Advisory Committee ('EAC') of the Institute of Chartered Accountants of India ('ICAI') has issued an opinion in respect of the Adoption of 'Net Book Value' method as one of the valuation techniques to measure the fair value of investments in equity instruments that do not have a quoted market price in an active market.

A Company is a wholly owned Government of India Company. Through public and private partnership (PPP) mode, the Company as a promoter shareholder had invested in A Corporation Ltd. Further, the Company held shares in two other entities, viz., its joint venture, X Ltd. and Y Consumer Co-operative Society Limited. All these three investments were disclosed in the 'Investment' schedule in the Company's balance sheet.

The Company has elected an option for the investments in equity instruments of A Corporation Ltd. for the subsequent measurement of such investments at fair value through OCI.

During the course of the supplementary audit, the C&AG audit team issued an audit query stating that "Valuation of investment in equity shares of A Corporation Ltd. as per net book value method instead of cost had resulted in an overstatement of Investments".

B. Key Issues:

Whether the adoption of 'Net Book Value' method by the Company as one of the valuation techniques to measure the fair value of investments in equity instruments of A Corporation Ltd. that did not have a quoted market price in an active market was in order or whether should be measured at cost?

C. Basis of opinion:

- Ind AS 109 – 'Financial Instruments'
- Ind AS 113 – 'Fair Value Measurements'

D. Key Principles Applied & Conclusion:

i. The query addressed by the committee is valuation of investment in equity instruments of A Corporation Ltd. (a closely held company) that do not have a quoted market price in an active market, and which is not an investment in the subsidiary, joint venture and associates.

ii. As per paragraphs B5.2.3 to B5.2.5 of Ind AS 109, all investments in equity instruments are to be measured at fair value irrespective of whether these are quoted or not quoted in an active market except in limited circumstances, where cost may be an appropriate estimate of fair value. There are examples given in the standard which indicate that the cost might not be representative of fair value. If these indicators are existing, then the Company has to measure the fair value and cost cannot be used as fair value.

iii. As per Ind AS 113, when measuring fair value, the objective is to estimate the price at which an orderly transaction to sell an asset or to transfer a liability would take place between market participants at the measurement date under current market conditions.

iv. There are three widely used valuation techniques, viz., the market approach, the cost approach and the income approach. The Standard prescribes to use valuation techniques consistent with one or more of these approaches to measure fair value; and that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

v. In some cases, a single valuation technique will be appropriate, while in other cases, multiple valuation techniques will be appropriate. Further, the Standard states that the availability of relevant inputs and their relative subjectivity might affect the selection of appropriate valuation techniques.

vi. However, the fair value hierarchy prioritises the inputs to valuation techniques, not the valuation techniques used to measure fair value._Ind AS 113 establishes a fair value hierarchy that categorises into three levels (i.e. Level 1, 2 and 3), the inputs to valuation techniques used to measure the fair value. The Standard does not prescribe the use of a specific valuation technique or a hierarchy of valuation techniques; rather it only provides a hierarchy of inputs to valuation techniques. .

vii. The fair valuation involves judgment not only when applying a valuation technique, but also in the selection of valuation technique. However, whichever approach or technique(s) is used, the objective of fair valuation should be kept in mind, i.e. an exit price at the measurement date from the perspective of a market participant that holds the asset.

viii. In spite of A Corporation Ltd. being an unlisted company and absence of availability of observable market transactions and other market information, the Company should determine the fair value considering its specific facts and circumstances using valuation technique(s) and using one or more observable and unobservable inputs; and keeping in view the objective of fair value measurement and other requirements of Ind AS 113.

ix. Further, where unobservable inputs are used to measure fair value, as per paragraph 64 of the Standard, if the transaction price is fair value at initial recognition and a valuation technique that uses unobservable inputs will be used to measure fair value in subsequent periods, the valuation technique should be calibrated so that at initial recognition the result of the valuation technique equals the transaction price.

x. The EAC opined that:

- While determining fair value, net book value/carrying amount of net assets could be used as the beginning point or as one of the inputs, which may require further adjustments as per valuation technique(s) considering the requirements of Ind AS 113, but the same itself cannot be directly considered as a substitute of fair value. Therefore, since the Company has not apparently followed the above approaches, techniques and methodology prescribed under Ind AS 113 to determine fair value in the extant case, the same is not appropriate.

- With regard to using 'cost' as the basis of valuation of equity instruments, the Committee is of the view that as per paragraphs B5.2.3 to B5.2.5 of Ind AS 109, all investments in equity instruments are to be measured at fair value irrespective of whether these are quoted or not quoted in an active market except in limited circumstances, where cost may be an appropriate estimate of fair value.

2. Timing of capitalisation of transmission lines and sub-stations as an item of Property, Plant and Equipment from capital-work-in-progress and also in case of modernisation work:

A. Background:

A wholly owned State Government Company (hereinafter referred to as 'the Company') was formed by carving out the generation, transmission and distribution function of the erstwhile State Electricity Board.

The Company had Property, Plant and Equipment (PPE) procured by way of acquisition, purchase, gift/consumers' contribution & construction of transmission lines and substations.

Work of construction of these substations and lines was carried out by the company through turnkey contracts. The installation of equipments at sub-station premises and drawing of transmission lines from one station to other was executed by turnkey contractors under the guidance and supervision of the company's engineers.

The contention of the Comptroller and Auditor General (C&AG):

(1) Approval of the Chief Electrical Inspector to Government (CEIG) shall be considered for capitalising as PPE, as the asset was in the location and condition necessary for it to be capable of operating in the manner intended by the management; and the asset was to be categorised and depreciation charged from the date of approval of CEIG.

(2) As station work was completed long back, the substation was ready to take the load, i.e., ready to use. Accordingly, the depreciation was to be charged from the date of completion/ ready to use irrespective of the fact of the no-source power line.

(3) As per paragraph 43 of Ind AS 16, each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item, shall be categorised and depreciated separately.

B. Key issues:

On the basis of the above, the opinion of the EAC was sought on the following issues:

i. Whether the date of capitalisation (from CWIP to PPE) of an asset should be the date of approval from CEIG or the date of asset commissioned certificate.
ii. Can the Company capitalise an asset, pending availability of a source line though all the equipments (Plant and Machinery) in the station were installed/erected but not tested
iii. Can the Company capitalise an asset pending output of power/energy from the station though all the equipments (Plant and Machinery) in the station were installed/erected, tested and CEIG approval was received?

iv. Whether the date of a successful test run is to be adopted as the date of capitalisation of an asset.
v. Whether on erection and connecting the equipment to the incoming source line, such equipment should be categorised though transmission of power could not be carried out.
vi. Whether the assets need to be capitalised when all the works mentioned in the Detailed Work Award (DWA) were completed by the Contractor (pending obtaining of CEIG approval and source line).
vii. Whether in case of modernisation work, the assets need to be capitalised on erecting part of the assets mentioned in the DWA though the end use of transmission of power not achieved.

C. Basis of opinion:

- Ind AS 16 – "Property, plant and equipment"

D. Key Principles Applied & Conclusions:

i. The EAC referred to the definition of Property, plant and equipment as given in Ind AS 16, 'Property, Plant and Equipment' and noted that an item of PPE shall be measured at cost which comprises its purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management and cost of dismantling/removing and restoring the asset, and the cost of testing whether the asset is functioning properly is also an example of directly attributable cost.

ii. The EAC further noted that the assets covered in the extant case were in the nature of self-constructed assets, and in terms of paragraph 22 of Ind AS 16, the cost of a self-constructed asset is determined using the same principles as for an acquired asset. Therefore, in the extant case, the principles for 'acquired assets' under Ind AS 16 shall be equally applicable to the self-constructed assets covered under the contract with the turnkey contractors in the extant case.

iii. The EAC viewed that an item of capital work in progress should be transferred to the gross block of PPE when such item is in the location and condition necessary for it to be capable of operating in the manner intended by management.

iv. It was noted that, when the asset on which modernisation work was carried out or a component/part thereof, could be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16, the same could be capitalised.

v. The EAC also mentioned that the company should also consider the impairment of assets, if any, considering the requirements of Ind AS 36 for assets that were taking longer time to complete due to the non-availability of the source line, etc.

vi. The EAC opined that, the date or point when an asset can be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16 and when an item of capital work in progress can be transferred to gross block of PPE is a matter of technological assessment and judgment. The company should consider various factors such as, technological assessments, safety parameters, various pre-requisite and substantive approvals from competent authorities, etc.

vii. Subject to the above overall guidance, EAC opined that:

- For key issues (i) and (vi): The CEIG approval date or the date of the asset commissioned certificate might not be the sole determinant(s) for capitalisation of the asset. Further, regarding the implication on capitalisation pending source line see (iii) and (v) below.

- For key issues (ii) and (iv): Before trial/test run, the plant/asset cannot be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by management as per the requirements of Ind AS 16.

- For key issues (iii) and (v): The timing of capitalisation to PPE is determined based on when the asset is ready to use and not when the asset is put to use. If the asset is ready to use but not put to use due to the non-availability of power supply in the extant case, capitalisation cannot be delayed.

- For issue (vii): In case of modernisation work, when the asset on which modernisation work is carried out or a component/part thereof, can be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16, the same should be capitalised.