



GOVERNANCE TRANSFORMATION IN INDIA: A CRITICAL APPRAISAL OF THE COMPANIES (ACCOUNTS) AMENDMENT RULES, 2025

Mr. Lakshmipathi S. and Mr. Mahesh Naik

Department of commerce and Management. Administrative Management College

ABSTRACT

Corporate governance is related to the direction and control of a company to ensure that the company operates ethically and accounts for its actions. This article basically analyses Companies (Accounts) Second Amendment Act, 2025 in terms of its strong and positive impact about corporate governance for companies under the Companies Act, 2013 arising out of The Companies (Accounts) Second Amendment Rules, 2025 and also the weakness and challenges arising out of the said amendment. The Companies (Accounts) Second Amendment Rules, 2025 have brought about many amendments in the accounting areas, related especially to digital accounting compliance, digital ledger reconciliation statement, enhanced directors' responsibility statements, more CSR disclosures requirements, MSME disclosures and forms AOC-1 and AOC-2. Under the Companies Act, 2013, this amendment has brought the country at par with the very few countries of the world which mandate digital audit trail reconciliation. The CSR disclosure norms have now become the most transparent globally. However, this amendment also suffers from many challenges arising out of lack of standard formats, auditors' confusion due to many requirements, technical readiness gap because of many countries using outdated version of Tally, QuickBooks, Busy etc., impact of heavy cost on companies and also the implications of cybersecurity.



KEYWORDS: Corporate governance, Amendment, Positive impact, corporate governance, Weakness and Challenges, Digital, CSR, MSME, Audit trail, etc.

1. INTRODUCTION

Corporate governance is the system of rules, processes and principles that directs and controls a company, ensuring that it operates ethically, and accounts for its actions. The Companies Act, 2013, through its various provisions related, inter alia, to accounts (Sections 128 to 138 of the Act) of the corporate organisations governed by the Act, has always been trying to make corporate governance better and better. The Companies (Accounts) Second Amendment Rules, 2025 notified the amendment in the rules in the month of October 2025. The key amendment introduced in the rules relate to digital accounting system compliance, digital ledger reconciliation statement, Directors' responsibility

Statement, CSR related disclosures, MSME disclosures, and amendment to the forms AOC-1 and AOC-2. These amendments in the rules of accounting of the companies governed by the Companies Act, 2013 are expected to have a far-reaching impact on the corporate governance basically through a higher level of disclosures. This article analyses the amendments in details, their positive impacts on the corporate governance accompanied by the challenges and shortcomings therein.

2. OBJECTIVE OF THE STUDY

The following are the main objectives of the study:

- 2.1. To analyse each of the amendments in the said amendment rules in detail along with the positive impact of the same on the corporate governance; and
- 2.2. To highlight the shortcomings, weaknesses, and challenges arising out of the said amendments from the point of view of the undesired impact on corporate governance.

3. RESEARCH METHODOLOGY

The research methodology adopted in this article is "Analytical/Critical Doctrinal Research". The reason is that it involves the Companies (Accounts) Second Amendment Rules, 2025 under the Companies Act, 2013 and the critical analysis thereof in the form of pointing out the positive points/strengths and also the shortcomings/weaknesses thereof.

4. Analysis of the amendments in the Companies (Accounts) Second Amendment Rules, 2025

4.1. Digital Accounting System Compliance The intended rule 8(xa) reads as under:

"Digital Accounting System Compliance:

The Board's Report shall include a statement confirming whether the company has maintained its books of account using a digital accounting system with audit trails enabled, and whether any part of the accounting or financial reporting process has been undertaken outside such system.

Where any such process has been undertaken outside the primary accounting software, the nature of such process, reasons therefor, and internal control measures implemented shall be disclosed."

Analysis: This amendment mandates the disclosures on digital audit trails, digital accounting system, and off-system accounting processes. The following may be stated as the positive points of this amendment:

- a) **Reduction in the risk of fraud:** This amendment eliminates or discourages the off-line manipulations and supports transparent and traceable accounting.
- b) **Alignment with global digital audit standards:** This is similar to US SOX audit trail controls and matches OECD's anti-base erosion transparency requirements.
- c) **Supporting automation and compliance system:** This amendment also encourages the companies to adopt ERP systems and reduce manual errors.
- d) **Improvement in board-level oversight:** The directors must certify audit trails and this definitely raises accountability.

Though the above matters are going to have the positive impacts, yet the following might be quoted as the genuine concerns arising out of the amendment:

- **MSME and small companies to face capability challenges:** The smaller companies may not have ERP systems and hence, the compliance cost may be very high for them.
- **Lack of clarity on primary accounting system:** It is quite possible that the companies using hybrid systems (Tally+ Excel+ Custom Billing) might struggle.

- Possible overreach on data residency: The requirement that the accounting data should be stored in India may be conflicting with cloud service design

Digital Ledger Reconciliation Statement The intended rule 8A reads as under:

“Digital Reconciliation Statement

- (1) Every company shall prepare a Digital Ledger Reconciliation Statement for the financial year reconciling the records maintained in the primary accounting software with the records maintained in any external system including billing software, inventory management systems, payroll systems or spreadsheets.
- (2) Such statement shall include details of variances, adjustment entries, reasons for discrepancies and the internal controls implemented for ensuring integrity of financial data.
- (3) The Digital Ledger Reconciliation Statement shall be approved by the Board of Directors and shall form part of the financial reporting documentation.”

Analysis: Positive points: This amendment ensures end-to-end data integrity. This also addresses a major corporate governance problem in the form of multiple software systems creating untraceable differences. This amendment also helps the auditors and regulators in detecting fictitious sales, manual back-dated inventory entries, payroll leakages and GST mismatches.

However, the following challenges arising out of this amendment can also not be overlooked:

- a) **Reconciliation efforts to be very heavy:** Some companies use 5 to 10 inter-connected systems. Hence, reconciling them each year may require huge manpower and consultancy costs.
- b) **No uniform DLRS system provided by the amendment:** This may lead to inconsistent practices.
- c) **Overlapping risks with the statutory audit:** This amendment might lead to the duplication of effort

with the CARO (the Companies Auditors’ Report Order) requirements.

4.2. Directors’ Responsibility Statement

The intended amendment to rule 9 by way of insertion reads as under:

“The Directors shall further certify that the books of account have been maintained in a digital accounting system with audit trails enabled and preserved, that no entry has been deleted or altered without generating a digital trail, and that the financial information has been reconciled with the digital logs for the relevant period.”

The following may be quoted as the positive points of this amendment:

Strong governance signal: Directors are now required to personally affirm digital system compliance. This really ensures discipline.

Better auditor-director alignment: When the auditors check audit trails, the directors acknowledge the same.

However, this amendment also suffers from the following risks:

- a) **Increase in the liability exposure of directors:** All the directors need not necessarily have the technical knowledge of the ERP systems. Therefore, certification from them is expected to be mechanical.
- b) **Conflict with I.T. and cloud architecture:** The directors have been made responsible for the issues which are beyond their control.

4.3. Amendment to CSR related disclosures

The amendment to rule 8(1) reads as under:

“The existing CSR disclosure table shall be substituted with the following, namely: —

A revised format requiring disclosure of:

- a) CSR projects completed, ongoing and discontinued;
- b) unspent CSR amount relating to ongoing projects and other than ongoing projects;
- c) reasons for shortfall in CSR spending;
- d) details of implementing agencies including CSR Registration Number;
- e) summary of impact assessment reports, where applicable.”

Analysis: The following are the positive points of this amendment:

- a) **Addressing misuse of CSR funds:** The more detailed disclosures about the ongoing, completed and discontinued projects might reduce ambiguity.
- b) **Significant increase in transparency:** This amendment requires to state the reasons for CSR underspending and thereby ensures that CSR is not merely a compliance tick-box.

However, this amendment also suffers from the following shortcomings:

Heavy compliance: CSR tables have become highly detailed and many companies lack capacity to maintain project level data.

Indirect litigation risk: The more the disclosures, the greater is the potential for scrutiny by the NGOs and civil society.

No clarity on the impact assessment summaries: It is unclear whether the summaries should include metrics or narrative.

4.4. MSME disclosures

“In rule 8, after the CSR clause, the following shall be inserted:

(xx) MSME Payments Disclosure-The company shall disclose the ageing schedule of amounts due to Micro and Small Enterprises as per the categories specified, the interest payable and paid under the Micro, Small and Medium Enterprises Development Act, 2006, the status of receipt of MSME declarations from vendors, and the reconciliation of MSME classification as at the end of the financial year.”

Analysis: The following may be quoted as the positive points of this amendment:

- a) **Perfect alignment with section 43B(h) of the Income Tax Act, 1961:** The tax disallowance for delayed MSME payments starts FY 2024–25. The amendment by the MCA also enforces parallel accounting transparency.
- b) **Ageing schedule to promote discipline:** The companies must segregate dues across time-bands and thereby forcing liquidity planning.
- c) **Strengthening of MSME protection:** This amendment brings out systemic delay problems. However, this amendment also suffers from the following drawbacks:
 - Ambiguities in vendor classification:** Many companies do not receive MSME declaration. Hence, the amendment does not address the root cause of the problem.
 - Risk of wrongful classification of MSME:** In this case, it may lead to incorrect disclosures ultimately resulting into penalties.
 - Cash flow pressures on companies:** The mandatory timely payments could strain the capital- intensive industries.

4.5. Amendment of Forms

The amendment of forms reads as under:

a) Amendment to Form AOC-1

In Form AOC-1, after the table relating to subsidiary companies, the following shall be inserted:

(g) Status of digital accounting system compliance of the subsidiary/associate/joint venture, including availability of audit trail and reconciliation of digital logs.

b) Amendment to Form AOC-2 In Form AOC-2, under the heading “Details of Related Party Transactions”, —

c) Details of transactions undertaken through digital platforms, netting arrangements, or transactions lacking digital timestamps along with reasons therefor.”

Analysis: The benefits of this amendment are there in the form of bringing the subsidiaries and related party transactions under digital compliance umbrella and also the reduction of related party manipulation risks. However, the issues arising out of this amendment are that many foreign subsidiaries do not use Indian style audit trail systems and hence, the compliance may be hard for multi-country groups.

5. CONCLUSION

The overall analysis of the amendments definitely indicates that India has become now one of the few countries of the world which mandate digital audit trail reconciliation. Also, the CSR disclosure norms become the most transparent globally. However, there are some areas where the risks still remain. The risks are that there is no clear integration with IFRS audit trail frameworks. Besides, there is no harmonisation with GST e-invoice and Income-Tax Act data retention policies. The following might be quoted as the implementation challenges arising out of this amendment:

(a) **Lack of standard formats:** Companies may interpret the requirements themselves which might certainly lead to inconsistencies.

(b) **Auditor confusion:** The auditors may also become confused with so many requirements in respect of their audit function.

6. (c) **Technical readiness gap:** Many countries use outdated versions of Tally, QuickBooks, Busy etc.

(c) **Impact of cost:** The heavy cost impact is alarming from the ERP upgrades, staff training and external audit costs.

(d) **Implications of cybersecurity:** The more the digital data, the higher the risk of cyberattack.

Based on the above detailed analysis, it may therefore be concluded that though this amendment is strong towards digital compliance, enhancing transparency, auditability, MSME protection and aligning the country with modern corporate accountability norms, yet it suffers from shortcomings in the form of heavy compliance burden for small and medium-sized companies, lack of detailed MCA guidance causing practical difficulties, increased director responsibility without the corresponding safe harbours and potential conflict with the cloud data residency requirements.

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