

FAQs on National Financial Reporting Authority (“NFRA”) Rules, 2018

By Shaifali Sharma | Executive
Vinod Kothari & Co. | Updated as on 12th December, 2019
corplaw@vinodkothari.com

Witnessing the ever-increasing corporate scams in India, the Ministry of Corporate Affairs, Government of India constituted an independent regulatory body for auditors and audit process on October 01, 2018 under section 132(1) of the Companies Act, 2013 (“Act”) named National Financial Reporting Authority (“NFRA”) and notified the National Financial Reporting Authority Rules, 2018 (“Rules”) vide Notification¹dated November 13, 2018, effective from November 14, 2018.

Government’s approach to independent regulatory model will prove beneficial to the audit profession making it more transparent and accountable. However, the Rules have given rise to a number of questions for corporate entities and auditors which we have analyzed and tried answered through these FAQs.

¹http://www.mca.gov.in/Ministry/pdf/NFRARules2018_13112018.pdf

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FAQs on NFRA Rules

Legislative background

1. What is NFRA?

National Financial Reporting Authority (“NFRA”) is an independent regulatory body for carrying out the functions *inter alia* monitoring compliance of accounting and auditing standards, oversee the quality of service of the professions associated with ensuring compliance with such standards, suggest measures required for improvement in quality of service. It is a quasi-judicial body constituted under the provision of section 132 of the Act.

2. What is the legislative background of the development of NFRA?

The evolution of NFRA can be understood in different phases detailed below:

a. *Under Companies Act, 1956*

Under section 210A of the erstwhile Companies Act, 1956, Central Government constituted an Advisory Committee called as National Advisory Committee on Accounting Standards (“NACAS”) to recommend it on the formulation of accounting policies and accounting standards for adoption by the companies.

However, the role of NACAS was limited and the power to formulate auditing standard remained vested with the ICAI.

b. *Standing Committee of Finance*

The Standing Committee on Finance in its 21st report proposed that NACAS, in addition to accounting standards, should also recommend auditing standards to the Central Government and change its name from NACAS to National Advisory Committee on Accounting and Auditing Standards (NACAAS). Furthermore, it was proposed to make such authority a quasi-regulatory body to supervise the quality of audit.

c. *Under Companies Act, 2013*

With the enactment of Companies Act, 2013, the NACAS was replaced by NFRA where the role was elevated from advisory body to an independent regulatory body as recommended by the Standing Committee of Finance. Section 132 empowered the Central Government to constitute NFRA to deal with the matters of accounting and auditing standards.

d. *Companies Law Committee*

The Companies Law Committee was constituted in the year 2015 to suggest amendments to the Companies Act, 2013. Considering some serious lapses in the profession, it felt the need of constituting an independent regulatory body at the earliest. Accordingly, recommended the Government the establishment of NFRA to oversee the profession of audit.

e. *Committee of Expert*

In the matter of *S. Sukumar v. The Secretary, Institute of Chartered Accountants of India & Ors*², the Hon'ble Supreme Court vide its judgment dated February 23, 2018 ordered the constitution of a 'Committee of Experts' to examine the need of an oversight body for the profession of auditors. The Committee submitted its report in October 2018 outlining various issues and recommendations.

Basis the recommendations, MCA appointed October 01, 2018 as the date of constitution of NFRA and notified the National Financial Reporting Authority Rules, 2018 ("Rules") vide notification dated November 13, 2018, effective from November 14, 2018

3. What is the need to constitute NFRA? What intent it is trying serve?

The statutory body regulating the profession of accountancy and audit in India is the Institute of Chartered Accountants of India ("ICAI"). Being a self-regulatory body, it enjoys wide range of powers. However, it lacks the quality of regulatory independence and unbiased oversight. The *Satyam scandal* and *PNB fraud case* are one among several financial scams in India evidencing this.

The Ministry of Corporate Affairs, based on the recommendation of Standing Committee on Finance, realized the need of constituting an independent regulatory authority for regulating the audit profession. Accordingly, with the objective to curb such fraudulent practices and to enhance the quality of audit in India, the Government established NFRA on October 01, 2018 under section 132(1) of the Act as quasi-judicial body to regulate certain big-sized entities and auditors and handle various other aspects of accounting and auditing.

Provisions of Law

4. What are the statutory provisions governing the NFRA?

²https://sci.gov.in/supremecourt/2013/35041/35041_2013_Judgement_23-Feb-2018.pdf

Companies Act, 2013

Section 132 of the Act provides for the constitution of NFRA, its compositions, functions, duties, powers, provision relating to appeal to Appellate Tribunal etc.

The National Financial Reporting Authority Rules 2018

The said Rules majorly cover the following areas:

- a. Applicability or the scope of NFRA
- b. Functions and duties of NFRA
- c. Powers of NFRA
- d. Disciplinary proceedings
- e. Role of chairperson and full-time members
- f. Financial reporting advocacy and education
- g. Confidentiality and security of information
- h. Avoidance of conflict of interest

The National Financial Reporting Authority (Manner of Appointment and other Terms and Conditions of Service of Chairperson and Members) Rules, 2018

These Rules prescribes the composition of NFRA, manner of appointment of its members and other procedural and internal matters of Authority.

5. What is the effective date of applicability of such provisions?

Relevant effective dates can be referred from the table below:

Particulars	Section/Rule	Effective Date	Link to notification
Composition of NFRA	Section 132(3)	March 21, 2018	http://www.mca.gov.in/Ministry/pdf/commencementNotification2103_21032018.pdf
Appointment of secretary and other employees by NFRA	Section 132(11)	March 21, 2018	
Constitution of NFRA	Section 132(1)	October 01, 2018	http://www.mca.gov.in/Ministry/pdf/ConstitutionNotificationNFRA_04102018.pdf
Functions, powers and other relevant section	Section 132(2),(4),(5),(10),(13), (14) and (15)	October 24, 2018	http://www.mca.gov.in/Ministry/pdf/CommencementNotification_24102018.pdf

NFRA Rules, 2018		November 13, 2018	http://www.mca.gov.in/Ministry/pdf/NFRARules2018_13112018.pdf
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About NFRA

6. What are the functions of NFRA?

The NFRA is tasked with numerous jobs which mainly includes the following:

- a. To make recommendation to the Central Government on formulation of accounting/auditing policies/standards;
- b. To monitor and enforce the accounting and auditing standards compliance;
- c. To oversee the quality of service of the associated professions ensuring compliance with such standards and suggesting improvement measures if required;
- d. Performing such other functions related to above functions.

7. What are its powers?

To ensure that NFRA justify its role of an independent audit regulator, the NFRA is empowered with substantial powers, which largely includes:

- a. Investigating into professional/other misconduct committed by any member/firm of Chartered Accountants;
- b. Power to impose penalty or debaring the auditors or audit firm for minimum 6 months and upto 10 years from practicing audit profession;
- c. Same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit;
- d. The Authority may require the personal presence of the officers of the company or body corporate and its auditor in connection with the review of the financial statements.

8. How the NFRA perform the role of a quasi-judicial body?

Section 132(4) is a non-obstante clause, permitting the NFRA to exercise the same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit, in respect of the following matters:

- a. discovery and production of books of account and other documents, at such place and at such time as may be specified by the
- b. summoning and enforcing the attendance of persons and examining them on oath;
- c. inspection of any books, registers and other documents of any person referred above at any place;
- d. issuing commissions for examination of witnesses or documents.

Scope and Applicability

9. What is the reach of Rule 3?

Rule 3 of NFRA rules has 4 clauses.

1. Clause 1 provides for the class of entities which shall be regulated by NFRA;
2. Clause 2 provides for the class of body corporates which will be required to do one-time filing of the e-Form NFRA-1;
3. Clause 3 provides for the class of body corporates which will be required to do one-time filing of the e-Form NFRA-1;
4. Clause 4 provides for the class of companies including body corporates that shall continue to be regulated by NFRA after ceasing to be companies / body corporate under clause 1.

10. Which all entities are governed by the NFRA?

Rule 3(1) of the Rules list out certain class of entities (companies, bodies corporate and persons) which shall be regulated by the NFRA. The list of such entities is as follows:

1. Companies whose securities are listed on any stock exchange in India or outside India;
2. Unlisted public companies fulfilling any of the following criteria as on the 31st March of immediately preceding Financial Year:
 - a. having paid-up capital of not less than Rs. 500 crores; or
 - b. having annual turnover of not less than Rs. 1000 crores; or
 - c. having, in aggregate, outstanding loans, debentures and deposits of not less than Rs. 500 crores.
3. Insurance companies, banking companies, companies engaged in the generation or supply of electricity, companies governed by any special Act or bodies corporate incorporated by an Act in accordance clauses (b), (c), (d), (e) and (f) of section 1(4) of the Act;
4. Body corporate/companies/persons or any class of them referred by Central Government to the Authority in public interest;
5. Foreign subsidiary(ies) and associate(s) of:
 - a. of the company or body corporate registered in India as referred in point (1) to (4) above; and
 - b. income or net worth exceeds 20% of the consolidated income or consolidated networth of such company or the body corporate.

Such associates and subsidiaries are hereinafter referred to as “material subsidiaries and associates”

11. Which all entities are not covered by Rule 3(1) i.e. not under the radar of NFRA?

Considering the provisions of applicability of the Rule 3(1) explained in above question, following companies shall not be governed by the Authority:

1. Unlisted private companies (unless referred by Central Government to the Authority in public interest);
2. Unlisted public companies with paid-up capital or turnover or aggregate of loans, debentures and deposits below the limit stated under Rule 3(1).
3. All LLPs incorporated in India which are otherwise not referred to NFRA by the Central Government in public interest
4. All foreign subsidiaries and associates which are not material under Rule 3(1)(e).

Reporting requirements with respect to appointment of auditors

12. What are the reporting requirements prescribed under the NFRA Rules?

In terms of Rule 3(2) and (3) of the said Rules, the particulars of the auditor is required to be reported to NFRA in e-Form NFRA-1. The filing requirement under said Rules is of two types:

Clause to Rule 3	Type of reporting	Timeline of reporting	Applicable Entities
Clause 2	Initial or one-time	On or before July 31, 2019 ³	<p>Body corporates other than companies regulated by NFRA in Rule 3(1) i.e</p> <ol style="list-style-type: none"> 1. Insurance / banking / electricity companies which are not incorporated under any Companies Act and are infact governed under special Act eg LIC Act, UTI Act etc or any other Act under clause (b) to (f) of section 1(4) of Companies Act, 2013 2. Such body corporates as may be referred to the Authority by the Central Government 3. Foreign material subsidiaries and associates.
Clause 3	Event based – Each time on	within 15 days of appointment of auditor	Indian body corporates + foreign material subsidiaries and associates

³http://www.mca.gov.in/Ministry/pdf/FormNFRA1_0207019.pdf

	the appointment of auditor		
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Further, NFRA has clarified from its FAQs that only those foreign subsidiaries/associates u/r 3(1)(e) shall file NFRA-1 which are having business in India.

13. What are the other reporting requirements prescribed under Companies Act, 2013 w.r.t appointment of auditors?

Third proviso to section 139(1) of the Act read with Rule 4(2) of the Companies (Audit and Auditors) Rules, 2014 requires every “company” appointing auditor under section 139(1) to file e-Form ADT-1 within 15 days of the meeting in which the auditor is appointed. However, filing of e-Form ADT-1 is not mandatory for the appointment of first auditor of company as per section 139(6).

14. Whether the requirement of filing Form ADT-1 applies on Government Companies?

The requirement of filing e-Form ADT- 1 comes from section 139(1), which is related to appointment of subsequent auditors only. Accordingly, every company appointing auditor in the manner prescribed under section 139(1) shall file e-Form ADT-1. However, in case of Government companies, the procedure of appointment is different as given under section 139(5) of the Act.

The expression “notwithstanding anything contained in sub-section (1)” used in sub section (5) means that while the auditor of a government company is appointed by CAG, the requirement contained in provisos to section 139(1) with respect to filing of e-Form ADT-1 on appointment of auditor shall continue.

15. Which classes of entities are required to comply with one-time filing?

Rule 3(2) requires every body corporate other than a company governed by the Rules to file NFRA-1 on one-time basis. On a plain reading it seems that all companies incorporated in India shall file the said Form except the companies actually governed by the Rules. However, the purpose of filing NFRA-1 is to inform the particulars of the auditors to the Authority, which are anyway provided by the Indian companies in e-Form ADT-1 under section 139 of the Act. Accordingly, out of the list of entities regulated by NFRA under Rule 3(1), only the body corporates (other than companies) shall comply with one-time filing.

16. Which classes of entities are required to comply with event based filing?

Rule 3(3) requires everybody corporate “*formed in India*” and governed by the Rules, other than a company defined under section 2(20) of the Act, to file the e-Form NFRA-1 in the event of appointment of auditor. The proviso to the Sub rule provides for filing of NFRA 1 by body corporate as specified under Rule(1)(e) of the Rules. Therefore, event based filing requirement arise in case following conditions are satisfied:

1. The entity shall be a body corporate incorporate in India; **and**
Exception: Such foreign body corporate as specified under Rule(1)(e) of the Rules [Proviso to Rule 3(3)]
2. Such body corporate falls under the class of entities specified under Rule 3(1); and
3. It shall not be a company incorporated under the Companies Act, 2013

NFRA has clarified from its FAQs that only those foreign subsidiaries/associates u/r 3(1)(e) shall file NFRA-1 which are having business in India.

It should be noted that no specific time limit for filing the Form by foreign body corporate under rule 3(1)(e) is prescribed.

17. Is there any time-limit of filing of the event based Form?

As per Rule 3(3), for bodies corporate incorporated in India, e-Form NFRA 1 is to be filed within 15 days of appointment of auditor.

There is no time limit mentioned for the filing of e-Form NFRA-1 for appointment of directors by foreign bodies corporate which are material subsidiaries / associates u/r 3(1)(e).

18. Whether private companies be governed by the Authority? If yes, whether it is required to file NFRA-1?

Unlisted private companies do not fall under the ambit of Rule 3(1) of the Rules, and therefore shall not be governed by NFRA. Further, in all cases, companies are excluded from any filing requirement.

19. Whether a foreign subsidiary company of a private company in India is required to file NFRA-1?

As per Rule 3(2) read with 3(1)(e) of the said Rules, the requirement of filing shall be applicable only to that body corporate which is a subsidiary or associate of an entity covered under clauses (a) to (d) of Rule 3(1) and is contributing more than 20% of the consolidated income or networth of the holding entity or investor entity

Since the unlisted private companies are not covered under Rule 3(1), no filing is required to be done by the foreign subsidiary company of a private company.

20. Whether LLPs be governed by the Authority?

No, LLPs are not explicitly included within the purview of NFRA Rules, 2018. However, Rule 3(d) specifies that Central Government may notify such class of bodies corporate or companies which will be required to comply with the provisions of the said Rules.

It is to be noted that till date no such class of bodies corporate have been specified by the Government. Accordingly, as per the current set of Rules, the LLPs are not required to comply with NFRA Rules, 2018.

21. Is there any filing requirement on the part of the auditors?

Yes, pursuant to Rule 5 of the Rules, every auditor governed by the NFRA shall file an Annual Return with NFRA on or before 30th November every year in Form NFRA-2.

Pursuant to the NFRA (Amendment) Rules, 2019⁴ dated 5th September, 2019, the due date of filing the said Form has been extended from 30th April to 30th November (every year).

Further, MCA vide its Circular dated 27th November, 2019⁵ has extended the last date of filing the said Form till 90th day from its deployment i.e. 12th December, 2019. Accordingly the last date for filing the same is 11th March, 2020.

Filing of NFRA-2

22. How to file Form NFRA-2?

The Form NFRA-2 is available on <https://nfra.gov.in/> and shall be filed online after creating Login Id on the portal. The technical requirements for submitting of Form on NFRA Portal can be referred from [here](#).

Further, the following details/documents are required by the Auditor(s) before filing Form NFRA-2:

1. Limited Liability Partnership Identification Number (LLPIN) or any other registration Number of the firm;
2. Income Tax PAN of Auditor (for Indian firm);
3. Registration number of Auditor with the regulator/agency;
4. The following details of the companies that need to be filled in:
 - Name of Company/Body Corporate
 - CIN/ PAN of Company/Body Corporate or FCRN of the company or Identity number of body corporate
 - Global Location Number of Company/Body Corporate (if applicable)
 - Details of the Fees received by the Auditor from Company/Body Corporate
 - Currency Conversion rate (if fees received in Foreign Currency);
5. Network Registration Number of the auditor with ICAI;
6. Details of the Partners of the auditor;
7. Number of employees employed by the auditor; and
8. Digital Signature Certificate (DSC) of User.

⁴<http://ebook.mca.gov.in/notificationdetail.aspx?acturl=6CoJDC4uKVUR7C9Fl4rZdatyDbeJTqg3j74XUrq+nvScRHVR0kXI0A==>

⁵http://www.mca.gov.in/Ministry/pdf/NFRA_27112019.pdf

Filing of NFRA-1

23. How to file Form NFRA-1?

The Form NFRA-1 is available on <https://nfra.gov.in/>. The said form is not like any other e-Form as available on MCA portal. It needs to be filled online only. For the same, user first has to register on the NFRA portal. Step wise instructions for user registration can be referred [here](#)

24. Who are the eligible ‘users’ to register on NFRA portable?

The entity which is required to file NFRA-1 form shall authorize an individual who is an official of the entity and is holding any of the following position in the entity:

1. Director
2. Chief Executive Officer
3. Chief Financial Officer
4. Manager
5. Company Secretary

Therefore, only the aforementioned officials of the entity are eligible to register on the portal on behalf of the entity.

25. How to make such officials authorized to register and submit NFRA-1 form?

The entities shall issue an authorization letter in the format prescribed by NFRA. (Format can be viewed [here](#)). Further, NFRA has clarified that certified copy of the Board resolution can also be uploaded as authority letter however the same should bear all the details as stated in the said sample letter.

Jurisdiction of NFRA on auditors

26. What is the meaning of the term ‘auditor’ used in the Rules? Is it different from what defined under Companies Act, 2013?

The term “*auditor*” is defined under Rule 2(1)(d) of the Rules as follows:

— (1) In these rules, **unless the context otherwise requires,**—

"(d) “auditor” means an individual or a firm including a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008 (6 of 2009) or any other Act for

the time being in force, who has been appointed as an auditor of a company or a body corporate under section 139 of the Act or under any other Act for the time being in force;"

From the aforesaid definition, it is clear that the auditor has to be a person who has been appointed as such under Companies Act, 2013 only.

Also, NFRA from its FAQs has clarified that the requirement of filing NFRA -1 form shall be applicable only to those foreign companies under Rule 3(1)(e) which has its business in India.

In terms of the said Rules and NFRA clarifications we can say that the auditors appointed by the foreign bodies corporate as per laws prevailing in the host countries are not covered under the aforesaid Rules.

Professional and other misconduct

27. What is meaning of the expression ‘professional and other misconduct’?

Explanation to the Section 132(4) of the Act draws the meaning of the expression ‘professional and other misconduct’ from section 22 of the Chartered Accountants Act, 1949.

It states that it shall deem to include any act or omission provided in any of the Schedules of such Act, but nothing in this Section shall be construed to limit or abridge in any way the power conferred or duty cast on the Director (Discipline) under section 21(1) to inquire into the conduct of any member of the Institute under any other circumstances.

28. What are the powers of NFRA in case of professional and other misconduct committed by any member of firm of chartered accountants?

If professional/other misconduct is proved, NFRA can -

- a. Impose penalty of not less than Rs. 1 lakhs in case of individuals & not less than Rs 5 lakhs in case of firms;
- b. Debar member/firm from engaging from practice as member of Institute for a minimum period of 6 months or for such higher period not exceeding 10 years as it may decide

29. Can the order of NFRA w.r.t professional and other misconduct be appealed?

Yes, in terms of section 132(5) of the Act, any person aggrieved by the order of the NFRA may prefer an appeal before the Appellate Tribunal in such manner and on the payment of such fee as may be prescribed.

Other reading materials on the same topic:

1. Article on 'NFRA to now regulate audit and auditors of vulnerable entities' can be viewed [here](#)
2. Article on 'MCA notifies NFRA Rules' can be viewed [here](#)
3. Our other articles on various topics can be read at: <http://vinodkothari.com/>

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