



VOLUME 59 | No. 6 | DECEMBER 2010 | ₹ 100

SET UP BY AN ACT OF PARLIAMENT

# THE CHARTERED ACCOUNTANT JOURNAL

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA



VOLUME 59 | No. 6 | DECEMBER 2010

THE CHARTERED ACCOUNTANT

₹ 100

## Forward March of the Profession

The faith that the legislators put in accountancy profession more than 61 years ago while passing the Chartered Accountants Act 1949 and granting autonomy, has, in return, paid rich dividends to the country ever since, and the phenomenon continues to this day. The story of accountancy profession in India has been a story of professional panache and perseverance wherein it took all trials and tribulations in stride to convert challenges into opportunities and emerge victorious. As such, over the last more than 61 years the CA profession has undergone a paradigm shift. The ICAI's persistent pursuit of perfection, skills and knowledge has placed the Chartered Accountant in an exalted position in present professional order of the country. Much of the credit goes to ICAI's central council, which recently met for a record 300<sup>th</sup> time (since 1<sup>st</sup> July, 1949) from 24<sup>th</sup> to 26<sup>th</sup> November this year. Having resolutely upheld a very demanding tradition of 'excellence, integrity and independence', the profession's mentor, regulator and guide i.e. the Council of The Institute of Chartered Accountants of India has made accountancy profession an integral part of India's success story.

Today, the Chartered Accountants are not only the backbone of Indian financial system but are also an 'institution of public trust' besides being 'conscience keepers of economy'. From traditional bean counters, the Chartered Accountants have now metamorphosed into a multi-dimensional professional, offering complete business solutions as 'information and decision specialists'. The role of CA has shifted from backroom to boardroom. He is no longer a statistician but a strategist.

Maintaining financial discipline in India for six decades, the profession has now also carved a distinct niche as one of the most vibrant forces of socioeconomic growth. With ever-expanding horizons of Indian economy, the accountancy profession has always been at the forefront, assuming new roles and responsibilities for nation's growth — fully justifying the CA professional's motto "*pride of service in preference to personal gain*". Today, the CA profession is not only spearheading the government accounting reforms but is also involved in the policy making processes at various levels of government. "*Chartered Accountants: Partners in National Development*" — These words of acknowledgement and recognition used by visionary former President of India Dr. A.P.J. Abdul Kalam for the Chartered Accountant fraternity amply sum up the great role, power and potential of the Accountancy profession in the country.

On its forward march to a bright future, the CA profession in India is today passing through a crucial phase of restructuring, upgradation, value addition, diversification and global integration. With accounting having become the language of global business, today's professional is no longer being seen as just a 'bean counter' but a versatile tool of modern day business. The profession is in a state of flux and Indian CA is fast evolving from traditional accounts keeper and auditor into a trusted business adviser equipped with multifarious skills. Growing from strength to strength over more than five decades both in terms of numbers and quality, the profession has truly come of age.

The rapid globalisation is fast expanding the professional horizons. The flourishing and spreading economy, wave of mergers and acquisitions, integration of India with world economy, stress on transparency and corporate governance and emergence of knowledge society have thrown up myriad of present and future opportunities for professionals be they in practice or industry. Starting with a small strength of just 1,685 as on 1<sup>st</sup> April, 1950, more than 165,000 CAs are today providing pivotal support, both behind and over the scenes, across different economic and business spheres right up to the level of CEOs and CFOs.

The accountancy profession has indeed come a long way but still there are miles to go. There are still many challenges to be met, many frontiers to be conquered. Newer and newer opportunities are emerging in the garb of challenges, particularly in domains of 'convergence with IFRS', 'e-Commerce', 'environmental accounting' 'BPO/KPO', 'arbitration', 'corporate governance', 'due diligence & valuation', 'ERP Control Design', 'ITATs', 'Internal Audit', 'Insurance and risk management', 'consultancy', 'international taxation', 'transfer pricing', 'cross border transactions', 'mergers and acquisitions', etc. The need of the hour is to have multi-disciplinary partnerships and build domain expertise and specializations because the days of generalists are getting over. Alvin Toffle has rightly said that "the illiterate of the 21<sup>st</sup> century will not be those who cannot read and write, but those who cannot learn, unlearn, and relearn". Further, the sheer pace of change makes it a big challenge for the profession in present hi-tech era of knowledge economy, liberalisation, privatisation and globalisation which has put sharper focus on role of accounting profession. Charles Darwin has rightly said that 'it is not the strongest of the species that survive, nor the most intelligent, but the one most responsive to

change'. Other key formidable challenges for the profession are 'ever-increasing expectations of the society and the so perceived utility-expectation gap', 'diversification of services beyond traditional accounting spheres', and 'attracting and retaining the highest quality of talent'.

The threat of intrusion of competing professions into CAs' traditional and specialized markets, manifold increase in stakeholder expectations, more than expected pace of changes in business and Information Technology environment, growing gulf between small and big accounting firms, increasing level of regulations, and WTO regime need to be dealt with effectively and promptly.

But these challenges are not insurmountable given the acumen and training of Indian professionals. What is needed is to make a fair assessment, envision the future challenges and opportunities in the emerging areas such as new audit and assurance needs, performance measurement services, change management services, strategy management, general practice specialisation, servicing global organisations, corporate governance, risk management, arbitration, consultancy, government accounting reforms, outsourcing etc.

And to cash in on these opportunities and come up to heightened expectations, the CAs need to sharpen their competitive edge by not only constantly updating and enriching their traditional knowledge but also by acquiring new skills, industry and technical expertise and a futuristic vision. Value-addition, diversification, networking and consolidation are a must for the profession to grow bigger and better in future.

It's time for the profession to adopt 'Vision 2021'— the year when India is likely to graduate from developing to developed economy. The CAs need to re-invent themselves and become 'total business solution providers' of the future.

Given the public trust, unique ability to fast adapt to the changes, burgeoning demand of CAs and a mammoth 600,000 students pursuing the CA course, the profession is well set on course of a very bright future, provided complacency does not creep in at any point of time. The ICAI motto "*Ya Esa Suptesu Jagariti*" (That person who is awake in those that sleep) has to be actually lived by the members in all times to come.

**Editorial Board**  
*ICAI – Partner in Nation Building*

EDITORIAL BOARD

EDITOR	CA. AMARJIT CHOPRA, President
JOINT EDITOR	CA. G. RAMASWAMY, Vice-President
MEMBERS	CA. JAYANT P. GOKHALE CA. JAYDEEP N. SHAH CA. SANJEEV MAHESHWARI CA. SHIWAJI B. ZAWARE CA. M. DEVARAJA REDDY CA. P. RAJENDRA KUMAR CA. SUMANTRA GUHA CA. SUBODH AGARWAL CA. ANUJ GOYAL CA. PANKAJ TYAGEE CA. LAXMINIWAS SHARMA CA. SUBHASH C. GOEL CA. DHARAM V. CHOPRA CA. VIMAL R. KHANNA SHRI VIJAY KAPUR NADEEM AHMED SUSANTA K. SAHU CA. NITIN JAIN Dr. N. K. RANJAN
SECRETARY	SHRI VIJAY KAPUR
ICAI EDITORIAL TEAM	NADEEM AHMED SUSANTA K. SAHU CA. NITIN JAIN Dr. N. K. RANJAN

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA  
ICAI Bhawan, Post Box No.7100, Indraprastha Marg,  
New Delhi-110002, Tel: +91 (11) 39893989.  
E-mail: icaicho@icai.org, Website: www.icaai.org

SUBSCRIPTION RATES

Inland subscribers :	₹ 1,000 per annum
Overseas :	\$ 150 per annum (subscribers by sea mail)

For Overseas Members/Subscribers

- Air Mail Surcharge : ₹ 2,100 per annum
- Sea Mail Surcharge : ₹ 1,100 per annum

CA Students	: ₹ 1,400 for 3.5 years ₹ 400 per annum
Other students & faculties	: ₹ 600 per annum

CLASSIFIEDS:

Minimum ₹ 1,000/- for the first 25 words or part thereof and ₹ 250/- for five words or part thereof over and above first twenty five words. Please contact: The Journal Section at ICAI Bhawan, A-29, Sector-62, Noida or call at +91(120) 3986955 or e-mail at eboard@icai.org

EDITORIAL SUPPORT, DESIGN, ADVERTISEMENT & MARKETING SPENTA MULTIMEDIA

Aishik Barua, Aaron Rodrigues, Nilesh Juvalekar & Ganesh Waradkar.  
**MUMBAI:** Spenta Multimedia, Peninsula Spenta, Mathuradas Mill Compound, N. M. Joshi Marg, Lower Parel, Mumbai-400013. Tel: +91 (22) 24811022/24811025, Telefax: -91(22) 24811021.  
**DELHI:** No.7, 1st Floor, Nizamuddin (West) Market, New Delhi-110013. Tel: +91 (11) 4669 9999.  
**BENGALURU:** Old No. 583, New No. 9, Sri Manjunatha Krupa, 80 Feet Road, 3rd Cross, Opp. Koramangala Police Station, Bengaluru-560095. Tel: +91(80) 4161 8966/77.  
**KOLKATA:** 206-Jodhpur Park, Kolkata - 700068. Tel: +91(33) 2473 5896. Telefax: +91(33) 2413 7973.  
**CHENNAI:** AKS Pooja Complex, 2nd Floor, Old No: 203 New No: 154, R. K. Mutt Road, Mandavelli (Next to Jagan Mohan Clinic), Chennai-600028. Tel: +91(44) 4218 8984/85.

**HYDERABAD:** H.No:8-2-684/3/R/1&2, Flat No: 304, Alankrith Apts, Gulmohar Avenue, Rd No: 12, Banjara Hills, Hyderabad. Tel.: +91 9676666691  
ICAI RESERVES THE RIGHT TO REJECT ADVERTISEMENTS  
Printed and published by Vijay Kapur on behalf of The Institute of Chartered Accountants of India (ICAI)

Editor — CA. Amarjit Chopra

Published at ICAI Bhawan, P.O. Box No. 7100, Indraprastha Marg, New Delhi - 110 002 and printed at Spenta Multimedia, Peninsula Spenta, Mathuradas Mill Compound, N. M. Joshi Marg, Lower Parel, Mumbai - 400013  
The views and opinions expressed or implied in THE CHARTERED ACCOUNTANT are those of the authors and do not necessarily reflect those of ICAI. Unsolicited articles and transparencies are sent in at the owner's risk and the publisher accepts no liability for loss or damage. Material in this publication may not be reproduced, whether in part or in whole, without the consent of ICAI.

DISCLAIMER: The ICAI is not in any way responsible for the result of any action taken on the basis of the advertisement published in the Journal. The members, however, may bear in mind the provision of the Code of Ethics while responding to the advertisements.

TOTAL CIRCULATION: 2,03,657  
Total No. of Pages: 164 including Covers  
Cover image: www.dreamstime.com  
Inside images and graphics: www.dreamstime.com



VOLUME 59 | No. 6 | DECEMBER 2010 | ₹ 100

SET UP BY AN ACT OF PARLIAMENT

# THE CHARTERED ACCOUNTANT JOURNAL

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

EDITORIAL .....	831
FROM THE PRESIDENT .....	834
INTERNATIONAL CONFERENCE	
• Accounting Profession Catalyst to Sustained Economic Growth at New Delhi.....	838
PHOTOGRAPHS .....	840
LEGAL UPDATE	
• Legal Decisions.....	844
• Circulars/Notifications.....	862
OPINION .....	866
NATIONAL UPDATE .....	959
INTERNATIONAL UPDATE .....	962
ECONOMIC UPDATE .....	964
ACCOUNTANT'S BROWSER .....	965
PRACTICE UPDATE .....	968
CABF DONORS LIST .....	970
ICAI NEWS	
• Invitation for Articles .....	971
• Expert Advisory Committee of The ICAI .....	971
• New Publication from the Auditing and Assurance Standards Board .....	972
• Empanelment Of Chartered Accountant Firms for the Year 2011-2012. ....	972
• Announcement from Committee on Management Accounting (CMA) .....	973
• Guidelines for Training of Articled Assistant Outside India .....	973
• Invitation for Faculty & Case Studies for Post Qualification Course on Information Systems Audit .....	974
• Invitation for Faculty & Case Studies for Certificate Course on Forensic Accounting & Fraud Detection using IT & CAATs .....	974
• Shifting of Some Departments/Committees to Newly Constructed Building of ICAI at Sector-62, Noida .....	978
MEF	
• Introduction to Multipurpose Empanelment Form .....	976
CLASSIFIEDS.....	979
EVENTS	
• Two Days National Conference at Guwahati .....	966
• National Conference at Ahmedabad .....	979
• Two Days National Conference on Excellence in Professional Approach at Agra .....	980
• Seminar on Social Audit at New Delhi .....	981
• National Conference on Direct Tax at New Delhi .....	981
• National Conference: CA Profession – Challenges and Opportunities at Jaipur .....	982
• National Summit on Networking and Capacity Building of CA Firms at Mumbai .....	983
• Workshop on Capacity Building Measures for CA Firms and New Professional Avenues at Baroda .....	984
• Two Days Workshop on Excellence in Service Tax at Mathura .....	984

## ACCOUNTING



- Transition to IFRS  
- CA. R.S. Raghavan **872**
- Accounting for Intangibles with Reference to IFRS  
Convergence: Some Relevant Issues  
- Dr. Pranam Dhar and Dr. Jafor Ali Akhan **878**
- IFRS – Fair Value Accounting a Non-Developed and  
Inadequate Science?  
- CA. Sanjay Tari **892**
- IFRS Adoption: Cut-Over Challenges  
- CA. Kanchan Mukherjee **896**

## TAXATION



- Special Provisions for Computing Profits and Gains of  
“Small Business” on Presumptive Basis  
- CA. Thakur Repudaman **904**
- Issues on Assessment of Charitable Trusts  
- CA.(Dr.) Tushar K. Doctor and CA. Zankhana Mehta **912**
- Provision of Section 14A read with Rule 8D  
and Recent Judicial Controversial Decisions  
- CA. Hemantkumar Salian and CA. Sheela Chitlangia **917**
- Minimum Alternate Tax - Latest Developments  
- CA. Dilip Chakraborti **925**
- New TDS Rules 2010  
- CA. Rajeev Khandelwal **928**

## CORPORATE SOCIAL RESPONSIBILITY



- Corporate Social Reporting: Evidence from Listed  
Companies in India  
- CA. (Dr.) Satyajit Dhar and Dr. Sarbani Mitra **938**

## CORPORATE AND ALLIED LAWS



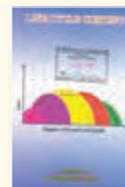
- Nominee vis-à-vis Legal Heir  
- CA. Manoj Deore **945**

## BANKING AND FINANCE



- Base Rate: A Pragmatic Shift in Banking Industry  
- CA. (Dr.) R. K. Agrawal **948**
- Foreign Investment in Real Estate  
- CA. Anup P. Shah **953**

## BOOK REVIEW



- A Useful Conceptual Analysis of Various Aspects of Life  
Cycle Costing **966**

## GENERAL

- All About Stress  
- CA. R.S. Sivaraman **986**



## BACKPAGE

Cross Word 054

Smile Please



**989**

## Dear All,

Let us begin with the words of a Scottish financial journalist, B. C. Forbes: *Without self-respect, there can be no genuine success. Success won at the cost of self-respect is not success. For what shall it profit a man, if he gains the whole world and loses his own self-respect?*

Self-respect is fundamental to all merits. It permeates all aspects of our lives. We can use it in disciplining ourselves. To us, if we want to be respected, we will have to learn first to respect ourselves, as it comes first from our own inside. Our difficulty is that we do not realise our worth and, therefore, do not consider what we lose when we simply follow others. Losing our identity is no humility. Humility lies in recognising what we are. In fact, true self-respect will make us humble. It will make us think of ourselves neither too high nor too low.

All of us have responsibility towards the society we live in. Let us realise the position of our profession and understand that we should better displease others and do what we know is right than we make others happy by doing what we realise is unjust. It is time to display courage and speak the truth, and acknowledge with zeal what the English playwright George Bernard Shaw had once said: *No man, who is occupied in doing a very difficult thing and doing it very well, ever loses his self-respect. We should respect our efforts, and, above that, ourselves.* All practitioners of accountancy profession in India must respect their root, i.e. the Institute. We must always identify with our Institute which has given all of us reasons to smile and live with respect in our life. We must add life to the Institute's standing by respecting and valuing it.

Let our profession stand tall forever with all its glory and heritage.

Now, let us get updated with some of the important proceedings and developments in the Institute in particular and accountancy profession in general over the last month:

### International Initiatives

**18<sup>th</sup> World Congress of Accountants: ICAI Call to Curb Irregularities:** The 18<sup>th</sup> World Congress of Accountants (WCOA) with the theme *Accountants: Sustaining Value Creation*, jointly organised by the IFAC and Malaysian

Institute of Accountants (MIA), addressed various accounting issues utilising a pool of about 200 internationally-known speakers from over 40 countries. Issues discussed included strengthening accounting professionals in emerging economies, integrated reporting framework and role of accountants in the future. This four-day Congress registered a record 6,050 delegates from 134 countries excluding some 1,000 students from Malaysia. The undersigned gave a comprehensive presentation on *Fighting Corruption & Money-Laundering — An Ongoing Battle for Accountants*. The presentation explained the basic understanding and causes of corruption and money-laundering while apprising the audience of the existing international initiatives to fight these evils of profession and suggesting the strategy and related role of external auditors in this regard. To us, it is a significant issue requiring immediate resolutions and that is why we will address this in our *January 2011 International Conference on Accountancy Profession* too. There is a need for IFAC to sit up and think in terms of some aspects of reporting to cover issues concerning corruption where there are such indicators. Expressing an opinion merely on true and fair view may not be only aspect which society may expect the auditors to report upon. The ICAI Vice-President CA. G. Ramaswamy spoke at length and stressed particularly on the vigilant aspect of audit profession while chairing a session on *International Auditing and Assurance Standards Board (IAASB) – A Global Perspective* in which the IAASB Chair Mr. Arnold Schilder presented a paper.

On the sidelines of this Congress, we had meetings with the New Zealand Institute of Chartered Accountants, where we were assured that there would be negotiations to finalise the MoU by February 2011. We also had meetings with CPA Australia to discuss the strategy for furthering the mutual relationships between the CPA, Australia, and the ICAI.

**Singapore Accountancy Convention: ICAI Focuses on Ethics and Governance:** We had the opportunity to attend Singapore Accountancy Convention organised by the Institute of Certified Public Accountants of Singapore recently, where the ICAI was a supporting organisation. The



undersigned delivered a session on *Ethics and Governance* and stressed that ethics have to be adhered to especially by bigger firms keeping in view of some of the recent instances of violation of ethics, while emphasising the issue of family-owned businesses. Even in family-owned businesses there has been a rise of professionalism. Responding to a question, the undersigned, however, stressed a need of ethics and corporate governance in bigger auditing firms connected herewith. The theme of the convention *A Profession on the Move* captured the dynamism and vibrance of the accounting profession and acknowledged the realities of an increasingly-globalised world. Then, the undersigned and ICAI Vice President CA. G. Ramaswamy met ICPAS President Dr. Ernest Kan to discuss the wish-list shared between the two Institutes, and had fruitful discussion on carrying forward the MoU dialogue.

### Meetings with Federal Ministers of Australia, CPA Australia and ICAA:

The undersigned along with ICAI Vice-President CA. G. Ramaswamy visited Sydney in Australia, where we met the officials of both CPA, Australia and ICAA to discuss the various aspects of the MRA already entered into. We would like to mention specially the name of Chief Executive of CPA, Australia, Mr. Alex Malley, as he was willing to share dais with us on a number of accountancy-related issues. In fact, Mr. Malley

suggested on the need for a group which may have future implications in the issues of IFRS Convergence. The undersigned also met Mr. Bill Palmer, Director Asia, ICAA, who was quite keen on conceptualisation of an accounting body for Commonwealth countries to develop a network for the benefit of global accountants. He suggested us for a membership of the International Forum of Independent Audit Regulators (IFIAR). We also discussed about sharing our respective professional opportunities and easing off of immigration rules in the interests of our members. We also had discussions with the Federal Member of Berowra Hon'ble Philip Ruddock and the Parliamentary Secretary to the Prime Minister Senator the Hon'ble Kate Lundy in a social function organised by the Indian chartered accountants and other eminent Indians in Australia. We visited and met the Senior Manager (India & UAE Desks, International Markets and Trade) from NSW Government Ms. Linda Taylor. We then met the Indian High Commissioner in Australia Ms. Sujata Singh. We are really happy to share with all of you that we were promised an unconditional support from them. The undersigned, along with the Chairman Sydney Chapter of the ICAI CA. Yateender Gupta proceeded to Canberra.

#### **Annual Toronto Chapter Programme:**

The undersigned attended the fourth Annual Programme of the Toronto Chapter of ICAI along with the ICAI Vice President CA. G. Ramaswamy. We spoke at length on CA profession in India. While pointing out to the condition of rising Indian economy, the undersigned predicted a possibility of reverse brain drain, as opportunities are on a rise on home soil. High Commissioner of India Shri Shashishekhar M. Gavia, who was present on the occasion, addressed our members of the Chapter. Mr. Steve Gupta, President & CEO, Easton's Group of Companies, delivered the keynote address. The programme got an overwhelming response.

#### **ICAI Accompanies MCA in Australia**

**Visit:** A senior delegation from the Ministry of Corporate Affairs headed by its Secretary Mr. R. Bandyopadhyay visited Sydney and Canberra in Australia recently to have in-depth discussion with senior Australian Government functionaries. The delegation consisting of representatives of ICAI, ICWAI and

ICSI met Dr. Ken Henry, Secretary of the Australian Treasury, Govt. of Australia, and they had an exchange of stance on economic policy and regulatory architecture at macro level and learning experiences and possible mutual synergies in governance, CSR, investor education, technical standards implementation, in particular roadmap to IFRS, etc., at micro level. Our Central Council colleagues CA. Vinod Jain and CA. Abhijit Bandyopadhyay, and ICAI Additional Secretary Shri Rakesh Sehgal represented ICAI in the delegation. Both the sides agreed to work together and play a leadership role in the region by adopting a joint voice in various international forums in areas of emerging paradigms. The delegation also met Financial Reporting Council Chair Mr. Jeffery Lucy and discussed corporate and standard business reporting, corporate governance and investor protection. This visit assumes importance in the wake of emerging trade scenario. Both sides agreed to leverage upon mutual synergies and regularly interact so as to jointly work on commonality of issues. Indian High Commissioner in Australia Ms. Sujata Singh also accompanied the delegation in these two meetings.

#### **Developments in Convergence with IFRS**

##### **Converged Accounting Norms-Agriculture and Banking Sectors:**

In course of our efforts of introducing accounting norms in India converged with globally-adopted International Financial Reporting Standards (IFRSs), we realised that we couldn't go ahead with the draft accounting standard for agriculture of the IFRSs due to our nation's concerns in assessing the fair value of the agricultural sector. When we decide not to announce the standards for agriculture, we should understand that it would not have any impact on our proclamation to converge our accounting standards with the IFRSs from April 2011. India is not the only one that has decided to defer the Standard on Agriculture. In agriculture, India may have diverging accounting norms or 'carve outs' as compared to the IFRSs.

##### **ICAI Proposal on Tax Implications Emanating from Convergence:**

We take this opportunity to inform that we had set up a Group consisting of nominees from the Ministry of Finance to identify tax implications emanating

from the IFRS convergence. The Group prepared a draft report identifying options to be adopted for achieving tax neutrality. The Group has met the MCA Secretary, where it was requested to submit a revenue-neutral proposal that should be acceptable to the Ministry and, at the same time, compatible with the IFRSs while meeting the requirements of corporations. The Group has decided to include only feasible and practically possible alternatives in the report to be given to the Government. The Group has authorised our Central Council colleague CA. Jayant Gokhale to discuss the possible alternatives with the officials of the Ministry and, thereafter, formalise the detailed aspects of alternatives for the final Report to be submitted to the Ministry.

#### **More Public Recognition: Tamil Nadu Street Named after ICAI**

It is a matter of pride and joy that the Sankaraperi Panchayat Union in Tamil Nadu has recently approved and sanctioned for naming a street as *ICAI Salai* (road) that houses our Tuticorin Branch of SIRC. We sincerely thank the Councillors of the Union for approving the same, and duly congratulate the Chairman of the Tuticorin Branch of SIRC, CA. H. Raman, for the recognition.

#### **ICAI Offers to Assist in Commonwealth Games Irregularities Probe**

As you might be aware, the Hon'ble Prime Minister of India has entrusted Shri V. K. Shunglu, former Comptroller and Auditor General of India, to head a high-level Committee to probe the alleged irregularities in the 2010 Commonwealth Games held in Delhi. We would like to share with you that we have sent a letter to Shri Shunglu offering our services. The response in the matter is awaited.

#### **NABARD Relents to ICAI**

We are happy to inform our members that on our continuous persuasion, the NABARD (National Bank for Agriculture and Rural Development) has agreed to delete the clause pertaining to negotiation from the policy circular regarding fixation of the fees of the auditors of State and District cooperative banks, which was to be made applicable from next year onwards. We are sure that the removal of the negotiation clause while fixing fee would ensure

more transparency and equitable distribution of work among auditors of the State and District cooperative banks. Several inhibitions like provision enabling change in auditor every year still remain in the process which we will continue to pursue with the Bank.

### ICAI Stands Tough against Fraudulence

We do not need to undergo any change post-Satyam fiasco in our system, but there is a need to process our disciplinary cases faster. Action against our members, i.e. auditors, is a reality, however the matter in some cases is sub-judice. We have made progress in cases, where stay order has not been granted. Currently, the scheme of our disciplinary mechanism does not allow us to proceed against erring firms. Therefore, we have proposed certain amendments in the Chartered Accountants Act, 1949. If amendments are approved, it will help us act against the erring firms, although in absolute exceptional circumstances. Let us understand that Satyam must never be identified as an accounting failure, rather it is a failure of all pillars of corporate governance, i.e. regulators, independent directors, shareholders and promoters. To update on the matter, the two auditors associated with the Satyam fiasco had been granted a stay order against the proceedings of our Disciplinary Committee on their petitions, but their petitions as well as the stay order were dismissed by the Hon'ble High Court of Delhi after hearing the counsels of both sides. Unfortunately in this case, only auditors' role has caught the public attention. We, of course, do not want to defend the auditors involved in that episode, which has become a case study for us to apprise our members about the significance of taking third-party confirmations. Role of independent directors of audit committee and search committee overseeing the function of companies needs to be redefined. It becomes difficult for auditors to ascertain the authenticity in the absence of confirmation, as forensic audit cannot be carried out for every audit.

### Initiatives for Members

#### 300<sup>th</sup> Meeting of ICAI Council - Some Significant Decisions:

1. Regarding the **formulation of guidelines for revival of derecognised Study Circles**, the

Council decided that a Study Circle which was earlier derecognised by the Council may be revived by the Continuing Professional Education Committee subject to the compliance with certain norms to be specified in this regard.

2. Regarding consideration of the issue regarding **recognition of fair value changes in investment property**, the Council agreed with the view of the ASB that instead of recognising the changes in fair value in investment property in profit or loss, where an entity adopts the option of measuring investment property at fair value as per the draft AS 37, *Investment Property*; the same should be recognised in other comprehensive income. The Council authorised the Chairman, Accounting Standards Board, to place the changes suggested in the Accounting Standard before NACAS. If the change is approved, it will eliminate the volatility of Profit & Loss account.
3. With a view to **ensure professional competence** of our members, the Council decided that where there has been a gap of 5 or more years between the removal of name and application for restoration of name, if the member applies for Certificate of Practice, he should undergo a specified refresher course of a duration of 30 hours in the modules to be developed by Board of Studies, either in physical form during weekends or in the online format. Alternatively, such members could attend CPE programmes and earn 30 CPE hours before the Certificate of Practice is restored/granted. The Council also decided that for the persons who have passed the Final Examination and become eligible for enrolment as a member but have not applied for membership within 5 years from the date of their becoming eligible should undergo the aforesaid refresher course for getting enrolled as a member. The same is subject to the changes in the regulations.
4. Regarding **modalities to be recommended for holding the office of Office Bearers** for the year 2011-12 and 2012-13 for those Branches where the majority of members of Managing Committee have held the office

of Chairman in the earlier years, the Council observed that holding of post of chairman of a branch again is not acceptable either from good governance point of view or from ethical point of view and therefore the Council decided that the Chairman of a Branch after demitting office should not seek re-election for or hold the post of Chairman of the said Branch in the year 2010-11 and 2012-13. However, he can hold any other post. If in the case of a Branch for the years 2011-12 and 2012-13, no member of Managing Committee is left who has not held the position of Chairman in earlier years, the Managing Committee will co-opt a member who will be the Chairman of the said Branch for the year 2011-12 or 2012-13 as the case may be.

5. To help our members carry out **assurance engagements at Service Organisations**, the Council cleared the Standard on Auditing (SAE) 3402, *Assurance Reports on Controls at a Service Organisation*, formulated by the Auditing and Assurance Standards Board.
6. The Council also decided on the development of alternative dispute resolution mechanism for dealing with the disputes. The details about this decision are elsewhere in the Journal in this issue. This decision will help in early settlement of disputes of our members as well as of students.

**Capacity Building Measures:** We have called a meeting of big Indian firms for discussing the consolidation and networking strategy how they can play a key role in building small and medium practitioners. We seek their help in capacity building exercise through making available sophisticated toolkits and other relevant research. We are of the opinion that bigger firms rather than taking over smaller firms and creating monopoly should do hand-holding exercise and improve the quality of audit profession at large.

**C&AG Ready to Reconsider Empanelment Criteria:** It is a matter of satisfaction that the office of the Comptroller and Auditor General (C&AG) of India has agreed on our request to re-consider the empanelment criteria for preparation of panel of CA

firms for conducting audit of public-sector undertakings. A group has been constituted for the purpose consisting of the undersigned, ICAI Vice President CA. G. Ramaswamy and our Central Council colleagues CA. S. B. Zaware and CA. Pankaj Jain.

**Issue of Surrogate Practices:** It is ironical for the profession in India that some well-known global accounting firms are operating their businesses in India through surrogate means, i.e. without even being registered in the country. We have raised questions on their modus operandi, as these auditing firms operate through their member-firms in India. We take a serious view of their practices being carried out in such a manner. We have approached the Government too in this regard. While auditing reports are signed on behalf of their member-firms, business is usually taken on behalf of these global parent firms. A debate has arisen how these firms can be made accountable to the disciplinary mechanism of the ICAI. We have called a meeting with our past-Presidents to seek their views on the matter.

**25<sup>th</sup> Regional Conference of WIRC:** The undersigned along with the ICAI Vice-President CA. G. Ramaswamy, attended the 25<sup>th</sup> Regional Conference organised by WIRC of the ICAI in Mumbai recently. Shri Chhagan Bhujbal, the then Deputy Chief Minister (now Cabinet Minister) of Maharashtra, was the Chief Guest at the Conference. We would like to inform that the Conference was well-organised and had a very good participation. Among others, CA. N. P. Sarda, CA. T. S. Vishwanath, CA. T. N. Manoharan and CA. M. M. Chitale also addressed the Conference. Council Members from the Western Region were also present on the occasion. We would like to offer our compliments to the Chairman of the WIRC and his team for successfully organising this Conference.

**Two-day National Conference on New Paradigms of Competitiveness:** Two-day national conference of ICAI on *New Paradigms of Competitiveness: Positioning CAs for Tomorrow's Challenges* was held recently in Bhubaneswar. The undersigned addressed the gathering on *Contemporary Issues in Auditing Special Emphasis to Reporting Compliance in the Changed Environment*. Other

distinguished speakers included our Central Council colleagues CA. Nilesh S. Vikamsey, CA. Sanjeev Maheswari, CA. S. Santhanakrishnan and CA. Sumantra Guha. Finance Minister of Orissa Shri Prafulla Chandra Ghadai was the guest of honour on the occasion. Other issues that were discussed included *Wealth Creation — A Professional Perspective*, *Direct Tax Code Bill 2010 — Changes in Conceptual Approach*, *Corporate Fraud and Forensic Audit*, etc. During the Conference, we proposed to set up a Centre for Excellence in Bhubaneswar to facilitate our about 600 members in the state, i.e. Orissa, and, in response to that Shri Ghadai immediately assured us for the land. We thank him for display of this noble intention.

**Study Material for ICAEW and CPA Australia Members:** We are really pleased to announce that the Board of Studies has released the study material for the Members of the ICAEW and CPA, Australia, who wish to seek membership of our Institute.

#### Initiatives for Students

**Common Proficiency Test:** The Council at its 300<sup>th</sup> meeting reviewed the requirement for passing the Common Proficiency Test and decided that a candidate shall have to obtain at one sitting, a minimum of 30 per cent marks (out of maximum marks specified by the Council for each Section) and a minimum of 50 per cent marks in the aggregate of all the Sections, subject to the principle of negative marking, in a manner as may be specified by the Council from time to time subject to proposed amendments in the regulations approved by the Central Government.

**Revised Final Study Material Available by January 2011:** We are really happy to inform that the Board of Studies had released the revised Final study material, which has been updated and modified. Entire study material along with Practice Manuals would be available at all our Branches by January 2011.

**Residential Course at Centre of Excellence, Hyderabad:** We are really pleased to inform that the registration for the second batch for six-week Residential Course at the Centre of Excellence, Hyderabad, has received an overwhelming response. The third batch will start from January 18, 2011.

The Board has proposed to run these batches on continuous basis. A three-month Residential Course at NIFM, Faridabad, has also been announced. However, in future, duration of residential courses at NIFM, Faridabad, will also be of six weeks instead of three months so as to bring uniformity in respect of such programmes conducted across the nation.

**International Conference of Students in Delhi:** The Board of Studies has proposed to hold an International Conference of Students in Delhi on December 28-29, 2010.

Our Past-President CA. V. Rajaraman rightly said in his address to the 300<sup>th</sup> Council Meeting: *It is a welcome sign that growth in the profession, as is witnessed, has spread to most cities and towns instead of concentrating in the state capitals and big cities only. It is bound to migrate to taluk headquarters and smaller towns. This would be necessity of the day and the only way perhaps for the profession to grow.* Then, he reminded us of the existing challenge: *Membership should be prepared for this change and it may not be a difficult task since social amenities are fast reaching the panchayat level and smaller towns.* We have always accepted and addressed the challenges that come in our way. We welcome them as we know they awaken us, strengthen our soul and make us courageous. December adds to our challenges, as we realise: time is passing by and that we have to accomplish a lot more.

December also reminds us of celebrations. On the eve of Christmas, let us take this opportunity to wish everybody— let us vow to give our heart to friends and our forgiveness to foes. Let us display our tolerance to adversaries and offer our services to clients. Let us set good examples before the young and pay respect to the old. Let us present our charity to all. Let the warmth and joy of this festival bring all of us closer than ever.

I wish all of you a Merry Christmas!



**CA. AMARJIT CHOPRA**  
President, ICAI  
November 26, 2010

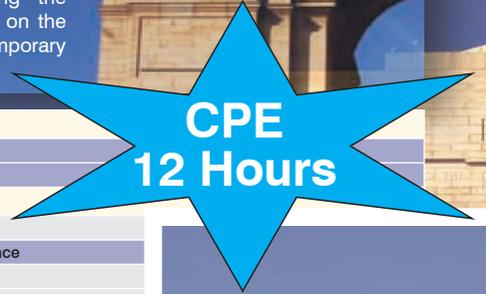
# International Conference on 'Accountancy Profession: Catalyst to Sustained Economic Growth'

4 – 6 January, 2011 at Vigyan Bhawan, New Delhi

As the world becomes 'The Global Village', the accounting profession as an integral instrumentality in the process of transition has witnessed a paradigm change in its contributory role in every sphere of the transformation. The shift in the business philosophies further emphasises on a broadened role for the accountancy professionals as strategy formulators and facilitators. While moving to such role of a value creator, the Institute of Chartered Accountants of India (ICAI) has endeavoured to imbibe the best practices model by analysing the best approach as available amongst varied corporates in different parts of

the world and has been playing the role of an enabler by getting the relevant stakeholders exposed to such best practices.

The ICAI, recognising its role and responsibilities to the stakeholder community at large is organising an International Conference on the theme 'Accountancy Profession: Catalyst to Sustained Economic Growth' on 4 – 6 January, 2011 at Vigyan Bhawan, New Delhi to dwell deeper in to emerging paradigm of Accountancy Profession and bring the Indian and global perspective together on the following broad issues that are of contemporary relevance.



## Day 1 (4<sup>th</sup> January, 2011)

INAUGURATION

DINNER

## Day 2 (5<sup>th</sup> January, 2011)

### SESSION I: Economic Resilience through Good Governance

**Key Note Address:** *Shri Vinod Rai, Comptroller & Auditor General, Govt. of India*

**Key Note Address: Financial Meltdown and Role of Accountancy Profession**  
*Mr. Ian Ball, Chief Executive, IFAC*

### SESSION II: Harmonisation of Global Standards on Accounting: Sharing Experiences

**Special Address:** *CA. Y. H. Malegam, Chair, NACAS, India*

**Session Chair:** *Mr. Dinu Hary, President, New Zealand Institute of Chartered Accountants, NZ*

**Panel Discussion**

*Mr. Bill Palmer, Director Asia, ICAA, Australia*

*Mr. Noriaki Shimazaki, Trustee, IFRS Foundation*

*Mr. Mark Spofforth, Vice-President ICAEW, UK*

*Mr. Atsu Kato, Vice Chair, Accounting Standards Board of Japan*

*Shri Prabhakar Kalvacherla, Board Member, IASB*

LUNCH BREAK

### SESSION III: Emerging Avenues for Profession

**Keynote Address: Roadmap for Goods and Service Tax – Role Chartered Accountants Can Play**

*Shri Asim Dasgupta\*, Chairman, Empowered Group of State Finance Ministers*

*Shri Sunil Mitra\*, Revenue Secretary*

**Special Address: Financial Inclusion and Social Context**

*Shri Arun Maira\*, Member, Planning Commission*

### Challenges for Accountancy Profession in Japan

*Mr. Toshio Kinoshita, CEO, Japanese Institute of Certified Public Accountants*

### Key Issues in Direct Tax Code

*Shri C. S. Kahlon\*, Member (Legislation & Computerisation), CBDT, India*

*Key Issues in International Taxation*

*Shri R. C. Vaish, International Taxation Consultant*

### SESSION IV: Emerging Contours in Financial Reporting

**Session Chairman:** *CA. G. Ramaswamy, Vice-President, ICAI, India*

**Special Address: Changing Paradigm of Governmental Accounting**

*By Shri C. R. Sundaramurti\*, Controller General of Accounts of India, Ministry of Finance*

### XBRL: Catalyst for Better Reporting

*Ms. Liv Watson, Vice-Chair XBRL International*

### Fair Value Accounting

*CA. Suresh Senapaty, ED & CFO, Wipro Technologies Ltd.*

### Implementation of IFRSs: Japanese Perspectives

*Mr. Tomoyuki Furusawa, Director, Corporate Accounting & Disclosure Division (FSA), Japan*

### Convergence with IFRS: Issues and Challenges

*CA. P. R. Ramesh, FCA*

**SPECIAL SESSION: Signing of MoU between Higher College of Technology, Ministry of Higher Education and Scientific Research, UAE and the ICAI**

**Address:** *CA. Amarjit Chopra, President, ICAI, India*

**Address:** *Dr. Tayeb Kamali, Vice Chancellor, Higher College of Technology*

Cultural Extravaganza (followed by Dinner)

## Day 3 (6<sup>th</sup> January, 2011)

### SESSION I: Landscaping Indian Chartered Accountants Globally

*CA. Gagan Gujral, Founder Secretary New York Chapter of ICAI*

*CA. Rajneesh Sapra, Chairman Toronto Chapter of ICAI*

*CA. Alok Gupta, Chairman Bahrain Chapter of ICAI*

*CA. Yateender Gupta, Chairman Sydney Chapter of ICAI*

*CA. Vikas Puri, Chairman Abu Dhabi Chapter of ICAI*

*CA. Surendra Jain, Chairman Dubai Chapter of ICAI*

*CA. Avadh Kishore, Chairman Muscat Chapter of ICAI*

*CA. Venkat Iyer, Chairman Singapore Chapter of ICAI*



**SESSION II: Bridging Expectation Gap: Post-Satyam Fiasco**

**Session Chairman:** Shri R. Bandyopadhyay\*, Secretary, Ministry of Corporate Affairs

**Panel Discussion**

CA. Amarjit Chopra, President, ICAI, India  
 Shri Siddharth Birla, Chairman, Xpro Ltd.  
 CA. T. S. Vishwanath, Past-President, ICAI, India  
 CA. T. V. Mohandas Pai\*, Executive Director, Infosys Technologies Ltd.

**LUNCH BREAK**

**SESSION III: Risk-Based Assessments – New Dimensions**

**Recent Developments in Auditing Standards**

Ms. Diana Hillier, IAASB Dy. Chair, IFAC

**Bridging Expectation Gap**

Mr. Kevin Dancey, President, CICA

**Internal Audit for Competitive Advantage**

CA. Narendra Aneja, FCA

**Beyond Risk-Based Assessment: Professional Perspectives**

Mr. Graham Meyer, CEO, ICAA, Australia

**SESSION IV: Professional Panorama**

**Leveraging Knowledge Economy for CA Profession**

Shri Raman Roy, CMD, Quattro BPO Services

**Corruption & Anti-Money Laundering**

Shri Anand Sinha\*, DG, RBI

**Cost Reduction Strategies : Role of Chartered Accountants**

Shri Kaushik Chatterjee\*, Group CFO, TATA Steel

**21<sup>st</sup> Century Accountant**

Mr. Tan Choon Seng\*, Group CEO, WBL Corporations Ltd., Singapore

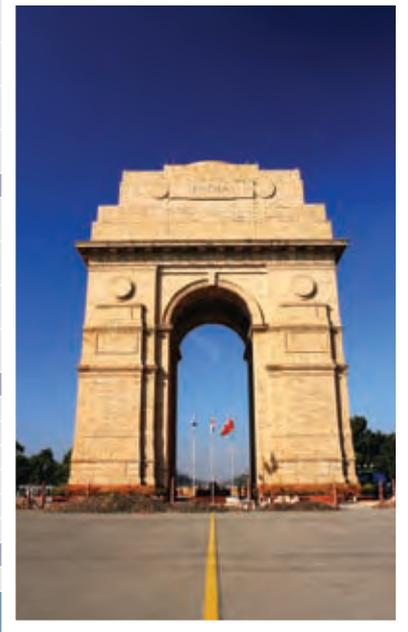
**SESSION V: Panel Discussion on Country Perspective on Governance & Ethics**

**Key Note Address:** Mr. Komal B. Chitrakar, President, SAFA

Mr. Jamal Uddin Ahmed, President, ICAB, Bangladesh  
 CA. Amarjit Chopra, President, ICAI, India  
 Shri Sunir Kumar Dhungel, President, ICAN, Nepal  
 Shri Abdul Rahim Suriya, President-ICAP, Pakistan  
 Shri Sujeewa Mudalige, President-ICA Sri Lanka

**CONCLUSION**

\* Confirmation Awaited



<b>CPE Hours</b>	<b>12 hours</b>	
<b>Delegate Fees</b>	<b>Members</b>	₹2,500
	<b>Accompanying Spouse</b>	₹2,500
	<b>Non Members</b>	₹4,000
	<b>Foreign Delegates</b>	US\$ 150
	<b>On the spot Registration</b>	<b>Members</b>
<b>How to make payment</b>	Pay online at <a href="http://www.icai.org">www.icai.org</a> or Demand Draft in favour of Secretary ICAI, International Conference 2011 A/c , Payable at New Delhi	
<b>Organizers</b>	<b>Conference Chairman</b> CA. Amarjit Chopra President, ICAI	<b>Conference Co-Chairman</b> CA. G. Ramaswamy Vice-President, ICAI
<b>For registration and other details please contact</b>	<b>Shri V. Sagar, Joint Secretary (Ph: 011-30210601)</b> <b>Shri Nitin Grover EO (Ph: 011-30110443)</b> <b>Shri Kunal Sharma EO (Ph: 011-30110542)</b> The Institute of Chartered Accountants of India ICAI Bhawan, Indraprastha Marg, New Delhi – 110 002 Fax: 011-3011 0591; E-mail: <a href="mailto:ic@icai.in">ic@icai.in</a> ; Website: <a href="http://www.icai.org">http://www.icai.org</a>	
<b>Sponsorship Opportunities</b>	<b>PLATINUM SPONSOR (₹50 Lakh)</b> <b>GOLD SPONSOR (₹25 Lakh)</b> <b>EMERALD SPONSOR (₹10 Lakh)</b> <b>SILVER SPONSOR (₹7.5 Lakh)</b> <b>PEARL SPONSOR (₹5 Lakh)</b>  <b>Other Avenues</b> Dinner (4 January, 2011) – ₹7,50,000 (1 event) Dinner + Cultural Evening (5 January, 2011) – ₹15,00,000 (1 event) Conference Lunch (3) (5-6 January, 2011) - ₹7,50,000 each Tea-Coffee Plaza (3) (5-6 January, 2011) - ₹1,50,000 each Delegate Kit - ₹15,00,000  <b>Souvenir-Advertisement</b> Back Cover Page - ₹3,00,000 Inside Front Cover Page - ₹2,00,000 Inside Back Cover Page - ₹2,00,000 Full Page Colour Advertisement - ₹1,50,000 Half Page Colour Advertisement - ₹75,000 Full Page B/W Advertisement - ₹50,000 Half Page B/W Advertisement - ₹25,000 DISPLAY STALLS - ₹50,000/Day	
<b>Attractions</b>	<b>Cultural Extravaganza</b> 5 <sup>th</sup> January, 2011	

For more details, please visit <http://www.icai.org>





300<sup>th</sup> Central Council Meeting

CA. V. Rajaraman, Past President of the ICAI addressed the 300<sup>th</sup> Central Council Meeting of the ICAI on 24<sup>th</sup> November, 2010 at New Delhi. ICAI President CA. Amarjit Chopra and ICAI Vice President CA. G. Ramaswamy greet him on the occasion in the presence of council members.



Chairman CBEC Visits ICAI

ICAI President CA. Amarjit Chopra greets Shri V. Sridhar, Chairman, Central Board of Excise & Customs (CBEC), who addressed the Central Council of the ICAI on 27<sup>th</sup> October, 2010.



MoU with Corporation Bank

Comptroller and Auditor General of India Shri Vinod Rai, Chairman & Managing Director of Corporation Bank Shri Ramnath Pradeep, Executive Director of Corporation Bank Shri Asit Pal, ICAI President CA. Amarjit Chopra and Central Council member Sanjeev Maheshwari on the occasion of signing of MoU between ICAI and Corporation Bank for liberalised loan scheme 'Corp CA' for ICAI members and CA firms on 13<sup>th</sup> October, 2010 in New Delhi.



Meeting with Madhya Pradesh Governor

ICAI Vice President CA. G Ramaswamy greets Madhya Pradesh Governor and Past President of ICAI CA. Rameshwar Thakur during a meeting in Bhopal recently.



ICAI President Visits Hisar

ICAI President CA. Amarjit Chopra during a seminar organised by Hisar branch of the ICAI on 31<sup>st</sup> October, 2010 in Hisar. Central Council members CA. Sanjay Agarwal and CA. Vinod Jain and NIRC Chairman CA. Atul Gupta were among other dignitaries present on the dias on the occasion.



ICAI President Visits Sonapat

ICAI President CA. Amarjit Chopra visited Sonapat branch of ICAI on 31<sup>st</sup> October, 2010. Central Council members CA. Sanjay Agarwal and CA. Vinod Jain, and NIRC Chairman CA. Atul Gupta were among the dignitaries present on the occasion.



Singapore Accountancy Convention 2010

ICAI President CA. Amarjit Chopra and ICAI Vice President CA. G. Ramaswamy with Dr. Ernest Kan, President, Institute of Certified Public Accountants of Singapore during Singapore Accountancy Convention 2010 on the theme 'A Profession on the Move'.

25<sup>th</sup> Regional Conference of WIRC

ICAI President CA. Amarjit Chopra and ICAI Vice President CA. G. Ramaswamy with the then Deputy Chief Minister of Maharashtra Shri Chhagan Bhujbal at the 25<sup>th</sup> Regional Conference of WIRC held on November 19, 2010 at Mumbai. Central Council member CA. Sanjeev Maheshwari and WIRC Chairman CA. Sanjeev Lalan were among those present on the occasion.



Visit to Australia

ICAI President CA. Amarjit Chopra and ICAI Vice President CA. G. Ramaswamy with Mr. Alex Malley, Chief Executive Officer, CPA Australia during their recent visit to Australia.



All India CA Conference 2010- Bhubaneswar

Minister of Finance, Orissa, Shri Prafulla Chandra Ghadai with ICAI President CA. Amarjit Chopra, Past Presidents of ICAI CA. V. Rajaraman and CA. R. Bupathy and other dignitaries at the inauguration of All India CA Conference - 2010 held at Bhubaneswar on November 13, 2010.

### Decision in 300<sup>th</sup> Meeting of Council: Regarding development of alternative dispute resolution mechanism (Arbitrator) for dealing with disputes of (i) Member vis-à-vis Member; and (ii) Member vis-à-vis Student

The Council decided:

1. In case of reconstitution of a firm, wherever form 18 duly signed by the remaining partners and the resignation letter of outgoing partner(s) is received, the office will take such reconstitution on record as per the current practice.
2. Wherever the firm is "at will" as per the deed of partnership and the retirement of a partner(s) is informed and form 18, accompanied by a certified copy of partnership deed, is submitted duly signed by the remaining/surviving partners of the firm. In such a case, the fact of such retirement will be informed to the outgoing partner(s) concerned giving a notice by recorded delivery mode of 14 days to inform the factual position. In case of no response is received, the reconstitution of the firm will be taken on record. If an objection is received, the reconstitution of the firm will not be taken on record and the firm as well as the outgoing partner(s) will be informed about the option of availing the forum of Dispute Resolution Mechanism of the Institute.
3. Wherever the firm is "at will" as per the deed of partnership and the partnership deed has vested in the Managing Partner of the firm to perform certain specified acts which includes reconstitution of firm on his own and if he, in pursuance of such authority, informs the Institute and submits form 18, accompanied by a certified copy of partnership deed, duly signed by the remaining/surviving partners of the firm, the fact of such Form 18 specifying the act will be informed to the outgoing partner(s) concerned giving a notice by recorded delivery mode of 14 days to inform the factual position. In case of no response or confirmation is received, the reconstitution of the firm will be taken on record. If objection is received, the reconstitution of the firm will still be taken on record and the aggrieved members can move the Dispute Resolution Mechanism.

LEGAL DECISIONS<sup>1</sup>

## DIRECT TAXES

**Section 12A of the Income-tax Act, 1961 - Charitable or religious trusts/ Institutions - Registration of**

*Even where trust has got its accounts audited and certificate obtained in Form No. 10B before assessment is completed, merely because such report could not be filed in course of assessment proceedings, it would not deprive a trust from getting exemption if it is otherwise entitled to it in law; omission may be rectified by filing report at a later stage before assessment is completed [Assessment Year 2006-07]*

**ITO v. Sir Kikabhai Premchand Trust, September 22, 2010 (ITAT-Mum)**

The Assessing Officer noticed that in the form of return of income, the assessee had not filed Audit Report in Form No. 10B with the return of income. According to the Assessing Officer in the absence of audit report in Form No. 10B the assessee was not eligible for exemption under Section 11 of the Act.

The Calcutta High Court in the case of *Commissioner of Income-tax v. Hardeodas Agarwalla Trust* 198 ITR 511 (Cal) had held that, even where the trust has got its accounts audited and the certificate obtained in Form No. 10B before the assessment is completed, merely because such report could not be filed in the course of the assessment proceedings, it would not deprive a trust from getting the exemption if it is otherwise entitled to it in law. The direction that the audit report should accompany the return is not mandatory as the omission to do it may be rectified by filing the report at a later stage before the assessment is completed.

The Mumbai Bench of Tribunal held that in the instant case along with return of income the assessee had filed report of auditor which was required to be given under the Bombay Public Trust Act, 1950. The said report of the auditor clearly mentioned that the assessee maintained profit and loss accounts and also disclosed receipts and disbursement correctly. This report had been filed along with return of income. In these circumstances the report in Form No.10B would not have been obtained by the assessee.

The plea of bonafide omission to file Form No.10B along with return of income deserved to be accepted. There was no reason why the affidavit of the CA filed in this regard should be rejected. The Assessing Officer even after the affidavit was filed, did not choose to controvert the allegations in the affidavit of the CA regarding the correct answer given by him. He had also not chosen to cross examine him. The reason assigned by the AO for not accepting the affidavit of the CA by the Assessing Officer was that there was no explanation why the report was not filed along with the return of income. The plea that it was omitted to be filed due to oversight was totally ignored by the Assessing Officer. Therefore, the plea of the assessee in this regard was to be accepted and it was to be held that the assessee had complied with the provisions of Section 12A(1)(b). Resultantly, the assessee was entitled to exemption under Section 11.

**Section 28(i) of the Income-tax Act, 1961 - Business and professional income – Chargeable as Mittal Court Premises v. ITO, July 17, 2009 (BOM)**

Where after purchasing flats from members of commercial housing society, the transferees were admitted as members of the society and flats were entered in their names only after the impugned payments of transfer fees were made to the assessee society and it was also found that the amounts were paid in excess of the Government Notification, the amount paid as transfer fees would be exigible to the tax.

**Section 80HHC of the Income-tax Act, 1961 - Deductions - Profits from Export Business**

*For purpose of computation of deduction under Section 80HHC, 90 per cent of recovery of freight, insurance and packing receipts, sales tax set off/refund and service income are to be excluded from profits of business within meaning of clause (baa) of explanation to Section 80HHC [Assessment Year 2002-03]*

**CIT v. Dresser Rand India Pvt. Ltd, April 8, 2010 (BOM)**

The controversy which was raised before the Supreme Court in *CIT v. K. Ravindranathan Nair* (2007) 295 ITR 228 did as a matter of fact require a determination of the nature of the receipts of a similar nature which are liable to be excluded under *Explanation* (baa) though they constitute a part of the profits of business. The Supreme Court has in several observations clearly held that processing charges which formed part of the gross total income constitute independent income like rent, commission and brokerage and that therefore 90 per cent of the sum had to be reduced from the gross total income to arrive at business profits. Having said this, the Supreme Court held that processing charges were includible in the total turnover as well in the formula prescribed by sub section (3) of Section 80HHC. Consequently, the principles laid down by the Supreme Court in *Ravindranathan Nair's* case constitute the ratio of the judgment which would bind this Court.

In *Ravindranathan Nair's* case (*Supra*) the Supreme Court has now categorically held that independent incomes like rent, commission, brokerage etc. though they formed a part of the gross total income have to be reduced by 90 per cent as contemplated in *Explanation* (baa) in order to arrive at business profits. The rationale for this which is indicated in the judgment of the Supreme Court is that profit incentives and items which constitute independent incomes have no element of export turnover and are consequently liable to be excluded to the extent that is stipulated in *Explanation* (baa).

The legislative policy underlying the provision is that items which are unrelatable to the export activity must be excluded in the computation of business profits in order to prevent a distortion in the computation of the deduction under Section 80HHC.

**Section 119 of the Income-tax Act, 1961 - Central Board of Direct Taxes - Directions to subordinate authorities**

*Where statutory auditors for multi state co-operative bank*

<sup>1</sup> Readers are invited to send their comments on the selection of cases and their utility at [ebboard@icai.org](mailto:ebboard@icai.org).

*were appointed by Central Registrar of Co-operational Societies on 3-9-2001 and said statutory auditors completed audit on 15-11-2001 while tax auditors completed audit on 28-11-2001, as a result of which, there was a delay in filing return, bank cannot be blamed for delay [Assessment Year 2001-02]*

**Bombay Mercantile Co-op Bank Ltd. v. Central Board of Direct Taxes, September 20, 2010 (BOM)**

The Petitioner is a Multi State Cooperative Bank operating under the Multi State Cooperative Society Act, 1984. The power to appoint the statutory auditors is that of the Central Registrar, who is the Registrar of the Co operative Societies, Maharashtra State. The said authority had appointed the statutory auditors on 3-9-2001. It appears that the said authority appointed Chartered Accountants to be statutory auditors in place of the Departmental Auditors. This change was made in respect of all the societies. The said statutory auditors completed the audit on 15-11-2001 and the tax auditors completed the audit on 28-11-2001 and, therefore, there was a delay in filing the return.

The Bombay High Court held that the petitioner cannot be blamed for the delay in carrying out its audit, as the same was beyond its control.

It was further held that though the departmental auditors might have started the audit in the year 2000, it appeared that pursuant to the policy decision, the departmental auditors were replaced by the Chartered Accountants to be the statutory auditors, by the letter dated 3-9-2001. Therefore, the reason mentioned by the bank in its application for the delay, deserves to be accepted.

**Section 133A of the Income-tax Act, 1961 - Survey**

*Though an admission is extremely important piece of evidence, it cannot be said to be conclusive and it is open to person who has made admission to show that it is incorrect [Assessment Year 2005-06]*

**CIT v. Dhingra Metal Works, October 4, 2010 (DEL)**

Section 133A does not mandate that any statement recorded would have evidentiary value. For a statement to have evidentiary value, the survey officer should have been authorised to administer oath and to record sworn statement. This would also be apparent from Section 132(4). While Section 132(4) specifically authorises an officer to examine a person on oath, Section 133A does not permit the same.

The word 'may' used in Section 133A(3)(iii) of the Act clarifies beyond doubt that the material collected and the statement recorded during the survey is not a conclusive piece of evidence by itself. In any event, it is settled law that though an admission is extremely important piece of evidence, it cannot be said to be conclusive and it is open to the person who has made the admission to show that it is incorrect.

During the course of survey, the tax officials noticed some discrepancies in stock and cash in hand. The partner of assessee-firm stated that he could not explain this difference at the moment and, therefore, to buy peace of mind offered additional income of ₹43 lakh. Subsequently, the assessee-firm contended that the statement about stock was incorrect and that the impugned discrepancy had

been reconciled as it was only a mistake. Consequently, the assessee withdrew the offer of additional income for taxation on account of excess stock.

The Delhi High Court held that the assessee had been able to explain the discrepancy in the stock found during the course of survey by production of relevant record including the excise register of its associate company. Therefore, the Assessing Officer could not have made the addition solely on the basis of the statement made on behalf of the respondent-assessee during the course of survey.

**Section 147 of the Income-tax Act, 1961 – Income escaping assessment**

*If after issuing, a notice under Section 148, Assessing Officer accept contention of assessee and holds that income about which he has initially formed a reason to believe had escaped assessment, has as a matter of fact not escaped assessment, it is not open to him, independently, to assess some other income; if he intends to do so, a fresh notice under Section 148 would be necessary, legality of which would be tested in event of a challenge by assessee [Assessment Years 1994-95 and 1995-96]*

**CIT v. Jet Airways (I) Limited, April 12, 2010 (BOM)**

Upon the formation of a reason, to believe under Section 147 and following the issuance of a notice under Section 148, the Assessing Officer has the power to assess or reassess the income which he has reason to believe had escape assessment, and also any other income chargeable to tax. The words "and also" cannot be ignored. The interpretation which the Court places on the provision should not result in diluting the effect of these words or rendering any part of the language used by Parliament otiose. Parliament having used the words "assess or reassess such income and also any other income chargeable to tax which has escaped assessment", the words "and also" cannot be read as being in the alternative.

Evidently, what Parliament intends by use of the words "and also" is that the Assessing Officer, upon the formation of a reason to believe under Section 147 and the issuance of a notice under Section 148(2) must assess or reassess (i) 'such income' and also (ii) any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this Section. The words 'such income' refer to the income chargeable to tax which has escaped assessment and in respect of which the Assessing Officer has formed a reason to believe that it has escaped assessment. Hence, the language which has been used by Parliament is indicative of the position that the assessment or reassessment must be in respect of the income in respect of which he has formed a reason to believe that it has escaped assessment and also in respect of any other income which comes to his notice subsequently during the course of the proceedings as having escaped assessment. If the income, the escapement of which was the basis of the formation of the reason to believe is not assessed or reassessed, it would not be open to the Assessing Officer to independently assess that income which comes to his notice subsequently only in the course of the proceedings under the Section as having

escaped assessment. If upon the issuance of a notice under Section 148(2), the Assessing Officer accepts the objections of the assessee and does not assess or reassess the income, which was the basis of the notice, it would not be open to him to assess income under some other issue independently. Parliament while enacted the provisions of Section 147 with effect from 1<sup>st</sup> April, 1989 clearly stipulated that the Assessing Officer has to reassess the income of the assessee which he had reason to believe had escaped assessment and also any other income chargeable to tax which came to his notice during the proceedings. In the absence of the assessment or reassessment of the former, he cannot independently assess the latter.

*Explanation 3* to Section 147 lifts the embargo, which was inserted by judicial interpretation, on the making of an assessment or reassessment on grounds other than those on the basis of which a notice was issued under Section 148 setting out the reasons for the belief that income had escaped assessment. Those judicial decisions had held that when the assessment was fought to be reopened on the ground that income had escaped assessment on a certain issue, the Assessing Officer could not make an assessment or reassessment on another issue which came to his notice during the proceedings. This interpretation will no longer hold the field after the insertion of *Explanation 3* by the Finance (No.2) Act, 2009. However, *Explanation 3* does not and cannot override the necessity of fulfilling the conditions set out in the substantive part of Section 147. An *Explanation* to a statutory provision is intended to explain to content and cannot be construed to override it or render the substance and core nugatory. Section 147 has this effect that the Assessing Officer has to assess or reassess the income (such income) which escaped assessment and which was the basis of the formation of belief and if he does so, he can also assess or reassess any other income which has escaped assessment and which comes to his notice during

the course of the proceeding. However, if after issuing, a notice under Section 148, he accepted the contention of the assessee and holds that the income which he has initially formed a reason to believe had escaped assessment, has as a matter of fact not escaped assessment, it is not open to him independently to assess some other income. If he intends to do so, a fresh notice under Section 148 would be necessary, the legality of which would be tested in the event of a challenge by the assessee.

Section 147(1) as it stands postulates that upon the formation of a reason to believe, that income chargeable to tax has escaped assessment for any assessment year, the Assessing Officer may as an assessor reassess such income "and also" any other income chargeable to tax which comes to his notice subsequently during the proceedings as having escaped.

#### **Section 194H of the Income-tax Act, 1961 - Deduction of tax at source - Commission or brokerage**

*It would be futile for any mobile service provider to contend that charges received for supply of SIM Cards and Recharge coupons are not amount for services rendered but for sale of goods [Assessment Years 2004-05 to 2007-08]*

#### **Vodafone Essar Cellular Limited v. Asstt. CIT, August 17, 2010 (KER)**

The assessee a mobile cellular phone operator took the stand that the supply of Sim Card, Recharge coupons etc. to the distributors under the prepaid scheme is sale of goods at discounted price by the assessee. Besides the discount given at the time of sale of these items, assessee is not paying any commission or crediting any commission in the account of the distributors and so much so, assessee is not liable to deduct and remit tax at source in terms of Section 194H. However, the Assessing Officer held that there is no difference between the services rendered by the distributor under the "post paid" and under the "prepaid" schemes and



so much so, he found that assessee was liable to recover and pay tax on the commission paid, though styled as discount by the assessee in the agreements with distributors. Since the assessee committed default in deduction of tax at source and remittance of the same on the commission paid under the prepaid scheme to the distributors, the Assessing Officer treated the assessee as an assessee in default and demanded tax in terms of Section 201(1).

The Kerala High Court held that a customer can have access to mobile phone service only by inserting Sim Card in his hand set (mobile phone) and on assessee activating it. Besides getting connection to the mobile network, the Sim Card has no value or use for the subscriber. In other words, Sim Card is what links the mobile subscriber to the assessee's network. Therefore, supply of Sim Card, whether it is treated as sale by the assessee or not, is only for the purpose of rendering continued services by the assessee to the subscriber of the mobile phone. Besides the purpose of retaining a mobile phone connection with a service provider, the subscriber has no use or value for the Sim Card purchased by him from assessee's distributor. The position is same so far as Recharge coupons or E Top-ups are concerned which are only air time charges collected from the subscribers in advance. There is no sale of any goods involved as claimed by the assessee and the entire charges collected by the assessee at the time of delivery of Sim Cards or Recharge coupons is only for rendering services to ultimate subscribers and the distributor is only the middleman arranging customers or subscribers for the assessee. The terms of distribution agreement clearly indicate that it is for the distributor to enroll the subscribers with proper identification and documentation which responsibility is entrusted by the assessee on the distributors under the agreement. It is pertinent to note that besides the discount given at the time of supply of Sim Cards and Recharge coupons, the assessee is not paying any amount to the distributors for the services rendered by them like getting the subscribers identified, doing the documentation work and enrolling them as mobile subscribers to the service provider namely, the assessee. Even though the assessee has contended that the relationship between the assessee and the distributors is principal to principal basis, this contention could be accepted because the role of the distributors as explained above is that of a middleman between the service provider namely, the assessee, and the consumers. The essence of a contract of agency is the agent's authority to commit the principal. In this case the distributors actually canvass business for the assessee, and only through distributors and retailers appointed by them, assessee gets subscribers for the mobile service. Assessee renders services to the subscribers based on contracts entered into between distributors and subscribers. The distributor is only rendering services to the assessee and the distributor commits the assessee to the subscribers to whom assessee is accountable under the service contract which is the subscriber connection arranged by the distributor for the assessee. The terminology used by the assessee for the payment to the distributors is immaterial and in substance the discount given at the time of sale of

Sim Cards or Recharge coupons by the assessee to the distributors is a payment received or receivable by the distributor for the services to be rendered to the assessee and so much so, it falls within the definition of commission or brokerage under *Explanation* (i) of Section 194H.

*Explanation* (i) of Section 194H is applicable or not is to see whether assessee has made any payment and if so, whether it is for services rendered by the payee to the assessee. In this case there can be no dispute that discount is nothing but a margin given by the assessee to the distributor at the time of delivery of Sim Cards or Recharge coupons against advance payment made by the distributor. The distributor undoubtedly charges over and above what is paid to the assessee and the only limitation is that the distributor cannot charge anything more than the MRP shown in the product namely, Sim Card or Recharge coupon. Distributor directly or indirectly gets customers for the assessee and Sim Cards are only used for giving connection to the customers procured by the distributor for the assessee. The assessee is accountable to the subscribers for failure to render prompt services pursuant to connections given by the distributor for the assessee. Therefore, the distributor acts on behalf of the assessee for procuring and retaining customers and, therefore, the discount given is nothing but commission within the meaning of *Explanation* (i) on which tax is deductible under Section 194H of the Act. The contention of the assessee that discount is not paid by the assessee to the distributor but is reduced from the price and so much so, deduction under Section 194H is not possible also does not apply because it was the duty of the assessee to deduct tax at source at the time of passing on the discount benefit to the distributors and the assessee could have given discount net of the tax amount or given full discount and recovered tax amount thereon from the distributors to remit the same in terms of Section 194H of the Act. Therefore, it cannot be said that recovery of tax is not permissible at the time of giving discount on the delivery of products to the distributors.

The mobile service providers are exonerated from sales tax liability and are liable to pay service tax to the Central Government under the Finance Act, 1994. It would be futile for any mobile service provider, to contend that the charges received for supply of Sim Cards and Recharge coupons are not for services rendered but amounts to sale of goods on which admittedly assessee is not paying any sales tax to the State Government.

#### **Section 234B of the Income-tax Act, 1961 - Interest - For defaults in payment of Advance tax**

*If person (payer) who had to make payments to non-resident, had defaulted in deducting tax at source from such payments, non-resident is liable to pay tax; however, question of payment of advance tax and, thus, interest under Section 234B would not arise [Assessment Year 2001-02]*

#### **Director of Income-tax v. Jacobs Civil Incorporated, August 30, 2010 (DEL)**

The assessee, a US company executed a project undertaken by the National Highway Authority of India. The

Assessing Officer found that there was short payment of taxes inasmuch as the advance tax was not paid by the assessee on due dates and therefore, the Assessing Officer was of the opinion that the assessee had incurred interest liability under Section 234B. The plea of the assessee was that, it was the obligation and the statutory duty of the National Highway Authority of India to deduct the tax at source and the assessee being a non-resident had no liability to pay any advance tax and thus interest under Section 234B.

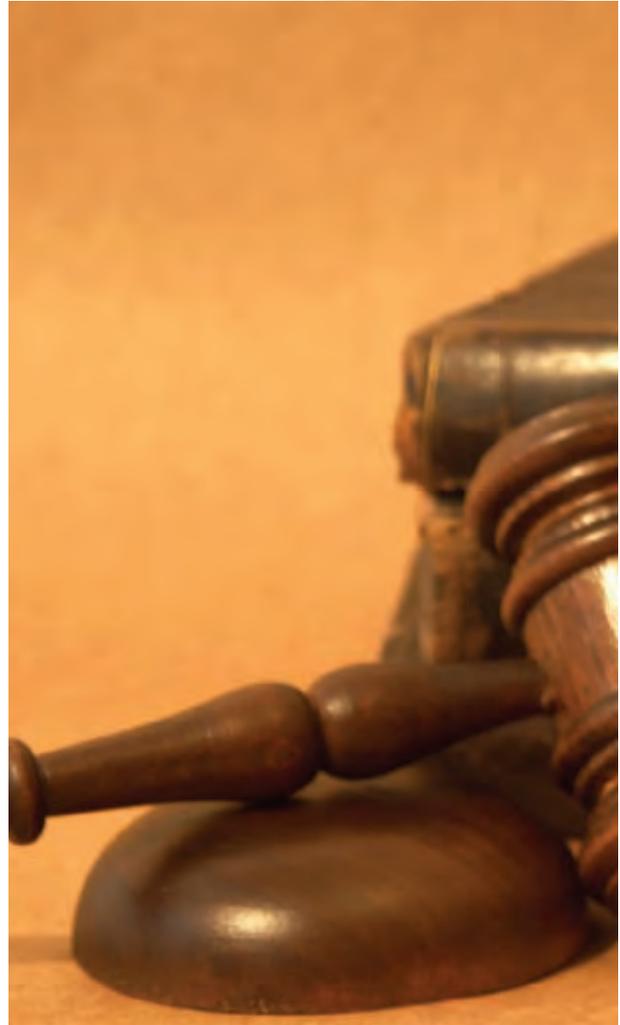
The Delhi High Court held that the scheme of the Act in respect of non-residents is clear. Section 195 puts an obligation on the payer, i.e., any person responsible for paying to a non-resident, to deduct income tax at source at the rates in force from such payments excluding those incomes which are chargeable under the head "Salaries". Therefore, the entire tax is to be deducted at source which is payable on such payments made by the payee to the non-resident. Section 201 of the Act lays down the consequences of failure to deduct or pay. These consequences include not only the liability to pay the amount which such a person was required to deduct at source from the payments made to a non-resident but also penalties etc. Once it is found that the liability was that of the payer and the said payer has defaulted in deducting the tax at source, the Department is not remedyless and, therefore, can take action against the payer under the provisions of Section 201 of the Income Tax Act and compute the amount accordingly. No doubt, if the person (payer) who has to make payments to the non-resident has defaulted in deducting the tax at source from such payments, the non-resident is not absolved from payment of taxes thereupon. However, in such a case, the non-resident is liable to pay tax, but the question of payment of advance tax would not arise. For this reason, it would not be permissible for the Revenue to charge any interest under Section 234B of the Act.

### Section 263 of the Income-tax Act, 1961 - Revision – Of orders prejudicial to revenue

*If a query is raised during the course of scrutiny by the assessing officer, which was answered to the satisfaction of the assessing officer, but neither the query nor the answer were reflected in the assessment order, this would not by itself lead to the conclusion that the order of the assessing officer called for interference and revision [Assessment Year 1982-83]*

#### CIT v. Vikas Polymers, August 16, 2010 (DEL)

It is a pre-requisite that the Commissioner must give reasons to justify the exercise of *suo moto* revisional powers by him to re-open a concluded assessment. A bare reiteration by him that the order of the Income-tax Officer is erroneous insofar as it is prejudicial to the interest of the revenue, will not suffice. The exercise of the power being quasi-judicial in nature, the reasons must be such as to show that the enhancement or modification of the assessment or cancellation of the assessment or directions issued for a fresh assessment were called for, and must irresistibly lead to the conclusion that the order of the Income Tax Officer was not only erroneous but was prejudicial to the interest of



the revenue. Thus, while the Income Tax Officer is not called upon to write an elaborate judgment giving detailed reasons in respect of each and every disallowance, deduction, etc., it is incumbent upon the Commissioner not to exercise his *suo moto* revisional powers unless supported by adequate reasons for doing so.

The provisions of Section 263 of the Act, when read as a composite whole make it incumbent upon the Commissioner before exercising revisional powers to: (i) call for and examine the record, and (ii) give the assessee an opportunity of being heard and thereafter to make or cause to be made such enquiry as he deems necessary. It is only on fulfillment of these twin conditions that the Commissioner may pass an order exercising his power of revision. Minutely examined, the provisions of the Section envisage that the Commissioner may call for the records and if he *prima facie* considers that any order passed therein by the assessing officer is erroneous insofar as it is prejudicial to the interest of the revenue, **he may after giving the assessee an opportunity of being heard and after making or causing to be made such enquiry as he deems necessary, pass such order thereon as the circumstances of the case justify.** The twin requirement of the Section is manifestly for

a purpose. Merely because the Commissioner considers on examination of the record that the order have been erroneously passed so as to prejudice the interest of the revenue will not suffice. The assessee must be called, his explanation sought for and examined by the Commissioner, and thereafter if the Commissioner still feels that the order is erroneous and prejudicial to the interest of the revenue, the Commissioner may pass revisional orders. If, on the other hand, the Commissioner is satisfied, after hearing the assessee, that the orders are not erroneous and prejudicial to the interest of the revenue, he may choose not to exercise his power of revision. This is for the reason that if a query is raised during the course of scrutiny by the assessing officer, which was answered to the satisfaction of the assessing officer, but neither the query nor the answer were reflected in the assessment order, this would not by itself lead to the conclusion that the order of the assessing officer called for interference and revision.

The Commissioner of Income-tax served a notice on the assessee-firm stating therein that, while completing the assessment the Income Tax Officer did not inquire into the genuineness of the capital investments of the two partners and unsecured loans taken from Chit Fund Company. The assessee firm furnished all documents sought to be seen by the Commissioner and explained the investment made by the partner. The Commissioner proceeded on the assumption that no such information, as was furnished to him, was furnished at the time of assessment. The Commissioner further mentioned that the Income Tax Officer has not examined the cash credits of the partners or deposits of Chit Fund.

The Delhi High Court held that assuming that the assessee had not filed certain documents on the record at the time of assessment, this would not justify the conclusion arrived at by the Commissioner that the assessing officer had shirked his responsibility of examining and investigating the case. Moreso, in view of the fact that the assessee explained that the capital investment made by the partners, which had been called into question by the Commissioner, was duly reflected in the respective assessments of the partners who were income-tax assesseees and the unsecured loan taken from the Chit Fund Company was duly reflected in the assessment order of the said Chit Fund which was also an assessee. Therefore, the revisional power exercised by the Commissioner was unjustified.

#### **Section 264 of the Income-tax Act, 1961 - Revision – Of other orders**

*Once the Commissioner is vested with the power of condonation of delay, then it is incumbent upon the Commissioner to take into consideration the reasons mentioned by the assessee seeking condonation of delay*

#### **Danny Denzongpa v. CIT, September 20, 2010 (BOM)**

The petitioner is an Indian National of Sikkimese origin. The petitioner was seeking certain benefits for the assessment years 1997-98 to 2005-06, which had been conferred on account of insertion of Section 10(26 AAA) by the Finance Act, 2008, which has been incorporated with retrospective effect from 1-4-1990. The petitioner's

assessment was already completed for the relevant years. The petitioner accordingly sought to claim benefit of the said provision and filed an Application under Section 264 on 4-9-2008, i.e., after four months of the President's assent to Finance Act, 2008 on 10-5-2008. The reasons for the delay were also stated for the consideration of Commissioner who had powers under Section 264 for condonation of delay. The Commissioner rejected the said applications.

The Bombay High Court held that the Finance Act, 2008 by which the said provision was introduced, received the assent of the President on 10-5-2008. The Petitioner had made application immediately after a period of four months of the said Finance Act, receiving assent of the President. This reason had been mentioned by the Petitioner in the applications for each of the relevant assessment years. However, the Commissioner had not even adverted to the reasons mentioned by the Petitioner in the application of condonation of delay and had in a cryptic manner rejected the said Application by observing that he was unable to entertain the Petitioner beyond the time limit prescribed. Once the Commissioner is vested with the power of condonation of delay, then it is incumbent upon the Commissioner to take into consideration the reasons mentioned by the assessee seeking condonation of delay. A reading of the impugned order, however, did not indicate that the reasons mentioned by the Petitioner had been considered. In fact, the said reasons had not even been adverted to by the Commissioner. In matters of this kind, wherein a benefit is sought to be given to an assessee that too with retrospective effect, a highly technical and pedantic approach is required to be eschewed and approach which furthers the intent and purport of the legislation is required to be adopted.

Therefore, the order of the Commissioner was to be set aside.

#### **OTHER ACTS**

##### **Banking Laws**

#### **Section 6 read with Sections 21 and 35A of the Banking Regulations Act, 1949 – Form and business in which banking companies may engage**

*Dealing in Non Performing Assets (NPAs) as part of the Credit Appraisal Mechanism and as a part of Restructuring Mechanism falls within Section 21 read with Section 35A of the Banking Regulation Act, 1949 and hence, it cannot be said that "transfer of debts/NPAs" inter se between banks is an activity which is impermissible under the Act*

#### **ICICI Bank Limited v. Official Liquidator, September 30, 2010 (SC)**

The Banking Regulation Act, 1949 (the Act) is an open-ended Act. It empowers RBI (regulator and policy framer in matter of advances and capital adequacy norms) to develop a healthy secondary market, by allowing banks inter se to deal in NPAs in order to clean the balance sheets of the banks which guideline/policy falls under Section 6(1) (a) read with Section 6(1)(n). Therefore, it cannot be said that assignment of debts/NPAs is not an activity permissible under the Act.



Thus, accepting deposits and lending by itself is not enough to constitute the "business of banking". The dependence of commerce on banking is so great that in modern money economy the cessation even for a day of the banking activities would completely paralyse the economic life of the nation. Thus, the Act mandates a statutory comprehensive and formal structure of banking regulation and supervision in India.

The guidelines issued by RBI dated 13-7-2005 itself authorises banks to deal inter se in NPAs. These guidelines have been issued by the Regulator in exercise of the powers conferred by Sections 21 and 35A of the Act. They have a statutory force of law. They have allowed banks to engage in trading in NPAs with the purpose of cleaning the balance sheets so that they could raise the capital adequacy ratio. All this comes within the ambit of Section 21 which enables RBI to frame the policy in relation to advances to be followed by the banking companies and which empowers RBI to give directions to banking companies under Section 21(2). These guidelines and directions following them have a statutory force. When a delegate is empowered by the Parliament to enact a Policy and to issue directions which have a statutory force and when the delegate (RBI) issues such guidelines (Policy) having statutory force, such guidelines have got to be read as supplement to the provisions of the Act. The "banking policy" is enunciated by RBI. Such policy cannot be said to be *ultra vires* the Act. The idea behind empowering

RBI to determine the Policy in relation to Advances is to enable banking companies to expand their business of banking and in that sense such guidelines also define - as to what constitutes banking business.

NPA means an asset or account receivable of a borrower, which has been classified by banks or financial institutions in terms of RBI Guidelines as sub-standard, doubtful etc. These guidelines are issued to improve quality of assets of the banks. The 2005 guidelines of RBI are not to eliminate NPAs but to restructure. The Act vide Section 21 empowers RBI in the interest of the Banking Policy to lay down guidelines in relation to advances to be followed by banking companies. The 2005 guidelines have been issued as "a restructuring measure" in order to avoid setbacks in the banking system. NPAs do not generate interest. 85 per cent of the Indian Banks' income comes from interest. Thus, NPAs adversely impact profits of the banks and hence, as a matter of Banking Policy, RBI as Regulator seeks through its guidelines under Section 21 read with Section 35A to manage these NPAs and not to eliminate. The said guidelines deal with restructuring of the banking system which is one of the objects behind giving authority to RBI to frame "banking policy".

NPAs are "Account Receivables". The impugned guidelines show that RBI considers inter se NPA assignment between banks to be a tool for resolving the issue of NPAs and in the interest of banking policy under Section 21 of



the Act. The object is to minimise the problem of credit risk. The corporate debt restructuring is one of the methods for reducing NPAs. Thus, such restructuring as a matter of banking policy cannot be treated as "trading". One has to keep in mind the object behind enactment of the Act. Thus, the said Guidelines fall under Section 21 of the Act. These Guidelines are a part of Credit Appraisal Mechanism. Thus, the impugned Guidelines are not *ultra vires* the Act. Dealing in NPAs as part of the Credit Appraisal Mechanism and as a part of Restructuring Mechanism falls within Section 21 read with Section 35A of the Act. Hence, it cannot be said that "transfer of debts/NPAs" inter se between banks is an activity which is impermissible under the Act.

On reading the provisions of the Act with the Guidelines of RBI issued from time to time in relation to Advances and Re-structuring/Management of NPAs it is to be held that the Act is a complete Code on banking and that dealing in NPAs inter se by the banks needs to be looked in the larger framework of "Re-structuring of banking System".

### CPC

#### **Order 41, Rule 27 read with Order 13, Rule 4 of the CPC read with Section 31 of the Trade and Merchandise Act, 1958 – Additional Evidence**

*Production of additional evidence is permissible under Order 41, Rule 27 and it can be taken on record as provided under Order 41, Rule 27 (b); however this should not be taken on record as evidence without giving defendants/respondents an opportunity to lead evidence in rebuttal of said documents*

#### **Shalimar Chemical Works Ltd. v. Surendra Oil & Dal Mills (Refineries), August 27, 2010 (SC)**

The appellant claims to be the registered owner of the trade mark "Shalimar" in Class 03 in respect of coconut hair oil and in Class 29 in respect of all edible oils included in that class. Alleging that the respondents were marketing their product in infringement of its registered trade mark, the appellant filed a suit before the City Civil Court, Hyderabad, seeking permanent injunction against the defendants. In course of the trial, the appellant produced before the Court, photocopies of registration certificates under Trade and Merchandise Marks Act, 1958 along with the related documents attached to the certificates which were "marked" as exhibits, "subject to objection of proof and admissibility". The Trial Court dismissed the suit of the appellant *inter alia* holding that the available evidence on record did not establish the case of the plaintiff and there was no *prima facie* case in favour of the plaintiff nor the balance of convenience was in favour of the plaintiff. The Trial Court arrived at its findings mainly because the appellant did not file the trade mark registration certificates in their original.

On appeal before the High Court, the appellant filed an application under Order 41, Rule 27 for accepting the originals of the trade mark registration certificates and the allied documents (of which Xerox copies were filed before the trial court) as additional evidence. The Single Judge allowed the application for additional evidence and set aside the judgment and decree passed by the trial court and allowed the appellant's suit granting decree of permanent injunction

against the defendants/respondents. However the division bench of the High Court took the view that there was no occasion or justification for admitting the original trade mark registration certificates at the appellate stage as additional evidence and accordingly dismissed the judgment of the Single Judge.

The Supreme Court held that serious mistakes were committed in the case at all stages. The Trial Court should not have "marked" as exhibits the Xerox copies of the certificates of registration of trade mark in face of the objection raised by the defendants. It should have declined to take them on record as evidence and left the plaintiff to support its case by whatever means it proposed rather than leaving the issue of admissibility of those copies open and hanging, by marking them as exhibits subject to objection of proof and admissibility. The appellant, therefore, had a legitimate grievance in appeal about the way the trial proceeded. The Single Judge rightly allowed the appellant's plea for production of the original certificates of registration of trade mark as additional evidence because that was simply in the interest of justice and there was sufficient statutory basis for that under clause (b) of Order 41, Rule 27. But then the Single Judge seriously erred in proceeding simultaneously to allow the appeal and not giving the defendants/respondents an opportunity to lead evidence in rebuttal of the documents taken in as additional evidence. The division bench was again wrong in taking the view that in the facts of the case, the production of additional evidence was not permissible under Order 41, Rule 27. As shown above the additional documents produced by the appellant were liable to be taken on record as provided under Order 41, Rule 27 (b) in the interest of justice. But it was certainly right in holding that the way the Single Judge disposed of the appeal caused serious prejudice to the defendants/respondents. In the facts and circumstances of the case, therefore, the proper course for the division bench was to set aside the order of the learned Single Judge without disturbing it insofar as it took the originals of the certificates of registration produced by the appellant on record and to remand the matter to give opportunity to defendants/respondents to produce evidence in rebuttal if they so desired.

### Competition Act

#### **Section 53A read with Sections 26 and 33 of the Competition Act, 2002 – Appeal before Appellate Tribunal**

*Taking a prima facie view and issuing a direction to Director General for investigation would not be an order appealable under Section 53A; however, while passing directions and orders dealing with the rights of the parties in its adjudicatory and determinative capacity, it is required of the Commission to pass speaking orders, upon due application of mind, responding to all the contentions raised before it by the rival parties*

#### **Competition Commission of India v. Steel Authority of India Ltd, September 9, 2010 (SC)**

In terms of Section 53A(1)(a) of the Act appeal shall lie only against such directions, decisions or orders passed by the Commission before the Tribunal which have been specifically stated under the provisions of Section 53A(1)



(a). The orders, which have not been specifically made appealable, cannot be treated appealable by implication. For example, taking a *prima facie* view and issuing a direction to the Director General for investigation would not be an order appealable under Section 53A.

Neither any statutory duty is cast on the Commission to issue notice or grant hearing, nor any party can claim, as a matter of right, notice and/or hearing at the stage of formation of opinion by the Commission, in terms of Section 26(1) of the Act that a *prima facie* case exists for issuance of a direction to the Director General to cause an investigation to be made into the matter. However, the Commission, being a statutory body exercising, *inter alia*, regulatory jurisdiction, even at that stage, in its discretion and in appropriate cases may call upon the concerned party(s) to render required assistance or produce requisite information, as per its directive. The Commission is expected to form such *prima facie* view without entering upon any adjudicatory or determinative process. The Commission is entitled to form its opinion without any assistance from any quarter or even with assistance of experts or others. The Commission has the power in terms of Regulation 17 (2) of the Competition Commission of India (General) Regulations, 2009 (Regulations) to invite not only the information provider but even 'such other person' which would include all persons, even the affected parties, as it may deem necessary. In that event it shall be 'preliminary conference', for whose conduct of business the Commission is entitled to evolve its own procedure.

The Commission, in cases where the inquiry has been initiated by the Commission suo moto, shall be a necessary party and in all other cases the Commission shall be a proper party in the proceedings before the Competition Tribunal. The presence of the Commission before the Tribunal would help in complete adjudication and effective and expeditious

disposal of matters. Being an expert body, its views would be of appropriate assistance to the Tribunal. Thus, the Commission in the proceedings before the Tribunal would be a necessary or a proper party, as the case may be.

During an inquiry and where the Commission is satisfied that the act is in contravention of the provisions stated in Section 33 of the Act, it may issue an order temporarily restraining the party from carrying on such act, until the conclusion of such inquiry or until further orders without giving notice to such party, where it deems it necessary. This power has to be exercised by the Commission sparingly and under compelling and exceptional circumstances. The Commission, while recording a reasoned order *inter alia* should : (a) record its satisfaction (which has to be of much higher degree than formation of a *prima facie* view under Section 26(1) of the Act) in clear terms that an act in contravention of the stated provisions has been committed and continues to be committed or is about to be committed; (b) It is necessary to issue order of restraint and (c) from the record before the Commission, it is apparent that there is every likelihood of the party to the lis, suffering irreparable and irretrievable damage or there is definite apprehension that it would have adverse effect on competition in the market.

The power under Section 33 of the Act to pass temporary restraint order can only be exercised by the Commission when it has formed *prima facie* opinion and directed investigation in terms of Section 26(1) of the Act, as is evident from the language of this provision read with Regulation 18(2) of the Regulations.

In consonance with the settled principles of administrative jurisprudence, the Commission is expected to record at least some reason even while forming a *prima facie* view. However, while passing directions and orders dealing with the rights of the parties in its adjudicatory and determinative capacity, it is required of the Commission to pass speaking

orders, upon due application of mind, responding to all the contentions raised before it by the rival parties.

#### FEMA

#### Rule 4 of the Foreign Exchange Management (Adjudication Proceedings and Appeal) Rules, 2000 – Holding of inquiry

*A noticee served with notice under Rule 4(1) requiring him to show cause why an inquiry should not be held against him, is not entitled to demand to furnish all documents in possession of Adjudicating Authority including those documents upon which no reliance has been placed to issue such notice*

#### Kanwar Natwar Singh v. Director of Enforcement, October 30, 2010 (SC)

The show-cause notice under Rule 4, to be so issued is not for the purposes of making any adjudication into alleged contravention but only for the purpose of deciding whether an inquiry should be held against him or not. Every such notice is required to indicate the nature of contravention alleged to have been committed by the person concerned. That after taking the cause, if any, shown by such person, the Adjudicating Authority is required to form an opinion as to whether an inquiry is required to be held into the allegations of contravention.

It is only then the real and substantial inquiry into allegations of contravention begins. While holding inquiry into allegations of contravention, every Adjudicating Authority shall have the powers of a Civil Court under the Code of Civil Procedure in respect of the matters, namely, (a) summoning and enforcing the attendance of any person and examining him on oath; (b) requiring discovery and production of documents; (c) receiving evidence on affidavits; (d) requisitioning any public record, document or copy of such record or document from any office; (e) issuing commissions for examination of witnesses or documents etc. That all proceedings before the Adjudicating Authority shall be deemed to be judicial proceedings within the meaning of Sections 193 and 228 of the Indian Penal Code; shall be deemed to be a Civil Court for the purposes of Sections 345 and 346 of the Code of Criminal Procedure, 1973.

Rule 4 does not require the Adjudicating Authority to supply copies of any documents along with the show cause notice. The Rule does not require the Adjudicating Authority even to furnish any list of documents upon which reliance has been placed by him to set the law in motion.

However, a noticee is always entitled to satisfy the Adjudicating Authority that those very documents upon which reliance has been placed do not make out even a *prima facie* case requiring any further inquiry. All such documents relied on by the Authority are required to be furnished to the noticee enabling him to show a proper cause as to why an inquiry should not be held against him though the Rules do not provide for the same.

Even the principles of natural justice do not require supply of documents upon which no reliance has been placed by the Authority to set the law into motion. Supply of relied on documents based on which the law has been set into motion would meet the requirements of principles of



natural justice. No Court can compel the Authority to deviate from the statute and exercise the power in altogether a different manner than the prescribed one. As noticed, a reasonable opportunity of being heard is to be provided by the Adjudicating Authority in the manner prescribed for the purpose of imposing any penalty as provided for in the Act and not at the stage where the Adjudicating Authority is required merely to decide as to whether an inquiry at all be held into the matter. Imposing of penalty after the adjudication is fraught with grave and serious consequences and therefore, the requirement of providing a reasonable opportunity of being heard before imposition of any such penalty is to be met. In contradistinction, the opinion formed by the Adjudicating Authority whether an inquiry should be held into the allegations made in the complaint are not fraught with such grave consequences and therefore the minimum requirement of a show cause notice and consideration of cause shown would meet the ends of justice. A proper hearing always include, no doubt, a fair opportunity to those who are parties in the controversy for correcting or contradicting anything prejudicial to their view. Lord Denning has added: "If the right to be heard is to be a real right which is worth anything, it must carry with it a right in the accused man to know the case which is made against him. He must know what evidence is given and what statements have been made affecting him: and then he must be given a fair opportunity to correct or contradict them" [see *Kanda v. Government of Malaya (1962) AC 322*].

On a fair reading of the statute and the Rules suggests that there is no duty of disclosure of all the documents in possession of the Adjudicating Authority before forming an opinion that an inquiry is required to be held into the alleged contraventions by a noticee. Even the principles of natural justice and concept of fairness do not require the statute and the Rules to be so read. Any other interpretation may result in defeat of the very object of the Act. Concept of fairness is not a one way street. The principles of natural justice are not intended to operate as roadblocks to obstruct statutory inquiries. Duty of adequate disclosure is only an additional procedural safeguard in order to ensure the attainment of the fairness and it has its own limitations. The extent of its applicability depends upon the statutory framework.

A fair reading of Rule 4 which is a complete compendium for holding of inquiry suggests that all the evidence and documents which the Adjudicating Authority may consider relevant for the purpose of inquiry may have to be furnished to a person facing the inquiry on the allegations of contravention of the provisions of the Act etc., alleged to have been committed by him. In addition, the Authority may require attendance of any person acquainted with the facts and circumstances of the case to give evidence and to produce any documents which in its opinion, may be useful for or relevant to the subject matter of the inquiry. Only upon consideration of the entire evidence produced, if the Adjudicating Authority is satisfied that the person has committed the contravention, he may by order in writing accordingly impose such penalty as he thinks fit in accordance with the provisions of the Act which of course is not final as it is subject to appeal. ■

## CIRCULARS/NOTIFICATIONS

### DIRECT TAXES

#### I. Circulars

##### 1. Circular No. 7/2010 dated 27-10-2010



**Clarification regarding period of validity of approvals issued under Section 10(23C)(iv), (v), (vi) or (via) and Section 80G(5) of the Income-tax Act, 1961**

For the removal of doubts about the period of validity of various approvals granted by the Chief Commissioners of Income-tax or Directors General of Income-tax under sub-clauses (iv), (v), (vi) and (via) of Section 10(23C) and by the Commissioners of Income-tax or Directors of Income-tax under Section 80G(5) of the Income-tax Act, 1961, the Central Board of Direct Taxes has, through, this circular clarified the following:-

1. In light of the amendment brought by Taxation Laws (Amendment) Act, 2006, it has been clarified that for the purposes of sub-clauses (iv) and (v) of Section 10(23C) any notification issued by the Central Government under the said clauses, on or after 13-7-2006 will be valid until withdrawn and there will be no requirement on the part of the assessee to seek renewal of the same after three years.
2. In light of the provisions of Rule 2CA, it has been clarified that for the purposes of sub-clauses (vi) and (via) of Section 10(23C) any approval issued on or after 1-12-2006 would be a one time approval and would be valid till it is withdrawn.
3. In light of the amendment brought by Finance (No.2) Act, 2009 it has been clarified that for the purposes of Section 80G(5), existing approvals expiring on or after 1<sup>st</sup> October, 2009 shall be deemed to have been extended in perpetuity unless specifically withdrawn. Further, any approval under section 80G(5) on or after 1-10-2009 would be a one time approval which would be valid till it is withdrawn.

#### II. Notifications

##### 1. Notification No. 80/2010 dated 19-10-2010

Deduction under Section 80C is available in respect of any sum paid or deposited to effect or to keep in force contract for such annuity plan of the Life Insurance Corporation or any other insurer as the Central government may, by notification in the Official Gazette specify in this behalf.

Accordingly, the Central Government, has, through this notification specified the Tata AIG Easy Retire Annuity plan of the Tata AIG Life Insurance Company Limited as the annuity plan of the ICICI Prudential Life Insurance Company Limited for the purposes of deduction under Section 80C.

The complete text of the above notifications/Circulars can be downloaded from the website of the Income-tax Department, [www.incometaxindia.gov.in](http://www.incometaxindia.gov.in), and the complete link may be downloaded from the home page of the Direct Taxes Committee of the Institute at [http://www.icaai.org/post.html?post\\_id=965&c\\_id=57](http://www.icaai.org/post.html?post_id=965&c_id=57).

*(Matter on Direct Taxes has been contributed by the Direct Taxes Committee of the ICAI)*

### INDIRECT TAXES

#### A. EXCISE DUTY

##### I Notification:



##### 1. Notification No. 33/2010-CE dated

**19.10.2010** : All excisable goods falling under the Schedule to the Central Excise Tariff Act, when supplied to the United Nations or an international organisation for their official use, have been exempted from the whole of the additional and special additional duty of the excise.

However, the above exemption will be available only if the manufacturer produces a certificate before the jurisdictional Assistant/Deputy Commissioner of Central Excise from the United Nations or the international organisation that the goods are intended for such use.

##### 2. F. No. 390/Misc./163/2010-JC dated 20.10.2010:

In view of the National Litigation Policy formulated by the Government of India to reduce Government litigation, following monetary limits have been prescribed vide an Instruction in respect of appeals to be filed by the Department in High Courts and Tribunal :

**High Courts:** Appeals would not be filed in cases where the duty involved or total revenue including fine or penalty is ₹2 lakh and below.

**Tribunals:** Appeals in the Tribunal would not be filed where the duty involved or the total revenue including fine and penalty is ₹1 lakh and below.

In case of appeals to be filed in the Supreme Court, the old policy as provided in Instruction vide *DO F No. 390/170/92-JC dated 13.1.93* of not filing appeals in cases where the duty involved is ₹5 lakh or less will continue to be followed.

In respect of appeals filed in the Supreme Court, the proposals are examined by the Board before filing. The Civil Appeals on matters relating to valuation and classification filed under Section 35L(b) of the Central Excise Act, 1944 and Section 130E(b) of the Customs Act, 1962 respectively are being filed after careful scrutiny by the Board and while examining, the amount involved is kept in mind. On all issues other than those relating to valuation and classification, SLPs are filed by the Board after obtaining the opinion of the Law officer from the Ministry of Law.

However, adverse judgments relating to the following would be contested irrespective of the amount involved:

- a) Where the constitutional validity of the provisions of an Act or Rule is under challenge.
- b) Where notification/instruction/order or Circular has been held illegal or ultra vires.
- c) Where audit objection on the issue involved in a case has been accepted by the Department

Wherever appeals would not be filed in pursuance of these instructions, which are aimed solely at reducing Government litigation, such cases will not have any precedent value. In such cases, there will be no presumption that the Department has acquiesced in the decision on the disputed issues in the case of same assessee or in case of any other assessees, if the amount involved exceeds the monetary limits.

Instruction issued vide *F No. 275/55/CX 8A dated 10.11.2008* has been rescinded and the above Instruction will be adhered to strictly for all appeals filed on or after 1.11.2010.

The complete text of above notification and instruction are available at [www.cbec.gov.in](http://www.cbec.gov.in)

*(Matter on Indirect Taxes has been contributed by the Indirect Taxes Committee of the ICAI)*

## CORPORATE LAWS

### 1. Public deposit' definition change in NBFC Regulations

[www.rbi.gov.in](http://www.rbi.gov.in)

The RBI has issued Notification No. DNBS.(PD) 216/CGM(US)-2010 dated 22.10.2010 amending the definition of 'public deposit' within the meaning of paragraph 2(1)(xii) of the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998 by excluding the amount raised by issue of infrastructure bonds by Infrastructure Finance Companies, as specified in the notification issued from time to time by the Central Government under Section 80CCF of the Income-tax Act, 1961. Earlier, the Central Government had, vide Notification No.48/2010/F.No.149/84/2010-SO (TPL) dated 9<sup>th</sup> July, 2010, specified certain bonds as long term infrastructure bonds for the purposes of section 80CCF of Income-tax Act, 1961, viz., bonds issued by Industrial Finance Corporation of India, Life Insurance Corporation, Infrastructure Development Finance Company and a Non-Banking Finance Company classified as an Infrastructure Finance Company by the Reserve Bank of India. One may refer to the above website for further details.



### 2. Banks' Exposure to Capital Market - Issue of Irrevocable Payment Commitments (IPCs)

[www.sebi.gov.in](http://www.sebi.gov.in)

The RBI has issued Circular No. DBOD.Dir.BC.52/13.03.00/2010-11 dated 28.10.2010 referring to the earlier circular whereby certain risk mitigation measures were prescribed in the context of banks issuing IPCs to various Stock Exchanges on behalf of Mutual Funds and FIs, as a transitional arrangement upto 31<sup>st</sup> October, 2011. Thereafter, several custodian banks expressed operational difficulties in complying with the requirement of incorporating a clause in the agreement with their clients which gives them an inalienable right over the securities to be received as payout in any settlement before 1<sup>st</sup> November, 2010 and hence it is now decided to grant an additional period of two months i.e. upto 31<sup>st</sup> December, 2010, to the custodian banks to fulfil this requirement. It is also clarified that in cases where transactions are pre-funded i.e. there are clear INR funds in the customer's account and, in case of FX deals, the bank's nostro account has been credited before the issuance of the IPC by custodian banks, the requirement of the clause of inalienable right over the security to be received as payout in the agreement with the clients will not be insisted upon. One may refer to the above citation for further details.

### 3. European Style Stock Options

[www.sebi.gov.in](http://www.sebi.gov.in)

The SEBI has issued Circular No. CIR/DNPD/6/2010 dated 27.10.2010 whereby Stock Exchanges would now be in position to offer either European style or American style stock options. After opting for a particular style of exercise, a Stock Exchange shall offer option contracts of the same style on all eligible stocks and all other contract specifications, including risk management framework applicable for American style stock options shall apply to European style stock options. Any modification shall require prior approval of SEBI. The Stock Exchanges interested to introduce European style stock options are advised to, (a) put in place proper systems and procedures for smooth introduction of European style stock options, (b) make necessary amendments to the relevant bye-laws, rules and regulations for introduction of European style stock options, and, (c) notify all categories of market participants, including general public, and also to disseminate the same on their websites, at least one month in advance of implementing the switchover in the exercise style. After opting for a particular style of exercise, a Stock Exchange may change to another style of exercise only after seeking prior approval of SEBI. One may refer to the above website for further details.

#### 4. Clarification on Trading Rules and shareholding in dematerialised mode

[www.sebi.gov.in](http://www.sebi.gov.in)

The SEBI has issued Circular No. SEBI/Cir/ISD/2/2010 dated 25.10.2010 trading rules and shareholding in dematerialised mode. It is now clarified that while computing the requirement of minimum 50 per cent shareholding of non-promoters in demat form in a company, the government holding in non-promoter category may be excluded. Also, the Stock Exchanges are advised to, (a) put in place the adequate systems and issue the necessary guidelines for implementing the above decision, (b) make necessary amendments to the relevant bye-laws, rules and regulations for the implementation of the above decision immediately, (c) bring the provisions of this circular to the notice of the member brokers of the Exchange and also to disseminate the same on the website, and, (d) communicate to SEBI, the status of the implementation of the provisions of this circular in the Monthly Development Report. One may refer to the above citation for further details.

#### 5. Additional fees to ROC increased

[www.mca.gov.in](http://www.mca.gov.in)

The Ministry of Corporate Affairs ("MCA") has issued a release revising the fees payable as per Section 611(2) of the Companies Act, 1956 (except for Form 5) as per below details with effect from 5<sup>th</sup> December 2010:

Period of Delay	Fixed rate of additional fee
Upto 30 days	Two times of normal filing fee
More than 30 days and upto 60 days	Four times of normal filing fee
More than 60 days and upto 90 days	Six times of normal filing fee
More than 90 days	Nine times of normal filing fee

The MCA has also advised that in order to avoid payment of additional fees, please file within stipulated time. One may refer to the above website for further details. 6. Prudential norms on investment in zero coupon bonds

#### 6. Code of Conduct for Investor Associations (IAs)

[www.sebi.gov.in](http://www.sebi.gov.in)

The SEBI has issued Circular No. Cir/OIAE/IAD/01/2010 dated 01.11.2010 on the above subject and in consultation with SEBI recognised Investor Associations, it has been decided that the Associations shall abide by a code of conduct enclosed to the above Circular available at the above citation. It has also been decided that every SEBI recognised Investor Association shall submit a letter of compliance with this

code of conduct every year in the first week of April for the preceding financial year and also along with the application for renewal of recognition. One may refer to the above website for further details.

#### 7. Portfolio Managers – clarification on minimum investment amount by clients, performance of portfolio and schemes

[www.sebi.gov.in](http://www.sebi.gov.in)

The SEBI has issued Circular No. Cir/IMD/DF/16/2010 dated 02.11.2010 stating that it has come across lack of uniformity in practice relating to certain issues pertaining to portfolio managers like, (a) there have been instances of portfolio managers accepting funds or securities less than ₹5 lakh from clients and opening client accounts on the basis of the client's commitment that ₹5 lakh would be brought in soon and also that there have been instances of committed amounts being higher than the prescribed minimum of ₹5 lakh while the initial amount collected from the client could be below ₹5 lakh, (b) it is seen that many portfolio managers are not making adequate disclosure regarding portfolio performance in the disclosure document, (c) SEBI had vide notification dated 11<sup>th</sup> August, 2008 deleted the word "Scheme" from PMS Regulations ; however, it is seen that in some cases, portfolio managers still group portfolios in separate investment categories and term them as "schemes". Now, in order to bring about greater uniformity, clarity and transparency with regard to above issues, portfolio managers are advised by SEBI by this Circular that, (a) to ensure compliance with regulation 15(1A) of SEBI (Portfolio Managers) Regulations, 1993, it is clarified that the first single lump-sum investment amount received as funds or securities from clients should not be less than ₹5 lakh, (b) to ensure compliance with regulation 14(2)(b)(iv) of SEBI (Portfolio Managers) Regulations, 1993, Portfolio Managers shall disclose the performance of portfolios grouped by investment category for the past three years as per the enclosed prescribed tabular format. Portfolio Managers shall also ensure that the disclosure document is given to all clients along with the account opening form at least two days in advance of signing of the agreement. In order to ensure that the clients have access to updated information about the portfolio manager, portfolio managers shall place the latest disclosure document on their website, wherever possible, and, (c) portfolio managers shall not organise investment portfolios as "Schemes" akin to Mutual Fund Schemes while marketing their services to clients. One may refer to the above website for further details.

*(Matter on Corporate Laws has been contributed by CA. Jayesh Thakur)*

# Accounting treatment of overlift/underlift quantity of crude oil.

*The following is the opinion given by the Expert Advisory Committee of the Institute in response to a query sent by a member. This is being published for the information of readers.*

## A. Facts of the Case

1. A public limited company (hereinafter referred to as the 'company'), which is a wholly owned subsidiary of a listed government company, is in the business of exploration and production of oil and gas and other hydrocarbon related activities outside India. Usually, the legal regimes applicable in most of the countries provide that the ownership of mineral resources (hydrocarbons) is with respective governments. Accordingly, the host governments grant the rights to explore, develop and produce hydrocarbons in certain specified geographical areas within their territories (hereinafter referred to as the 'Rights') to the companies on some equitable consideration under various regimes. The activities of the company, thus, include securing such Rights and then to explore, develop and produce hydrocarbons. Such Rights are secured either on a 100 per cent basis, wherein the company or its affiliates themselves take the entire risks and rewards of such Rights or in consortium with other participants (such consortia usually being unincorporated joint ventures) wherein the joint venture participants share the risks and rewards in certain agreed proportions. Such Rights are granted by the host governments in accordance with the applicable legal and fiscal regime in the host country which are incorporated into binding contractual arrangements entered into with the host governments.
2. One such regime is production sharing agreement (hereinafter referred to as 'PSA'), under which the host government, which has the ownership rights over the hydrocarbons, grants the Rights to a company or consortium (usually called contractor) subject to certain obligations/payments by the contractor including sharing of the hydrocarbons, with the government or its nominated agency as per the principles detailed in the PSA.
3. The company is a participant in one such PSA along with other companies (hereinafter referred to as the 'consortium') with the government of a foreign country (hereinafter referred to as the 'State') in respect of certain geographical area specified in the PSA (hereinafter referred to as the 'area'). Under the PSA, the State granted the exclusive Rights to the consortium to conduct hydrocarbon operations in the area subject to the terms and conditions of the PSA. The joint venture arrangements among the consortium partners are governed by the Joint Operating Agreement (hereinafter referred to as the 'JOA') entered into by the consortium participants.
4. The area consists of offshore fields. The consortium has drilled production wells from nearby onshore location and also from an offshore platform to produce oil and gas from the area. Produced hydrocarbons are brought to onshore processing facility through a pipeline, processed in the onshore processing facility and then transported through another pipeline to the storage tanks. Storage tanks have stirring and heating facility which can be used to heat and/or to stir the crude oil. After heating on need basis in storage tanks, crude oil passes through metering system and then transported through an undersea pipeline to Single Point Mooring facility (SPM) where it is loaded into the tankers (ships) for transporting to the export destination.
5. The querist has stated that relevant article of the PSA provides that the title to hydrocarbon to which consortium is entitled to shall, unless an earlier separation point is agreed upon between the State and the consortium, pass to consortium at the delivery point. Further, according to the querist, relevant article of the JOA provides that each participant shall have the right and obligation to offtake (i.e., of crude oil) in kind and separately dispose of its participating interest share of total production due to the participants pursuant to the PSA. JOA contains provisions enabling participants to enter into an 'Offtake Agreement for Crude Oil' (hereinafter referred to as the 'COA') to cover the offtake of crude oil produced under PSA and lays down the following principles (among others) on which the COA is to be based:
  - (A) Title and risk of loss of each participant's participating interest share of crude oil shall pass to that participant at the delivery point.
  - (B) As between the participants, each participant shall have the right to offtake in each period a volume equal to its participating interest share of the total participating production of crude oil for the period (such volume is hereinafter referred to as a

- participant's 'basic entitlement'). A participant shall have the right to request either a deferral of lifting of a portion of such participant's basic entitlement or an overlift of such participant's basic entitlement, provided such deferral or overlift does not adversely affect the production and/or lifting schedule. The operator shall have the right to approve or disapprove such underlift or overlift; provided, however, approval shall not be unreasonably withheld.
- (C) To the extent that distribution of basic entitlement on such basis is impracticable due to unavailability of facilities or minimum cargo sizes, a method of making period adjustments shall be determined which provides substantially equivalent economic benefits to all the participants.
6. Accordingly, as per the querist, 'Crude Offtake Agreement (COA)' has been entered into by the participants. COA contains provisions (among others) for lifting schedule determination, cargo allocation and overlift/underlift.
7. 'Allocation Rules of the COA' , inter alia, provide for the following:
- (a) In developing each lifting schedule, the operator shall take into consideration the type and rate of production from the area, storage capacity at the terminal, the total number of the liftings from the terminal, the cumulative overlift and underlift of each party, and other operational and technical details pertinent to avoiding a shutdown or reduction of production.
  - (b) The operator shall have the discretion to allow the lifting of a cargo of a size less than, or more than, a standard cargo, provided that such lifting would not affect or unreasonably risk the lifting of another party, unless any party that would be affected by such lifting has notified the operator that such party does not disapprove such lifting.
  - (c) Overlift/Underlift:
    - (i) Each party may be designated to lift quantities, which would cause such party to overlift for
-

the month when the operator has assigned the party a lifting of a standard cargo and the party's entitlement is not sufficient to load a full standard cargo plus any allowable upward operational tolerance.

- (ii) Each party may be designated to lift quantities which would cause such party to underlift for the month when the final lifting schedule developed according to relevant article of the COA has the party not lifting its full entitlement for the month.
  - (iii) Any arrangements with other parties which violate the overlift/underlift restrictions set forth in this agreement shall be rejected by the operator, unless in the reasonable judgment of the operator, such arrangements will not affect the lifting of another party, or unless each party, that in the reasonable judgment of the operator, will be affected by such overlift or underlift has notified the operator that it does not disapprove of such overlift or underlift.
  - (iv) The operator shall be authorised to reject any arrangement with other parties, which results in an overlift or underlift position of one or more parties, if in the reasonable judgment of the operator, rejecting such nomination is necessary in order to avoid shutting down or reducing production from the Area or exceeding the storage capacity tolerance of the Terminal.
8. Thus, according to the querist, given the fact that title and risk of loss of each participant's participating interest share of crude oil shall pass to that participant at the delivery point, the participants are entitled to overlift/underlift crude oil in accordance with the provisions of JOA and COA. The underlift/overlift of a participant is adjusted in lifting schedule for the next month.
  9. The querist has stated that in view of the above provisions of the PSA, JOA and COA, the company is accounting for the overlift/underlift quantity of its basic entitlement as per its declared accounting policy reproduced below:  
"15. Revenue Recognition:  
15.1 Revenue from sale of products is recognised on transfer of custody to customers. Any difference as of the reporting date between the entitlement quantity minus the quantities sold in respect of crude oil (including condensate), if positive is treated as inventory and, if negative, is adjusted to revenue by recording the same as liability."
  10. The querist has further stated that as on 31<sup>st</sup> March, 2009, the company overlifted quantity over and above its basic entitlement. Following the above-stated accounting

policy, the company reduced the sales arrived at by multiplying overlift quantity by the sale price of crude oil realised by the company for its last sold cargo during March 2009 and created liability for the same.

11. The querist has also stated that had there been a case of underlift as on the balance sheet date, the company would have treated the underlift quantity as inventory of the company and would have valued it in accordance with the requirements of Accounting Standard (AS) 2, 'Valuation of Inventories' at cost or net realisable value, whichever is lower.
12. The above treatment, as per the querist, did not attract any adverse comment/observations either from the statutory auditors or the Comptroller and Auditor General of India (C&AG) till the financial year 2007-08. However, C&AG auditors while carrying out their review under Section 619(3)(b) of the Companies Act, 1956 for the financial year 2008-09 objected to the accounting for overlift quantity as liability and contested that the company should treat overlift quantity as its own share of production and should have booked sales of ₹789 million for the overlift quantity simultaneously recognising expenditure (cost of hydrocarbon, transportation charges and royalty etc.) amounting to ₹248 million on the basis of its recent cost figures, i.e., for fourth quarter (Q4) of the financial year 2008-09 in the extant case. Further, the C&AG auditors contended that government's take of profit oil should have also been reduced from the sales on the basis of applicable percentage of government's share of profit oil (i.e., for Q4 2008-09) as was recognised for normal sales of the company in accordance with its practice of showing sales 'net of government share of profit oil', as stated by way of footnote in Schedule-15, Sales to the company's final accounts.

## B. Query

13. The querist has sought the opinion of the Expert Advisory Committee of the Institute of Chartered Accountants of India on the appropriate accounting treatment of overlift/underlift quantity of crude oil by the company, i.e., whether
  - (i) the accounting policy of the company in recognising overlift quantity as liability and underlift quantity as inventory is appropriate and whether the accounting treatment carried out by the company in respect of overlift quantity of crude oil by recognising the same as liability at recent sales price of the crude oil realised by the company is appropriate; or
  - (ii) the production quantity related to overlift quantity should be treated as the company's share and accounted for in the manner specified by the C&AG

auditors; or

- (iii) there is any other appropriate accounting treatment /disclosure of such overlift/underlift quantity.

### C. Points considered by the Committee

14. The Committee notes that the basic issue raised in the query relates to the accounting for overlift and underlift quantity of crude oil. The Committee has, therefore, considered only this issue and has not examined any other issue that may arise from the facts of the Case, such as, accounting for government's share of profit oil, interpreting the terms of the PSA, JOA and COA, accounting for the joint operations, propriety of recognition of revenue on the transfer of custody of oil to customers, etc. In the absence of any information to the contrary, the Committee presumes that the company is being charged for its proportionate share in the production cost of the oil as per its basic entitlement and not as per the quantity lifted during the period.
15. As far as accounting for overlift quantity of crude oil is concerned, the Committee notes that the definition of the term 'revenue', as provided by Accounting Standard (AS) 9, 'Revenue Recognition' states that ***"Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, from the rendering of services, and ..."***. Accordingly, in the view of the Committee, the total amount of consideration arising from the sale of crude oil (including the sold quantity from the overlift of crude oil) should be recognised as revenue.
16. The Committee further notes the definition of the term 'liability', as provided in paragraph 10 of Accounting Standard (AS) 29, 'Provisions, Contingent Liabilities and Contingent Assets', which states as follows:  
***"A liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits."***

The Committee notes from the Facts of the Case that the underlift/overlift of a participant is adjusted in the lifting schedule for the next month. Thus, the Committee is of the view that the overlift of crude oil gives rise to an obligation on the company to transfer future economic benefits (by foregoing the right to receive equivalent future entitlement in the crude oil). Accordingly, a liability should be provided for by the company by way of charge to the profit and loss account for overlift quantity keeping in view the

presumption stated in paragraph 14 above that the company is charged only for the proportionate share of production cost as per its basic entitlement and not for the actual quantity lifted. The above treatment is based on the fundamental accounting principle of 'accrual' as contained in paragraph 10(c) of Accounting Standard (AS) 1, 'Disclosure of Accounting Policies', which provides as below:

"c. *Accrual*

Revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate."

17. The amount of provision for the liability in respect of overlift quantity should be determined on the basis of the best estimate of the expenditure required to settle the present obligation at the balance sheet date as per the requirements of paragraph 35 of AS 29. In the extant case, it would be the best estimate of the company's proportionate share of production expenses as per the JOA/PSA in respect of the quantity of crude oil foregone in future period towards settlement of the overlift quantity of crude oil.

18. As regards underlift situation, the Committee is of the view that to the extent it is the settlement of an overlift situation of the earlier periods, it should be recognised by debiting the liability provided for under the overlift situation and crediting/reducing the company's proportionate share in the production cost. In respect of other underlift situations (i.e., not arising due to settlement of an overlift of crude oil in an earlier period), the Committee notes that the Framework for the Preparation and Presentation of Financial Statements, issued by the Institute of Chartered Accountants of India, provides that "an asset is a resource controlled by the enterprise as a result of past events from which future economic benefits are expected to flow to an enterprise". Accordingly, the Committee is of the view that an underlift represents a right to future economic benefit through entitlement to receive equivalent production in the future and is therefore, an asset. In respect of the nature of that asset, the Committee notes the definition of the term 'pre-paid expense', as provided under the 'Guidance Note on Terms Used in Financial Statements', issued by the Institute of Chartered Accountants of India, which states as follows:

**"13.07 Pre-paid Expense**

Payment for *expense* in an accounting period, the benefit for which will accrue in the subsequent accounting period(s)."

Since in the present case, the company is charged

for the proportionate share of production cost as per its basic entitlement, but the quantity of crude oil lifted is less than its basic entitlement, the amount paid in excess is 'prepaid expense'. The Committee is of the view that under the underlift situation, the company should recognise a pre-paid expense by crediting its proportionate share of production cost as per the joint operating agreement/production sharing agreement.

19. In situations where an overlift situation has arisen due to settlement of an earlier underlift, the Committee is of the view that the same should be recognised by crediting the earlier recognised 'pre-paid expense' for the underlift and debiting the share of production cost for the current period.

**D. Opinion**

20. On the basis of the above, the Committee is of the following opinion on the issues raised in paragraph 13 above:

- (i) The accounting policy of the company in recognising overlift quantity as liability is appropriate, however, recognition of liability by reversing the sales/revenue of the company at the recent sales price of the crude oil is not appropriate. The accounting policy of recognising the underlift quantity as inventory is also not appropriate.

(ii)&(iii) Refer to paragraphs 15 to 19 above.

1	The Opinion is only that of the Expert Advisory Committee and does not necessarily represent the Opinion of the Council of the Institute.
2	The Opinion is based on the facts supplied and in the specific circumstances of the querist.
3	The Compendium of Opinions containing the Opinions of Expert Advisory Committee has been published in twenty eight volumes. A CD of Compendium of Opinions containing twenty eight volumes has also been released by the Committee. These are available for sale at the Institute's office at New Delhi and its regional council offices at Mumbai, Chennai, Kolkata and Kanpur.
4	Recent opinions of the Committee are available on the website of the Institute under the head 'Resources'.
5	Opinions can be obtained from EAC as per its Advisory Service Rules which are available on the website of the ICAI, under the head 'Resources'. For further information, write to <a href="mailto:eac@icai.org">eac@icai.org</a> ■

## TRANSITION to IFRS



Счетный период (год)	Классификация (код)	Сумма по данным бухгалтерского учета	20%	Сумма по данным ИФРС
4	5	6	7	8
			X	X
38	услуга	38,833	38,83	X
708	услуга	292,708	292,71	X
			331,54	X
			0,00	X
X	X	X	X	X
			0,00	
			0,00	
	X			
		X		

Companies incorporated in India have many stakeholders, particularly after the post financial sector reforms during the last two decades. They are primarily grouped into shareholders, governments, regulators and investors. These entities have set mind or mindset for evaluating performance in a particular way on select parameters. Measurement methodology and yardstick need to be changed in future, as the entities adopt new norms, converging, if not conforming, to International Financial Reporting Standards (IFRS). This is no more a choice, once the financial year 2011-12 begins, i.e., effective from April 2011, as it is a compulsion for Indian companies for convergence of Indian Generally Accepted Accounting Principles (Indian GAAP) with the IFRS and this includes banks.



### CA. R.S Raghavan

(The author is a member of the Institute.  
He can be reached at [eboard@icai.org](mailto:eboard@icai.org))

The fundamental principle of IFRS is the need to adopt many of the principles retrospectively even at the time of first application. Comprehensive IFRS statements have to cover the comparative figures for the period before the one actually being reported. Commercial entities that adopt IFRS effective from 1<sup>st</sup> April, 2011 and file their first return under IFRS norms for the year ending March 2012, would need to select accounting policies based on the IFRS and retrospectively apply these policies and standards

so as to derive the opening financials for 2010-11 under the IFRS norms. Therefore, the mapping process of chart of accounts should begin at the earliest during the early part of the financial year 2010-11, to take on the challenges squarely. There is an early mover advantage in this regard as earlier the conversion process started, the more time the institution will have to solve any teething problem in the roadmap to IFRS transition. Present IT and information system, may not meet the requirements to readily

generate information required to retrospectively apply these standards. All, sooner or later, will have to adjust to the accounting changes enforced by IRFS as the Reserve Bank of India accounting guidelines more often imbibe principles of IFRS, particularly when it comes to financial instruments such as derivatives, in terms of Indian Accounting Standards (IAS) 39.

In January, 2010, the Ministry of Corporate Affairs issued a roadmap for the IFRS convergence by companies, other than banking and insurance sectors for which the roadmap would be rolled out later. A phased role out is the need of the hour, as there are very few accounting professionals who are trained in the IFRS concepts, despite the fact that the ICAI is coming out with Accounting Standards, based on the International Accounting Standards, the erstwhile IFRS.

### Accounts and IFRS

The outstanding balance reflected in the accounts is considered as impaired when it is expected that all contractual cash flows would not be recovered. An impaired account will be measured on the present value basis using effective interest rates for the exposure on discount rates. Thus, entities will have to get used to the concepts such as effective interest rate and discount rates. Conversion from Indian GAAP to IFRS is not just a book entry and nothing is more simplistic than this. In the IFRS mode, de-recognition of financial assets is a complex process, multi-layered area and in the Indian context, this will impact the securitisation activity. Instead of being driven on the basis of ownership, consolidation is more on the controlling power, which is a management issue. Further, IFRS demands and requires more disclosures than what is mandated by Indian GAAP and this is apart from the disclosure requirements

**The outstanding balance reflected in the accounts is considered as impaired when it is expected that all contractual cash flows would not be recovered. An impaired account will be measured on the present value basis using effective interest rates for the exposure on discount rates. Thus, entities will have to get used to the concepts such as effective interest rate and discount rates.**

dictated by Basel II norms, as far as Banks are concerned. One need to operationalise the systems to extract hidden information and present it in the manner as required, with the I T support.

In order to obviate the inherent limitations in the Indian GAAP in the IFRS mode, the classification and measurement of financial instruments – financial assets and financial liabilities, assumes greater significance. The IFRS involves doing away with the present classification of financial assets consisting of investments and receivables into Held for Trading (HFT), Available for Sale (AFS) and Held to Maturity (HTM) and loans and advances by treating on an ongoing basis at amortised cost over a period of time or at its fair value.

Following are some of the terminologies having wafer thin gap in its interpretation on the IFRS framework /literature:-

- Unavoidable, no alternative,
- Highly, most, majority, substantially, major, more likely than not
- May, probable, possible, likely, expects, commonly
- Abnormal, unlikely, rarely,
- Reasonably/virtually certain
- Primarily, in principle, normally

In the IFRS literature, the accountants are expected to interpret the terminologies in the context of what the Accounting Standards require.

Therefore the potential hazards/hassles in interpreting a principle based IFRS cannot be wished away, even by the accounting professionals.

### Fair Value Challenge

In the normal market, fair value accounting would not have been a subject of debate. However, in a boom or bust period, fair value accounting may result in notional or accounting gain or loss as eventual settlement of price of the subject financial instrument, be it asset or liability, could be substantially different. If a business entity extends credit to its clients for a period of six months or more, then the nominal or absolute amount receivable after that period would normally be different from the fair value of the amount. It may not be a sound logic to mark the assets to the market to the prevailing throw away or unreasonably rock bottom prices, as the owner of the instrument may not be willing to part with or sell the asset in advance of meeting the liability at those values. As most of the value of assets and liabilities, which determine the true net worth of a business entity, are stated at historical cost, the current value of net worth is hard to find out. In the IFRS mode, financial assets are initially recognised at the fair value and later on the loans and advances as well as investments made with the intention of holding till maturity date are to be measured at amortised cost using effective interest method and all others at the fair value method.

Irrespective of the intention of the owner not to sell the asset at distressed value, liquidity pressure may compel to make the forced sales and any accounting methodology that fails to bring out the liquidity risk, in similar way to fair value accounting norms, is not worth the salt and in the interest of various stakeholders, as Corporate Governance comes into play.

When many of the financial products do not have an active

market, many methods and inputs for estimating the fair value may not be that much reliable. Therefore, one may think of limiting the application of fair value concept, only to those assets and liabilities that have real and determinable market value coupled with disclosure requirements. There is no point in blaming or finding fault with the fair value concept, for it is only a tool to determine the shortcomings in the instrument.

Fair value measures reflect the most current and complete estimations of the value of the asset or obligation, including the amounts, timings, and risk involved in the future cash flows attributable to the asset or obligation. Opponents of fair value reporting argue that measuring and recognising assets and liabilities at fair value in the financial statements introduces volatility into the financial statements. It is difficult to argue in favour of historical cost measurement in situations where IFRS mandates fair value measurement. Almost every IFRS that requires fair value measurement provides guidance on how to estimate the fair value.

### IFRS Journey and Deadline

The journey to IFRS needs to be meticulously planned and carefully executed. Successful implementation of IFRS would entail usage of IFRS as the basis for primary financial reporting on daily basis and also performance tracking. Hence, wisdom suggests that it is better to adopt IFRS across the board, instead of in a phased manner. The perception is that IFRS is relatively less prescriptive and distances from prescribing specific accounting treatment. To question whether India is prepared to adopt IFRS from April 1, 2011 is to demean the accounting profession and the professional skills of analysts. It is true that the fair value measurement of assets and liabilities poses a challenge, but the Indian accounting profession is capable of handling it.

As convergence is imminent and transition time is limited, besides being now on the reducing trend, the journey of claiming the mountain of IFRS norms should begin now, before it becomes too late. It is a food for thought for all concerned such as regulators, corporate/banks, accounting firms, standard setters, etc to draw a detailed roadmap for smooth transition of IFRS norms. The Core Group specially formed for evolving a roadmap for transition to IFRS has suggested certain time table, depending on the size of the company, category or sector to which the company belongs, etc. in broadly three phases, as tabulated herein below:

ENTITIES	TRANSITION w e f
Companies with over ₹1,000 cr Net Worth and Companies Listed in Sensex - 30 / NIFTY - 50 / Overseas Stock Exchanges	01. 04.2011
Listed and unlisted companies with a Net Worth of > ₹500 cr	01. 04. 2013
All listed companies with a NW of < or = ₹500 cr	01. 04. 2014
SMEs and unlisted companies with a NW < or = ₹500 cr	Presently exempted
Banking and Insurance Companies	Separate roadmap to be drafted

Most of the entities may choose to publish IFRS numbers for 2011-12, with comparatives data for 2010-11. Accordingly, accounts preparation for 2010-11 may have to be on two modes, viz Indian GAAP to satisfy statutory reporting and IFRS to enable comparative numbers (as previous year reporting while preparing accounts for 2011-12). This is more logical and meaningful for all the users of the audited financial data. In the process, quarterly financial reporting may be attempted from June 2011, i.e first quarter of the FY 2011-12. Apart from this, interim financial reporting mechanism should also be fine-tuned.

Moreover, in the recently concluded G-20 Summit held in Pittsburgh, US, members reassured the international forum that globally, convergence to IFRS would be achieved by June 2011 and India's efforts are in tune with this.

As could be made out, India has clearly deferred transition by at least one year, if not more, for the initial transition date was envisaged at 1-4-2010. Perhaps, looking at the ground realities and lack of preparedness on the part of India Inc., the authorities concerned decided for deferment. Whatever said and done, it is a smart move to defer the issue, instead of landing up in mess as far as implementation of IFRS is concerned. The huge cost of implementation would initially be borne by the large entities while the smaller one would incur lower cost as they need not reinvent the wheel of accounting standards through the IFRS learning mode. It is estimated that while the initial cost of putting in place the IFRS mode is expected to be around 0.40 percent of annual turnover with the recurring cost at 0.09 percent. But more than the annual turnover, it is the IT platform and skill set of employees that would determine the cost of implementation.

**In the normal market, fair value accounting would not have been a subject of debate. However, in a boom or bust period, fair value accounting may result in notional or accounting gain or loss as eventual settlement of price of the subject financial instrument, be it asset or liability, could be substantially different. If a business entity extends credit to its clients for a period of six months or more, then the nominal or absolute amount receivable after that period would normally be different from the fair value of the amount.**

Entities, which are not yet brought under the above referred roadmap, particularly subsidiary, joint ventures, or associates of the parent companies covered therein can use their parent company's IFRS accounts reported in consolidation purpose, for the stand-alone statutory reporting of financials.

InACT is a body of finance professionals, engaged in institutionalisation of the best practices among various corporates in accounting, corporate governance, knowledge sharing, risk management, treasury management etc. Speaking at a conference organised by Dun & Bradstreet (D & B) a global information knowledge and insight, in association with Indian Association of Corporate CFOs and Treasurers (InACT), several corporates here expressed their intention are mulling to approach the International Accounting Standards Board (IASB) to seek deferment in implementation deadline of IFRS. One of the issues that come out strongly is that the India Inc. is not ready to implement IFRS by 2011.

### **Banks and IFRS**

It may be interesting to know as to how the financial institutions such as banks adopt themselves to the IFRS requirements, as it would be a very challenging assignment, as they have to move from the existing accounting practices that are driven more by the regulators. Presently, banks provide for and make provisions based on the RBI guidelines, which are prescriptive in nature. Contrast to this, evaluation of loan provisioning is a judgmental process and is a case by case analysis. The quantum of provisioning and the coverage of the same have become a dynamic process, depending on the financial market and economic environment. Major components of the Balance Sheet items would have to be fair valued compared to the current practice of carrying it at the historical cost. Fair value methodologies need to be validated, time tested and back tested in current market conditions.

Business and financial risk assessments do not undergo radical transformation due to the new information requirement disclosure. What gets reduced is actually information risk, which is the fear of the unknown. It may be understood that the rating agencies of repute do not just go by the figures disclosed, but make adjustments to derive correct information. IFRS does not recognise the adjustments resulting from court schemes and pronouncements.

The provisioning requirements in banks normally range from 10 to 100 per cent of the balance outstanding depending on the quality as well as value of asset on security front and the age of the impaired asset. Further, on the basis of board approved policy on provisioning, banks can make additional specific provisions as could be noticed from the risk perceived in the portfolio, as what is prescribed by the regulator, viz RBI, is the minimum one. In view of this flexibility to banks, heterogeneous provisioning practice has set in.

A graded provisioning mechanism starting from 20 per cent being graduated to 100 per cent over a period of five years may be thought of as the new Provisioning Coverage Ratio (PCR) of 70



per cent is being imposed on banks by RBI. The status with regard to floating provision mechanism can be left to the bank concerned depending on the profit generation. As far as impaired asset on account of default due to fraud, misappropriation of funds, etc may attract full provision, ab initio, as per the present practice.

### Conclusion

Preparation, compilation and publication of financial data of a business entity would serve better if common standards are used for better reading and comparability, particularly during the inter – company or intra-industry comparison. With the 1<sup>st</sup> April, 2011 deadline for implementation of International Financial Reporting Standards (IFRS) in India getting closer, Chief Financial Officers are having a tough time making their companies adhere to the mandate. Fair value accounting concept is yet to be assimilated even by those in the accounting and auditing field and availability of specialist may be quite inadequate. Nevertheless, convergence approach implies that the authorities allow some acceptable differences in measurement, recognition, presentation, disclosure, etc. during the transition period.

It is not known whether the regulatory prescriptions on provisioning, being revised from time to time, would eventually meet and match the requirements mandated in the IFRS norms. Therefore, it is understood that the IBA has sought for the postponement of implementation of IFRS amongst banks, from the slated date of April 2011. This is because, banks need to build the requisite financial models and put in place assessment methodology for the loan and investment value erosion, by truly assessing the recoverability and timing of future cash inflows from the financial asset. The valuation methods adopted by banks need to be validated and back tested fully under the dynamic market environment. A dry run of reporting of accounts under IFRS mode would throw the issues to be ironed out while rolling out. A lackadaisical approach coupled with the mindset that the subject matter of reporting of accounts under IFRS mode can be best left to consultants, would not take the organisation to any way near the compliance mode.

Indian Accounting systems should move from rule based to principle based and hence, a number of policy decisions in the banks, regulatory requirements by multiple regulators and

“ A graded provisioning mechanism starting from 20 per cent being graduated to 100 percent over a period of five years may be thought of as the new Provisioning Coverage Ratio (PCR) of 70 per cent is being imposed on banks by RBI. The status with regard to floating provision mechanism can be left to the bank concerned depending on the profit generation. As far as impaired asset on account of default due to fraud, misappropriation of funds, etc may attract full provision, ab initio, as per the present practice. ”

accounting body are to be dovetailed in proper co-ordination, before the banks and Indian companies plunge into the proper implementation of IFRS norms and implement it quite smoothly, through a properly laid IFRS roadmap by planning the transition properly. In the run up to the IFRS implementation, some of the statutory acts/laws, such as Companies Act, Income Tax Act, Banking Regulation Act, Direct Tax Code, etc. need to be amended/modified for which an active role should be played by the government. ■

# Accounting for Intangibles with Reference to IFRS Convergence: Some Relevant Issues



The purpose of Financial Accounting is to provide users of financial statements with information that is useful for efficient decision making. Financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit, and similar decisions. Consequently, any event that is likely to affect a firm's current financial position or its future performance should be reflected in its annual accounts. During the last two decades there has been a progressive movement into a knowledge-based, fast changing, technology intensive economy in which investments in human resources, information technology, research and development, and advertising have become essential in order to strengthen the firm's competitive position and ensure its future viability. Furthermore, the implementation of IFRS is set to happen in India in phased manner from next year. In this context, the valuation and accounting for intangibles have become the most critical issue. As intangible assets are intangible, they are also tricky to define and quantify. This study deals with a comprehensive discussion about the economic nature, definition and classification of intangibles, a brief discussions about the International Financial Reporting Standards and the relevant provisions in the IFRS regarding the accounting for intangibles.



## Dr. Pranam Dhar and Dr. Jafor Ali Akhan

*(The authors are Readers in Commerce at West Bengal State University- Barasat, and Kabi Nazrul College, Muraroi, Birbhum respectively. They can be reached at pranamdharit@yahoo.com)*

## Backdrop

The purpose of Financial Accounting is to provide users of financial statements with information that is useful for efficient decision making. According to the FASB (1978, par. 34), financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit, and similar decisions. Consequently, any event that is likely to affect a firm's current financial position or its future performance should be reflected in its annual accounts. Investors and

creditors have traditionally been considered as the main users of accounting information. Since they usually have no direct control on the process of preparation of accounting statements, financial accounting standards have been developed in order to ensure that stakeholders are provided with relevant, reliable and timely information (representing the true and fair view of the firm's financial position), on the basis of which they can make efficient allocation decisions (FASB, 1980). Within the firm, accounting information is also

essential for efficient decision making; managers need timely and reliable information in order to carry out the budgeting process and implement control mechanisms. The traditional accounting model has become insufficient because innovative activities are not considered as strategic variables. Technological development is a challenge for accounting not only in the area of financial reporting, but also in the realm of management control (Cañibano and Sanchez, 1992).

During the last two decades there has been a progressive movement into a knowledge-based, fast changing, technology intensive economy in which investments in human resources, information technology, research and development, and advertising have become essential in order to strengthen the firm's competitive position and ensure its future viability. As Goldfinger (1997) states, the source of economic value and wealth is no longer the production of material goods but the creation and manipulation of intangible assets. In this scenario, firms feel a growing need to make investments in intangibles, that in most cases are not reflected in the balance sheet but on which the future success of the company is based to a large extent. As a consequence, financial statements are becoming less informative on the firm's current financial position and future prospects (Lev and Zarowin, 1998). A sign of the loss of relevance of accounting information is the increasing gap between the market value and the book value of equity of most companies in most countries. Lev and Zarowin (1998) document a significant increase in the market-to-book ratio of US firms, from a level of 0.81 in 1973 to a level of 1.69 in 1992 (which means nearly 40 per cent of the market value of companies is not reflected in the balance sheet). In their view, this represents not only a revolutionary change in the process of economic

**“The implementation of IFRS is set to happen in India from next year. This will create tremendous opportunity for fair valuation work. It is an area most corporate houses need to start addressing very proactively. It requires a lot of efforts as one has to be a mind reader sometimes to carry out a fair valuation. Again, valuing intangibles is always a grey area as we don't get to do too much intangible valuation work in India. It is a fascinating science.”**

value creation, but also a decline in the value relevance of traditional financial measures. In other words, the traditional accounting model, developed to fit firms whose activity is primarily of a manufacturing or mercantile nature, needs to be modified or at least broadened to reflect intangibles, so as to enhance the usefulness of accounting information. According to Vickery and Wurzburg (1992), there are strong arguments for rethinking the measurement and treatment for a range of intangibles. Among the new challenges faced by the accounting standard setters are how to account for alliances and partnerships, the use of financial instruments and investments in intangible assets (Swieringa, 1997).

The growing number of mergers and acquisitions, both at the domestic and transnational level, is another factor that has highlighted the relevance of goodwill and the problems of how to account for it (Gray, 1991). Camino and Trecu (1995) state that a significant number of the mergers, acquisitions and joint ventures taking place at the international level are primarily driven by the intention to exploit a competitive advantage based on the existence of technology, knowledge and other intangible assets. The existence of significant differences in

the criteria adopted for the recognition, measurement and depreciation of intangible assets across countries, may affect the ability of certain firms to compete for capital in financial markets. Full expensing of goodwill would penalise firms operating in some countries when competing with a foreign company for a business acquisition, as its reported earnings would be lower after the combination (Johnson and Tearney, 1993). Managers need to identify their firms' fundamental value drivers, enhance their impact on the future performance of the organisation, and implement controls to protect them. Among those value drivers, intellectual capital is fundamental. In order to assist the managers of business enterprises and their providers of capital in their decision making processes, standard setting bodies currently face the need to develop guidelines for the identification of intangible elements, a set of criteria for their valuation, new standards for financial reporting, and guidelines for the measurement and successful management of intangibles within the firm.

Furthermore, the implementation of IFRS is expected to happen in India by 2011. This will create tremendous opportunity for fair valuation work. It is an area most corporate houses need to start addressing very proactively. It requires a lot of efforts as one has to be a mind reader sometimes to carry out a fair valuation.

Again, Valuing intangibles is always a grey area as we don't get to do too much intangible valuation work in India. It is a fascinating science. Different intangibles are valued using different approaches. Like, for instance, a brand is typically valued using a royalty savings method and the implication is that if you own a brand you do not have to licence it from somebody. And what we tried to do once is that take a situation where one had to

licence the brand how much royalty would you have had to pay. And for that you look at certain comparable transactions for which there are certain databases which are available as you cannot simply take a transaction that happened with a particular brand as your comparable benchmark. You have to apply judgement again. While certain things may be comparable, there would be others that may not be. That's one method of doing it.

### Accounting Harmonisation Initiatives & Accounting For Intangibles

During the last decades, countries practising the Continental accounting tradition have been developing towards, and strongly influenced by, the Anglo-Saxon standard (Smith, 2006). This became especially clear in the year of 2002, when, in its pursuit to create a single capital market, the European Union announced the adoption of the International Financial Reporting Standard (IFRS) developed by International Accounting Standard Board (IASB). The standard was to be implemented from 2005, and is to a large extent based on the Anglo Saxon accounting tradition and previous work by the Financial Accounting Standards Board (FASB). One of the standards that have been frequently discussed since the implementation of IFRS is the one regulating intangible asset; IAS 38. Today, companies consist of an increasing amount of intangible assets. For example, Doyle (2000) & Kanodia (2004) states that in some companies, intangible assets are today the majority of a firms total assets. Gupta et al (2004) states that intangible assets are increasingly important to shareholders, and Riahi-Belkaoui (2003) declares intangibles assets to "provide a sustainable source of wealth creation for companies". Consequently, how to treat intangible assets has been a major topic of discussion for scholars

and professionals within accounting (von Colbe et al, 2005, Kanodia, 2004). For example, Lev (2001) describes that "the accounting profession struggles with the task of determining the financial value of intangible assets". In order to examine how the IFRS regulation has been received in different markets, it was preferred to examine markets that previously were regulated in different ways. Many scholars have criticised the way IFRS deals with goodwill and other intangible assets with unlimited life span. For example Moehrle & Reynolds (2001) argue that impairment-testing gives a less comprehensive effect on the result, and Huefner & Largay (2004) also state that due to the effect on the result, it thereby lessens the possibility to analyse the result over time. Further, the valuation of intangible assets has also been frequently discussed. For example Choi et al (2000) have shown that depending on which valuation method that is used, different values will be given. They also shows that companies with high contents of intangibles are more likely to give an incorrect picture in its financial report. Also Kumar (2005) discusses the problems of valuing intangibles, and points out that biotechnology companies, due to their high content

**Withwell et al (2006) states that the confusion around intangible assets could potentially have a large impact on the market economy, and that it has resulted in a number of recent accounting scandals. Further, they argue that "over-valuation of intangible assets was the principal cause of corporate crashes such as WorldCom and Enron in the USA, and HIH and One Tel in Australia". An agreed way of handling intangibles would decrease the risk of this happening again.**

of intangibles, are especially difficult to value. The relation between market value of equity and book value of equity has also been of interest for scholars. Among them are Stewart (1997), Kaplan (1998), Fincham & Roslender (2003) and Kanodia (2004) who have illuminated the difference between these two values, and suggested different explanations for the discrepancies. Fincham & Roslender (2003) have argued that the difference can be explained as the intangible assets of a company. Gauffin & Nilsson (2006) have criticised the way companies account for intangible assets in relation to the acquisitions. Further, they argue that a common practice of how intangibles should be accounted for is needed. This is something also discussed by Whitwell et al (2006), who argue that there are large flaws in the accounting of intangibles due to the lack of appropriate regulation and controls. Withwell et al (2006) states that the confusion around intangible assets could potentially have a large impact on the market economy, and that it has resulted in a number of recent accounting scandals. Further, they argue that "over-valuation of intangible assets was the principal cause of corporate crashes such as WorldCom and Enron in the USA, and HIH and One Tel in Australia". An agreed way of handling intangibles would decrease the risk of this happening again (Withwell et al (2006).

### Research Questions

The above discussions have shown that there are a number of challenges when it comes to accounting of intangible assets, and naturally with the IFRS regulation. The discussion on harmonisation among countries agreeing on one standard set the path to investigate how the IFRS implementation has been received different markets. Based on this, and the different scholars discussing the

high content of intangibles in almost all the industries, lead to the main question of this study has been defined as:

- *What are the relevant provisions in the IFRS Regulations for valuing and accounting the Intangible Assets ?*
- *Whether these provisions have been accepted to be followed by the Indian corporate sector in the forthcoming implementation stage around 2011 ?*

### Objectives of the Study

Keeping the above research questions in mind, the purpose of this study is to gain further knowledge in how the IFRS implementation has affected accounting practice, specifically in respect of accounting and valuation of intangibles. Therefore, this study intends to deal with the following objectives:

- A comprehensive discussion about the economic nature, definition and classification of intangibles,
- A brief discussions about the International Financial Reporting Standards and the relevant provisions in the IFRS regarding the accounting for intangibles,
- To have a close watch to the fact whether the Indian corporates are ready to implement the provisions regarding the valuation and accounting of intangibles in the forthcoming years.

### Intangibles Defined

As intangible assets are intangible, they are also tricky to define and quantify. Encyclopedia Britannica defines "intangible" as something not tangible, and "incapable of being perceived by the sense of touch". Further, they define "intangible assets" as something "existing only in connection with something else, or as the goodwill of a business".

According to the SFAC 5 (FASB,

1984), the balance sheet does not report all assets and liabilities of the firm, but reflects only those meeting specific recognition criteria. The critical issue in reporting intangibles is to determine what intangible assets are, that is, under what circumstances an intangible element may be considered as an asset for the purposes of accounting recognition and disclosure. For an item to be included in the balance sheet, it must match four requirements: First, it must qualify as an element of financial statements, either asset or liability. Second, it must have a reliably measurable relevant attribute. Third, the information provided by the item must make a difference in users' decisions; and fourth, the information must be representationally faithful, verifiable and neutral. Intangible assets are often identified (with goodwill) as the excess of the cost of an acquired company over the value of its tangible net assets. In most cases, intangibles are simply defined as (capital) assets that lack physical substance but which are likely to yield future benefits.

According to the FASB's (1985a) SFAC 6, par. 25, assets are probable future economic benefits controlled by and accruing to a particular entity as a result of past transactions or events. Although there seems to be a general agreement in the accounting community that whenever those probable future economic benefits lack physical form, they should be considered as intangible assets, there does not seem to be any widely accepted precise definition of intangible assets in the accounting literature. A major problem with intangible assets is that they are often difficult to identify separately, and thus, may not match one of the fundamental requirements for accounting recognition. It is difficult to separate intangible assets from other intangible assets and from current expenditures. Moreover, intangibles are nonphysical in nature and may be considered

not to follow the same patterns of depreciation as tangible assets. Therefore, some as Hendriksen and van Breda (1992). argue that standard valuation procedures developed for tangible assets may not be applicable. Intangible assets are divided into two main categories: goodwill and other identifiable intangibles. There are two basic views of goodwill: it may be understood as the consequence of a firm's above-normal ability to generate future earnings, or as a set of assets controlled by an acquired company but not reported in its financial statements.

Identifiable (separable) intangibles are those which can be sold or acquired separately (NZSA, 1988, par.4.2). However, certain standard setting bodies such as the ASB, support the idea that all intangibles should be kept under the umbrella of goodwill, on the grounds that it is unlikely that they can be sold without selling the whole business (Scicluna, 1994). Napier and Power (1992) make an interesting distinction between *entry separability* and *exit separability*. Entry separability means that the asset can be identified as it is produced or acquired by a firm: it therefore requires that the costs of production or acquisition can be accurately assessed and identified with the asset. This idea is present in all accounting standards such as ED52, (ASC, 1990), that require the historical cost of an intangible asset to be ascertainable, as a basic premise for recognition. On the other hand, exit separability implies that the asset can be traded separately from other intangibles of the firm or from the firm as a whole. This is the notion of separability underlying SSAP 22 (ASC, 1989, par. 27). These and other issues are in the center of the current debate<sup>5</sup> on intangibles. It appears that a generally accepted definition of Intangible Assets should have been the necessary starting point of that debate. Although there are certain

items (such as goodwill, intellectual capital, human capital, organisational innovation, investments in R&D and advertising, brands and patents) which are generally considered as intangible assets of firms, there seems to be little agreement in the literature as to what exactly intangibles are, when they should be recognised, whether or not they should be reported in the financial statements, how they should be measured, accounted for and depreciated. Intangible assets are usually defined (as in Belkaoui, 1992), as assets which lack a physical substance, but result from legal or contractual rights and are likely to produce future benefits. Belkaoui distinguishes two main types of intangible assets: identifiable intangible assets such as patents, and unidentifiable assets, such as goodwill. As White, Sondhi and Fried (1994) state, *in most cases, goodwill and other intangible assets arise as residuals in purchase method acquisitions, and they represent the portion of the purchase price that cannot be allocated to the tangible assets. Goodwill represents the premium paid for the target's reputation, brand names, or other attributes that enable it to earn an excess return on investment, justifying the premium price paid. Hence the name of goodwill.*

Australian intangibles exposure draft, AARF ED 49 (1989) states that intangible assets means non-monetary assets without physical substance and includes but is not restricted to brand names, copyrights, franchises, intellectual property, licenses, mastheads, patents and trademarks. In our view this definition is not adequate, as non monetary assets without physical substance include tangible assets such as prepayments and long-term investments. Hendriksen (1982) stresses that the lack of physical substance may not be considered as the main difference between tangible and intangible assets. Conversely,

he suggests that the most important single attribute of intangibles is the high degree of uncertainty associated to the future benefits expected from them.

The Intangibles Research Center of the Stern School of the New York University provides a broad definition of intangibles as *nonphysical sources of future economic benefits to an entity or alternatively all the elements of a business enterprise that exist in addition to monetary and tangible assets. They also provide a narrower definition of intangibles as nonphysical sources of probable future economic benefits to an entity that have been acquired in an exchange or developed internally from identifiable costs, have a finite life, have market value apart from the entity, and are owned or controlled by the entity.*

Egginton (1990) proposes that tangible assets are those which entail legal rights in relation to specific persons (real or corporate) as well as assets with a physical existence. He defines intangible assets as those which either entail legal rights in relation to persons at large (such as patents or trade names usually referred to as separable intangible assets), or entail expectations of economic benefits which carry no legal right (goodwill).

In 1992, the OECD suggested intangible investments cover all long-term outlays by firms aimed at increasing future performance other than by the purchase of fixed assets. In its 1992 National Accounts, the French Statistical Institute defined intangible investment as those business expenditures, which develop the production capacity and enhance the value of the firm by creating a capital which could be depreciated or long-term tradable assets.

Also in 1992, Arthur Andersen proposed a definition of intangibles as resources controlled by the enterprise which are non-physical in nature, capable of producing future economic net benefits and protected legally or

through de facto right.

Stickney and Weil (1994) define intangibles as assets which can provide future benefits without having physical form. Among intangible assets, they include investments in research and development, patents, advertising and goodwill.

In the final version of IAS 38, the IASC (1998) defines intangible assets as *non-monetary assets without physical substance held for use in the production or supply of goods or services, for rental to others, or for administrative purposes: (a) that are identifiable; (b) that are controlled by an enterprise as a result of past events; and (c) from which future economic benefits are expected to flow to the enterprise.* This definition, which is the central point of IAS 38, is very restrictive (and rather disappointing), as it explicitly excludes from the scope of the standard (and thus does not consider as intangible assets) some of the firms' most significant intangible investments, such as resources allocated to human resources and advertising.

A much broader view on intangibles is provided by Hendriksen and van Breda (1992), who argue that they arise when cash (or its equivalent) is expended on services. Accordingly, together with *traditional intangibles*, they list a number of *deferred charges*, which in their view have the same nature.

Vosselman (1998) proposes an operational definition of intangible investment as *comprising the current capital expenditure for (in)tangible products that became available in the period under review and that remain in use for more than one year. Notwithstanding, he acknowledges that the distinction between investment and operating costs is difficult for intangibles, as they are usually related to services.* A fundamental question remains unanswered: if intangible

assets are a relevant determinant of the value of companies, why are they not reported by all corporations and only arise in certain acquisitions? One among all the possible answers might be that we still have not proved capable to develop a generally accepted set of guidelines for the identification and measurement of intangibles and the disclosure of relevant (and not only) information on the financial position of the firm.

In sum, although most definitions seem to agree in that intangible assets are sources of probable *future economic profits, lacking physical substance, which are controlled by a firm as a result of previous events or transactions* (self-production, purchase or any other means of acquisition), there is still a need for a generally accepted definition and classification of intangible investment.

### Provisions of IFRS on Intangible Assets

IAS 38 is the part of the IFRS regulation that deals with how intangible assets, such as described in the previous section, should be treated in accounting. IAS 38 was issued in early

2004 as a part of "IFRS 3 – *Business Combinations*", by the International Accounting Standards Board. The Standard requires an enterprise to recognise an intangible asset if, and only if, certain criteria are met (Artsberg, 2005). The standard also specifies how to measure intangible assets and requires certain disclosures.

By IFRS, an intangible asset is defined as "a non monetary asset without physical substance" (IAS 38:8). Examples that are given in the standard are computer software, patents, copyrights, motion picture films, customer lists, mortgage servicing rights, licenses, import quotas, franchises, customer and supplier relationships, and marketing rights. According to Smith (2006), the central problem with intangibles is the fact that they are intangible, and how to classify and value them. Therefore, IAS 38 consists of a number of requirements in order for intangibles to be recognised. The three main ones are identifiability, control, generation of future economic benefits and reliable measurement of these benefits (IAS 38:8).

According to IAS 38:12, identifiability can be achieved in two ways. Firstly, if

the asset can be separated. Secondly, if the asset was created as the consequence of a contract or other legal rights. By separated means that the assets should be able to separate from an entity and transferred by some way, be it sold, rented, licensed or exchanged (Epstein & Miraz, 2005). The second criteria points out that even if the asset cannot be separated from the entity and transferred, it is still accepted as separable if it was created as the consequence of an action (Smith, 2006).

The control criteria are discussed in IAS 38:13-16, and is said to be met when a company controls the future economic benefits deriving from the asset. This includes that the company must be able to stop others from obtaining those economic benefits (Epstein & Miraz, 2005).

The last criteria mentioned above, of future economic benefits from IAS 38:17, states that unless the asset will create revenues, cost savings, or other benefits for the company, it cannot be recognised as an asset (Epstein & Miraz, 2005). Moreover, if the economic benefits cannot be reliably determined, it cannot be recognised on the balance



sheet. Further, the standard states that the assumptions of these cash flows must be made on probable grounds, and that the assumptions must be made with concern to all relevant and available information (IAS 38:21-23). Unless all the above-mentioned criteria are met, the cost for acquiring the asset should be expensed and not capitalised (IAS:68).

If an asset has been defined as an intangible asset and also reaches the criteria to be capitalised, the questions arise on how to determine the value of the asset. There are two different methods concerning this, based on if the asset came into the company's possession by acquisition or created by the company itself (IAS 38:38). For intangibles that were bought, there are two options here too, depending on if the asset was bought as a part of a larger acquisition or if it was only the asset that was being bought. If the asset was paid for separately, that price should be used on the balance sheet as well (Artsberg, 2005). If the asset was a part of an acquisition, the assets needs to be able to separate and be identifiable if it should be separated from the goodwill from an acquisition.

Under IFRS, internally generated goodwill can never be capitalised (Artsberg, 2005). Although, identifiable and separatable intangible assets can be capitalised under certain circumstances. All projects run within a company are divided in to either research or development phase. Projects that are labelled as research cannot be capitalised, but should be expensed (IAS 38:54). This is due to the uncertainty of them generating future benefits for the company (IAS 38:55). In contrast, projects that are labelled as development should be capitalised (Nilsson, 2005). But, if they can be classified as development depends on the character of the project. IAS 38:57 stipulates that costs can be classified as development costs

only "after technical and commercial feasibility of the asset for sale or use have been established". The meaning of this is that the enterprise must be able to demonstrate how the asset will generate future economic benefits (Artsberg, 2005).

Moreover, some types of internally generated intangible assets can never be capitalised (Smith, 2006). The standard mentions that "brands, mastheads, publishing titles, customer lists and items similar in substance" and are internally generated should not be recognised as assets on the balance sheet (IAS 38:63). Further, there are other types of costs that also never can be capitalised under IFRS, for example internally generated goodwill (IAS 38:48), "start-up, pre-opening, and pre-operating costs", "training cost", "advertising costs", and "relocation costs" (IAS 38:69). The main reason why IFRS does not allow these assets to be capitalised is that they are "complex and difficult to measure" (Srivastava et al, 1998).

After the first valuation, the company has the choice to value the asset by either a cost model, or a revaluation model (IAS 38:72). This must be done for each kind of intangible assets (Epstein & Miraz, 2005). A cost model, described in IAS 38:72, states that "assets should be carried at cost less any amortisation and impairment losses". A revaluation should be based on the price from an active market (IAS 38:75), which severely limits the possibility to use these methods for the many assets that are not frequently traded (IAS 38:78), like most intangibles (Epstein & Miraz, 2005).

Depending on the intangible, IAS also stipulates that the asset is classified as either "infinite life" or "finite life". An asset should be classified as having a finite life if it is determined to only having a limited period of benefit. Infinite life is consequently given to assets with "no foreseeable limit to the

period over which the asset is expected to generate net cash inflows for the entity." (IAS 38:88). As for assets with finite life time, they should be amortised over their expected life (IAS 38:97). However, assets with infinite life spans, should not be amortised (IAS 38:107). Instead it should be reviewed each reporting period to determine whether "events and circumstances continue to support an indefinite useful life assessment" (IAS 38:109). Both kinds of assets should also be assessed for impairment as stipulated in IAS 36 (IAS 38:111).

For goodwill, IFRS 3 is even more specific. As mentioned above, internally generated goodwill can never be capitalised. However, by IFRS 3:51, goodwill should be recognised if acquired. Further, it stipulates that it should be measured as the "excess of the cost of the business combination over the acquirer's share of the net fair values of the acquiree's identifiable assets, liabilities and contingent liabilities" (IFRS 3:51). Amortisation of goodwill is by IFRS 3:54 prohibited, and instead it should be tested for impairment as by IAS 36, at least annually.

### Questions Raised on Some Points of IFRS Provisions on Intangibles and Answers by IVSC

1. Because IAS 38 only permits intangible assets for which there is an active market to be carried at their revalued amount, and that the definition in IAS 38 of an active market includes a requirement that the assets traded are homogenous, or identical, it is necessary to further define the characteristics of assets that are "identical, similar and different".
2. Because IAS 38 effectively directs that the fair value of qualifying identical assets

is based on prices that are available to the public, valuers need guidance for which assets a valuation technique other than a straight forward price x quantity calculation may be used when valuing intangible assets under other IFRSs.

3. IAS 38 contains a precise definition of an "active market", which describes not only the characteristics of the market but also the nature of the assets traded, i.e. they must be homogenous. This has led some commentators to the view that markets that either do not meet the criteria in IAS 38 or involve heterogeneous assets should logically be termed "inactive markets". Others consider that this is misleading, as activity in markets is not dependant upon whether the goods being traded are similar, but upon supply and demand and the extent to which either is elastic. They point to the fact that there are many active markets involving assets that are not homogeneous.
4. Some experts consider that in order to improve consistency of intangible asset valuations prepared for use under IFRSs, it is necessary to explore and define what is meant by a "market" and by sub descriptions such as "active", "inactive", "accessible", etc.

Exposure Draft GN 16 for Valuation of Intangible Assets for IFRS Reporting Purposes, issued by the International Valuation Standards Council (IVSC), in January, 2009, is intended to answer the above questions and also to provide valuers with a briefing of the valuation objectives under various IFRSs. It is not intended to be a guide to the accounting requirements. Consequently, only selected extracts

from relevant IFRSs documents have been referred to, and elsewhere the IFRSs requirements have been paraphrased or précised.

### Provisions of ED GN 16 For Valuation of Intangible Assets for IFRS Reporting Purposes, Issued by IVSC

#### (1) Intangible assets arising from a business combination recognised in accordance with IFRS 3 and IAS 38: Relevant requirements of IFRS 3 and IAS 38 -

An amended version of IFRS 3, issued in January 2008 and becoming effective on or after 1 July 2009, requires that intangible assets arising from a business combination are recognised at their fair value at the acquisition date irrespective of whether the assets had been recognised by the acquiree before the business combination. In practice, insignificant separately identifiable assets may not need to be separately valued.

IAS 38 suggests that that if an intangible asset arises from a business combination, then sufficient information will exist for the fair value of the intangible to be reliably measurable. The standard also notes that when there is a range of possible outcomes in the estimates used to measure fair value, uncertainty enters into the measurement of fair value. However, the standard makes clear that just because an intangible asset may be difficult to value that does not mean it should not be recognised at fair value.

Appropriate methods for the valuation of intangible assets are set out in GN 4. The valuation inputs to be used in whichever valuation approach is adopted should reflect those that would be

made by market participants.

#### (2) Measurement of goodwill

Under IFRS 3, the initial measurement of the goodwill arising from a business combination is the difference between A and B as shown below.

"A" comprises:

(a) the consideration transferred, the fair value of any equity issued as consideration and any liabilities or obligations assumed; (b) the amount of any non-controlling interest in the acquiree, calculated as set out and (c) the acquisition-date fair value of the acquirer's previously-held interest in the acquiree, if any.

The "consideration transferred" is the total amount of cash plus the fair value of any assets used as consideration

"B" comprises:

the net sum of the acquisition-date fair values of the identifiable assets acquired and liabilities assumed.

The reporting entity can choose to measure the amount of any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's identifiable net assets.

If the amount of the non-controlling interest is measured at fair value, it will include any goodwill attributable to the non-controlling interest.

If the amount of the non-controlling interest is measured at the proportionate share of the acquiree's identifiable net assets, it will exclude any goodwill attributable to the non-controlling interest.

Thus, there is a choice as to whether goodwill is recognised in the balance sheet at: (a) the full amount of goodwill relating

to both the stake the acquirer has purchased and the stake, if any, that the acquirer has not purchased and remains as a non-controlling interest; or (b) the acquirer's share of the goodwill, i.e. that relating only to the stake in the acquiree that the acquirer has purchased.

**(3) Aggregation of intangible assets for valuation purposes**

IAS 38, paragraphs 36 and 37, addresses the circumstances in which it is appropriate to combine certain tangible and intangible assets for the purposes of determining their fair value following a business combination. IAS 38, paragraph 36, notes that it is appropriate to combine an intangible asset with another intangible asset or with a tangible asset, if the underlying intangible asset is not separable and its fair value is not reliably measurable. The paragraph cites:

**(a)** as an example of intangible assets that may not be separable individually, a magazine's publishing title and its subscriber database; and **(b)** as an example of a tangible and intangible asset that may not be separable individually, a trademark for a natural spring water and the spring itself.

IAS 38, paragraph 37, considers the term 'brand'. It notes that this term is a general marketing term that is often used to refer to a group of complementary assets such as a trademark and its related trade name, formulas, recipes and technological expertise. The paragraph notes the following. **(a)** "The acquirer recognises as a single asset a group of complementary intangible assets comprising a brand if the individual fair values of the complementary assets

are not reliably measurable". This is a required aggregation of the underlying assets. **(b)** "If the individual fair values of the complementary assets are reliably measurable, an acquirer may recognise them as a single asset provided the individual assets have similar useful lives." This is a permitted aggregation of the underlying intangible assets.

The aggregation of portfolios of intangible assets such as these allows cancellations, renewals and default levels on contracts to be assessed on a portfolio basis rather than at an individual asset level. In this way, historical patterns for a portfolio can be used to predict future expectations. This is likely to lead to more robust assumptions than trying to predict patterns without using portfolio evidence.

The valuer should take account of the extent to which the individual intangible assets share the same characteristics in deciding how this aggregation should be effected. Any such aggregation, the nature of the underlying assets, and the characteristics of the underlying assets rendering aggregation appropriate for valuation purposes should be documented in the Valuation Report.

**(4) Cross checking the valuation**

Prior to performing any valuation of the intangible assets in a business combination, it is common practice to value the whole of the acquired business. This will necessitate forecasting cash flows for the business and discounting them at a suitable cost of capital to reflect the risks specific to the acquired business. If the cash flows are discounted at the weighted average cost of capital of the acquired business, the net present value arising from

the DCF exercise represents the 'enterprise value' of the business. The value of the equity in the acquired business is determined by deducting the net debt from the enterprise value. This should be compared with the price paid for the equity purchased.

If the two figures are relatively close, the projections and the discount rate used in the valuation of the business are effectively supported by the price paid for the acquisition. In this case the projections and the discount rate can be used as starting points in the determination of the corresponding valuation inputs in the valuation methods applied to the intangible assets. In the case of the discount rate, adjustments will be required, to make the discount rate suitable for intangible assets rather than the business as a whole.

If the DCF-derived value for equity and the price paid for the combination are not relatively close, this would suggest that one or more of the following has occurred (a) the projections used to value the business were not realistic; (b) the discount rate used to value the business was not realistic; (c) the price paid for the business was low and a bargain purchase has been achieved; or (d) the price paid for the business was high and the purchase may have been made at an overpayment.

In this case, judgement has to be used to determine whether the projections and/or discount rate should be adjusted before using them as starting points for the determination of the corresponding valuation inputs in the valuation of the intangible assets. The internal rate of return implicit in the acquisition of the



business or the weighted average return on assets could be also be used to provide support for both the projections and the discount rate used in the valuation.

**(5) Valuations in accordance with IAS 36, 'Impairment of Assets' Relevant requirements of IAS 36**

IAS 36 requires that intangible assets are carried in the balance sheet at no more than their recoverable amount. IAS 36 sets out a test, 'the impairment test', which reporting entities must perform in order to ensure that their goodwill and identifiable intangible assets are not carried in the balance sheet at more than their "recoverable amount".

IAS 36 requires: (a) identifiable intangible assets with an indefinite life, and hence which are not amortised, to be tested for impairment annually; (b) purchased goodwill to be tested for impairment annually; and (c) identifiable intangible assets with a finite life, and hence which are amortised over that finite life, to be tested for impairment only when one or more indicators of impairment as defined by IAS 36 are present.

The recoverable amount is defined as the higher of fair value less costs to sell or value in use. If the basis of value measured

results in a value at least as high as the carrying value of the asset, the impairment test is passed. The difference between these valuation approaches is now discussed.

**(6) Testing intangible assets for impairment by reference to their fair value less costs to sell**

IAS 36, paragraph 25, notes '*the best evidence of an asset's fair value less costs to sell is a price in a binding sale agreement in an arm's length transaction, adjusted for incremental costs that would be directly attributable to the disposal of the asset*'. Thus, if there is a binding contract in place for sale of an asset, either individually or as part of a group of assets, that price is normally taken as evidence of value and no valuation techniques are required.

IAS 36, paragraph 26, notes "if there is no binding sale agreement but an asset is traded in an active market, fair value less costs to sell is the asset's market price less the costs of disposal." Thus, for (those rare) intangible assets traded in an active market for which there is no binding sale agreement, fair value less costs to sell will be measured by reference to the market price. By definition, this will be available at the individual asset level for an asset traded in an active market.

IAS 36, paragraph 27, notes "*if there is no binding sale agreement*

*or active market for an asset, fair value less costs to sell is based on the best information available to reflect the amount that an entity could obtain, at the balance sheet date, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal. In determining this amount, an entity considers the outcome of recent transactions for similar assets within the same industry.*"

The valuation inputs to be used are therefore those that would apply to market participants. Appropriate methods of valuation are set out in GN 4. The costs of disposal will include not only the transaction costs, eg any advertising, commissions or legal fees, but also any directly consequential costs, eg costs involved in separating the asset or cash generating unit from the remainder of the business.

As recent transactions must be considered when assessing fair value, the level of aggregation implicit in those transactions should be considered and compared to the appropriate level of aggregation to be used in estimating the fair value of the subject asset or assets.

As set out in IAS 36, in some cases, fair value less costs to sell may be determined for the cash generating unit of the reporting entity that contains the subject intangible asset. In such cases, the techniques used to value the cash-generating unit should be those appropriate to valuing a business. These are described in IVS Guidance Note 6, 'Business Valuation'. Valuation inputs used in the business valuation should again be consistent with those that would be used by market

participants.

IAS 36 requires that where impairment is tested by reference to a cash-generating unit (CGU) the fair value less cost to sell determined for the CGU should be compared with the sum of the carrying values of the assets in the CGU. Care should be taken that comparisons are performed on a consistent basis so that, for instance, if debt is deducted in valuing the CGU, debt is also deducted in determining the carrying value of the CGU.

**(7) Testing intangible assets for impairment by reference to their value in use**

Estimating the value in use of an asset involves estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal. An appropriate discount rate is then applied to those future cash flows. IAS 36 para 30 provides that the following elements shall be reflected in the calculation of an asset's value in use: (a) an estimate of the future cash flows the entity expects to derive from the asset; (b) expectations about possible variations in the amount or timing of those future cash flows; (c) the time value of money, represented by the current market risk-free rate of interest; (d) the price for bearing the uncertainty inherent in the asset; and (e) other factors, such as illiquidity, that market participants would reflect

in pricing the future cash flows the entity expects to derive from the asset.

The value in use of the asset is then determined using DCF techniques. IAS 36, paragraph 33 et seq., provides guidance on how the cash flows should be forecast and how the discount rate should be determined.

**(8) Valuations in accordance with IFRS 5, Assets Held for Sale and Discontinued Operations**

Under IFRS 5, intangible assets whose carrying amount will be recovered principally through a sale transaction rather than through continuing use, are recognised in the balance sheet at "fair value less costs to sell". There are specific requirements set out in IFRS 5, especially paras 6 et seq. and 16 et seq., that provide further guidance on determining when an asset's carrying amount is expected to be recovered principally through a sale transaction rather than through continuing use.

As fair value less costs to sell requires market participant inputs for the valuation input parameters, the appropriate level of aggregation in the measurement of intangible assets carried at fair value less costs to sell is the level at which fair value less costs to sell can be measured for market participants.

Appropriate methods for the valuation of such intangible assets are set out in GN 4. The valuation inputs to be used are those that would apply to market participants.

In certain situations, an intangible asset is not classified as held for sale on its own but in conjunction with other assets and liabilities. In such cases, the intangible asset is part of a "disposal group" as

described in IFRS 5 at para 4 and fair value less costs to sell should be determined for the disposal group containing the intangible asset rather than the intangible asset alone.

The techniques set out in GN 6, 'Business Valuation', should be followed for determining the fair value of a disposal group.

**(9) Revaluations of intangible assets in accordance with IAS 38, Intangible Assets**

Under IAS 38, intangible assets may be carried in the balance sheet under either the cost model or, provided certain conditions are met, the revaluation model.

The revaluation model may only be used for those assets for which fair value can be determined by reference to an "active market".

In practice, it is rare for intangible assets to come from an active market and extremely rare for intangible assets to be revalued to fair value in the balance sheet, and since only assets with quoted prices may be carried at current value, valuation techniques are redundant.

**(10) Reporting the Valuation**

A valuation report should be prepared in accordance with IVS 3 Valuation Reporting.

**Valuation of Intangibles in India as a Late Adopter of IFRS**

Sooner than later Indian companies will have to adapt to International Financial Reporting Standards (IFRS), and align with the accounting standards of the rest of the world.

There are various reasons that make us think why valuation services are going to be extremely important in India. The most obvious one being the fact that Indian companies are going global in their outlook whether they are accessing capital or making



acquisitions abroad. Secondly, international accounting standards are more fair value-oriented. So you don't state your balance sheet based on historical cost but based on what is the true and fair value of your assets.

And as companies start doing this more and more, when they access capital in the international markets they will have to restate their balance sheets on international accounting standards thus requiring a fair valuation to be done. We entered the Indian market three months ago and have already started getting good number of enquiries and have won a few engagements too.

The implementation of IFRS is set to happen in India from next year. This will create tremendous opportunity for such fair valuation work. It is an area most corporate houses need to start addressing very proactively. It requires a lot of efforts as one has to be a mind reader sometimes to carry out a fair valuation.

For example, let's say company A wants to acquire company B. And because the company A sees certain synergies in the acquisition they are willing to pay a certain price for company B. Now those synergies may not necessarily be documented in any place and are usually known only to the management of the acquiring company. And when we do the purchase price allocation post the acquisition, we analyse and try to divide it into various components. The purpose is to understand what the management thinks they would get out of it and thus ascribe a value to it.

All of that requires much greater level of scrutiny leading to detailed, in-depth documentation of information. That is something companies will have to start thinking about from now rather than waiting for IFRS to get implemented in 2011.

The valuation work certainly revolves in and around the transaction. Usually valuation is carried out prior to

a transaction whereby the company wants to know what the right acquisition price to be paid is. That is something that makes intuitive sense. But now with the IFRS implementation, or Indian companies accessing capital abroad, one needs to carry out a valuation post the transaction as well. The purpose of this valuation is not to find out if the company paid the right price for the acquisition being made but to put together a break-up plan in terms of ascribing a value to say land and building, plant and machinery, patented technology, customer relationship and the brand.

The difference is that when you are doing the pre-valuation work the approach is to look at the company as a whole. At that point in time, the focus is more on arriving at a right price for the company. Also to be taken into account is the fact that there would be three other bidders for the same acquisition. So the price arrived at should be able to outdo the counter bids. Also, the promoters will have to ascertain on an overall basis how much value will the company get them. Say if the company is worth US\$ 150 million so the acquirer will be willing to pay US\$ 100 or US\$ 120 million for the same.

And after the acquisition is being done at say US\$ 120 million, we have to divide into various components. Earlier the acquiring company may have thought about the various synergies and the brand they will get by acquiring the company. However, how much are they paying for the various components and the brand is something they weren't really concerned about as the transaction was being looked at in a more holistic manner.

In the subsequent valuation process, since the promoter have more time and it's mainly for reporting purposes one starts stripping down various layers and try to come out with a value for each layer.



A very large amount of the work that we do is actually post transaction. The confidentiality aspect is not as crucial at this stage as relevant announcements are already being made to the public and governing authorities at large. However, there is something the Indian market still has to witness like companies operating in the international markets. Despite the confidentiality issues, in the international markets, companies are getting people like us involved even before the deal has happened in order to ascertain whether the deal will be value-accretive or value-decretive.

This is because in the international markets, the company's stock is worth whatever has been reported in the latest quarter. Let's take the earlier example of US\$ 100 million acquisition. In the post-acquisition valuation US\$ 10 million each is allocated to plant and machinery and real estate respectively. The balance is allocated to an asset called in-process research and development.

What used to happen before is that the entire US\$ 80 million would get allocated to goodwill and it would never be amortised. However, under accounting laws the acquirer is required to expense the in-process research and development cost at once. And since amortising of that

asset will have to be done immediately, it will have a significant impact on the company's profit and loss account (P&L). Hence, in spite of reporting an excellent acquisition that will eventually give the company good amount of cash flows, the P&L statement gets affected considerably as a result of this amortisation. The market perceives this as a loss-making quarter thereby affecting the stock price.

When companies like us get involved in the deal process from the beginning, we are able to tell them that certain assets are going to fall under the category that will get impaired very quickly. So we are in a position to tell the promoters that from the market perspective it may not be such a good deal or it would possibly make more sense if they paid slightly less for the acquisition.

This approach has started seeping into the company promoters' minds in the international markets since the last few years. I feel that Indian companies will soon wake up to this reality when IFRS become mandatory.

According to some accounting experts in India, they are not going to be able to change anything as there is only some amount of play in the valuation. It is a soft science involving a lot of judgement and by taking different assumptions one can make some changes to the value. But the primary objective behind this exercise is to tell the management that this is what the implication will be from an accounting perspective.

Intangible valuation work in India, is a fascinating science. Different intangibles are valued using different approaches. Like, for instance, a brand is typically valued using a royalty savings method and the implication is that if you own a brand you do not have to licence it from somebody. And what we tried to do once is that take a situation where one had to licence the brand how much royalty

would you have had to pay. And for that you look at certain comparable transactions for which there are certain databases which are available as you cannot simply take a transaction that happened with a particular brand as your comparable benchmark. You have to apply judgement again. While certain things may be comparable there would be others that may not be. That's one method of doing it.

According to the valuation experts of Intangibles, they can ask ourselves whether we can take the judgement factor out of valuation. Because judgement also means some amount of subjectivity. We have to ask ourselves whether the process can be made more objective. The issue is that in valuation, we have to take into account the future cash flows. And discount them back to the present value.

The valuation profession should be regulated better. People who do the valuations have the necessary qualification to do the job. They need to have the right amount of skills. A bill called the 'Valuation Professionals Bill,' I think, is being tabled. The idea behind it is that all the valuation professionals need to be regulated in India. They have to follow the proper guidelines.

### Concluding Remarks

We are witnessing one of the most critical times in the history of accounting. Since developed economies have become knowledge-based and technology-intensive, our view of the firm has significantly changed and new (intangible) elements have become the fundamental determinants of value. Thus far, Accounting has failed to provide an accurate view of such value drivers and therefore traditional (historical cost) financial statements have experienced a dramatic loss of relevance (although they have maintained their reliability). As a consequence, there is currently a significant gap between the accounting

book value of the firm and the market value of its equity. Therefore, standard setting bodies are facing the (urgent) need to develop new guidelines for the recognition, valuation and reporting of intangibles. On the other hand, managers need to understand the nature and value of intangibles in order to be able to strengthen the firms' competitive position and maximise shareholders' wealth. The first step in that direction is the achievement of a consensus on the economic nature, definition and classification of intangibles. For only on the basis of that consensus, will it be possible for policy makers to issue new standards for the recognition of intangibles in firms' financial statements.

Of course, there is a reasonable level of awareness, in this respect, till date. It is for organisations like the big accounting firms to get this message across to corporations. Some think it is onerous and it will increase the costs to become IFRS compliant. Indian companies will speak the same language as global companies. Already 100 countries have adopted IFRS. Therefore, India is in a minority. So, if an Indian corporate presents its balance sheet to foreign companies or to foreign stock exchanges then the foreign community will not know that it is in accordance with global norms and they can take it at face value. So if Indian companies are IFRS-compliant, the compatibility gets greater. They become more reliant on accounts. Currently the discount rate for valuations of Indian companies is much greater than IFRS-compliant companies. There is a very clear distinction. If you are forced to raise capital, you are forced to raise at higher rates. So, Indian standard-setting bodies like ICAI and other subsidiary bodies, including our association, has a great role to play to make the accounting and valuation of Intangibles IFRS-complaint in India in the forthcoming years. ■

## IFRS – Fair Value Accounting a Non-Developed and Inadequate Science?



IFRS's has completely changed certain concepts and basic assumptions in accounting in the modern world. IFRS requires the financial statements (generally) to be presented on fair value basis. The fair value as a concept although well understood, has many aspects to it when it is used practically. This is because fair value is related, in part, to human beings and their psychology. This article tries to bring out the deficiencies of "fair value accounting", that IFRS compliant financial statements are required to be reported on. With most of the countries in the world now converging to IFRS including India, the businesses and the regulators should be aware of the shortcomings of the standards. Read on to know more.

We graduated as accountants during the time when accounting was based on three assumptions – Mercantile system of accounting/ accrual concept, going concern and concept of conservatism or prudence.

Accounts and accountants were always known to be conservative in recognising gains and profits. Gains and profits were being recognised only when realised.

The whole world has known the benefits of conservative system of accounting. Conservatism helps businesses in the long run.

However, with the advent of complex financial instruments and undue importance being placed on the stock markets rather than the economy (the stock markets taking precedence as head of the cart rather than an indicator of economic

### CA. Sanjay Tari

*(The author is a member of the Institute. He can be reached at [eboard@icai.org](mailto:eboard@icai.org))*

**“The measuring concept of fair value (for quoted shares) itself is not perfect as the people who deal in stock exchange are doing it for various purposes like speculation or driven by sentiments. Why, then value investments based on these superficial values and then take gains/ losses into account. This will result in wide fluctuations in Balance sheet, if the stock markets were to fall the next reporting period or rather the next day.”**

performance), the accounting concept of conservatism has lost its relevance.

IFRS place importance or rather require accounting mostly on fair value basis as opposed to conservatism.

Where does fair value mainly apply in IFRS:-

Fair value concept arises mainly for-

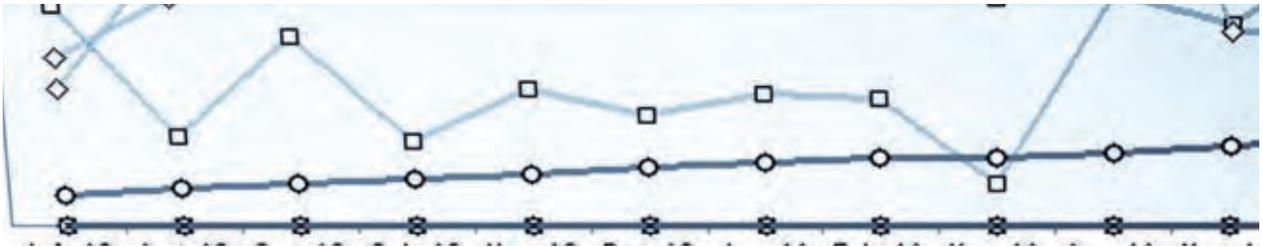
- a) Valuation of financial assets like - equity shares, loans and receivables and financial liabilities. (IAS 39)
- b) Valuation of investment properties (IAS 40)

Valuation of financial assets is covered by IAS 39 with disclosure requirements covered in IFRS 7. Recently, IFRS 9 has been drafted as an improvement over IAS 39, after the financial crises. IFRS 9 would eventually replace IAS 39.

IAS 39 for valuation of equity investments requires fair valuation of investments by reference to various parameters: if the investments are listed on stock exchanges, the bid values as on the reporting dates are considered as fair value for valuation. The gain or loss on revaluing the investments (unrealised) is taken either to Profit or Loss Statement or as Fair Value Reserve in the shareholders' equity in the Balance Sheet. For unlisted investments the same are valued based on other valuation techniques (like DCF, PB ratio etc.) with appropriate assumptions.

Using this fair value concept for valuing investments results in huge fluctuations in the financials. If, unrealised gains or losses were not being adjusted in the financials the same would look more stable. The main culprit in fair value concept is the measuring of fair value. IAS 39 states that the readily available stock prices on listed exchanges are the best available measure of fair value. Recent stock exchange fluctuations can tell a common man that these prices are ruled by erratic thinking of the traders, speculators and driven mainly by sentiments. If an investment is potentially giving good returns then there would be no reason for it to fall/rise suddenly in the market. Further, such fall in prices should not affect the owner of the stock if held for a long term.

The measuring concept of fair value (for quoted shares) itself is not perfect as the people who deal in stock exchange are doing it for various purposes like speculation or driven by sentiments. Why, then value investments based on these superficial values and then take gains/ losses into account.



This will result in wide fluctuations in Balance sheet, if the stock markets were to fall the next reporting period or rather the next day.

Does a manufacturing company value inventory on market price basis? It values inventory on cost or Net Realisable Value (NRV) whichever is lower and then books only realised profits. The same concept should apply to investments. Applying fair value would not only show wide fluctuations but it is a short way of showing profits by the management.

The financial crises happened because of the fair value concept, where overzealous management packaged and repackaged investments into complex financial products, got them valued in some manner (valuation itself is an inaccurate science) and showed non-existent and unrealised gains. Eg: The banks loaned an amount of US\$ 1 million for a house to an individual based on the house being collateralised. They then made this loan into 1 million units and started trading on these units. The prices of these units in this trading rose multifold like for example it may have become US\$ 10 million when the underlying asset was only US\$ 1 million.

Such problems would continue to arise in future in spite of whatever further amendments made to the IFRS. Since "Valuation" is an inexact science, it is open to interpretation and would be interpreted in beneficial ways by the enterprises. The stock markets are imperfect as the people who deal in it may or may not be rational and therefore the bid prices used for valuation are imperfect.

IFRS 9 is just augmenting the problem further prompting firms to show profits somehow in spite of crises. The Phase 1 of IFRS 9 requires, equity investments, to be classified as "Held for trading (HFT)" or "Investments held at Fair Value through Other Comprehensive Income (FVOCI)". Once classified, the same cannot be changed. All realised and unrealised gains/ losses on HFT are taken to Income Statement. However, in case of FVOCI all realised and unrealised gains/ losses are taken only through Other Comprehensive Income(OCI). That means whatever gains/ losses made on FVOCI would not be considered in calculating EPS. Thus, as some companies reported huge losses due to impairment (write off) of investments in 2008/ 2009 would be able to avoid the same (restating the earlier financials) by showing some investments in FVOCI and routing the realised and unrealised gains/ losses through OCI. Further, in spite of all the above changes, the balance sheet of

the companies would widely fluctuate due to changes in fair value that is reflected.

Earlier, general purpose financial statements included:

1. Balance Sheet
2. Statement of Income / Profit or Loss Statement
3. Statement of Changes in Equity
4. Statement of Cash Flows

After the recent changes there are following general purpose financial statements:

1. Statement of Financial Position (new name for Balance Sheet)
2. Statement of income
3. Statement of Other comprehensive OCI
4. Statement of changes in equity
5. Statement of cash flows

It is not very hard to imagine why changes in IFRS are done to benefit the Companies. IFRS is trying to converge in on US GAAPs. IFRS just plainly ignores the old tried and tested accounting concept of "prudence" or "conservatism". They are just trying to make accountants do what the valuation experts are doing and in the process violating all the accounting conventions.

The world might know the perils of fair value accounting when the next crises come in few more years. Then they might say – "oh let's keep accounting and valuation separate and let's value everything as was being done for the last 40-50 years: cost or market price whichever is lower".

The only solution is to return back to conservatism – value at cost or market price whichever is lower and do not take into account unrealised gains. ■

**It is not very hard to imagine why changes in IFRS are done to benefit the Companies. IFRS is trying to converge in on US GAAPs. IFRS just plainly ignores the old tried and tested accounting concept of "prudence" or "conservatism". They are just trying to make accountants do what the valuation experts are doing and in the process violating all the accounting conventions.**



## KEY to Corporate World's Success

Creation of employment opportunities, enhancing knowledge and skill sets and recognition of the exemplary work of members in industry are the primary goals of the Committee for Members in Industry (CMII). Keeping this in mind, the CMII will organize this unique Annual Corporate Forum in Kolkata from 28<sup>th</sup> January to 30<sup>th</sup> January, 2011. The ICAI forum comprises of Four high-profile concurrent events as follows :

- **Career Ascent** - Mid Career Campus
- **Corporate Conclave** - In Pursuit of Excellence
- **Capital Advantage** - Invest & Buy Mart
- **ICAI Awards 2010** - Corporate CA Achiever's Acclaim

ICAI's Corporate Forum will be a unique opportunity for the members of ICAI to participate in an event which will provide them knowledge, Career Opportunities and the chance to be recognized amongst the best in the profession.

Complete details have been hosted at the Institute's Website.

**For details please visit :**  
[www.icai.org/forum](http://www.icai.org/forum)



**Committee for Members in Industry**  
**The Institute of Chartered Accountants of India**  
(A statutory body established under an Act of Parliament)  
ICAI Bhawan, Indraprastha Marg, New Delhi - 110002  
[www.icai.org](http://www.icai.org), [www.cmii.icai.org](http://www.cmii.icai.org), <http://jobs4cas.icai.org>

**For Details Contact :**

**Chairman, CMII**

Tel: +91 (11) 30110555/491

Email: [cmii@icai.org](mailto:cmii@icai.org)

**Secretary, CMII**

Tel: +91 (11) 30110491

Email: [secretarycmii@icai.in](mailto:secretarycmii@icai.in), [cmii@icai.org](mailto:cmii@icai.org)

**Deputy Secretary, EIRC**

Tel: +91(33) 30211132 Email: [ircs@cmii@icai.in](mailto:ircs@cmii@icai.in), [absc@icai.in](mailto:absc@icai.in)

# IFRS Adoption: Cut-Over Challenges



International Accounting Standards Committee has been in existence since 1973. The first companies to adopt IFRS were banks and a handful of pharmaceutical companies. Today we have well over 100 countries already using IFRS. This article attempts to list some of the key cut over challenges that were faced during first time adoption of IFRS. The experience of a major European Bank, Barclays plc is cited here to illustrate the complexity and solutions adopted. Also the situations faced by Axa, British Petroleum, Glaxo Smith Kline and Mark and Spencers have been given. In India we are at the threshold of commencing the convergence with IFRS and we hope to draw lessons from Europe.



## CA. Kanchan Mukherjee

(The author is a member of the Institute.  
He can be reached at [eboard@icai.org](mailto:eboard@icai.org))

International Accounting Standards Committee has been in existence since 1973. The first companies to adopt IFRS were banks and a handful of pharmaceutical companies. When the EU was formed, they needed a common accounting standard. With Europe adopting IFRS as their common accounting standard with effect from 2005, IFRS became truly a global standard. Today we have well over 100 countries already using IFRS. The next wave of countries adopting IFRS in the 2011-14 time frame are major economic centres such as India, Canada, Japan, Brazil and Nigeria.

## Cutover Challenges: IFRS Transition Preparedness Index

Certain areas will arise in a cutover for IFRS convergence, the list being non-inclusive in nature but, will certainly give a frame work how a preparation can be made for the transition and implementation.

- Net worth changes and Comparative figures restatement
- Chart of Accounts changes
- Fixed assets transfer of balance
- Determination of useful life
- Leases reclassification
- Water tight segregation of research expenses

- Determining warranty obligations
- Discounting of liability
- Periodic actuarial valuations
- Revenue recognition
- Foreign exchange fluctuation
- Recognition and measurement of financial instrument and derivatives
- Derecognition on securitisation
- Practical problems in putting fair value to use.
- Goodwill allocation
- Business combinations: consolidation and reconciliation
- Effects on financial statements and deferred tax
- Stopping the use of LIFO, completed contract method, purchase method for amalgamations, share based payments by intrinsic value method.

### Cutover Challenges

The list of top twenty areas which needs to be taken into consideration for implementing IFRS is provided:

- **Net Worth Changes and Comparative figures restatement:** *The first time adoption with reconciliation in shareholder's equity and profit for the period will result in changes in equity, so a pro forma opening balance sheet would be helpful in phased transition.* The effect of changes in prior period financial statements will be adjusted in equity under the specific reserves or retained earnings if books of accounts cannot be opened. A circular by Ministry of Corporate Affairs in 2003 (General circular No.1:17/75/2002-CL.V) allows to reopen and revise the annual accounts after their adoption in the annual general meeting. Restating comparative figures as per IFRS will be optional in transition during first phase.
- **Chart of Account:** The changes in Chart of Accounts are to

**The first time adoption with reconciliation in shareholder's equity and profit for the period will result in changes in equity, so a pro forma opening balance sheet would be helpful in phased transition. The effect of changes in prior period financial statements will be adjusted in equity under the specific reserves or retained earnings if books of accounts cannot be opened.**

reflect the changes in financial statements. The challenge will be differentiating a financial instrument both at amortised cost and at fair value and also for non current asset class at fair value or at carrying cost if a change is required subsequent to the preparation of group chart of accounts. Corporates which will follow IAS 39 in its convergence in 2011 will need to modify the classification according to IFRS 9 in subsequent year. Planning of the possible changes has to be done till the chart of accounts can be changed.

- **Fixed Assets Transfer of balance:** Measuring the assets at the values as per IFRS principles indicates deriving the relevant carrying cost based on useful life or the fair value of the assets. Whereas the various assets in a fixed asset register may not be reflecting this, it's advisable to make the changes as per the components for future benefits if deemed cost from fair value cannot be used.
- **Determination of useful life:** Under this policy it becomes impractical to calculate life of average assets exactly. The total lives range from approximately 15 to 50 years for buildings, and 5 to 15 years for plant and

equipment. We require regulation for useful life of assets, industry wise. Impairment can be done if useful life has reduced from the expected useful life.

- **Leases:** The ramification of reclassifying a transaction from a finance lease to an operating lease will be huge. For a lessor, the asset will be shown along with Property, plant and equipment and would be at fair value similar to the net present value of the amount receivable. In the reverse scenario, it will be taken out from the asset register and shown as receivable on the net present value basis. The lessee in a finance lease will amortise the asset as per the lease period or useful life whichever is less.
- **Finance lease on land and building** will be bifurcated to understand whether the ownership of land would be transferred to the lessee also. If not, the finance lease on land will be derecognised. Under IAS 40, property held by a lessee under an operating lease can be classified as investment property and accounted for as if it were a finance lease.
- **Segregation of development expenses:** Various associations of industries like pharmaceuticals and technology can provide the percentage of a development expense vis a vis the research element as U.S. GAAP allows companies to expense their research and development costs as one item.
- **Warranty Obligations:** Additional provision will be made on an estimate based on claims notified and past experience. Where the dealer and secondary sales network also provides warranty services, the floating stock of various equipments and spare parts will now be included in the

provision based on an estimate or assumption.

- **Discounting of liability:** As effect of time value is material, amount recognised is the present value of the estimated expenditures for provisions which give rise to cash flow after one year or more. *The discount rates used are required to be updated on an annual basis at each annual balance sheet date. It can be the government bond rate for a bond of similar time period.* In the present higher inflation rate RBI has reduced the interest rate for government bonds; a review for this will be required.
- **Actuarial Valuation:** The difficulty in obtaining actuarial liability will increase as the detailed actuarial valuation to determine the present value of defined benefit obligation is to be carried out with regularity so that it matches with the period end reported figure also. The inputs include the benefits of the plan, the data for the employees, the financial and demographic assumptions like x% for discount rate before and after retirement, y% for price inflation and cost of living adjustment, z% for salary increase assumptions.
- **Revenue Recognition:** The present scenario suggests that IFRS will not be affecting balance sheet adjustments only and interest income will be shown more following effective interest method; even revenue recognition will be less in case of loyalty programmes when the terms and conditions are not met. The pre tax method will increase the income from finance leases and contracts under IFRIC 4.
- **Foreign Exchange Fluctuation:** Mismatch with functional currency may occur with foreign currency convertible bonds. However, change in functional currency

should be carried out prospectively only. If a gain or loss on a nonmonetary item is recognised in equity (e.g., property, plant, and equipment revalued under IAS 16), any foreign exchange gain or loss element is also recognised in equity.

- **Foreign Currency Monetary Item Translation Difference Account:** The notification issued by the Ministry of Corporate Affairs on 31<sup>st</sup> March, 2009, permitted several companies to either capitalise such foreign exchange differences or accumulate such exchange differences in the Foreign Currency Monetary Item Translation Difference Account. If a deemed cost is approved and adopted there is no need to segregate the capitalised foreign exchange differences.
- **Recognition and measurement of financial instrument and derivatives** at fair value will be applicable by using the business model test and security with underlying asset backing (e.g. some cash collateralised debt obligations) and service concession receivables would be fair valued to correct the mismatch.
- **De recognition on securitisation** will not limit to existing control below 10 per cent in Special Purpose

**The notification issued by the Ministry of Corporate Affairs on 31st March 2009, permitted several companies to either capitalise such foreign exchange differences or accumulate such exchange differences in the Foreign Currency Monetary Item Translation Difference Account. If a deemed cost is approved and adopted there is no need to segregate the capitalised foreign exchange differences.**

Entity's capital. Repurchase at the end of the scheme for clean up will not constitute effective control. (where residual value is below 10 per cent of original amount sold to SPE) .

- **Fair Value:** Without a crystal ball, *fair value will always be subject to measurement uncertainty until there is an actual transaction with an arms-length third party confirming the stated value or estimate.* Practical problems in fair valuation exists in the following cases:
  - In a finance lease, the fair value of the asset is often required to judge the nature of lease, net present value of the receivables should be near the fair value also.
  - Fair value will be referred in determining revenue in barter/exchange sales and bifurcation of revenue in customer loyalty programmes.
  - Fair values for share based payments can be calculated at the date of grant using Binomial, Black-Scholes or Monte Carlo model.
  - Fair value of the plan assets in employees retirement benefit plan is to be considered periodically.
  - Fair value of agricultural assets, intangible assets, property, plant and equipments and investment property, financial instruments, derivatives and non monetary grants and accompanying assets are required.
- **Business Combinations require consolidation** with period end revaluation for fair value, foreign exchange adjustments, hedging adjustments, data validation and elimination of intercompany profits, adjustments in statement of changes in equity and preparing

reconciliation with Indian GAAP on first time adoption. While the net worth determined for first time adoption of IFRS by banks is on 31-3-2011. i.e. after a gap of two years from the net worth determination of other companies, consolidation of both the bank and other companies will be possible only from 2013.

- **Goodwill** is measured as the excess of the cost of the acquisition over the acquirer's interest in the net fair value of the identifiable assets, liabilities, and contingent liabilities. It may be difficult to separate the value of goodwill from the fair value of other intangible assets.
- **Effects on Financial statements** will be increase or decrease in assets, liabilities, equity, income and expense by significant percentages which will streamline subsequently. Deferred taxes will be calculated on temporary differences on carrying amount of asset and liability and its tax base so it will cover more items. If IFRS conversion results in increase in asset value over tax base, deferred tax liability sets in.
- **Discontinued Accounting Policies:**
  - (i) **LIFO** is not relevant in India, but an entity already following US GAAP will require to change the valuation method by using transaction SAP transaction code MRF4 over a period of time prior to first time adoption.
  - (ii) **Completed Contract method abolished:** Moving out from conservative estimate in completed contract method will now increase revenue.
  - (iii) **Pooling of interest method** stopped as it did not reflect the dynamics of a merger and goodwill was not recognised.

Occasionally it may be difficult to identify an acquirer, but normally there will be indications as to who exercises control e.g. disinvestment in public sector is meant to give control to business partners who are from private sector.

- (iv) **Value of share based payments by intrinsic value method:** Any adjustment for change in method of valuation will be taken in statement of changes in equity if books of account can not be opened.

### Post IFRS Transition

- **Consolidation of entities:** *Subsidiaries with period ending difference of more than 3 months will have to make financial statements as on the date of the holding company.* Recognition of special purpose vehicles in consolidation will be studied in every period ending.
- **Streamlined mergers and acquisitions:** By adopting purchase method uniformly all mergers and acquisitions will be adopted but the valuation of intangibles and goodwill will require further diligence.
- **Intangible assets** may have indefinite useful life but will be reviewed for impairment periodically.
- **Projected unit credit method** will be followed for actuarial valuation of employees long term benefits. This method is based on the probability of personnel remaining with companies in the Group until retirement, the foreseeable changes in future compensation, and the appropriate discount rate. Specific discount rates are adopted for each monetary zone. Valuation will be prepared by a qualified actuary who carries out a full annual valuation of the plans.

**Projected unit credit method will be followed for actuarial valuation of employees long term benefits. This method is based on the probability of personnel remaining with companies in the Group until retirement, the foreseeable changes in future compensation, and the appropriate discount rate. Specific discount rates are adopted for each monetary zone. Valuation will be prepared by a qualified actuary who carries out a full annual valuation of the plans.**

- **Presentation of treasury shares:** Presenting treasury shares in equity is a new requirement, the consideration paid is deducted from shareholders' equity as treasury shares until they are cancelled. Where such shares are subsequently sold or reissued, any consideration received is included in shareholders' equity.
- **Income tax calculations:** Changes in accounting practices will be not be applicable for tax calculation purposes. As we are making phased transition the tax rules will change in subsequent years also.
  - (i) Dividend on redeemable preference shares will not be a deductible expense in Income tax.
  - (ii) Taking depreciation for a smaller useful life will effect the difference in taxable profit and book profit.
  - (iii) As deferred income liability is recognised in IFRS and deferred revenue expenses is not recognised in IFRS in many situations, the taxable profit and the book profit will be different.
  - (iv) Recognition of liability for warranty cost, employees long term benefit cost, and

discounting of liability will lead to contentions and debates for certain changes in income tax laws.

- **Minimum Alternate tax** effect will be judged on the gross value of the assets (as per the proposed Direct Tax Code). Would the fair value adjustments for investments and derivatives under IFRS, be considered at least for MAT calculations or would it be restricted to gross block of the assets?

### Post IFRS Transition: Change of Method or Approach in Subsequent Period

- **Change from equity method consolidation:** If the entity does not want to hold the investment it can change from equity method and value it as per IFRS 9. However, if a financial investment accounted in equity method is to be reversed and taken at fair

**“Different business units are managed differently. In retail banking business the objective is to collect the contractual cash flows of loan assets and in investment banking business, the objective is to realise fair value changes through the sale of loan assets prior to their maturity. The financial instruments give rise to cash flows that are payments of principal and interest in the retail banking business they may qualify for amortised cost measurement even if similar financial instruments in the investment banking business do not. Cash flow will change from investing to operating activity if retail investment is now shifted to investment banking portion.”**

value, the increase in value from proportionate profit of the invested entity will be corrected to market value of the financial instrument in retained earnings. Proportionate consolidation accounting method should be used for an investment in an associate where it is operating under severe long-term restrictions—for example where the owner or the management of a company has temporary control over the associate which may get nationalised. The Group's share of the assets, liabilities, income, expenses and cash flows of jointly controlled entities are combined with the equivalent items in the Financial Statements on a line-by-line basis.

- **Reclassification of financial instruments:** Different business units are managed differently. In retail banking business the objective is to collect the contractual cash flows of loan assets and in investment banking business, the objective is to realise fair value changes through the sale of loan assets prior to their maturity. The financial instruments give rise to cash flows that are payments of principal and interest in the retail banking business they may qualify for amortised cost measurement even if similar financial instruments in the investment banking business do not. Cash flow will change from investing to operating activity if retail investment is now shifted to investment banking portion.

### Post Transition Education

- **Adaptability of system to new changes in dual standards:** The local standards will be in place for IFRS transition so that system changes can be carried out to make IFRS compliant statements methodical. The first time adopters

in first phase of transition will give comparative figures for previous year as per Indian accounting standards. Snippets of key areas of change and its effect on financial statement may be given in quarterly statements to bring in to the minds of the educated investors of the areas of concern.

- **Investor Education:** *Investor's interest is to be protected when the transition to IFRS is made. The comparison and reconciliation of income statement and financial statement with Indian GAAP for the next couple of years will satisfy their needs and questions.* The Ministry of Corporate Affairs will increase the investor education programs tenfold in the coming years.

### Post IFRS Transition Approach For Banking and Finance Sector

- Profit planning and budgeting have to be changed to incorporate the expected increase in the income statement volatility arising out of the increased use of fair values as a measurement attribute. 'Unrealised profits' in fair valuation and hedging reserve may not be used to distribute dividend.
- Limits on the proportion of hedging that can be done, the kind of derivative instruments that can be used for hedging, and the level of hedging that can be done by subsidiaries or group companies will be fine tuned.
- De recognition of Financial Assets and Liability: Consolidate and determine whether the principles should be applied to a part or all of an asset (or group). Currently, only loss of control is considered for derecognition on securitisation.
- *When a loan is identified as impaired, the impairment loss is measured as the difference between the carrying amount of*

**“ Goodwill acquired may be allocated at segment level or profit center level to distribute the impairment loss. Goodwill will be accounted only on acquisition for the surplus of purchase consideration over the carrying amount of the assets and liabilities. If the acquisition is providing a value addition as a brand, the goodwill will be allocated to the level below segments so that, if required for test of impairment the amount charged off will be lesser. ”**

*the loan and the net present value of expected future cash flows. Interest revenue will be recognised on the balance loan amount.*

- Under IFRS, the accretion of the net present value of the written down amount of the loan due to the passage of time is recognised as the interest revenues; under Indian GAAP this is derived from RBI's guidelines. IMPACT: Higher provision for credit losses under IFRS.

#### Example:

- Bank gives a loan of ₹10,000; Repayment of ₹2,000 has been made; Carrying Amount of the loan: ₹8,000; There is an indicator to impairment in 2009. Say, expected future cash flows: ₹6,000. Net Present Value of expected future cash flows: ₹5,000
- RBI's prudential norms on income recognition, asset classification and provisioning introduced in 1992, eliminated the subjective element in these areas and introduced objectivity in phased manner to a large extent which will again be reversed. Under the relaxed NPA norms set by RBI in 2009: Provision for loss will be limited to nil if the borrower had submitted a plan for

reschedulement and if the asset was standard in 2008, else it would have taken as sub standard with say 10 per cent provision for loan loss which would have increased in similar manner for 5 years period if there was no specific reason to understand the reduction in the value of the security held by the bank.

- Under IFRS: Provision for impairment loss – (₹8,000 – ₹5,000) = ₹3,000 Hence, higher provision for credit losses.
- In 2010, RBI has classified infrastructure projects as non-performing loans (NPL) only when commercial production is behind schedule by four years as against earlier requirement of two years. These are prudential norms or disclosure norms but, have nothing to do with the computation or taxability of the provisions for NPA under the IT Act. For NBFCs the Provision for NPA made in terms of the RBI Directions does not constitute expense for purposes of Section 36(1)(vii). The said provision is for presentation purposes and in that sense it is notional. This was decided by the Supreme Court of India, Appeal No: 1337/2003, in the case of: M/s Southern Technologies Ltd. versus Joint Commissioner of Income Tax.

#### For Insurance Sector:

The popular types of insurance contracts in India are life insurance, general insurance, endowment plan, unit linked and annuity business which undergo solvency tests also. Insurance Contract Assets and Liabilities are to be recorded at Current Exit Value, the amount that would be received today if the entire obligation is sold to a third party.

- Under IFRS, life assurance products are to be divided into investment contracts, which are

accounted for under IAS 39 and insurance contracts under IFRS 4.

- *In case of Axa in 2005, in accordance with IFRS 4, insurance and investment contracts with a discretionary participating feature were accounted for under previous accounting policies provided certain conditions were met. Investment contracts with no discretionary participating features (0.2 per cent of total) were accounted for under IAS 39.*
- Deferred acquisition costs (DAC) and Value of Purchased Life Business in Force (VBI). The extent to which acquisition costs are deferred is a significant factor in the reported profitability in a period. The value of related policyholders' liabilities at the date of acquisition net of VBI will represent the estimated fair value of such business on such date as defined by market practice.
- Product design, pricing and offerings will change based on the information supplied by the adoption of IFRS.
- Increased disclosure on calculation of risk is required. In order to estimate the cash flows in the market on a consistent basis, there is a need to integrate internal and external data into a consistent format.

#### For Utilities sector:

- Impairments should be assessed on a low level as oil wells. As a lessee, the assets used for power generation will be recorded in its books in case agreement suggests a finance lease.
- A schedule for measuring the decommissioning liability can be used (as per IFRIC 1 and 5).
- IFRIC 18 Transfers of Assets from Customers is particularly relevant for the utility sector, whereby revenue is not recognised on such transactions.



#### For Industrial sector:

- Cost of major overhauls in Property Plant and Equipments are to be capitalised. Componentisation should be effected as per industry norms. As a matter of prudence useful life of depreciable assets would be redefined in a certain interval of time which may match with Income Tax depreciation rates. Impairment can be done if useful life has been reduced from the expected useful life.
- *There can be unexpected hedging losses for a corporate which procures raw materials from abroad. Derivatives software services that evaluate and monitor complex financial transactions can be used for online risk management.*
- British Petroleum had adopted IFRS 6; the unit-of-production rate for the amortisation of field development costs takes into account expenditures incurred to date, together with sanctioned future development expenditure.
- The majority of Glaxo Smith Kline's intangible assets related to the acquisition of rights to compounds in development

stage, amortisation commenced with use of the product.

#### For Consumer goods sector:

Operating segments must be identified based on the financial information that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance.

- Revenue recognition with respect to the equipment delivery is deferred until the installation process is completed, unless a separate entity takes up the installation. Alternatively, the fair value for the service of installation will be deducted from the invoice and the fair value of delivery of the equipment will be recognised as revenue.
- If mergers and acquisitions are common in this sector so will be the requirement to follow IFRS 5 for disclosing discontinued operations once an agreement to hive off is done for a particular brand, plant or business unit. To stop depreciation charge the assets can be transferred as 'held for sale'.
- Goodwill acquired may be allocated at segment level or profit center level to distribute the impairment loss. Goodwill will be accounted only on acquisition for the surplus of purchase consideration over the carrying amount of the assets and liabilities. *If the acquisition is providing a value addition as a brand, the goodwill will be allocated to the level below segments so that, if required for test of impairment the amount charged off will be lesser.*

#### For Information technology, communication and entertainment sector:

Revenue at fair value from franchisee, sponsorship and rights are transferred to other entities as per contract.

- Intangible assets at fair value

and goodwill from combinations will be maintained as per various mergers and contracts at Cash Generating Unit /segment level for impairment testing.

- Licence fees paid to governments, which permit telecommunication activities to be operated for defined periods is to be amortised from the time the network is available for use to the end of the licence period on a straight line basis.

#### For Retail sector:

- Award credits in customer loyalty programmes are accounted for as a separate identifiable component of a sales transaction, with the consideration allocated between the award credits and the other components of sale.
- Revenue arising from the interconnection of voice and data traffic between other telecommunications operators will be recognised at the time of transit across the group's network.
- Lease incentives in the form of rent-free periods and developer contributions are to be spread over the lease term.
- If rentals are based on revenue or profit generated from the outlet or premises, then the contracts must be analysed for embedded derivatives.

**The principle based accounting in IFRS puts much more value to work of the consultant who can make this conversion and also on the management to make a proper gap analysis and estimate of the cut over challenges which will unfold on conversion. It may not be possible to understand the ramifications and disclosure requirements at an early stage, so the plans and efforts for conversion should begin now to avoid last minute problems.**

**For Public Sector:**

Government grants are not directly credited to shareholders interest but, shown as income with matching costs. Grants related to fulfillment of certain obligations will be deferred income. Grants related to assets are settled as deferred income or deducted from assets.

**Key Impacts in IFRS Implementation at Barclays**

The bank deferred the adoption of IAS 32 and 39 to 1-1-2005 instead from 2004. It recorded 12 per cent increase in equity in its successful IFRS transition with early adoption, good project management, giving training to its dedicated staff, IT and HR support. The adjustments in equity for its convergence were:

- **Capital Instruments:** £ 1999 million funding instruments were included in undated loan capital being reclassified as equity.
- **Goodwill:** £ 301 million as amortised amount in 2004 is written back.
- **Dividend:** £ 977 million as dividend will be deducted from

equity in next year.

- **De recognition:** £ 228 million, derecognising securitisation structures, remeasure of customer accounts, remeasurement and reclassification of customer loyalty provisions from provisions to financial liabilities.
- **Pension costs:** £ 1819 million as liability for unrecognised actuarial losses and past service costs is to be shown by reducing equity.
- **Consolidation and presentation:** £ 163 million as linked Special Purpose Entities are presented separately.
- **Loan Impairment:** £ 24 million, though general provision is not made, this offsets the excess provision as impairment loss is measured as difference between the carrying amount of the loan and the net present value of expected future cash flows.
- **Effective Interest :** £ 145 million from uniform application of effective interest rate basis.

**Conclusion**

India's phased IFRS convergence

timelines have been issued in the beginning of 2010. The convergence timelines for banks, non-banking finance companies and insurance companies have now been issued also by the Ministry of Corporate Affairs for IFRS convergence in India. The actual IFRS converged standards will be issued and regulatory amendments need to be made to fully rationalise the convergence roadmap. The circular by the Securities and Exchange Board of India permitting early adoption of IFRS for consolidated financial statements has given the opportunity to the finance professionals to act first.

The principle based accounting in IFRS puts much more value to work of the consultant who can make this conversion and also on the management to make a proper gap analysis and estimate of the cut over challenges which will unfold on conversion. *It may not be possible to understand the ramifications and disclosure requirements at an early stage*, so the plans and efforts for conversion should begin now to avoid last minute problems. ■

Set out below are the reconciliations of UK GAAP to IFRS for the Group and the Bank in accordance with IFRS 1.

The Group	Notes	1st January 2005 £m	31st December 2004 £m	1st January 2004 £m
Shareholders' equity including minority interests (UK GAAP)		-	18,482	16,768
Shareholders' equity (IFRS – except IAS 32, IAS 39 and IFRS 4)		16,849	-	-
Consolidation	(a)	-	(163)	(157)
Life assurance	(b)	-	(708)	(592)
Goodwill	(d)	-	301	1
Share-based payments	(e)	-	(18)	(26)
Pensions	(f)	-	(1,819)	(1,697)
Intangible assets	(g)	-	13	35
Financial guarantees	(h)	-	(34)	(33)
Leasing	(i)	-	(196)	(188)
Dividends	(j)	-	977	883
Other		-	14	13
Derivatives, financial instruments and hedge accounting	(n,o)	175	-	-
Capital Instruments	(q)	1,999	-	-
Loan impairment	(r)	(24)	-	-
Effective interest	(s)	(145)	-	-
Insurance contracts	(t)	98	-	-
Derecognition and financial liabilities	(u)	(228)	-	-
<b>Shareholders' equity (IFRS)</b>		<b>18,724</b>	<b>16,849</b>	<b>15,007</b>

[From Annual Report of 2005 of Barclays plc]

# Special Provisions For Computing Profits And Gains Of “Small Business” On Presumptive Basis

**The Income-tax Act, 1961 provides for taxation of income on presumptive basis, inter alia, in respect of Civil construction business, Transport business, and Retail business, etc. The Finance (No. 2) Act, 2009 extends the scheme of taxation of income on presumptive basis to all small business (other than transport) w.e.f. 1-4-2011, i.e. from Assessment Year 2011-12. Vide this amendment Section 44AD is being substituted to enlarge the ambit of the presumptive taxation. In this write up the author has elaborately analysed the provisions of amended Section 44AD.**



**CA. Thakur Repudaman**  
(The author is a member of the Institute.  
He can be reached at  
thakur\_repudaman@yahoo.com)

## Introduction

The Income-tax Act, 1961 (the Act) provides for taxation of income on presumptive basis, inter alia, in respect of the following businesses:

- Civil construction business [Section 44AD]
- Transport business [Section 44AE]
- Retail business [Section 44AF]

The Finance (No. 2) Act, 2009 extends the scheme of taxation of income on presumptive basis to all small business (other than transport). For the purpose, amendments are carried out in the following provisions w.e.f. 1-4-2011, i.e., Assessment Year 2011-12:

- Section 44AA providing for maintenance of books of account;
- Section 44AB providing for audit of books of account;
- Section 44AD is being substituted to enlarge the ambit of the presumptive taxation; and
- Section 44AF to provide for the sunset clause (as Section 44AD would also cover retail trade).

Apart from the above, Section 44AE is also amended by Finance (No. 2) Act, 2009 w.e.f. 1-4-2011, i.e. Assessment Year 2011-12, so as to increase the presumptive amount of income arising from goods vehicles as follows:

Presumptive Income		
Type of vehicle	Before Amendment	After Amendment
Heavy Vehicles	₹3,500 per vehicle for every month or part	₹5,000 per vehicle for every month or part
Vehicles other than heavy vehicles	₹3,150 per vehicle for every month or part	₹4,500 per vehicle for every month or part

## Section 44AD(1)

Section 44AD(1) of the Act states that notwithstanding anything to the contrary contained in Sections 28 to 43C, in the case of an eligible assessee engaged in an eligible business, a sum equal to eight per cent of the total turnover or gross receipts of the assessee in the previous year on account of such business or, as the case may be, a sum higher than the aforesaid sum claimed to have been earned by the eligible assessee, shall be deemed to be the profits and gains of such business chargeable to tax under the head “Profits and gains of business or profession”.

**Explanation — For the purposes of this Section,—**

- (a) “eligible assessee” means,—
- (i) an individual, Hindu undivided family or a partnership firm, who is a resident, but not a limited liability partnership firm as defined under clause (n) of sub-section (1) of Section 2 of the Limited Liability Partnership Act, 2008 (6 of 2009); and
  - (ii) who has not claimed deduction under any of the Sections 10A, 10AA, 10B, 10BA or deduction under any provisions of Chapter VIA under the heading “C. - Deductions in respect of certain incomes” in the relevant assessment year;
- (b) “eligible business” means,—
- (i) any business except the business of plying, hiring or leasing goods carriages referred to in Section 44AE; and
  - (ii) whose total turnover or gross receipts in the previous year does not exceed an amount of ₹40 lakh.

Notes: Finance Act, 2010, w.e.f. 1-4-2011, i.e. Assessment Year 2011-12, has increased the threshold limit for the purpose of presumptive taxation under Section 44AD from ₹40 lakh to ₹60 lakh.

### Comments

**a)** Section 44AD starts with “Notwithstanding anything to the contrary contained in Sections 28 to 43C”.

It may be noted that Section 44AD overrides Sections 28 to 43C i.e. Chapter IV-D, but does not override Chapter VI. Therefore, the current year losses and the brought forward losses can be set off against the income deemed under this Section. However, current year and brought forward depreciation cannot be set off against the deemed income since that is governed by Section 32.

To recapitulate, the new provision excludes applicability of the provisions of Sections 28 to 43C. However, Section 145 of the Act does apply in respect of income derived from business, i.e., the assessee is free to choose either cash or mercantile system of accounting.

In brief, Sections 28 to 43C deal with the following aspects relating to computation of income chargeable under the head ‘Profits and gains of business or profession:

- These include certain types of income as income chargeable under that head.
- These permit deduction of certain expenses subject to fulfillment of conditions.
- Certain trading losses are allowed to be set off against profit.
- These grant certain special allowance, like, contribution to certain association, depreciation, weighted deduction in respect of certain contribution, etc.
- These define certain words and phrases.
- These also provide for certain

disallowances, either on account of non-business user or specific disallowances, like, cash payment in excess of ₹20,000 etc.

The effect of non-application of the above provisions is explained by considering the following illustrative situations:

- An assessee has contributed a certain amount (to a national laboratory), which qualifies for weighted deduction under Section 35(2AA). If he chooses to return his income on the basis of the specified amount, he cannot claim weighted deduction in respect of the contribution.
- He has paid sales tax in respect of earlier years and gets refund during the year. Such refund cannot be included under Section 41(1) of the Act. It would be considered as included in the specified amount.
- He has paid ₹22,000 in cash for purchase of goods. No disallowance can be made under Section 40A(3) of such cash payment. Similarly, no disallowance can be made under Section 43B or Section 40(a) or other provisions of Section 40A.
- An assessee engaged in small business could not set off of full depreciation on the assets in Assessment Year 2010-11 for ₹50,000. In Assessment Year 2011-12, he desires to be governed by Section 44AD(1). He would not be in a position to set off unabsorbed depreciation of ₹50,000 in as much as it would be deemed to have been allowed in computing the specified profits under Section 32 of the Act, which forms part of Sections 28 to 43C under which a deduction is presumed to have been allowed. If he wants to claim set off of the unabsorbed depreciation, he may declare a lower income and prove it. Had it been unabsorbed business

loss, it would be allowed to be set off against the specified profit inasmuch as such loss is allowed to be carried forward and set off under Section 72, application whereof is not excluded by the new provision.

- The new provision creates a fiction only with respect to the amount of profit chargeable under the head ‘Profits and gains from business or profession’. In other words, the fiction does not extend to income chargeable under other heads of income. Accordingly, such income(s) could be separately included in computing total income as per the applicable provisions.

### Example

An assessee carrying on small business owns a shop and a part thereof is let out. Income from letting property is chargeable as house property income and it would not be included or considered as part of business profits. It would be separately taxable.

In the same manner, gains arising on sale of depreciable assets used in small business would be separately chargeable to tax under Section 45 read with Section 50 of the Act as short term capital gains.

In the above case, Assessing Officer can enquire into sources of investments in shop, etc., and/or any loan obtained by the assessee and if he is not satisfied with the explanation, he can make assessment of the concerned items as unexplained investments or cash credit.

### c) Pre-Requisite for Operation of New Provision of Section 44AD

- The provision applied to an ‘eligible assessee’
- The assessee is engaged in eligible small business.
- The turnover/receipts of the assessee in the previous year do not exceed ₹60 lakh.

If these pre-requisites are satisfied, the profits and gains from small

business will be chargeable to tax on a deemed basis as the higher of the following sum:

- A sum equal to 8 per cent of the turnover or receipts from small business during the previous year; or
- A higher amount claimed to have been earned by the assessee as profits and gains from small business.

Notes:

- 1) Section 44AD is mandatory in nature, subject to the options provided, as discussed in brief earlier.
- 2) When an assessee chooses to claim a higher amount, computation of the higher amount may be either based on normal provisions of Sections 28 to 43C and the assessee may consider the deduction available or he may declare such higher amount on some other basis including an adhoc basis.
- 3) Department bound by the option exercised.

Insofar as the Income Tax Department is concerned, it is bound by the obligation of the specified amount as profits of small business and it cannot substitute a higher amount in place of the specified amount even if it is ascertainable from the account books or any other document filed, produced or available with the assessee.

- 4) Effect of returning specified amount as income where a higher income is earned.

#### Example

X is carrying on small business along with other business. The turnover is ₹50 lakh. The profit as per his accounts or calculations is ₹5 lakh. However, he opts to return the income from small business at the specified amount of ₹4 lakh [i.e., 8 per cent of ₹50 lakh]. The proceeds of business are deposited in a bank account.

X has an option to declare only the specified amount although he has made a higher profit, he need not claim the same.

While examining sources of investments, made from sale proceeds banked, Assessing Officer notices that the income from small business returned was ₹4 lakh, whereas investments are to the tune of ₹5 lakh, out of income arising from small business.

Can the Assessing Officer add the difference as income from undisclosed sources?

- No, for the following reasons :
  - i) The language of Section 44AD(1) requires 'claim' by an eligible assessee for returning a higher amount. If, there is no claim, there cannot be any higher amount.
  - "Claim" signifies assertion of rights. It is not an obligation.

The Legislature has conferred a right on the assessee to claim that he has earned a higher amount, but not an obligation. Had the intention been otherwise, the Legislature could have employed the language which suggests adoption of an amount 'whichever is higher'. To illustrate, Section 44AE specifically provides so.

- *Samta Construction Co. v. Pawan Kumar Sharma, Deputy Director of Income Tax (Investigation) & Ors. (2000) 244 ITR 845 (MP)*

When the language used is plain and unambiguous and is susceptible of only one meaning the Act speaks for itself - due effect has to be given to the words of the Statute - if the words have been used in a precise and unambiguous manner they must be understood in their natural ordinary sense.

- *AC, Bangalore v. Velliappa Textiles Ltd. and Another (2003) 263 ITR 550 (SC)*
- *CIT v. Avind Mills Ltd. (1992) 193 ITR 255 (SC)*

The Apex Court in *AC, Bangalore v. Velliappa Textiles Ltd. and Another (2003) 263 ITR 550 (SC)* held that there is no scope for intendment based on the general purpose or object of law. If the Legislature has left a lacuna, it is not open to the court to paper it over on some presumed intention of the Legislature. The doctrine of *casus omissus*, expressed in felicitous language in *CST v. Parson Tools and Plants [1975] 4 SCC 22/ [1975] 35 STC 413, 418* is:

"If the Legislature willfully omits to incorporate something of an analogous law in a subsequent statute, or even if there is a *casus omissus* in a statute, the language of which is otherwise plain and unambiguous, the court is not competent to supply the omission by engraving on it or introducing in it, under the guise of interpretation, by analogy or implication, something what it thinks to be a general principle of justice and equity. To do so would be entrenching upon the preserves of the Legislature (*Prem Nath L. Ganesh Dass v. Prem Nath L. Ram Nath, AIR 1963 Punj 62, per Tek Chand J.*)

The maxim "Judicis est jus dicere, non dare" pithily expounds the duty of the court. It is to decide what the law is and apply it and not to make it.

- ii) The expression 'as the case may be' as per *Khan Chand Tiloka Ram v. State of Punjab (1966) AIR 423 (Punj.)* is:

"The expression indicates one out of the various situations indicated and not otherwise".

Thus, the phrase signifies that an eligible assessee can choose between the specified amount and the higher amount because:

- The option is an incentive to induce small business owners to comply with the Act.
- Accordingly, even if an eligible

assessee has earned a higher amount, he is not obliged to declare a higher amount and pay tax.

- iii) If an assessee chooses to return the specified amount as his income in the return of income, unless he has some other income, the assessment may be completed by sending an intimation under Section 143(1)(a) of the Act and there would be no cause for scrutiny as the amount of income is determined by the Section itself. However, the Assessing Officer may scrutinise certain other information, like gross receipts, cash credits, sources of investment, and claims for deductions under Chapter VI-A, etc.

**d) Scheme is Applicable to Eligible Assessee**

*Explanation (a)* to Section 44AD of the Act defines 'eligible assessee' to mean that:

- an individual, Hindu undivided family or a partnership firm (other than limited liability partnership), who is a resident, and
- Such individual, Hindu undivided family or a partnership firm has not claimed deduction under "Chapter III", i.e. Sections 10A, 10AA, 10B, 10BA or Chapter VIA under the heading "C. - Deductions in respect of certain incomes", i.e. Sections 80H to 80TT, in the relevant assessment year;

The definition of 'eligible assessee' is quite restrictive and hence, excludes the following from the definition of eligible assessee:

- An assessee, who is not a resident, even an individual or Hindu undivided family or a partnership firm, would not be an eligible assessee.
- Limited Liability partnership, whether Indian or foreign.
- Companies, whether Indian or foreign.

- An association of persons or body of individual, whether incorporated or not.
- A local authority.
- Every artificial juridical person.
- Any individual or Hindu undivided family or partnership firm claiming 'Chapter III deductions' or 'Chapter VI-A deductions' under the heading "C - Deductions in respect of certain incomes" in the relevant assessment year.

**e) Small Business or Eligible Business**  
*Explanation (b)* to Section 44AD of the Act which defines Eligible business to mean that:

- any business except the business of plying, hiring or leasing goods carriages referred to in Section 44AE; and
- total turnover or gross receipts in the previous year does not exceed an amount of ₹60 lakh.

The scope or ambit of eligible business covers any business except transport business. The only reason for excluding transport business is because it is governed by a specific provision (Section 44AE) and the presumption amount of profit is quantified in absolute terms.

Thus, any manufacturing, trading (including speculation) or service business is eligible for the scheme. The only condition is that Revenue of such business should not exceed ₹60 lakh.

**f) Whether any Professional Activity can be regarded as Eligible Business**

There is a distinction between business and profession. Even the Apex Court has held in *G.K. Choksi & Co. v. CIT* (2007) 295 ITR 376 that for the purposes of Section 32(1)(iv) of the Act 'business' referred therein does not include profession of Chartered Accountancy.

In the context of new provision, it was observed:

- Although, it is included under Chapter VI-D dealing with income from business or profession, the provision makes a reference only to business and not profession.
- The legislature is aware that in case of profession, a separate limit is specified for audit obligation under Section 44AB of the Act. Even then, for specifying limit of gross receipts, the amount specified is ₹60 lakh, a limit applicable to a business for the audit obligation under Section 44AB of the Act.
- Reference to gross receipts is for service business contemplated by the provision.

In the light of the above, it appears that the scheme does not envisage and cover a profession.

**g) Engaged in an Eligible Business, Connotation of:**

The phrase implies that it does not contemplate an isolated act or transaction, rather carrying on of the business as a continuous process. Further, the Supreme Court has held in *Remington Rand of India v. Tahil Ali* (1975) 62 AIR 1896 (SC) that the phrase "engaged in any business" means a continuity of transactions and not a single casual or solitary transaction.

**h) More than One Activity**

An eligible assessee may carry on more than one activity, say, trading in consumer durables and providing maintenance and repair services.

If the aggregate turnover/receipts of the activities [which may be regarded as one business having regard to unity of control and management – *Setabganj Sugar Mills Ltd. v. CIT* (1961) 41 ITR 272 (SC) and *B.R. Ltd. v. V.P. Gupta, CIT* (1978) 113 ITR 647 (SC)] carried on by an eligible assessee do not exceed ₹60 lakh, the scheme should apply.

If the turnover of trading activity is, say, ₹50 lakh and receipts of the maintenance activity are, say, ₹11 lakh, the aggregate turnover/receipts of the activities, which may constitute one business, are more than ₹60 lakh. In that case, the scheme would not apply and, hence, the assessee will have to compute its profits and gains of the business, as per the provisions of Chapter IV-D of the Act.

**i) Receipts Forming / Not Forming Part of Total Turnover or Gross Receipts**

Receipts forming part of turnover	Receipts not forming part of turnover
1) Sales tax or any other levy	1) Advance or deposits received, say, in the case of dealer in petroleum products
2) Sale of unusables, empties and packages	2) Consideration received on sale of fixed assets employed in the business
3) Service charges charged for delivery may form part of turnover, having regard to terms of contract.	3) Any security or other deposit obtained from employees
	4) Interest and other receipts of similar nature
	5) Incentive received from the suppliers should actually go to reduce the cost of purchase and should not form part of turnover. Similarly, cash or other discount received on purchase should not form part of turnover.
	6) Value of stock-in-trade

**j) Satisfaction of the Condition of Explanation (b)**

In the application of the Explanation or otherwise, it may be necessary to establish that the turnover or receipts does not exceed the specified amount.

In case of an assessee carrying on small business, there is no requirement under the new provision as to the

maintenance of books of account. Determination and proving of turnover beyond the limit may not be difficult, if an assessee maintains books of account. However, otherwise, if the books of account are not maintained, it could cause some difficulties and for the purpose of proving turnover the following records or documents or evidence may be relevant:

- Cash memos and other bills issued by the assessee
- Rough cash book/cash records
- Purchase bills
- Bank statements
- Quantity details, if any, maintained
- Size and nature of business, area in which it is carried on, etc.
- Returns, if any, filed under sales tax/service tax laws

If an assessee returns profits from small business by applying the new provision, he may have to establish with evidence, total turnover or receipts as declared by him in the return and that it does not exceed the limit laid down. For the purpose, an Assessing Officer may, in a given case, issue notices under Section 142 or 143(2), as the case may be.

**k) Determination of Turnover or Receipt at a Different Amount (Lower or Higher)**

On the basis of the evidence relating to determination of turnover or receipts, an Assessing Officer may find that the amount of turnover or receipts is lower or higher and hence, the following consequences will follow:

**A) Effects of lower turnover or receipts**

- The specified amount would reduce and would be accordingly assessable
- It could result into a lower tax liability, refund of tax, if any, paid in excess, interest thereof, etc.

This may be done by passing an order under Section 143(3).

**B) Effects of Higher turnover or**

receipts

**i) If it is below ₹60 lakh after adjustments:**

- Not only the specified amount, but also the tax liability would increase accordingly;
- It could result into penalty, if any, under Section 271(1)(c) depending on the facts of the case.

This may be done by passing an order under Section 143(3).

**ii) If it is above ₹60 lakh, after adjustments:**

- The case would not fall under Section 44AD and, accordingly, all the provisions thereof would not apply.
- The computation of profits from small business would be made in accordance with normal provisions of Section 28 to 43C.
- The requirements as to maintenance of books of account (if not maintained) and audit (if not carried out) may be considered as not complied with.
- The assessee would be obliged to furnish such evidence and particulars which enable Assessing Officer to determine the profit/loss and the sum payable. In absence of books of account, etc. and non-compliance with notices, the assessment could be made under Section 144 as best judgment assessment.
- The consequences of non-payment of advance tax, if any, may follow.

There could be penal consequences and prosecution, depending on the facts and circumstances.

**l) Other Provisions of the Act to Apply**

The new provision of the Act deals only with the computation of profits chargeable under the head 'Business or profession'

- For computing total income liable to tax, the other provisions of the

Act would apply. Thus, an assessee would be able to set off the brought forward losses or unabsorbed losses; set off of losses under other heads; and also claim deduction under Chapter VI-A (Other than under the heading "C. - Deductions in respect of certain incomes", i.e., Sections 80H to 80TT), in the relevant assessment year;

Thus, in case of an assessee engaged in the specified business, computation of total income and tax thereon may be on the following lines:

• Profits of the business (as per Section 44AD)	xxx
• Other income, if any	xxx
	-----
• Income before loss	xxx
Less: Set off loss	xxx
	-----
• Gross total income	xxx
Less: Deduction under Chapter VI-A	xxx
	-----
(Say under Section 80C / 80D)	

Net taxable income	xxx
	=====
Tax payable	xxx
	=====

Thus, the new provision does not deem profit as total income.

An assessee would also have to comply with other obligations under the Act, procedural or otherwise, viz., to pay tax, to file return, to deduct tax at source, wherever applicable, etc.

### Section 44AD(2)

Section 44AD(2) of the Act states that any deduction allowable under the provisions of Sections 30 to 38 shall, for the purposes of sub-section (1), be deemed to have been already given full effect to and no further deduction under those Sections shall be allowed:

Provided that where the eligible assessee is a firm, the salary and interest paid to its partners shall be deducted from the income computed

under sub-section (1) subject to the conditions and limits specified in clause (b) of Section 40.

### Comments

i) Section 44AD(2) presumed the allowability of expenses and allowances as per the provisions of Sections 30 to 38 and thus, prevent the possible claim of double deduction.

However, it does not touch upon the applicability of Sections 28, 29, 39 to 43C. Hence, the other provisions including Section 40A (or the like) which deal with the disallowances or other matters are equally applicable.

ii) Further, proviso to Section 44AD(2) provides that from 8 per cent profit of small business, a firm would be entitled to deduct remuneration/ interest paid to partners, subject to the conditions of Section 40(b).

### Example

A firm has turnover of ₹50 lakh. Remuneration and interest payable, respectively, are ₹1,00,000 and ₹20,000. Profits of small business of the firm would be 8 per cent of ₹50 lakh, i.e., ₹4 lakh and profits includible in total income of the firm would be ₹2,80,000 [4,00,000 – (1,00,000 + 20,000)].

### Section 44AD(3)

Section 44AD(3) of the Act states that the written down value of any asset of an eligible business shall be deemed to have been calculated as if the eligible assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.

### Comments

i) Section 44AD(3) lays down manner of computation of 'written down value' (w.d.v.) of an asset used in small business. Determination of w.d.v. is essential for:

a) Allowance of depreciation in the year in which provisions of such Section 44AD(1) do not apply; and

b) Computation of gains, if any, on sale of asset used in small business.

Section 44AD(2) excludes applicability of Section 32 (therefore, rules framed thereunder). However, for computing w.d.v. under Section 44AD(3) the rate of depreciation as applicable under rules should be applied in as much as under Section 44AD(2), depreciation is presumed to have been allowed under Section 32 and no further depreciation could be allowed.

ii) Determination of w.d.v. of the asset sold during the year

### Example

Ques: An assessee purchased an asset (subject to depreciation at the rate of 15 per cent on 1-11-2010 for ₹4,00,000/- and opted for Section 44AD for the financial year 2010-11. In the financial year 2011-12, he opted for lower amount. In the next financial year 2012-13, he opted for Section 44AD. The asset was sold for ₹3,00,000/- on 1-1-2014.

Ans.:

	₹
Cost of asset on 1-11-2010	4,00,000
Less: Depreciation on 31-3-2011 [4,00,000 x 15% x ½] – Deemed to have been allowed during the financial year 2010-11	30,000
W.D.V. as on 31-3-2011	3,70,000
Less: Depreciation on 31-3-2012 [3,70,000 x 15%] – Actually allowed	55,500
W.D.V. as on 31-3-2012	3,14,500
Less: Depreciation on 31-3-2013 [3,14,500 x 15%] – Deemed to have been allowed during the financial year 2012-13	47,175
W.D.V. as on 31-3-2013	2,67,325
Sale on 1-1-2014	3,00,000
W.D.V. as on 31-3-2014	Nil

- Calculation of Capital gain during the F.Y.: 2013-14

Sale on 1-1-2014	3,00,000
W.D.V. as on 31-3-2013	2,67,325
Short term capital gain under Section 50	32,675

### Section 44AD(4)

Section 44AD(4) of the Act states that the provisions of Chapter XVII-C: Advance payment of tax shall not apply to an eligible assessee in so far as they relate to the eligible business.

### Comments

It implies that the exemption from payment of advance tax is restricted to profits and gains of eligible business. In respect of the other income of an eligible assessee, he would be liable to pay advance tax thereon, in terms of the provisions of Chapter XVII-C of the Act.

### Section 44AD(5)

Section 44AD(1) of the Act states that notwithstanding anything contained in the foregoing provisions of this Section, an eligible assessee who claims that his profits and gains from the eligible business are lower than the profits and gains specified in sub-section (1) and whose total income exceeds the maximum amount which is not chargeable to income-tax, shall be required to keep and maintain such books of account and other documents as required under sub-section (2) of Section 44AA and get them audited and furnish a report of such audit as required under Section 44AB.

### Comments

- a) Exemption from Maintenance of Books of Account and Audit

If an assessee engaged in the eligible business chooses to declare in his return of income the specified profit or a higher amount, the provisions

relating to maintenance of books of account (Section 44AA) and audit (Section 44AB) would not apply.

- b) When Accounts Compulsory Irrespective of Turnover

Clause (iv) has been inserted in Section 44AA(2) by the Finance (No. 2) Act, 2009 w.e.f. 1-4-2011 i.e. from Assessment Year 2011-12 to provide that where an eligible assessee claims that the profit of the eligible business is lower than the specified amount, and his income exceeds the maximum amount, which is not chargeable to tax, he shall maintain books of account.

In other words, the monetary minimum limit of ₹1,20,000 of income and of ₹10,00,000 of sales/turnover specified in Section 44AA will not apply to those assesseees, who claim that profit from small business is less than the deemed profit of 8 per cent of turnover/receipts.

- c) When Audit Compulsory Irrespective of Turnover

Clause (d) has been inserted in Section 44AB by the Finance (No.2) Act, 2009 w.e.f. 1-4-2011 i.e., Assessment Year 2011-12 to provide that where an eligible assessee claims that the profit of the eligible business is lower than the specified amount, and his income exceeds the maximum amount, which is not chargeable to tax, he shall have the books of account audited and furnish report thereon.

In other words, the monetary minimum limit of turnover of ₹60,00,000 specified in clause (a) of Section 44AB will not apply to those assesseees, who claim that profit from small business is less than the deemed profit of 8 per cent of turnover / receipts.

### Conclusion

The scheme of presumptive tax, as applicable to small business, in brief, is as follows:

- 1) Section 44AD provides for a

method of estimating income from the small business (other than transport) having a maximum total turnover or gross receipts (Revenue/Turnover/Receipts) of ₹60,00,000.

- Gross receipts are the amount received from the clients for the contract and will not include the value of material supplied by the client – *CIT v. Guruswami* (1973) 92 ITR 90 (Mad.)
- 2) The scheme would apply to resident individuals, HUF and partnership firms, other than LLP (i.e., Limited Liability Partnership) and the persons who avail deduction(s) under Sections 10A, 10AA, 10B, 10BA ( Chapter III deductions) or deduction(s) as per provisions under the heading 'C- Deductions in respect of certain incomes' of Chapter VI-A ('Chapter VI-A deductions).
- 3) Presumptive amount of profit at the rate of 8 per cent of Revenue is comprehensive, i.e., no further deduction will be allowed under Sections 30 to 38. However, in the case of firm, a normal deduction under Section 40(b) shall be allowed.
- 4) The scheme is optional and a person can claim that his income from small business is lower than the specified limit, subject to obligation of maintaining accounts and have these accounts audited.
- 5) An assessee opting for the scheme is exempted from payment of advance tax on income relating to small business.
- 6) An assessee opting for the scheme is not obliged to maintain the accounts or have the accounts audited, unless he claims that his income is lower than the presumptive amount. ■

# Career Ascent, The Mid-Career Campus

Coming up with better opportunities



Rotary Sadan, Kolkata  
28th - 30th January, 2011,  
10.00 a.m. to 6.00 p.m.

**Climb the ladder of your Career**

**Committee for Members in Industry (CMII) of ICAI  
is bringing the Career Ascent**

to provide experienced Chartered Accountants with a platform  
to assess their potential and refinement in work,  
which they have acquired during their working tenure.

**The Corporates are welcome to participate in Career Ascent.**

**Find the perfect business solution provider of your requirements.**

For details please visit: [www.icai.org/forum](http://www.icai.org/forum)



Committee for Members in Industry,  
The Institute of Chartered Accountants of India  
(A Statutory body established under an Act of Parliament)  
ICAI Bhawan, P. O. Box No. 7100  
Indraprastha Marg, New Delhi - 110 002  
[www.icai.org](http://www.icai.org), [www.cmii.icai.org](http://www.cmii.icai.org), <http://:jobs4cas.icai.org>

For details contact:  
Chairman, CMII

Tel: +91 (11) 3011 0491 E-mail: [placements@icai.org](mailto:placements@icai.org),

Secretary, CMII

Tel: +91 (11) 3011 0450 E-mail: [mii@icai.in](mailto:mii@icai.in), [secretarycmii@icai.in](mailto:secretarycmii@icai.in)

Deputy Secretary, EIRC

Tel: +91 (33) 3021 1132 E-mail: [eircevents@icai.in](mailto:eircevents@icai.in), [abasu@icai.in](mailto:abasu@icai.in)

## Issues on Assessment of Charitable Trusts



The authors in this article discuss the issues like whether deficit (excess application) of earlier years can be set off against surplus of subsequent years; If capital expenditure is incurred as application of income, whether it disentitles the assessee to claim deferred expenditure on the same asset by way of depreciation; and Whether repayment of loan can be treated as application of income.

### Whether deficit (excess application) of earlier years can be set off against surplus of subsequent years?

Excess application of income in earlier years should be considered as application out of the income of the current year for the purposes of Section 11 of the Income-tax Act, 1961 (the Act). Section 11 of the Act states that income derived from property held under trust is to be excluded for the purposes of computing income of the trust for the purpose of assessment to the extent to which such income is applied to charitable or religious purposes in India. This Section now here limits or states that the income should have been applied for charitable or religious purposes only in the year in which the income has arisen. The word 'applied' here means 'put to

use to meet expenses for charitable/religious purpose'. Application takes place in the year in which the income is adjusted to meet the expenses (even if expenses have been incurred in an earlier year). Further as income of trust is to be computed on commercial basis, it is but natural that excess expenses incurred in earlier year have to be adjusted against income of subsequent year and it will have to be regarded as application of income in the subsequent year in which such adjustment has been made having regard to the benevolent provisions contained in Section 11 of the Act.

In *CIT v. Maharana of Mewar Charitable Foundation* (1987) 164 ITR 439 (Raj), their Lordships of the Rajasthan High Court held that if the expenses for charitable and religious purposes have been incurred in the earlier year and the said expenses



**CA. (Dr.) Tushar K. Doctor and  
CA. Zankhana Mehta**

(The authors are members of the Institute. They can be reached at [eboard@icai.org](mailto:eboard@icai.org))

are adjusted against the income of a subsequent year, the income of that year can be said to be applied for charitable and religious purposes in the year in which the expenses incurred for charitable and religious purposes had been adjusted. Adjustment of excess expenditure against income of following year would amount to application of income for charitable purpose.

This view was reiterated by the Gujarat High Court in *CIT v. Shri Plot Swetambar Murti Pujak Jain Mandal* (1995) 211 ITR 293 (Guj) and by the Madras High Court in *CIT v. Matriseva Trust* (2000) 242 ITR 20 (Mad). In these cases it was held and observed that where on charitable and religious purposes had been incurred in an earlier year, such expenditure if adjusted against the income of the subsequent year, the income of that subsequent year can be said to have been applied for charitable or religious purposes in the year in which the expenditure was incurred. It was also held that income derived from trust property has to be determined on commercial principles and the application of such commercial principles also warrants the conclusion that the expenditure incurred in an earlier year can be set off against the income of the subsequent year.

In *Trustees of Balkan-Ji Bari* (1979) 10 CTR (Trib.) 22, the Bombay Bench of the Tribunal upheld the assessee's contention that it should be allowed the adjustment of excess amount spent towards charitable purposes in the earlier years against current income to determine the funds available with the assessee for the purpose of Section 11(1) of the Act.

Under Section 11 (1)(a) the income from property held in trust for charitable purposes is exempt to the extent it is applied for such purposes in India. It is not necessary that the amount must be spent in the year in which the trust has derived income from property held in trust. This view has also been taken in

**“ Adjustment of excess expenditure against income of following year would amount to application of income for charitable purpose. The emphasis of the Section 11 is on spending of the income and not on confining to the source of the amount spent or what income is earned during the previous year. ”**

the case of *Siddaramana Chettiar Trust vs. CIT* 96 ITR 275 (Mysore). In the case of *Chotanagpur Diocesan Trust vs. ITO* 19 ITD 175 (Patna) IT Appellate Tribunal has taken the view that it is not necessary that the amount to be spent on charitable purposes must be out of income earned during the previous year only. Even if the amount is spent out of income of the earlier year, the excess amount spent in the earlier years will be allowable for set off against the income in the subsequent years. In this case the Tribunal has stated that the emphasis of the section is on spending of the income and not on confining to the source of the amount spent or what income is earned during the previous year.

In the case of *CIT vs. Sacred Heart Church* 278 ITR 180 (Guj), the High Court held that adjustment of expenses incurred by a trust for charitable purposes in any earlier year against the income earned by the trust in the subsequent year will amount to applying the income of the trust for charitable purposes in the subsequent year in which adjustment has been made. In other words, if a trust has incurred expenditure exceeding the income of an earlier year, the excess of the expenditure incurred in an earlier year can be adjusted against the surplus of the subsequent year and this surplus in the subsequent year will not be liable to tax if the excess amount spent in the earlier years together with

the expenditure incurred in the year in which there is a surplus exceeds 85 per cent of the income of the subsequent year.

In the case of *CIT vs. Institute of Banking Personnel Selection* 264 ITR 110 (Bom), the A.O. disallowed the claim for carry forward of deficit of the earlier years for adjustment against the surplus of the subsequent years on the ground that such carry forward loss was applicable only to income under the head “Profits & Gains of Business” and was not permissible in case of income under Sections 11 to 13 of the Income-tax Act. The Bombay High Court held that income derived from the trust property is to be computed on commercial principles. Accordingly, adjustment of expenses incurred by the trust for charitable purposes in the earlier years against the income earned by the trust in the subsequent year will have to regard as application of income of the trust in the subsequent year. The High Court has also held that the depreciation debited in the books should be treated as expenditure for this purpose.

In the case of *Gem & Jewellery Export Promotion Council vs. ITO* (68 ITD 95) IT Appellate Tribunal Mumbai has held that where the assessee has made excess application of income in the earlier years, such excess should be considered as application out of the current year for the purpose of Section 11. IT Appellate Tribunal Mumbai has also held in this case that the income of the trust is to be computed on commercial principles.

**“ If capital expenditure is incurred as application of income, whether it disentitles the assessee to claim deferred expenditure on the same asset by way of depreciation? ”**

For the purpose of determining the income of the Trust eligible for

exemption under Section 11, income arising from property held under Trust constitutes the income of the Trust. It will mean income from property, business, dividends, interest on securities or other interest. In other words, the income for the purpose of Section 11 is the income as per the accounts of the Trust. It means, income in the commercial sense, without reference to the heads of income specified in Section 14, i.e. the book income and not total income as defined in Section 2(45), 'being the total amount of the income ..... computed in the manner laid down in the Act'. This position is confirmed in *CIT v. Trustees of H.E.H. Nizam's Supplemental Religious Endowment Trust* (1981) 127 ITR 378 (A.P.), *CIT v. Rao Bahadur Calwala Cunnan Chetty Charities* (1982) 135 ITR 485 (Mad.) and *CIT v. Estate of V. L. Ethiraj* (1982) 136 ITR 12 (Mad.). This position is also confirmed by the CBDT vide its Circular No. 5-P (LXX-6) dated 19<sup>th</sup> June, 1968.

The concept of commercial income necessarily envisages deduction of

depreciation on assets of the Trust. This view is supported by the following decisions.

Even as depreciation on assets of a Trust is to be deducted for the purpose of calculating income of a Trust. This is because of the fact that the concept of commercial income necessarily envisages deduction of depreciation on assets of the Trust. The Tribunal has decided in some cases that even reasonable depreciation on assets and interest on Sinking Fund or Repairs Reserve are to be deducted. [*Balkan-Ji- Bari* (1979) 2 Taxman 377 (Bom.)]

The Bombay High Court has rejected the reference application of the Income Tax Department in the case of *CIT v. Framjee Cawasjee Institute* (1993) 109 CTR 463, holding that the answer to the question whether depreciation was allowable to a charitable Trust was self-evident, even if the capital value of the assets on which depreciation was claimed had been allowed as a deduction under Section 11 as an application of income

**“Income derived from trust property has to be determined on commercial principles and the application of such commercial principles also warrants the conclusion that the expenditure incurred in an earlier year can be set off against the income of the subsequent year.”**

for religious or charitable purposes. Once again in *CIT v. Institute of Banking Personnel Selection (IBPS)* 264 ITR 110, the Bombay High Court held that depreciation should be allowed even on assets, the cost of which had been allowed as exempt under Section 11 in the preceding years. The Bombay High Court also held that depreciation should be allowed even on assets received on transfer from another charitable Trust on which no cost was borne by the assessee Trust.

Other High Courts which have also taken the view that depreciation is deductible are the Karnataka High



Court in the case of *CIT v. Society of the Sisters of St. Anne* (1984) 146 ITR 28 and the Madhya Pradesh High Court in the case of *CIT v. Raipur Pallottine Society* (1989) 180 ITR 579.

In *CIT v. Seth Manilal Ranchhoddas Vishram. Bhovan Trust* (1992) 105 CTR (Guj) 303 it was held that depreciation should be allowed while computing such income under Section 11(i)(a).

Many times Assessing Officers take the stand that "provision of computation of income under Section 11 does not contain any provision which may entitle an assessee to claim weighted deduction for any expenses incurred." This statement is not acceptable as Section 11 provides that the income of the trust is to be computed on commercial basis i.e. as per normal accounting principles. Normal Accounting Principles clearly provide for deducting depreciation to arrive at income. Now, the income so arrived at (after deducting depreciation) is to be applied for charitable purpose. Capital expense is application of the income so determined. So there is no double deduction or double claim of the same amount as application. Thus depreciation is to be deducted to arrive at income and it is not application of income. In support of their stand, the department relies on the decision of the Supreme Court in *Escorts Ltd.* 199 ITR 43.

However in this case the issue before the Supreme Court was that whether

**The concept of commercial income necessarily envisages deduction of depreciation on assets of the Trust. Section 11 provides that the income of the trust is to be computed on commercial basis i.e. as per normal accounting principles. Normal Accounting Principles clearly provide for deducting depreciation to arrive at income.**

both depreciation under Section 32 and capital expenditure on scientific research under Section 35(1)(iv) can be claimed as deduction. Reference to this decision cannot be drawn as in *Escort's* case both were deductions under the head 'business income' whereas in case of a charitable trust depreciation is a deduction to arrive at income and capital expenditure is application of such income. The aforesaid decision of *Escorts Ltd.* cannot be applied to determine taxable income for a trust as the provisions to determine taxable income of the trust are totally different and normal provisions for computing income under five heads cannot be applied.

### Whether repayment of loan can be treated as application of income?

Repayment of loan is to be treated as application based on following favourable decisions and CBDT Circular.

In *CIT v. Janmabhumi Press Trust* (2000) 242 ITR 457 and 703 the Karnataka High Court held that the repayment of a debt incurred by the trust for construction of the building, which in turn would augment its income, should be treated as application of the income of the trust for charitable purposes. In this respect, the Court followed the view earlier taken by the Madras High Court in *CIT v. Kannika Parameswari Devasthanam & Charities* (1982) 133 ITR 779 and the Kerala High Court in *CIT v. St. George Forana Church* (1988) 170 ITR 62.

### Circular No. 100 dated 24<sup>th</sup> January, 1973 (1973) 88 ITR (St.) 66

Ques: Where a trust incurs a debt for the purposes of the trust, whether the repayment of the debt would amount to an application of the income for the purposes of the trust?

Ans: The loan was taken by the trust to fulfill the objects of the trust.

**Depreciation is to be deducted to arrive at income & it is not application of income. Repayment of loan is to be treated as application of the income of the trust for charitable purposes.**

Therefore, the repayment of the loan will amount to an application of the income for charitable and religious purposes.

In the case of *CIT v. Maharana of Mewar Charitable Foundation* (1987) 164 ITR 439, the Rajasthan High Court has considered the Circular and held as follows:

"In the Circular dated 24<sup>th</sup> January, 1973, the Central Board of Direct Taxes has considered the question to whether where a trust incurs a debt for the purpose of the trust, the repayment of the debt would amount to an application of income for the purposes of the trust. In the said circular, the Central Board of Direct Taxes has expressed the view that the repayment of the loan originally taken to fulfill one of the objects of the trust will amount to an application of the income for charitable and religious purposes. In other words, according to the said circular, if the trust wants to spend more money on charitable and religious purposes, then, in a particular year, it can take a loan and the said loan can be repaid out of the income of the subsequent year and the repayment of the said loan out of the income of the subsequent year would amount to application of income for charitable and religious purposes under Section 11(1)(a) of the Act".

Also in a recent decision of 2009 in the case of *DDIT (E) v. Govindu Naicker Estate* (Mad) 227 CTR 283 it was held that repayment of loan is to be treated as application under Section 11. ■

# Provision of Section 14A Read With Rule 8D and Recent Judicial Controversial Decisions



**Section 14A has been inserted in the Income-tax Act, 1961 by the Finance Act, 2001, with retrospective effect from 1-4-1962. This Section was amended vide Finance Act, 2006 w.e.f. 1-4-2007 and for the assessment year 2007-08. Rule 8D of the Income-tax Rules, 1962 which provided for “Method for determining amount of expenditure in relation to income not includible in total income” was amended on 24-3-2008. The authors in this article discuss various judicial decisions/controversies on Section 14A and Rule 8D.**

## Introduction

Section 14A has been inserted in Chapter IV of the Income-tax Act, 1961 (the Act) by the Finance Act, 2001, with retrospective effect from **1-4-1962**. This Section provides for disallowance of expenditure incurred in relation to earning of Income which does not form part of Total Income of the Assessee i.e. exempt income.

The explanatory memorandum issued with the Finance Bill, 2001, gives the purpose for which the amendment is made reads as under:

*“Certain incomes are not includible while computing the total income as these are exempt under various provisions of the Act. There have been cases where deductions have been claimed in respect of such exempt income. This, in effect means that the tax incentive given by way of exemptions to certain*

*categories of income is being used to reduce also the tax payable on the non-exempt income by debiting the expenses incurred to earn the exempt income against taxable income. This is against the basic principles of taxation whereby only the net income, i.e., gross income minus the expenditure, is taxed. On the analogy, the exemption is also in respect of the net income. Expenses incurred can be allowed only to the extent they are relatable to the earning of taxable income.*

*It is proposed to insert a new Section. 14A so as to clarify the intention of the legislature since the inception of the Income-tax Act, 1961, that no deduction shall be made in respect of any expenditure incurred by the assessee in relation to income which does not form part of the total income under the*



**CA. Hemantkumar Salian and  
CA. Sheela Chitlangia**

*(The authors are members of the Institute. They can be reached at [ebboard@icai.org](mailto:ebboard@icai.org))*

**Plain reading of explanatory memorandum makes it clear that the intention of the Legislature was to disallow direct expenditure incurred for earning of Exempt Income.**

*Income-tax Act.*

*The proposed amendment will take effect retrospectively from 1-4-1962 and will accordingly apply in relation to the Asst. year 1962-63 and subsequent assessment years."*

Plain reading of above explanatory memorandum makes it clear that the intention of the legislature was to disallow direct expenditure incurred for earning of Exempt Income. Even before the insertion of this Section various High Courts and also the Supreme Court has held that direct expenditures which were incurred for earning of exempt income can not be allowed in computing total taxable income of the assessee. Therefore, even in the absence of a specific provision contained in the new Section 14A, the law was well settled.

Over a period of time a lot of litigation has cropped up due to different interpretation of Section 14A by the Department and the assessee. Assessee in the course of earning income incurs various kinds of expenditure. Some of the expenditures can be directly attributable to earning of exempt income. Expenses which are directly attributable to earning of Exempt Income such as interest paid on acquisition of shares etc. need to be fairly disallowed and hence no litigation. However, expenditures which are incurred indirectly for earning of exempt Income paves way for litigation between the Department and the Assessee. It is very difficult to attribute expenditures which are common in nature. To resolve the situation sub-sections (2) and (3) of Section 14A

were inserted by the Finance Act, 2006 w.e.f. 1-4-2007 (Assessment Year 2007-08). By this amendment sub-sections (2) and (3) were added in Section 14A and the existing provision contained in Section 14A was renumbered to sub-section (1). These newly inserted sub-sections (2) and (3) provided that A.O. shall determine the amount of expenditure incurred in relation to the exempt income in accordance with such method as may be prescribed by Rules. The reasons for making this amendment in Section 14A was explained in Paras 11.1 to 11.3 of CBDT Circular No. 14/2006 of 28-12-2006. As per this Circular the Legislature has clarified that the intention of insertion of sub-sections (2) and (3) was to provide a method for computing the expenditure incurred in relations to earning of exempt Income, which was missing in the erstwhile Section 14A.

Before understanding the analogy of Section 14A, let us go through the provisions of Section 14A as appearing in the Act:

**Section 14A: Expenditure incurred in relation to income not includible in total income**

- (1) *For the purposes of computing the total income under this Chapter, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under this Act.*
- (2) *The Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income under this Act in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part*

*of the total income under this Act.*

- (3) *The provisions of sub-section (2) shall also apply in relation to a case where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under this Act :*

**Provided** *that nothing contained in this Section shall empower the Assessing Officer either to reassess under Section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under Section 154, for any assessment year beginning on or before the 1st day of April, 2001."*

The reading of sub-section (1) of Section 14A makes it amply clear that no deduction shall be allowed in respect of expenditure which has been incurred in earning of Exempt Income. Sub-section (2) empowers the Assessing Officer to determine the amount of Expenditure which is attributable to earning of Exempt Income as per the method prescribed, if the Assessing Officer is not satisfied with the claim of Assessee. Further sub-section (3) clarifies that the provision of sub-section (2) would even apply in the cases where an assessee contends that he has not incurred any expenditure in earning of Income which does not form part of his Total Income. Proviso to Section 14A restricts the power of the Assessing Officer to either reassess under Section 147 or to pass an order altering the Total Income under Section 154 (i.e. mistakes apparent from records) for any assessment year beginning on or before the **1<sup>st</sup> day of April, 2001.**

In exercise of the powers given under Section 14A (2) CBDT vide Notification No. S.O. 47(E) on 24-3-2008 (299 ITR (ST) 88) had amended the Income-tax Rules by insertion of a new Rule 8D providing for a

**“Method for determining amount of expenditure in relation to income not includible in total income”.** Rule 8 is reads as under –

**Rule 8D: Method for determining amount of expenditure in relation to income not includible in total income**

(1) Where the Assessing Officer, having regard to the accounts of the assessee of a previous year, is not satisfied with—

- (a) the correctness of the claim of expenditure made by the assessee; or
- (b) the claim made by the assessee that no expenditure has been incurred, in relation to income which does not form part of the total income under the Act for such previous year, he shall determine the amount of expenditure in relation to such income in accordance with the provisions of sub-rule (2).

(2) The expenditure in relation to income which does not form part of the total income shall be the aggregate of following amounts, namely :—

- (i) the amount of expenditure directly relating to income which does not form part of total income;
- (ii) in a case where the assessee has incurred expenditure by way of interest during the previous year which is not

directly attributable to any particular income or receipt, an amount computed in accordance with the following formula, namely :—

$$\begin{array}{r} B \\ A \quad X \quad - \\ C \end{array}$$

**Where,** A = amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year;

B = the average of value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

C = the average of total assets as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

(iii) an amount equal to one-half per cent of the average of the value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year.

(3) For the purposes of this rule, the “total assets” shall mean, total assets as appearing in the balance sheet excluding the increase on account of revaluation of assets but including the decrease on account of revaluation of assets.”

A plain reading of Rule 8D makes it clear that sub-rule (1) is a reproduction of sub-sections (2) and (3) of Section 14A.

**Limb 1**– the amount of expenditure directly relating to income which does not form part of total income (Direct Expenditure).

**Limb 2**– the Interest Expenditure (other than those included in Limb 1) in the proportion of Average Investment to

Average Asset. For the purpose of this limb average Investment and average Asset would be calculated on the basis of Opening and Closing corresponding figures appearing on the balance sheet of the Assessee.

**Limb 3**– on presumptive basis i.e. at 0.5 per cent of Average Investment.

It may be noted that for the purpose of ‘Investment’ in Limb 2 and 3, only those investment should be considered which are capable of giving rise to Exempt Income. In short, Investments such as Bank Deposits, Bonds etc. which would give rise to non exempt income should not be considered.

### Recent Judicial Decisions/ Controversies on Section 14A and Rule 8D

**1. Cheminvest Ltd v. ITO (ITAT Delhi Special Bench)(Decided on 5<sup>th</sup> August, 2009)**

In this case a Special Bench was constituted by the President to dispose and decide an appeal containing following issue –

“Whether disallowance u/s. 14A of the I.T Act can be made in a year in which no exempt income has been earned or received by the Assessee?”

**Facts:** Assessee Company had borrowed a huge sum of money and invested a part of the same in the Shares and securities which were earmarked as Long Term Investment. Such Investment did not earn any Exempt Income during the relevant financial year. The Assessing Officer disallowed a part of interest paid on proportionate basis, though no exempt income was earned during the year. The contention of the Assessee was that the provision of Section 14A would be triggered only when an Exempt Income is earned. Assessing Officer

**Section 14A was amended by the Finance Act, 2006 by inserting sub-sections (2) and (3) which provided that the Assessing Officer shall determine the amount of expenditure incurred in relation to the exempt income in accordance with such method as may be prescribed by the Rules.**

rejected the contention of the Assessee and held that Section 14A would be applicable when Investment is made in a security which is capable of giving rise to Exempt Income.

**Decision of the Tribunal:** Tribunal upheld the Order of Assessing Officer of disallowing the Expenditure even though no Exempt Income was earned by the Assessee.

**2. Income Tax Officer v. Daga Capital Management (P.) Ltd. [2009] 117 ITD 169 (MUM) (SB) [Decided on October 20, 2008]**

President of ITAT has constituted a Special Bench to hear and decide on following appeal –

*“Whether, in the facts and in the circumstances of the case and in law, the provisions of Section 14A of the Income-tax Act, 1961, are applicable with respect to dividend income earned by the assessee engaged in the business of dealing in shares and securities, on the shares held as stock-in-trade and when earning of such dividend income is, therefore, incidental to trading in shares?”*

Subsequently the President of ITAT has directed the Bench to dispose off the following appeals also –

1. *M/s. Cheminvest Ltd, New Delhi v/s. ITO, New Delhi* ( 2 Appeals )
2. *M/s. Maxopp Investment Ltd. v/s. ACIT, New Delhi.*

**Facts:**

- a. Daga Capital Management (P) Ltd.

The Assessee was engaged in the business of dealing in shares in the year under consideration and declared loss of ₹12,87,780/-. Assessee has claimed expenditure by way of interest amounting to ₹9,58,325/-. Assessee has earned a Dividend of ₹1,78,163/-, which was claimed as exempt from tax

under Section 10(33) of the Act. The A.O. disallowed a sum of ₹9,58,325/- under Section 14A on the ground that borrowed funds were mainly used for making investments in shares and securities of other companies with long term perception in mind to earn lump sum dividend without contributing anything to the exchequer on account of Income tax. AO further observed that the assessee has not done any business in shares and securities except for few transactions and only income earned during the year was dividend income. AO however, accepted the loss of ₹2,86,240/- incurred on account of dealing in shares.

- b. *M/s. Cheminvest Ltd, New Delhi.* Assessee is engaged in the business of dealing in shares and securities. Assessing Officer determined the disallowance of interest at ₹1,00,49,752/- on pro-rata basis. Similar basis was adopted for A.Y. 2002-03.
- c. *Maxopp Investments Ltd.* Assessee is an investment company primarily holding shares of Max India Ltd. Assessing Officer applied the provisions of Section 14A of the Act and made disallowance of ₹67,74,175/- on pro rata basis.

**Arguments/Contention of the Assessee (Daga Capital Management):** The assessee was engaged in the business of dealing in shares and securities and not to make any investments in shares on long term

**“ Though Section 14A has been inserted with retrospective effect from 01.04.1962 and since Rule 8D has been notified only on 24.03.2008, it would be effective only from Assessment Year 2008-09 onwards. ”**

basis. The intention of the assessee was always to hold the shares as stock-in-trade and dividend income was only the by-product of the trading activity and therefore, there was no relation between the expenditure by way of interest and the exempted income. In view of the above facts, Interest disallowed by the A.O. should be allowed under Section 36(1)(iii) and the provision of Section 14A should not be applied.

**Judgment/Finding of the Tribunal:**

Tribunal observed that total income of the assessee is to be computed under various heads of income specified in Section 14. The requirements for computation of income under various heads are provided in Sections 15 to 57 of the Act. Instead of making various provisions for disallowance under various heads, Section 14A has been inserted at the inception i.e. prior to the computational provisions under various heads. Thus, the intention of the legislature is clear i.e. to disallow all the expenditures incurred in relation to income not forming part of total income. The Tribunal was convinced that the Section 14A has an overriding effect over the computational provisions under various heads. Hence the contentions of the Assessee that no disallowance can be made under Section 14A if the deduction is permissible under Section 36(1)(iii) of the Act is not acceptable. Which in short means that any expenditure incurred by an assessee even though allowable under Section 36(1)(iii) or Section 37 or any other Section of Income Tax for that matter can be disallowed under Section 14A if such expenditure has been incurred in relation to the income not forming part of total income.

In case of an assessee who carries on a business which is capable of earning both Taxable Income as well as Exempt Income, the question does arise as to how to determine the

nature of the connection between the expenditure incurred and the income earned. The answer to this question would depend upon the intention/object with which the expenditure was incurred. Where an assessee has earned both taxable as well exempt incomes, then disallowance can be made under Section 14A on proportionate basis in accordance with the provision of sub-sections 2 and 3 of Section 14A of the Act. In the case of dealers of shares, the shares are purchased not with the intention of earning dividend Income but the dominant and immediate object behind acquisition of shares is to earn profit on sale of shares at the earliest point of time which is chargeable to tax. In such cases, the dividend income earned is incidental only since the dominant and immediate connection exists only between the expenditure incurred and profit on sale of shares. Since the existence of dominant and immediate connection is the condition precedent for invoking the provisions of Section 14A of the Act, the ITAT held that mere receipt of dividend income incidentally in the case of dealer in shares would not be sufficient for invoking the provisions of Section 14A of the Act. Onus of proving that there exists dominant and immediate connection between the expenditure incurred and the income not forming part of total income would lie on the A.O. On the other hand, where the assessee claims deduction under Section 36(1) (iii) or Section 37, the onus would be on assessee to prove that the expenditure was for the purpose of the business. Once this onus is discharged, it would shift to the A.O to establish that there exists dominant and immediate connection between expenditure incurred and income exempt from tax if provisions of Section 14A are invoked by him.

It may be noted that one of the member of the Bench, Shri. K C Singhal was of the opinion that in case

**“For earlier Assessment Years, though the expenses pertaining to exempt income are not allowable, the disallowance has to be on a reasonable basis having regard to the accounts of the assessee and after furnishing a reasonable opportunity for the assessee to place all germane material on record.”**

of dealer in shares, no disallowance under Section 14A can be made merely because some dividend is received incidentally unless it is established that there was dominant and immediate connection between the acquisition of shares and the earning of dividend income. However, this view was not accepted by other two members of the Bench namely Shri G.C. Gupta (Judicial Member) and Shri R.S. Syal, (Accountant Member). They were of the view that plain reading of Section 14A did not specify any such distinction at all and therefore held that the provision of Section 14A would even be applicable in case where shares are held as stock-in-trade.

Thus, on the basis majority, the appeal was decided against the Assessee and in favour of the Revenue.

However, in case of *M/s. Cheminvest Ltd* and *M/s. Maxopp Investment Ltd*, the Tribunal held that the Assessee company was engaged in investment activity rather than dealing activity i.e. assessee has acquired shares of Max India Ltd and Gaylord Impex Ltd with the intention of long term investment and not to earn profit from immediate sale and as such the intention from the factual details of holding of the Assessee only reveals the fact that earning of dividend income was dominant and immediate connection of the Assessee. Therefore, the disallowance under Section 14A was justified.

The Tribunal further held that sub-section 2 and 3 of Section 14A are procedural provisions for determining the disallowance of the expenditure in relation to income not forming part of total income. Since it is a settled principle in law that a procedural law would be applicable to all pending matters, the ITAT held that the provisions of Section 14A alongwith Rule 8D would be applicable for A Y 2001-02 and 2002-03 also.

**Note: In the case of *Godrej & Boyce Mfg. Co. Ltd*, Mumbai, the Bombay High Court took a difference view. (Discussed separately in this Article)**

**3. ACIT -1(2), *Mumbai v. Mc. Indexport Limited*, ITAT Mumbai [ITA No. 1941/MUM/2004 decided on January 29, 2009]**

The issue raised by the Income Tax Department before the ITAT, Mumbai, was as under –

*“On the facts and in the circumstances of the case, the Ld CIT(A) erred in restricting without giving any reason for disallowance of expenses incurred by the Assessee to earn the exempt Income under Section 14A to 5 per cent against 10 per cent made by the AO”*

**Facts:** Assessing Officer by invoking the provision of Section 14A and disallowance made in the earlier years by adopting the ratio of investments attributable to dividend and tax free receipts to total investment including current assets had worked out the interest attributable to tax free receipts and also estimated 10 per cent of other expenses being attributable to tax free receipts and had disallowed a sum of ₹15,20,473/-. The CIT(A) on elaborate consideration of the investment made by the assessee in the tax free securities and after considering the Cash Flow Statement filed by the Assessee confirmed the disallowance

on account of interest expenditure. However, the CIT(A) reduced the disallowance on account of estimated other expenses attributable to tax free income from 10 per cent to 5 per cent. The grievance of the revenue is with regard to said reduction in the estimated other expenses held to be incurred for the earning of tax free income. The assessee has raised the issue of allowability of the balance expenditure. The Learned AR for the assessee also pointed out that the Tribunal in assessee's own case in the earlier years had allowed the claim of the assessee in entirety.

**Decision of the Tribunal:** Relying on the decision of the Special Bench Mumbai Tribunal in Daga Capital Management Pvt. Ltd's case (Supra) the Tribunal held that the provisions of Rule 8D of the Income-tax Rules are explanatory in nature and are applicable in all pending assessments. Accordingly, the Tribunal remitted the matter back to the AO with a direction to re-work the disallowance under Section 14A in line with the ratio laid down Daga Capital Management' case (Supra). Further it was held that the disallowance shall be restricted to the original disallowance made by the AO as the assessee cannot be put in a position worse off than it was originally in. Thus, the ground raised by the Revenue was allowed for statistical purpose.

**4. CIT – II v. M/s. Hero Cycles Ltd. (Punjab and Haryana High Court) [ITA No. 331 of 2009 decided on November 4, 2009]**

The following substantial question of Law was raised by the Income Tax Department before the High Court of Punjab & Haryana –

*"Whether on the facts and in law, the Hon'ble ITAT was legally justified in deleting the disallowance of ₹3,48,04,375/- under Section. 14A of the Income-tax Act, 1961*

*ignoring the evidence relied on by the Assessing Officer and holding that a clear nexus has not been established that the Interest bearing funds have been in vested for Investments generating tax free dividend Income."*

**Facts:** Assessee company was engaged in the business of manufacturing cycles and parts of two wheelers in various units. It earned dividend Income which were claimed as exempt under Sections 10(34) and 10(35) of the Act.

**Argument of Department:** The learned counsel of the Department argued that directly or indirectly some expenditure is always incurred which must be disallowed under Section 14A

**Decision of the High Court:** High Court dismissed the petition of the Department by observing that no substantial question of Law was involved in the present appeal of the Department. Following are the observations of the High Court –

*" ..... Disallowance under Section 14A requires finding of incurring of expenditure. Where it is found that for earning exempted Income no expenditure has been incurred, disallowance u/s. 14A cannot stand. In the present case finding on this aspect, against the revenue is not shown to be perverse.*

**“ The disallowance under section 14A read with Rule 8D cannot exceed actual expenses debited in the P & L A/c and that the notional disallowance specified in the Rule 8D(2) cannot exceed the actual expenditure incurred by the assessee, as an expenditure which has not been incurred and claim cannot be disallowed. ”**

*Consequently, disallowance is not permissible....."*

**5. C.I.T.v. Smt. Leena Ramachandran, Kerala High Court [ITA No. 1784 of 2009 decided on June 14, 2010]**

**Facts:** Assessee was running a business as proprietary concern engaged in trading of goods. The assessee paid an interest of ₹17,44,310/- at the rate of 24 per cent p.a on funds borrowed for purchase of shares in a company. Assessee's claim was that the acquisition of shares with borrowed funds was for the purpose of controlling the company which was engaged in Leasing Business and the assessee as proprietrix of the business sold such articles to the said leasing company. Since the borrowed funds were utilised for acquisition of shares of the company under the control of the assessee, assessee contended that the utilisation of borrowed funds was for business purpose entitling her for deduction of interest under Section 36(1)(iii) of the Act. Assessing Officer however, contended that the Assessee made investments by utilising borrowed funds in the form of acquisition of shares in the company and the only benefit assessee got was dividend Income. In fact, Assessee has earned dividend of ₹3 lakh out of such Investment in shares during the year. Accordingly he disallowed the whole of interest expenditure of ₹17,44,310.

**Argument of the Assessee:** Counsel appearing for the assessee contended that assessee's business was inextricably linked with the business of the leasing company in as much as the items sold by the assessee to the company only were leased out by that company to earn business income at the hands of the company. Since financial stability of the company was required to promote its business which in turn helps the assessee to do her business, the funds invested were for

business purpose and the decision of the Supreme Court referred in the case law of *S.A. Builders Ltd. v/s. CIT (2007) 288 ITR 1* was squarely applicable to the instant case.

**Decision of the High Court:** High Court upheld entire disallowance made by the Assessing Officer of interest paid on borrowed funds by observing the following –

“..... So much so, in our view, disallowance was rightly made by the Assessing Officer. In fact, the Tribunal itself has estimated disallowance of ₹2 Lakh by applying Section 14A. We do not know how the Tribunal can restrict the disallowance to ₹2 lakh and allow balance above ₹15 lakh when the whole borrowed funds were utilised by the assessee for purchase of shares in the company. In our view, the reasoning given by the Tribunal for disallowance of ₹2 lakh i.e. by applying Section 14A, squarely applies for the interest paid on borrowed funds because it is on record that the entire funds borrowed were utilised for acquisition of shares by the assessee in the company. In fact, in our view, assessee would be entitled to deduction of interest Section 36(1)(iii) of the Act on borrowed funds utilised for the acquisition of shares only if shares are held as stock in trade which arises only if the assessee is engaged in trading in shares. So far as the acquisition of shares is in the form of investment and the only benefit assessee derived is dividend income which is not assessable under the Act, the disallowance under Section 14A is squarely attracted and the AO, in our view, rightly disallowed the claim

.....the assessee is not entitled to deduction of any amount towards interest paid on

*funds borrowed by way of fixed deposits taken for acquisition of shares in the company, which helped the assessee only to earn some dividend. Consequently we allow the appeal by reversing the order of the Tribunal and by restoring the disallowance confirmed in first appeal.”*

**6. Godrej & Boyce Mfg. Co. Ltd, Mumbai v/s. Dy. Commissioner of Income Tax (Bombay High Court) [Order pronounced on 12<sup>th</sup> August, 2010]**

**Facts:** For Assessment Year 2002-03, the assessee claimed a dividend of ₹34.34 crore as exempt from total taxable income. Assessee contended that it has not incurred any expenditure in earning of exempt income. Assessing Officer bifurcated interest paid amounting to ₹51.71 crore in the proportion between investments attributable to dividend receipts (₹125.54 crore) to the total assets of the Assessee (₹938.11 crore). On this basis, the interest attributable to dividend receipts was computed at ₹6.92 crore which was disallowed by the A.O. CIT(A) following earlier years order held that no expenditure was attributable to the earning of the Dividend received and accordingly deleted the additions made by the AO. The Tribunal, following its decision in Daga Capital Management' case (Supra) held that sub-sections 2 and 3 of Section 14A are procedural in nature and have retrospective effect and accordingly remanded back the matter to the Assessing Officer for a fresh examination on the basis of the provisions of Section 14A(2).

Assessee filed an appeal before Bombay High Court, wherein it raised following substantial question of law:

a. *Whether on the facts and in the circumstances of the case, the Tribunal ought to have held that as*

*limited issue raised by Respondent No. 1 in the Assessment Order was as to the quantum of the exemption under Sections 10(33) that was available and not to disallow any part of the expenditure claimed, hence it was not open to the Revenue to expand the scope of appeal by invoking the provisions of Section 14A of the Act to disallow the expenditure incurred;*

b. *Whether on the facts and in the circumstances of the case, the Tribunal ought to have held that no disallowance could be made under Section 14A of the Act and hence erred in setting aside the issue relating to calculation of disallowance under Section 14A of the Act to Respondent No. 1;*

c. *Whether the Tribunal erred in directing Respondent No. 1 to apply Rule 8D of the Rules for computing the amount of disallowance under Section 14A of the Act.”*

In addition to aforesaid Appeal the assessee filed a Petition under Article 226 of the Constitution challenging the constitutional validity of the provisions of Section 14A as well as Rule 8D.

**Arguments of the Assessee:**

Assessee contended that a major portion of its dividend was received from group companies and of the total shares, 95 per cent consisted of Bonus Shares for which no cost had been incurred. The assessee further contended that it had reserves of ₹274 crore and capital of ₹6.55 crore which would be more than adequate to cover the investments.

**Contention of Assessing Officer:**

Assessing Officer observed that in the common pool of funds, it was difficult to ascertain whether investments had been made out of internal accruals or from borrowed funds. A.O was of the view that if the Assessee had not made investments in these securities, it would

not have been required to borrow funds to that extent and consequently, the interest burden could have been reduced.

**Decision of High Court:** The High Court has touched upon various issues and case laws to decide the sanctity of Section 14A and Constitutional validity of Rule 8D. During the course of hearing, the Assessee even contented that income received from Shares and Mutual Funds cannot be termed as Exempt Income, since the company has already paid tax under the provision of Sections 115O or 115R respectively.

However, the Bombay High Court decided as follows:-

- a. Dividend Income and income from Mutual Funds falling within the ambit of Section 10(33) or (34) or (35) of the Act, as was applicable for Assessment Year 2002-03 is not includible in computing the total income of the assessee. Consequently, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to such income which does not form part of the total income under the Act, by virtue of the provisions of Section 14A(1).
- b. The payment by a domestic company under Section 115O(1) of additional income tax on profits declared, distributed or paid is a charge on a component of the profits (which is distributed) of the company. The company is chargeable to tax on its profits as a distinct taxable entity and its pays tax in discharge of its own liability and not on behalf of or as an agent for its shareholders. In the hands of the shareholders as the recipient of dividend, income

by way of dividend does not form part of the total income by virtue of the provisions of Section 10(33) or 10(34). Dividend received from Mutual Funds units which are exempt under Section 10(35) also stands on same footing.

- c. The provisions of sub sections (2) and (3) of Section 14A of the Act are constitutionally valid;
- d. The provisions of Rule 8D of the *Income-tax Rules as inserted by the Income Tax ( Fifth Amendment ) Rules 2008* are not ultra-virus the provisions of Section 14A, more particularly sub-section (2) and do not offend Article 14 of the Constitution;
- e. The provision of Rule 8D of the Income-tax Rules which have been notified with effect from 24<sup>th</sup> March, 2008 **shall apply with effect from Assessment Year 2008-09;** Even prior to Assessment Year 2008-09, when Rule 8D was not applicable, the Assessing Officer has to enforce the provisions of sub section (1) of Section 14A. For that purpose, the Assessing Officer is duty bound to determine the expenditure which has been incurred in relation to income which does not form part of the total income under the Act. Assessing Officer must adopt a reasonable basis or method consistent with all the relevant facts and circumstances after furnishing a reasonable opportunity to the assessee to place all germane material on the record. Assessing Officer at the first instance has to determine the correctness of the claim of the assessee, having regard to the accounts of the Assessee.
- f. The proceedings for Assessment Year 2002-03 of the Appellant

Company shall stand remanded back to the AO. The Assessing Officer shall determine as to whether the assessee has incurred any expenditure (*direct or indirect*) in relation to dividend income / income from mutual funds which does not form part of the total income as contemplated under Section 14A. A.O can adopt a reasonable basis for effecting the apportionment. While making that determination, the A.O shall provide a reasonable opportunity to the assessee of producing its accounts and relevant or germane material having a bearing on the facts and circumstances of the case.

**7. CIT v. Walfort Share & Stock Brokers (P) Ltd. [ 2010 ] 192 Taxman 211 ( SC ) [Decided on 6<sup>th</sup> July, 2010]**

**Facts:** Assessee is a member of Bombay Stock Exchange and earns income from Share trading and brokerage. During the Financial Year 1999-2000, it has earned dividend from Mutual Fund unit, which was claimed as exempt under Section 10(33) of the Act. This was the clear case of dividend stripping wherein the Assessee purchased unit of Mutual fund on record date and earned Dividend Income, which was claimed as exempt and booked the loss on Sale of Mutual Fund immediately on next working day as Normal Business Loss. Such loss arose out of fall in NAV of the Unit upon declaration of dividend. Thus assessee was able to recover back his investment made in Mutual Fund and also book the Loss which approximated to the amount of



Dividend. Assessing Officer accepted the Dividend Income as exempt under the Act but disallowed the loss claimed by the assessee inter alia on the ground that a Dividend stripping transaction was not a business transaction and the transaction was coloured with the intention to create artificial loss in a very systematic and pre-designed set of transaction. CIT(A) upheld the order of Assessing Officer. The Special Bench deleted the disallowance by holding that the assessee was entitled to set-off the said loss from such transaction against its other income chargeable to tax. The Order of Tribunal was affirmed by the High Court.

#### Summary of the Transaction

Date	Particulars	Amount
24-03-2000	Purchase of Mutual Fund	8,00,00,000
24-03-2000	Record date for Dividend	1,82,12,862
27-03-2000	Sale of Mutual Fund Unit (Immediately Next working Day)	5,90,55,207
	Incentive Income Earned	23,76,778

#### Working of Business Loss claimed by Assessee

Income from Sale of Mutual Fund Unit	5,90,55,207
<b>Less:-</b> Cost of Purchases	8,00,00,000
<b>Business Loss</b>	<b>- 2,09,44,793</b>

Dividend Income (Claimed as Exempt u/s. 10(33) of Income-tax Act, 1961.)	1,82,12,862
---	-------------

**Contention of Department:** In the instant case, expenditure of ₹1,82, 12,862/- should be treated as Expenditure incurred for the purpose of Earning exempt Income and accordingly be disallowed under Section 14A, since this expenditure can be directly related to earning of dividend income by the Assessee.

**Contention of Assessee:** The learned counsel for the Assessee argued on the point that there is a difference

between the applicability of Section 14A and Section 94(7). Former deals with expenditure incurred for earning of exempt Income whereas the later deals with acquisition and sale of securities or units and provides for a consequence where the purchase and sale take place within a specified time period. Each provision operates in its own field. When Section 14A refers to disallowance of expenditure in relation to non-taxable income for computing the total income, what is meant is that such expenditure should be taken into account only for determining the quantum of the net non-taxable income. This would result in the exempt dividend being reduced by the alleged expenditure. The only impact on the exempting provision of Section 10(33) for unit income is by Section 94(7) and one cannot interpret Section 14A as leading to the same conclusion as then Section 94(7) will be rendered nugatory. In other words, the two provisions operate in different time and space zones. The two term “**expenditure**” and “**loss**” are conceptually different. According to the assessee, the embargo in Section 14A on the deductibility of expenditure applies where admittedly expenditure has been incurred and a deduction is claimed specifically in respect thereof. In this connection, reliance was placed on the word “allowed” in the said Section. In the present case, the assessee has not made any claim for deduction of ₹1,82,12,862/- and, therefore, the question of the disallowing the said sum did not arise.

**Decision of the Supreme Court:** The Supreme Court has held that for the purpose of attracting the provision of Section 14A, there has to be a proximate cause. In the absence of a proximate cause for disallowance, the provision of Section 14A cannot be invoked. What can be disallowed under Section 14A is actual expenditure debited to Profit &

Loss Account. Loss on sale of securities does not constitute an “expenditure incurred” in terms of Section 14A.

#### Conclusion

Though the Judgment of the Bombay High Court has some extent provided relief to the assessee by deciding that the Rule 8D would be applicable for Assessment Year 2008-09 and onwards, but still it has left a large number of assesseees in grey area especially Finance Companies, NBFC’s, Banks etc. and even Manufacturing Companies having huge amount of Investments which are made out of own funds. In view of scope of Jurisdiction of Bombay High Court decision, all other decision of ITAT which are contrary to aforesaid decision would be superceded in alignment with the above Judgment.

On a perusal of the various decisions of ITAT and now the final decision of Mumbai High Court in the case of Godrej & Boyce, a view emerges that:

1. Though Section 14A has been inserted with retrospective effect from 01.04.1962 and since Rule 8D has been notified only on 24.03.2008, it would be effective only from Assessment Year 2008-09 onwards.

2. For earlier Assessment Years, though the expenses pertaining to exempt income are not allowable, the disallowance has to be on a reasonable basis having regard to the accounts of the assessee and after furnishing a reasonable opportunity for the assessee to place all germane material on record.

3. This in effect would mean that the disallowance under Section 14A read with Rule. 8D cannot exceed actual expenses debited in the P & L A/c and that the notional disallowance specified in the Rule 8D(2) cannot exceed the actual expenditure incurred by the assessee, as an expenditure which has not been incurred and claim cannot be disallowed. ■

# Minimum Alternate Tax - Latest Developments

**It is a well known remark that equity and taxation are strangers. Now if a company, by availing various tax exemptions and through tax planning within the frame work of Income Tax laws, is not required to pay income tax then Minimum Alternate Tax (MAT) comes into operation and such corporate assessee is asked to pay taxes. All the careful efforts and initiatives are not appreciated instead the assessee is required to pay taxes by way of advance tax installments. Now to bring and promote equity among companies, tax rates under MAT are also gradually increased (effective rate 19.93 per cent). It appears that equity is not so stranger now-a-days rather they are complementary to each other. This article analyses the latest developments of MAT which has been quite established in statute book at present.**

After the withdrawal of Section 80VVA, the concept of taxing the Zero Tax (but profitable) companies under Section 115J has come a long way since 1988 and now is well established in statute book. Originally, the laws were simple but year after year the calculations, procedure and conditions of arriving the tax payable amount became elaborated through litigations and subsequent counter legislative amendments. In this article, some recent developments of this MAT aspect are discussed and analysed for better understanding of the present scenario.

## **Advance Tax and Section 234B, 234C**

Over a period of several years, this controversy whether advance tax payable or not was floating and remained uncertain with conflicting court judgements coming in both favour and against of the applicability of advance tax in Section 115J, Section 115JA and later Section 115JB. As it stands now things have settled down to a position that advance tax is very much payable and non-compliance will attract Section 234B and Section 234C. The Companies were explaining that estimation of correct income was quite unpredictable before the year end and hence payment of installment wise (right from 15<sup>th</sup> June) advance taxes keeping in mind the MAT parameters was a difficult task. Often the finalisation work of statutory audit remained incomplete or the AGM scheduled

to be held in July/August. This was actually the position several years back and entire Accounts Department used to remain excessively busy with late hours working at office everyday. There cannot be any denial of this scenario few years back say upto year 2000.

In reality, barring few companies of small sizes (as private limited entities) which may not be so organized and systematic the remaining corporate bodies at large (which are operational and active) prepare monthly accounts i.e. Balance sheet, Profit & Loss Account, Trial balance, operating results etc. especially in the present day computer age after year 2000.

This view is clearly described by a recent Tribunal Special Bench in ACIT. V. *Ashima Syntex Ltd.* (2009) 117 ITD 1 (Ahd) wherein Para 44 of the judgement says -

“..... Even before the introduction of the provisions of Section 115J of the Act, companies had been estimating their total income even providing deductions admissible under the Act. In fact, all assesses who maintain books of account have to undertake this exercise for the purpose of payment of advance tax. If a profit and loss account can be drawn up on estimate basis for the purpose of the Income Tax Act, it is not understood as to why a similar profit and loss account on estimate basis under the Companies Act cannot be drawn up”. The argument that Taxable income and Book profit for MAT purpose can

### **CA. Dilip Chakraborti**

*(The author is a member of the Institute. He can be reached at eboard@icai.org)*

be determined only after the close of the books of account at the end of the year is now not a fair and tenable logic acceptable to judiciary.

The para 44 (Supra) also said “there is no scope for considering the hardship of the assessee as the levy is automatic and does not require any opportunity to be given to the assessee”.

Moreover, the provisions of Section 115JA (4) and later Section 115JB(5) specifically stipulate the applicability of all other provisions of the Act, which obviously include the incidence of advance taxes also. The absence of a similar sub-Section (4)/(5) in erstwhile Section 115J was one of the main reason for controversies which led to subsequent litigations.

### Change in Tax Rates u/s 115JB

The Finance Act, 2001 introduced Section 115JB almost on the same lines like Section 115JA except for the methodology of arriving the ‘tax payable’ amount. Section 115JB inserted a straight percentage basis to be applied on the ‘book profit’ to calculate such taxes payable if the tax otherwise arrived under normal computation of income is lesser. But this tax percentage inserted in 2001 w.e.f. Assessment year 2001-02 on such deemed income (Book Profit) moved upwards rapidly as under –

Relevant Finance Act	Basic Tax rate	Applicable period
Finance Act, 2001	7½%	Asst. year 2001-02 to Asst. year 2006-07
Finance Act, 2006	10%	Asst. year 2007-08 to Asst. year 2009-10
Finance Act, 2009	15%	Asst. year 2010-11 only.
Finance Act, 2010	18%	Asst. year 2011-12 onwards

Apparently pro-corporate (equity and justice) reasons have been given and explained in order to justify the incidence and the gradual increase in the MAT rates.

The Budget Speech 2009 of

**“The provisions of section 115JA (4) and later Section 115JB (5) specifically stipulate the applicability of all other provisions of the Act, which obviously include the incidence of advance taxes also. The absence of a similar sub-Section (4)/(5) in erstwhile Section 115J was one of the main reason for controversies which led to subsequent litigations.”**

Finance Minister (delivered on July 9, 2006), explained in Para 94 as –

“Minimum Alternate Tax (MAT) was introduced to address inequity in taxation of corporate tax payers. In the quest for greater equity, I propose to increase rate of MAT to 15 per cent of book profits from the present rate of 10 per cent. However, to grant relief to corporate tax payers, I also propose to extend the period allowed to carry forward the tax credit under MAT from seven years to ten years”.

After eight months, the same Finance Minister in his Budget Speech 2010 (delivered on 26<sup>th</sup> February, 2010) reiterated in para 129 his stand to promote greater equity among corporate taxpayers and raised the basic tax rate to 18 per cent from 15 per cent for Assessment year 2011-12. We are, of course, not sure as to

what may come in next annual budget and as such, how long this 18 per cent rate (effective rate 19.93 per cent) will remain is a difficult prediction when viewed from the fact that Government needs more and more money to

meet the increasing, expenditure. We only hope that Minimum Alternate Tax should not turn into Maximum Alternate Tax. However, the set off period of such MAT levy in subsequent years have been extended from seven years to ten years (why not indefinite?) . But this right to carry forward and set off under Section 115JAA which covers both Section 115JA and Section 115JB does not take into account or consider any compensatory interest claim nor the inflationary aspect over the period till the ‘tax paid’ is finally adjusted. This unfettered right of assessee is of course automatic-that is no compliance or pre-condition like timely (by due date) return filing, tax payments, any set-off provisions or even confirmation by Assessing officer is not necessary.

### Provision for Diminution in the Value of Asset

The Finance Act, 2009 has inserted a line “the amount or amounts set aside as provision for diminution in the value of any asset” in sub-Section (2) of Section 115JB whereby all such provisions if debited to Profit & Loss Account of the Company shall be added to get “book profit”.

This amendment nullified various court judgements and moreover, the retrospective application from 1<sup>st</sup> April, 2001 will upset the already concluded assessments. Such retrospective application is not assessee-friendly at all and has now become a disturbing exercise in recent annual budgets. Again the computation of total income under Section 115JB may get disturbed since the various diminutions of asset (e.g. provision for Doubtful Debts, provision for diminution of Investments etc) are normally ascertained at the year end and that too at the time of finalisation of statutory audit when compliance to Schedule VI of Companies Act, 1956 and various applicable Accounting Standards are seriously considered. As such, in practice the calculation of

current income under MAT for advance tax purpose by anticipating such items is quite a difficult task and unfortunately there will be no escape from incidence of Section 234B & Section 234C.

The main argument for insertion of such a clause appears to be that these debits in Profit & Loss Account are in respect of some asset (not a liability or expense) and as such writing of the asset values in Profit & Loss Account to reduce 'book profit' though necessary from accounting compulsion was however found unacceptable under Section 115JB.

### Depreciation as per Income Tax Rules

A corporate entity has to prepare Annual Accounts in accordance with the guidelines prescribed under Schedule VI of Companies Act, 1956 and charging of depreciation is a regular item in Profit & Loss Account before arriving at the annual profit or loss of the company. Section 115J which originally contained the MAT provisions i.e., deemed income in case of 'Zero tax' companies did not make any distinction between private company or public company anywhere in the sub-sections.

Again, a private company has certain exemption/privileges as regards the application of some

sections (e.g., Section 349/350/355) of the Companies Act, 1956 – but that aspect is purely a matter of concern for purpose of corporate administration and management. As far as income tax is concerned, more particularly when a special provision like Section 115J is calculated – there is no scope for making any discriminatory treatment and every company (be it a public or private) has to abide by Schedule VI guidelines for annual accounts to be placed at Annual General Meeting. This practice appears to be a better course from the angle of good governance, uniformity and comparative studies. Moreover, such exemption should not automatically enable a private company the discretionary right to charge depreciation as per Income tax rules (which is higher than the rates prescribed in Schedule XIV of companies Act, 1956) even in absence of specific prohibition.

Recently, in the case of Dynamic Orthopedics Pvt. Ltd. V. CIT (2010) 321 ITR 300 (SC) the issue as to possibility of claiming depreciation as per Income Tax Rules, 1962 for the purpose of computing book profit under Section 115J of Income Tax Act, 1961 was elaborately discussed and the judgement already delivered by Supreme Court in *Malayala Manorama Co. Ltd. V. CIT* (2008) 300 ITR 251 (SC) was doubted here.

The situation finally was that judges in Dynamic Orthopedics Pvt. Ltd. case favoured the rates of depreciation as per Schedule XIV of the Companies Act, 1956 while the judges in Malayala Manorama case had already decided for charging depreciation rates as per IT Rules 1962. In view of this contradictory position, the issue has been rightly sent to a larger Bench of Supreme Court for reconsideration. The issue when resolved by larger Bench will allow no discretion as regards specific application of depreciation rates, more particularly for private companies, even in the context of Section 115JB

**“The DTC 2010 contains the MAT provisions for companies under Computation of book profit (Chapter V) within Section 104 to 107. The tax calculation method via book profit under DTC 2010 which is quite akin to the existing provisions of Section 115JB of IT Act, 1961 is a welcome insertion as against the original DTC 2009 where the emphasis was on gross asset value. The new DTC 2010 contains specific items of additions and deductions followed by adjustments of earlier losses with net profit as per Profit & Loss Account to finally arrive at the desired book profit on which a tax rate of 20 per cent has been prescribed.”**

existing at present.

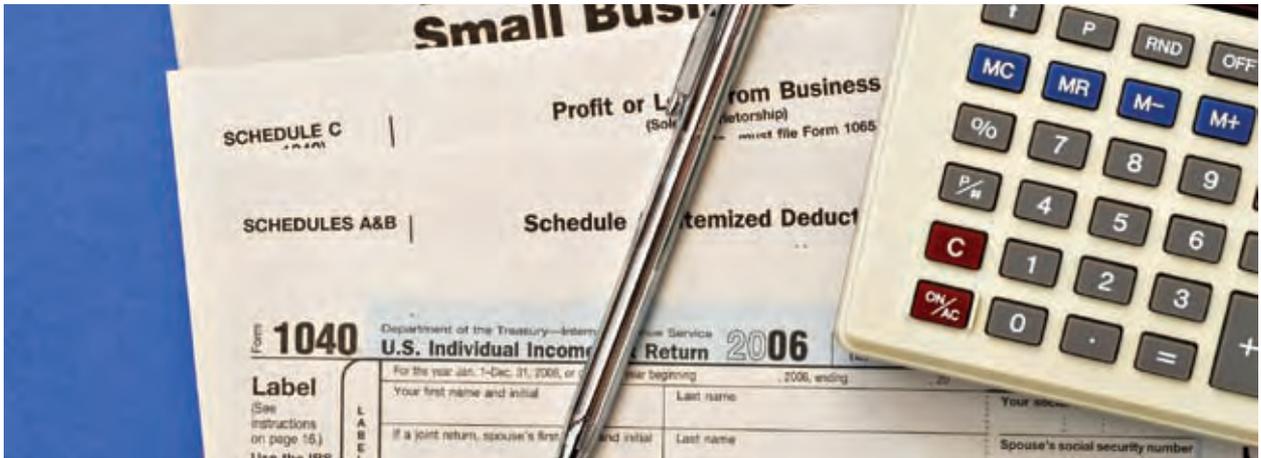
### Direct Taxes Code Bill 2010

The DTC 2010 contains the MAT provisions for companies under Computation of book profit (Chapter V) within Section 104 to 107. The tax calculation method via book profit under DTC 2010 which is quite akin to the existing provisions of Section 115JB of IT Act, 1961 is a welcome insertion as against the original DTC 2009 where the emphasis was on gross asset value. The new DTC 2010 contains specific items of additions and deductions followed by adjustments of earlier losses with net profit as per Profit & Loss Account to finally arrive at the desired book profit on which a tax rate of 20 per cent has been prescribed. However, the carry forward right of tax credit (without interest) of assesses (which was absent in DTC 2009) has now been extended to a comfortable 15 years.

As regards applicability of other provisions of the Code, Section 107 here is similar to existing Section 115JB (5) of IT Act, 1961. ■

**“The Finance Act, 2009 has inserted a line “the amount or amounts set aside as provision for diminution in the value of any asset” in sub-Section (2) of Section 115JB whereby all such provisions if debited to Profit & Loss Account of the Company shall be added to get “book profit”. This amendment nullified various court judgements and moreover, the retrospective application from 1<sup>st</sup> April, 2001 will upset the already concluded assessments.”**

## New TDS Rules 2010



Consistency is one of the pillars on which an efficient and effective tax regime is based. Frequent changes result in chaos and confusion. E-filing of TDS/TCS returns is a learning experience not only for us but for the Income Tax Department and the allied agencies like NSDL. This is the basic reason for change. But changes should be well thought of and attempt should not be made to achieve stupendous results overnight. This time another set of changes have been made. These changes appear to be rational and achievable. Some due dates have been rationalised. Obsolete forms have been abolished. But as usual, there are some open issues which need clarification. This article provides an overview of new TDS Rules 2010.

Once again significant changes have been made in the rules relating to TDS/TCS by the Income Tax 6<sup>th</sup> Amendment Rules, 2010. These rules are applicable to TDS/TCS deducted/collected on or after 1<sup>st</sup> April, 2010. Impliedly, earlier rules would apply in case of TDS/TCS certificates and Quarterly Statements of TDS/TCS for F.Y. 2009-10. Unlike in the past, this time a month and a half was given to the deductors to prepare

themselves for the first quarterly statements for FY 2010-11 as the rules were notified on 31<sup>st</sup> May, 2010 and 15<sup>th</sup> July was the last date for filing TDS/TCS returns for Q1 of FY 2010-11.

### Changes in Due Dates

Some significant changes have been made in due dates of various TDS/TCS compliances. The same are as follows:

Obligation	Existing Due Date	Revised Due Date
Deposit of Non salary TDS deducted from Mar 1-30	April 7	April 30
Deposit of Non salary TDS deducted on Mar 31	May 31	April 30
Issue of Form 16	April 30	May 31
Issue of Form 16A	Monthly: End of next month Yearly: April 30	Quarterly: July 30, October 30, January 30 & May 30.
TDS Returns (24Q, 26Q, 27Q) for Q4	June 15	May 15
TCS Return (27EQ) for Q4	April 30	May 15



### CA. Rajeev Khandelwal

(The author is a member of the Institute. He can be reached at [khandelwal.rajeev@icai.org](mailto:khandelwal.rajeev@icai.org))

### Quarterly Deposit of TDS

The due dates for deposit of tax quarterly (after special permission of Assessing Officer and Joint Commissioner of Income Tax) have also been streamlined as follows:

Quarter	Existing Due Date for TDS deducted on Salary	Existing Due Date for TDS deducted on Interest, Commission or Insurance Commission	Revised Due Dates for Salary, Interest, Commission or Insurance Commission
Apr-Jun	Jun 15	July 15	July 7
Jul-Sep	Sep 15	October 15	October 7
Oct-Dec	Dec 15	January 15	January 7
Jan-Mar	Mar 15	April 15	April 30

### Postponed

**TCS Return of Q4:** The due date for filing TCS returns for Q4 has been shifted from 30<sup>th</sup> April to 15<sup>th</sup> May to streamline the same with due dates of other quarterly statements.

**Form 16:** The date of issue of Form 16 has been postponed to ensure that it is issued after the filing of Form 24Q for the last quarter also. This will ensure that the acknowledgment numbers of all the four quarters are shown in Form 16. There will be no need to mention "Yet to be furnished" which happens in most cases now.

### Preponed

**TDS on year end provisions:** Many dates have been preponed. One of the most significant instance is that due date of deposit of TDS on year end provision of expenses. This time, the period has been significantly reduced from two months to one month i.e. TDS has to be deposited in these cases by 30<sup>th</sup> April. This will impact big corporates having several branch offices spread throughout the country as their accounts department will have to work overtime to collect information about the year end provision of expenses.

The major reason for reducing this time seems to be to give less time to unscrupulous businessmen to cook their books by booking fictitious expenses. Such people should bless their stars as grapevine is that there

was even a proposal to ask deductors to pay tax on year end provisions also within the next seven days. When the assessee can be asked to pay service tax & excise duty for March by 31<sup>st</sup> March itself, then why is this not possible? But thankfully, this has not been implemented (as of now).

### Different Accounting Year

For most assessee, accounting year is the same as the financial year. (Even in this article this has been presumed). However, in case of many MNCs etc. accounting year is different from the financial year due to the global practice. So the calendar year may be accounting year in many cases. Earlier tax deducted on the last day of the accounting year could be deposited within two months. Now the words used are "where the income or amount is credited or paid in the month of March". The extra time of two months and now one month for deposit of TDS is given keeping in view the yearly closing of accounts. But now those having a different accounting year would have to deposit tax on year end provisions within seven days only.

**TDS deducted in March:** Some

relief has been given as TDS deducted throughout the month of March shall be allowed to be deposited by 30<sup>th</sup> April. Till now the extra time of two months was given only for provisions made on year end. TDS deducted in rest of the last month was to be deposited within seven days. This has been done to synchronise it with the provisions of Section 40(a)(ia) wherein expenses incurred throughout the month of March are allowed as deduction if TDS thereon is deposited till the due date of filing of Income tax return.

**Due date for deposit of March tax by Government deductors/collectors:** Finally, some harshness to government deductors even where they deposit tax by challan like their private counterparts. They are supposed to pay tax deducted during March by 7<sup>th</sup> April only unlike private deductors who can deposit it by 30<sup>th</sup> April. This appears to be in inadvertent error which would be rectified soon.

**TDS Returns of Q4:** Once tax has been deposited, filing of TDS returns should not be an issue. So, the due dates for filing of TDS returns for the last quarter have also been proposed by one month to 15<sup>th</sup> May. In a way this is good as till now there was only a one

**Mode of payment of taxes has been incorporated in the IT rules now. Changes have been made in the rules to allow e-payment of TDS/TCS by Debit card also besides internet banking. This is a welcome change as giving transaction access to internet banking account is not safe and may be misused. Allowing the use of Debit card shall encourage more people to go for e-payment. It is expected that this facility shall be made operational soon. One wonders why credit card facility has not been allowed.**

month gap between Q4 returns and Q1 returns of the next fiscal and many lazy souls postponed it to a later date.

### TDS/TCS E-payment by Debit Card

Mode of payment of taxes has been incorporated in the IT rules now. Changes have been made in the rules to allow e-payment of TDS/TCS by Debit card also besides internet banking. This is a welcome change as giving transaction access to internet banking account is not safe and may be misused. Allowing the use of Debit card shall encourage more people to go for e-payment. It is expected that this facility shall be made operational soon. One wonders why credit card facility has not been allowed. Probably the IT department does not want people to pay tax by credit card and then default on payment to the credit card company.

### Scope of E-TDS/TCS Statements Enlarged

Presently, e-filing of quarterly TDS/TCS statements is mandatory for corporates, government deductors, others to whom tax audit is applicable in the preceding year and those whose any quarterly statement of *preceding year* has 50 or more entries of deduction of tax.

The list of e-filers shall grow bigger now as e-filing from FY 2010-11 is mandatory for those deductors whose deductee records in any quarterly statement of the CURRENT financial year are 20 or more. Earlier, this responsibility was shifted to the next year. In other words, once the number of deductee records is 20 or more in any of the quarters in any one of Form 24Q, 26Q or 27Q, each one of them shall have to be filed electronically in the current year even if there is a single entry in other statements. This is not a continuing responsibility. Therefore, if in the next year there are less than 20 entries in all the quarterly statements,

the deductor can file paper returns.

TCS is still a distant cousin as it is not clubbed with TDS statements. TCS quarterly statement has to be filed electronically in the above case only when Form 27EQ of any quarter of the current financial year has 20 or more entries of collection of tax. Even if TDS returns have to be filed electronically due to more entries, Form 27EQ may be filed manually if it has lesser entries and vice versa.

### Analysis of Changes in TDS/TCS Certificates Form 16AA Omitted

Form 16AA was a TDS certificate cum income tax return for low paid employees. This lost relevance when new IT return forms were notified few years ago. But it appears that taxmen were too busy with other things and they did not get time to strike it off from the statute books. Thankfully, this has been done now and Form 16 has to be issued in case of all employees. Additionally, Form 12BA in respect of perquisites has to be issued in case of employees drawing salary exceeding ₹1.50 lakh per annum. Even this form could be omitted as information about perquisites is not separately being asked for in Form 24Q also. This form is mainly for the consumption of employees as in this

**“ IT department clarified vide Circular 2/2007 dated 21-5-2007 that digitally signed Form 16 is as valid as that signed manually. Though not widely used, digitally signed Form 16 are in vogue in big corporates as it results in saving of cost of paper and dispatch (it can be e-mailed) and of efforts of the person signing them. The option to digitally sign Form 16 has now been incorporated in the IT Rules. ”**



era of annexureless returns the same is not to be furnished to the income tax department. But who knows, details of perquisites may stage a comeback in Form 24Q as the controversial Fringe Benefit Tax (FBT) has been abolished.

### Form 16

Certain significant changes have been made in Form 16. Now it is divided into 2 parts:

**Part A:** Earlier information was filled in Form 16 to the extent it was available but now it is **compulsory** to fill the following information in Form 16 in part A:

- **TAN of the employer.** PAN of employer can be mentioned in Form 16 though it is not mandatory. However, PAN is mandatory in TDS/TCS statements for non-government deductors.
- **PAN of the employee.** It is not clear what is to be done if the employee does not have PAN or does not furnish it. Should Form 16 not be issued? What about the penalty of ₹100/- per day per certificate in case of delay.
- **Receipt nos. of Original Form 24Q** of all the quarters. Again, it is not clear what is to be done if Form 24Q of any quarter is not filed till the due date of furnishing Form 16. Should "yet to be furnished" be mentioned against acknowledgement nos. or should Form 16 not be issued till all Form 24Q are filed?

- Besides, this part contains the usual details like name and address of the employer, name and designation of employee, period and assessment year.
- The quarterwise TDS deducted and deposited of the individual employee has also to be mentioned. Normally, the two should be same. The format is as follows:

Quarter	Receipt nos. of Original Form 24Q	Amount of TDS in respect of employee	Amount of TDS deposited/remitted in respect of employee
Quarter 1			
Quarter 2			
Quarter 3			
Quarter 4			
<b>Total</b>			

- The address of the CIT (TDS) of the deduction is also to be mentioned now. This shall be available from [www.tin-nsdl.com](http://www.tin-nsdl.com). Probably, this will help the employee to know who to complain to in case of problems, non-receipt of certificates etc. *This part **MUST** be issued for the relevant period by each employer with whom an employee has worked during a financial year.*

**Part B:** This part contains the breakup of salary, exemptions, deductions and tax payable. Tax deposited and refund/tax payable has been removed from this part as people panicked on seeing the figures of tax payable/refund due even though there was a genuine reason for the same. Now one may have to work out this figure. Tax payable on perquisites by employer is also conspicuous by its absence.

As per the new Form 16, the value of perquisites is to be as per Form 12BB. But there is no such form as 12BB. It seems that the person drafting the new form was newly married and in his dreams he mentioned the forms as 12BB instead of 12BA. Even otherwise, it is difficult to handle even

1 BB(wife), who can dare to think of a dozen!! Males do not chuckle, it is equally applicable to husbands also. This beautiful mistake had crept in the last Form 16 (which was later on scrapped) but the mistake has been retained in the current form also. By the corrigendum dated 19<sup>th</sup> July, 2010, this mistake has been rectified in case of perquisites but it still persists in case of

profits in lieu of salary in the very next line of Form 16!!!

Part B of Form 16 may be issued by:

- Each employer with whom an employee has worked during a financial year or

**“ Practically, most deductors issue a consolidated TDS/TCS certificate for the full year. Even big corporates going for the monthly option, prepare them at the year end and despatch the same in one go. Even from the point of view of parties, a consolidated TDS certificate is a better option as they tend to misplace multiple certificates received over a period of time. The income tax department should have made consolidated certificate as the default option. But it does not seem to understand the problems of multiple certificates. It also does not seem to be eco friendly as quarterly certificates would result in a quantum jump in the use of paper. ”**

- The last employer, at **the choice of the employee.**

The Income tax department had clarified on 13-4-2004 that in case of employees working with more than one employer in a financial year, each employer had to show only the details of salary paid by him and TDS deducted by him in Form 24(Form 24Q now) issued by him. From the same analogy, Form 16 is to be issued by each employer separately. However, in practice in many organisations, particularly banks, insurance companies etc., the last employer issues Form 16 for the entire year which covers the salary and tax details of earlier employers also.

Just because some deductors are not doing their duty properly, it does not mean that all others also be asked to follow the incorrect practice. And even if this practice was to be allowed, the single certificate could be allowed in all cases. Giving the option to the employee would complicate things further. The employer should be free to formulate the policy for issue of a consolidated/ separate Form 16 and not be left at the mercy of employee for the same. Issue of a consolidated certificate for 70 per cent employees and separate ones for the balance 30 per cent or vice –versa would result in more confusion and chaos. And who knows, the employee may take Form 16 from each employer individually and then request the last employer to issue a consolidated one too. How the



last employer would certify the details of salary, TDS deducted and deposited of another employer also remains to be seen. Whether he should insist and keep the original of Form 16 from the previous employers or whether a declaration/certificate from the previous employer/employee would suffice? Clarifications are needed from the CBDT on such issues.

**Verification:** The changes in verification have been marked in italics and bold.

I \_\_\_\_\_ S/o/D/o \_\_\_\_\_ working in the capacity of \_\_\_\_\_ do hereby certify that a sum of ₹ \_\_\_\_\_ (₹ \_\_\_\_\_) has been deducted and **deposited** to the credit of Central Government. I further certify that the information given above is true, **complete** and correct **and is** based on the books of account, documents, **TDS statements**, **TDS deposited** and other available records.

- The use of the word “deposited” in place of “paid” appears more appropriate but we had got used to it and so hardly bothered about it.
- Now the responsible person has to certify not only the truth and correctness of Form 16 but also its completeness. Now that is expecting too much from him. If the certificate is true and correct, is that not sufficient? Completeness has

**“Till now, Form 16A had to be issued sectionwise. That is if, the contractor is also the landlord, TDS had to be deducted under Sections 194C & 194I separately and TDS certificates had to be issued separately for both the sections. But now since the nature of payment/credit is to be mentioned separately for each payment, it appears that a single Form 16A can also be issued for all kinds of payments to a single party.”**

a much wider connotation. Even if some minor detail or insignificant figures are not mentioned in Form 16 deliberately or otherwise, Form 16 may be taken as incomplete. So those signing TDS certificates better be more careful now.

**Details of Tax Deposit:** The summary of TDS deposited has to be given in an annexure. Earlier tax deposit details had to be furnished in the same format for all deductors. But now a separate format has been prescribed for tax deposited by book entry by government deductors and that deposited by challan.

**Annexure A:** Government deductors who deposit tax by book entry or transfer voucher have to give details of tax deposit in Annexure A. The amount of TDS pertaining to the relevant employee in each transfer voucher is to be given.

The following will constitute **BIN** (Book Identification No.) (The sarkari (government) cousin of CIN)

- Receipt no. of Form 24G (explained later) which has replaced the transfer voucher no.
- Drawing & Disbursing Officer (DDO) sequence no. in the Book Adjustment Mini Statement
- Date of deposit.

It is mandatory to mention bin in Annexure A, If applicable.

**Annexure B:** Private deductors or government deductors who deposit tax by challan have to give information in Annexure B. Earlier, in case of government deductors, the only option was to deposit tax through book entry. But now they have been given an option to pay either by book entry or challan. It appears that in due course even government deductors would have to deposit tax by challan only.

There is a single column for tax and breakup in tax and cess is not required. The note says that surcharge is also to be clubbed but as of now surcharge is not applicable to individuals (it may

crop up sometime later). Cheque no is also not to be mentioned now. CIN consisting of BSR code of the bank branch, challan no and date of deposit has to be mentioned.

It is mandatory to mention cin in Annexure B, If applicable.

*Note: The form says that the Employer to provide payment wise details of tax deducted and deposited with respect to the employee. But in fact, here only the details of tax deposited have to be given.*

### **Digitally signed Form 16**

IT department clarified vide Circular 2/2007 dated 21-5-2007 that digitally signed Form 16 is as valid as that signed manually. Though not widely used, digitally signed Form 16 are in vogue in big corporates as it results in saving of cost of paper and dispatch (it can be e-mailed) and of efforts of the person signing them. The option to digitally sign Form 16 has now been incorporated in the IT Rules. The various issues to be borne in mind while issuing digitally signed Form 16 mentioned in the said circular have also been incorporated in the rules like the form should not be capable of being altered once it is digitally signed, it should have a control no. and a proper log should be maintained.

### **Form 16A**

#### **Confusion about single or consolidated certificate**

Till now Form 16A for TDS deducted during a month had to be issued by the end of next month. Option was also available to the parties to request for a consolidated TDS certificate for the whole year and this had to be issued by 30<sup>th</sup> April. However, for provision of expenses made on 31<sup>st</sup> March, tax could be deposited by 31<sup>st</sup> May and certificate could be issued by 7<sup>th</sup> June. There was a lot of confusion amongst corporates and professionals whether the consolidated certificate could

be issued by 7<sup>th</sup> June or 2 separate certificates should be issued: one by 30<sup>th</sup> April, (for deductions made till 30<sup>th</sup> March) & another by 7<sup>th</sup> June (for deductions on 31<sup>st</sup> March). The income tax department never felt the need to clarify this issue and it was left to the wisdom of the professional or the deductor to do what he felt was the best. The more cautious ones issued 2 certificates as there is a penalty of ₹100 per day per certificate for delay in issue of TDS certificates. Others issued a single certificate. But it seems that the income tax department did not bother much as long as Form 16A were issued.

### Quarterly Certificate

The confusion has not been resolved. In fact it has been done away with altogether. Neither 1 nor 2 TDS certificates have to be issued now. Instead, they have to be issued on a quarterly basis within 15 days from the due date of TDS statement of the relevant quarter. In other words, TDS certificates from FY 2010-11 have to be issued as under:

Quarter	Due Date for TDS Statement	Due Date for Form 16A
April-June	July15	July 30
July-September	October15	October 30
October-December	January15	January 30
January-March	May 15	May 30

Similar changes have been made for issue of quarterly TCS certificates in Form 27D also which till now had to be issued on a half yearly basis or monthly basis.

### Quarterly certificate how effective?

Practically, most deductors issue a consolidated TDS/TCS certificate for the full year. Even big corporates going for the monthly option, prepare them at the year end and despatch the same in one go. Even from the point of view of parties, a consolidated TDS certificate is a better option as they

**“ A duplicate TDS certificate can be issued in case of loss of the original one. However, now it has been specified that it should be certified as “Duplicate” by the deductor. Probably, the person making changes in the rules was watching Shah Rukh’s film by the same name and found it apt to use its title. ”**

tend to misplace multiple certificates received over a period of time. The income tax department should have made consolidated certificate as the default option. But it does not seem to understand the problems of multiple certificates. It also does not seem to be eco friendly as quarterly certificates would result in a quantum jump in the use of paper.

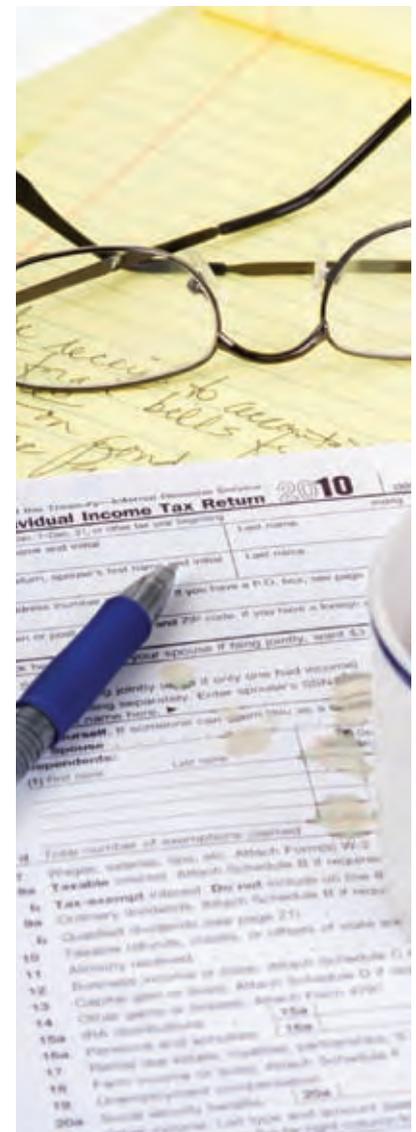
The basic objective of quarterly certificate seems to be to allow a party to know and check whether his TDS has been deposited or not and whether he has been given credit for the same or not, on a timely basis. This will help him to follow up with the

deductor immediately, rather than wait for the full year. But this objective can be achieved only when TDS certificates are actually issued on a quarterly basis on the due dates.

### Important changes in Form 16A

**Mandatory information:** TAN of deductor, PAN of party, receipt no. of the relevant Original Quarterly statement, address of CIT (TDS) are all mandatory as in case of Form 16. Again it is not clear whether the quarterly Form 16A should be delayed in case of delay in filing the relevant Form 26Q/27Q?

**Summary of Quarterly TDS:** The total amount of TDS deducted and deposited for the party has to be mentioned in Form 16A now. Normally the two should be same. The acknowledgment number of the TDS statement submitted for the relevant quarter shall also have to be given in Form 16A issued to all parties for the relevant quarter. Presently, the receipt number of all the quarterly statements filed till the date of issue of the certificate had to be given. In case of issue of certificate before filing of return, “yet to be furnished” had to be mentioned in Form 16A.



**Details of Payment, Tax Deduction & Deposit of Tax:** Till now, all entries of deduction of TDS had to be shown in Form 16A. e.g. if tax had been deducted 100 times during the year for a party, the Form 16A contained the date wise breakup of all the 100 payments in the following format.

S No.	Amount paid/ credited	Date of payment/ credit	TDS	Surch-arge	Education Cess	Total tax deposited	Cheque/ DD No. (if any)	BSR Code of Bank branch	Date on which tax deposited	Transfer voucher/ CIN

The above detail has now been broken into two parts :

(A) **Summary of payment:** The various details to be provided here are as under:

Amount paid/ credited	Nature of Payment	Date of payment/ credit

**Important issues for consideration:**

1. Since, the nomenclature of the above detail is "Summary of payment", it seems that only the total amount of payment/credit has to be mentioned here in a single line. The mention of "Nature of payment" here also supports this view.
2. The mention of "date of payment/ credit" creates confusion as if there

are multiple payments made on different dates, which date should be mentioned. One view could be that the last date of the quarter can be mentioned here in case of multiple payments.

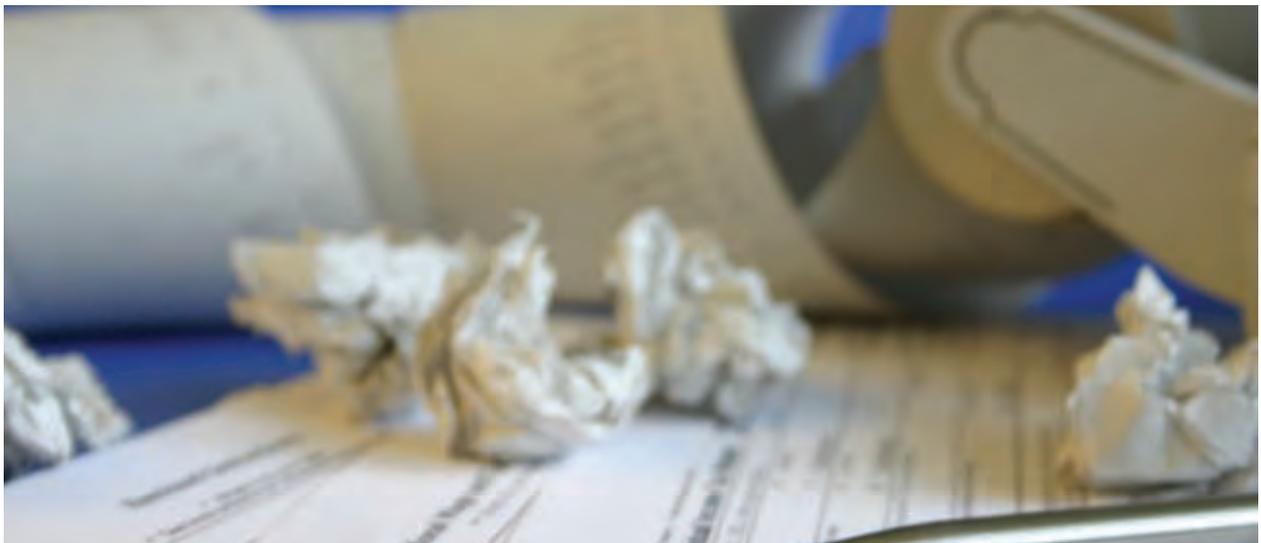
3. Another view could be that each payment has to be mentioned

separately and its distinctive date mentioned against it. The Corrigendum dated 19<sup>th</sup> July, 2010 also supports this view as it states that "Separate annexure may be attached for Summary of payment

**“ A single Form 24G has to be prepared each month by an AO giving details of transfer vouchers for Form 24Q, 26Q, 27Q & 27EQ of DDOs under him. The total TDS deducted and deposited has to be shown separately for each DDO and for each type of payment i.e. salaries, other payments to residents etc. Thus, there can be a maximum of 4 entries per DDO in every month. ”**

in case number of payment/credit during the relevant quarter is more than one". The use of the word "may" signifies that it is optional to give details of amount paid. One wonders, why details should be given in a separate annexure and not in the main body of the Form

4. Till now, Form16A had to be issued sectionwise. That is if, the contractor is also the landlord, TDS had to be deducted u/s 194C & 194I separately and TDS certificates had to be issued separately for both the sections. But now since the nature of payment/credit is to be mentioned separately for each payment, it appears that a single Form16A can also be issued for all kinds of payments to a single party.
- (B) **Details of Deposit:** Details of deposit are the same as in Form 16. The deposit details for government deductors is in Part A whereas for private ones is in Part B. Government deductors also have to use part B if tax has been deposited by challan.



The various details to be provided in case of deposit by cheque are as under:

S No.	Tax Deposited in respect of the deductee	BSR Code of the Bank Branch	Date on which tax deposited	Challan Serial Number

e.g. Payment to Naman Printers is made as follows:

S No.	Date of Payment	Amount of Payment	Amount of TDS
1.	15-4-2010	25,000	500
2.	25-4-2010	50,000	1,000
	<b>Total</b>	<b>75,000</b>	<b>1,500</b>

Tax is deposited by a single challan. Now the above information can be shown in 2 ways:

#### Option 1:

S No.	Tax Deposited in respect of the deductee	BSR Code of the Bank Branch	Date on which tax deposited	Challan Serial Number
1.	1,500	6390340	7-4-2010	01252

#### Option 2:

S No.	Tax Deposited in respect of the deductee	BSR Code of the Bank Branch	Date on which tax deposited	Challan Serial Number
1.	500	6390340	7-4-2010	01252
2.	1,000	6390340	7-4-2010	01252
<b>Total</b>	<b>1,500</b>			

The deductionwise breakup of challan was fine in the earlier Form 16A as the details of payment and TDS



had to be given together in a single row. But what is the need for giving deductionwise breakup of challan in the new Form 16A. However, the use of the sentence "The Deductor to provide payment wise details of tax deducted and deposited with respect to the deductee" signifies that the breakup of challan has to be given as per Option 2. The language of the sentence has been slightly modified in the current Form 16A but the meaning more or less remains the same.

#### Credit of TDS in IT Return

The concept of Unique Transaction Number (UTN) was proposed earlier for giving credit of TDS to assessees. UTN was to be generated for each TDS entry in the proposed challan called Form 17. However, UTN and Form 17 have been given a quiet burial as the same was a classic case of act in haste and repent at leisure.

As per CBDT Press Release dated 2<sup>nd</sup> June, 2010, credit in IT Return shall be available on the basis of **Unique Identification** which will consist of :

- PAN of Assessee
- TAN of Deductor.
- Receipt no. of TDS statements of Deductor.

These three together shall help an assessee to claim credit of TDS/TCS deducted/ collected. However, this still seems to be in the pipeline as there was no mention of the same in the revised Rules. Till such time, the credit of TDS shall be available as per the existing procedure. For this let us have a look at Schedule TDS 2 in income tax returns. The format is as follows:

S. No.	TAN of Deductor	Name & Address of Deductor	Amount Paid	Date of Payment/ credit	Total tax deducted	Amount of tax deducted claimed this year

The details of payment and TDS were in a single line in the earlier Form 16A and it was easy to fill Schedule TDS 2 from the same. But now if either the payment details or challan details

**Certain merits of the proposed rules which were scrapped could have been retained. A consolidated challan for all types of payments was a welcome change. When we have a single return 26Q for various non-salary payments made to residents, why tax should be deposited section wise. The concept of assessment year could also have been given a final goodbye as it creates confusion amongst accountants and junior staff and sometimes tax is mistakenly deposited for a different year than for which it is required.**

are summarised in the new Form 16A, the party would find it difficult to fill Schedule TDS 2 and claim benefit of TDS in his income tax return. If he mentions consolidated figures in his return of income, the same would not match with the individual payments shown by the deductor in the TDS statements filed by him. This may result in mismatch of TDS and the assessee may suffer on account of the same. A very important conclusion of this is that brain storming sessions between those in charge of TDS and Income tax should take place before making such changes. Otherwise, one step forward might take us several steps backward, if it is in another direction.

#### What Should the Deductor Do?

The detailed analysis above supports

the view that the information of both payments and challans should be detailed. Even in that case the assessee would have to correlate the two for filling Schedule TDS 2 in his IT return.



So what was the need for change in the format of form 16A?

## OTHER ISSUES

### Duplicate TDS Certificates

A duplicate TDS certificate can be issued in case of loss of the original one. However, now it has been specified that it should be certified as "Duplicate" by the deductor. Probably, the person making changes in the rules was watching Shah Rukh's film by the same name and found it apt to use its title.

### Digitally signed Form 16A

IT Rules have been amended to allow digitally signed Form 16 but there is no such corresponding change for Form 12BA, 16A or 27D. Even Circular no. 2/2007 dated 21-5-2007 was quiet about their digital signing. All the reasons which were relevant for allowing digitally signed Form 16 are relevant for other TDS/TCS certificates also. But for some strange reason, this e-facility has not been provided for other certificates. So the question arises whether Form 16A, 12BA etc have to be necessarily in paper format and the issuer has to physically sign each certificate. Such questions are particularly relevant for big corporates where thousands of Form 16A etc have to be issued and the authorised person has to gulp down several pain

killers to bear the back ache of signing the same.

Thankfully, there is a way out. Section 5 of Information Technology Act, 2008 provides legal sanctity to Electronic Signature. It states:

*"Where any law provides that information or any other matter shall be authenticated by affixing the signature or any document should be signed or bear the signature of any person then, notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied, if such information or matter is authenticated by means of digital signature affixed in such manner as may be prescribed by the Central Government.*

From the above, it is clear that any document which needs to be manually signed can also be signed by using digital signature even if the law does not specifically provide for it. Therefore, persons responsible for signing Form 12BA, 16A, 27D may not be allowed additional chutti (holiday) to relieve them from the pain of signing hundreds and thousands of certificates. Help can be taken from the IT (Information Technology) guy to help in digitally signing and e-mailing the same to the parties. It is hoped that suitable changes shall be made in the IT rules also in the near future regarding digital signing of other TDS/TCS certificates so that there is no confusion about their legal validity.

### Form 27D (TCS Certificate)

Above changes in Form 16A shall apply *mutatis mutandis* (no this is not an abuse, it only means with necessary changes) to Form 27D also. It will also now be issued on a quarterly basis instead of half yearly or monthly basis.

### Deposit of TCS

*TCS is to be deposited for:*

- Government collectors (who deposit tax by challan): On or before seven days from the end of the month of deduction.
- Others: Within a week from the last day of the month of deduction. Before scratching your heads, be assured that it means TCS has to be deposited by seventh of the next month for all collectors. Inadvertently, different words have been used in the two cases. **Further, the liberty to deposit TCS for March cases by 30<sup>th</sup> April, is not available. It has to be deposited by 7<sup>th</sup> April only.**

### Form 24G: Monthly Return for Government Deductors

- Form 24G is TDS/TCS Book Adjustment Statement (TBAS). Hope it does not become a disease like TB (Tuberculosis) for the IT department.
- It is a Monthly Form of details of credit of TDS/TCS to be filed electronically by Government deductors (24G: G for government)

where tax has been deposited by book entry.

- This form shall replace TDS/TCS Book Adjustment Form (TBAF) which had to be filed electronically on a quarterly basis.
- It has to be filed within 10 days from the end of each month.
- Filing of this form is the responsibility of the person designated for this purpose in the office of Pay and Accounts Officer (PAO), Treasury Officer (TO) or Cheque Drawing and Disbursing Officer (CDDO).
- In Government Accounting, there are several Drawing & Disbursing Officers (DDOs) under an Accounts Officer (AO).
- An AO processes the bills prepared by DDOs under him.
- A single Form 24G has to be prepared each month by an AO giving details of transfer vouchers for Form 24Q, 26Q, 27Q & 27EQ of DDOs under him. The total TDS deducted and deposited has to be shown separately for each DDO and for each type of payment i.e. salaries, other payments to residents etc. Thus, there can be a maximum of four entries per DDO in every month.
- Furnishing of either DDO Registration no. or DDO code is compulsory. DDO Registration number to be shown is the one provided by the Central Record Keeping Agency (CRA) under New Pension Scheme.
- Book Identification No. (BIN) has to be intimated by the responsible person to each DDO.
- Form 24G for the first few months of FY 2010-11 is already due. But extension will have to be given as the data structure for e-filing is under process.

### The Final Word

Consistency is one of the pillars on which an efficient and effective tax regime is based. Frequent changes result in chaos and confusion. But by now all of us have got used to changes in TDS rules, provisions, forms, data structure etc. In fact, something seems amiss if there is no change for a considerable period of time. This is in stark contrast to the paper regime where changes were seldom made and we could use the same TDS certificates and TDS returns year after year.

E-filing of TDS/TCS returns is a learning experience not only for us but for the income tax department and the allied agencies like NSDL. This is the basic reason for change. But changes should be well thought of and attempt should not be made to achieve stupendous results overnight. Income Tax (8<sup>th</sup> Amendment) Rules, 2009 notified on 25<sup>th</sup> March, 2009, is the case in point. It came out with Form 17 in which deductee wise breakup of challan had to be e-filed each month. A new TDS and TCS Compliance Statement (Form 24C) was envisaged in which monthly breakup of expenses under each section had to be given.

Such drastic measures cannot be implemented overnight, particularly when the machinery is not ready for the same. But better late than never. At the fag end of the next fiscal these proposed rules were scrapped and status quo was maintained. (Income Tax (First Amendment) Rules, 2010 dated 17<sup>th</sup> February, 2010)

This time another set of changes have been made. These changes appear to be rational and achievable. Some due dates have been rationalised. Obsolete forms have been abolished.

But the format of Form 16A and 27D has been changed without any valid reason for the same. Further, the same have been made quarterly. The prevalent system of issue of consolidated yearly certificates was good enough and should not have been tinkered with, as it does not seem to serve any purpose. A consolidated certificate is also preferred as mistakes noticed during the year can be rectified. In case of a quarterly certificate, what if mistakes are discovered later on or some bills are cancelled? In that case, an option should also be given to issue a Corrected TDS/TCS certificate.

Adding another responsibility for the government deductors (Form 24G) could also have been avoided. Additional information in the quarterly statements could have sufficed.

Certain merits of the proposed rules which were scrapped could have been retained. A consolidated challan for all types of payments was a welcome change. When we have a single return 26Q for various non-salary payments made to residents, why tax should be deposited section wise. The concept of assessment year could also have been given a final goodbye as it creates confusion amongst accountants and junior staff and sometimes tax is mistakenly deposited for a different year than for which it is required. ■



## Corporate Social Reporting: Evidence from Listed Companies in India



CSR is becoming an investment differentiator, benefiting companies that have clear ethical and sustainable mission complemented by tangible and transparent reporting. Company's brands, customer retention levels, and intellectual capital are of intense interest to investors. Companies that report more comprehensively on these important non-financial assets can often improve their valuation in the capital markets. Corporate social responsibility disclosure is considered to be a part of social accounting. Corporate social reporting generally includes disclosure in the annual report or disclosure through other medium like website, separate communiqué to stakeholders, advertisement etc. Through such reporting, a company discloses about its performance in the areas like, employee relations, environment and other issues of sustainability, community involvement, product, energy, etc. There is no uniformity regarding such reporting. Such reporting is voluntary in most of the countries. Read on to know more. This article reports on the findings of a study that sought to measure empirically the extent of corporate social reporting in annual reports of Indian listed companies.



**CA. (Dr.) Satyajit Dhar and  
Dr. Sarbani Mitra**

*(The authors are faculty of University of Kalyani (Kalyani) and Institute of Social Welfare and Business Management in Kolkata respectively.)*

The role of business in society has undergone a sea change. From the exhortation that there are no social obligations for business to the understanding that being socially responsible is critical, corporate social responsibility (CSR) has come a long way. The more traditional business perspective is now giving way to a realisation that corporate responsibility touches not only economic issues but also the social community, including

employees and customers. The inspiring and important development of CSR has started to gain legitimacy and is now being recognised as a strategic element of many leading companies of all types and sizes.

However, different organisations have framed different definitions of CSR. Although no universally accepted definition of CSR exists, the World Business Council for Sustainable Development (WBCSD, 2000) defines

CSR as *"the commitment of business to contribute to sustainable economic development, working with employees, their families, the local community and society at large to improve their quality of life."*

Corporate social responsibility means the obligations, which a corporation owes to the society. It is no longer considered a tripartite venture, i.e. owners, workers and consumers, but it has become a multiparty system. It includes government, financial institutions, banks, owners, workers, consumers and society. All these classes have their own objectives to be achieved from the business. Thus, the meaning of CSR is two fold. On one hand, it exhibits the ethical behaviour that an organisation exhibits towards its internal and external stakeholders. On the other hand, it denotes the responsibility of an organisation towards the environment and society in which it operates.

CSR is becoming an investment differentiator, benefiting companies that have clear ethical and sustainable mission complemented by tangible and transparent reporting (Hawkins, 2006: 257). A growing body of evidence indicates that companies that fall short of the transparency benchmark risk significant damage to management credibility. In the worst case, companies face an erosion of shareholder confidence that can, in turn, do damage to market capitalisation, credit, and liquidity. But along with negative pressures, there are also positive reasons for going transparent. The market mechanism has already moved on from corporate valuations being based strictly on assets, turnover, profitability and market share. Company's brands, customer retention levels, and intellectual capital are of intense interest to investors. Companies that report more comprehensively on these important non-financial assets can often improve their valuation in

**“Corporate social responsibility disclosure is considered to be a part of social accounting (Mathews, 1993: 59). Social accounting attempts to broaden the scope of accounting discipline by considering the issues and audiences that have not been addressed by traditional mainstream accounting development. It is noted that social accounting is an area where accountant had ventured much earlier. Estes (1973: 252) pointed that accountants should be involved in determination of social costs (also called valuation of externalities) as “cost determination is more of the forte of accountants than of engineers and economists”.**”

the capital markets. All over the world, several organisations such as: World Commission on Environment and Development (WCED), Commission of the European Communities, International Organisation for Securities Commission (IOSCO), Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) have actively promoted the disclosure by firms to improve transparency of financial information. This concern is extended to all stakeholders knowing that greater disclosures of value-relevant accounting information are more likely to have higher international capital mobility. Corporate social reporting generally includes disclosure in the annual report or disclosure through other medium like website, separate communiqué to stakeholders, advertisement etc. Through such reporting, a company discloses about its performance in the areas like, employee relations, environment and other issues of sustainability,

community involvement, product, energy, etc. There is no uniformity regarding such reporting. Such reporting is voluntary in most of the countries. At the outset, it may be mentioned that we have used the terms like corporate social responsibility (CSR) disclosure, social reporting, corporate social reporting, and sustainability reporting to mean the same thing.

While a good number of researches have been undertaken on CSR disclosure practices in the economic and organisational contexts of Europe and the United States of America, hardly a few studies have looked at corporate social responsibility disclosure practice and its determinants in developing countries like India. Given this scenario, the authors see reporting as an important communication tool or channel, specifically in case of Indian corporate sector, which can ensure greater corporate transparency and enable a better engagement with multiple stakeholders.

### Literature Review

Corporate social responsibility disclosure is considered to be a part of social accounting (Mathews, 1993: 59). Social accounting attempts to broaden the scope of accounting discipline by considering the issues and audiences that have not been addressed by traditional mainstream accounting development. It is noted that social accounting is an area where accountant had ventured much earlier. Estes (1973: 252) pointed that accountants should be involved in determination of social costs (also called valuation of externalities) as “cost determination is more of the forte of accountants than of engineers and economists”. However, interest in area of social accounting waned out due to the fact that valuation of externalities involved subjective assessment and accountants generally resist involvement in such effort. But corporate

social responsibility disclosure remains as a field of research as it has certain role in the process of corporate financial reporting. A good review of corporate social reporting literature is available in Gray et al. (1995) and Mathews (1993).

In the free market system there is little scope of assumption of social responsibility objectives by corporate organisations. A number of economists from Adam Smith to Milton Friedman objected to the notion that corporate entities have any social responsibility other than economic responsibilities to the shareholders. According to Friedman, social responsibility expenditure should not be made as those are tax levied by managers on shareholders (Friedman, 1970: 89).

However, several arguments have been put forward by different authors to support the assumption of corporate social responsibility and disclosure of CSR practices by corporations.

Garriga and Melé (2004) reviewed the CSR literature and classified CSR theories under four broad categories: economic or instrumental theories, political theories, integrative theories, and ethical theories. According to them, other theories such as institutional and signal theories have also attempted to explain CSR practices.

According to the instrumental theories, companies implement CSR to increase profit or to maximise shareholder value. Thus, CSR related practices are advocated as a business case or market related arguments and it is argued that social responsibility disclosure has a positive effect on market performance. There are several studies on CSR reporting and market performance (Alexander and Bucholtz, 1978; Spicer, 1978; Ullmann, 1985; Waddock and Graves, 1997; McWilliams and Siegel, 2000; Cox et al., 2004; Brammer et al., 2006) and such studies exhibit mixed results.

Political theories on CSR argue

that companies should use their power and influence in society. Social contract theory is a political theory that maintains that any social institution including business operates in society through a social contract, expressed or implied. Accordingly, survival or growth of a business unit depends upon the delivery of some socially desirable ends to society.

Integrative theory tries to integrate social demands and corporate responses to such demands to achieve prestige, social acceptance and social legitimacy. Various authors have argued that companies should report corporate social responsibility to project a legitimate image (Deegan et al., 2000; Wilmshurst and Frost, 2000; Milne and Patten, 2002; Mobus, 2005).

Ethical theories on CSR are basically stakeholder approach to CSR. Under the stakeholder theory, a company is not only responsible to shareholders but also is responsible to all stakeholders, who are affected by the activities of a company. Freeman is considered to be the father of

**“The results of our analysis of the content of annual reports of 96 sample companies showed that 79.17 per cent of the companies made some form of CSR disclosure. Regarding Indian practice of CSR the survey results show that there is scope of improvement. Organisations are not reporting material matters that reflect the concerns of stakeholders. Separate sustainability or corporate social report is not common barring a few companies. Of the various possible CSR disclosure themes, it was found that human resources accounted for 67 disclosures; the next highest number was community involvement (62) and products (58).”**

stakeholder theory (Laplume et al., 2008) for his seminar work, strategic management. Ullmann (1985) used a model based on stakeholder theory to explain CSR practice. Using the Ullmann's model Roberts found that stakeholder theory is an appropriate model to explain practice of corporate social reporting. Some authors pointed out that acceptance of stakeholder theory have resulted in stakeholder management through corporate social reporting. According to such authors corporate social responsibility disclosures are only means of managing (or influencing or manipulating) stakeholders (e.g. Roberts, 1992).

Institutional theory relates to role of values in creating long-term stability and persistence of organisations. Further, Scott (1987) pointed out that institutions adapt over time evolving historically. Even regulations force companies to adapt more quickly than being unregulated. In this context, Tolbert and Zucker (1983) found that as there is increase in adoption of new structures, there will be increase in the institutions legitimacy. Signal theory posits that corporate social responsibility announcements may be value relevant (i.e. firm value may be dependent on nature of announcement, positive or negative).

Gray et al. (1987: ix) defined corporate social reporting as “the process of communicating the social and environmental effects of organisation's economic actions to particular interest groups within society and to society at large”. In this context, many researchers made a number of empirical studies on corporate social reporting practice and analysed the empirical results relating to the extent of social responsibility disclosure practices in case of various sample units.

Ernst and Ernst survey in 1978 identified six areas - environment,

energy, fair business practices, human resources, community involvement and other, in which companies might choose to report on social responsibilities (Perks, 1993: 85).

Abreu and Carreira (2008) evaluated social responsibility disclosure practices in annual reports of the largest listed firms of the Portuguese Stock Index in the Euronext *Lisbon* aiming to assess the value of the firm.

Islam *et al.* (2005) made an examination of corporate environmental disclosure by the Bangladeshi public limited companies. They have found that only 16 per cent companies have disclosed environmental information under a separate heading in the annual reports.

Holder-Webb *et al.* explored the CSR disclosure practices of a size- and industry-stratified sample of 50 publicly-traded U.S. firms. In disclosure practices they put stress on community matters, health and safety, diversity and human resources matters, and environmental programs.

Parsa and Deng (2008) have made a study on capital markets' reactions to social information announcements taking sample of 465 companies joined London Stock Exchange (LSE), aiming to investigate whether the LSE reacts to social information announcements by new entrants to LSE over a period of five years.

Azim *et al.* (2009) empirically investigated corporate social reporting practices in annual reports (published in 2007) of listed companies from Bangladesh, where corporate social reporting is a matter of voluntary disclosure. The study covered an extensive survey of the contents, form, nature, and extent of corporate social reporting practices of listed companies.

In India, research works concerning the corporate social reporting are only a few. The important ones are mentioned below.

**“ On an overall basis, there is scope of improvement in corporate social reporting practices of Indian companies. Although, a few companies have started to publish separate sustainability or corporate social report, there is lack of objective and informative reporting as demonstrated by this survey. Multitude of directives regarding CSR reporting pose a challenge on having a simple and credible framework for analysing CSR initiatives of the reporting companies.”**

Empirical studies, made by eminent researchers viz., Lal (1985); Banerjee (2001); Paul and Pal (2001); Raman (2006); Pramanik *et al.* (2007); Malarvizhi and Yadav (2008); Parsa and Deng (2008) have examined corporate reporting practices in Indian perspective. Amongst them, the remarkable findings related to the present study were obtained from Raman (2006) and Malarvizhi and Yadav (2008). Raman (2006) conducted an exploratory study on how top management perceives and reports CSR. Using the technique of content analysis he looked at the chairman's message section in the annual reports of the top 50 companies in India to identify the extent and nature of social reporting. Malarvizhi and Yadav (2008) examined corporate environmental internet reporting practices of selected Indian companies grouping them into manufacturing and non-manufacturing sectors to understand practices of corporate environmental reporting by companies operating under different sectors.

## **Data, Sample and Methodology**

### **Sample Design**

Initially, we have considered listed companies of Bombay Stock

Exchange (BSE) comprising BSE 500 index as our population. BSE 500 is a broad-based index and represents 94 per cent of market capitalisation of all listed companies of BSE. Considering time and resource constraints, it was decided to restrict the survey among 20 per cent of those 500 units. Accordingly, annual reports for total 100 numbers of listed companies were planned to be reviewed. We selected 100 companies out of 500 companies on a random basis. The process of sampling was called random sampling without replacement. These 100 sample units were target units for further analysis. We have taken 2007-08 financial year (i.e. year ending 31<sup>st</sup> March, 2008) as our study period, being the latest period for which annual reports are available. In a few cases, year end date falls between 30<sup>th</sup> June, 2006 to 31<sup>st</sup> December, 2007. Out of 100 companies, we could not consider four companies due to non-availability of annual report or firm level data in Centre for Monitoring in Indian Economy (CMIE) Prowess database. Thus our final sample consists of 96 listed companies.

### **Data and Methodology for the Study**

CSR disclosure items are hand picked from the annual reports of the sample units after a thorough examination of the contents of annual reports. Literature survey was used for the selection of corporate social reporting indicators or disclosure items and their major sub-indicators. For measuring the extent of corporate social reporting in annual reports of the companies, we have constructed an unweighted disclosure index based on the previous empirical studies with some modifications, where one item scores one if disclosed and zero if not disclosed. It was decided to attribute some weightage to each of the indicators or disclosure items. Although attributing weightage is fraught with

subjectivity to some extent (Das *et al.*, 2008), it was considered unavoidable given the lack of uniformity in CSR disclosure.

### Selection of Indicators

There being no regulatory requirement (except energy efficiency related disclosure in Director's Report) CSR disclosures are not structured. In certain studies, fair business practices is categorised as a separate categories (Perks, 1993), but we included it under other, separate fair practice with regard to supplier etc. having received minimal attention in Indian Company reports. To show the trends in corporate social responsibility disclosures and to analyse the extent and type of disclosure in a systematic manner, selection of some indicators was considered necessary. Based on the previous studies (e.g., Guthrie, 1982; Guthrie and Mathews, 1985; Perks, 1993; Gray *et al.*, 1995; Holder-Webb *et al.*), the study concentrated on four primary indicators and some major sub-indicators. Content analysis was used to place information within following four dimensions/indicators:

1. Theme
2. Evidence
3. Location
4. Amount

'Theme' was based on categories such as environment, energy, human resources, products, community involvement and others. In India, there is hardly any regulation regarding corporate social responsibility disclosure. As per section 217 of the Companies Act, companies are required to report certain pieces of energy efficiency and technology absorption related information in the Directors' Report. There is a requirement to disclose long outstanding dues to the units belonging to small scale industry sector. We have not considered disclosure of these pieces of mandatory information as

social reporting. However, disclosure through corporate governance report and management discussion and analysis are considered to find out the extent of corporate social reporting. Although such reports are mandatory there being no structure of such report, disclosures relating to corporate social responsibility within such reports are considered voluntary. 'Evidence' described the form of disclosure: monetary, non-monetary, and declarative (qualitative) and none. 'Location' referred to a choice between management reviews, a separate social disclosures section, parts of other sections of the annual report and a separate booklet on social responsibility. 'Amount' was the familiar measure by the proportion of pages devoted to social responsibility matters (Guthrie and Mathews, 1985).

### Assignment of Score

Considering nature of work, we were required to consider corporate social responsibility of the sample units, which were diverse in nature and generally lacking any structure. It was decided to attribute some score/weightage to first two indicators mentioned above considering their perceived importance towards CSR disclosure activity for any unit. We have avoided assignment of scores in case of the remaining two indicators, since considerations of first two indicators are enough for the purpose of evaluation of the extent of disclosure. The break up of maximum achievable score for each indicator is given below:

Primary Indicator	Score/Importance
Theme	100
Evidence	100
Total	200

As each of the above indicators has some sub-indicators, the total score was distributed to each of the sub-indicators under each indicator according to its perceived importance. Though it was subjective, but it was

considered unavoidable (Wallace *et al.*, 1994). It is pertinent to mention here that after designing the scorecard, some revision was made based on discussion with the academicians, auditors as well as company executives working in the field of finance. The detailed scorecard that showed the CSR disclosure score value for each of the indicators and sub-indicators is given in Table I.

Table I. CSR Disclosure Scorecard

Sl. No.	Parameter	Score
<b>1</b>	<b>Theme (100)</b>	
1.1	Environment and Energy	20
1.2	Human Resources	20
1.3	Products	20
1.4	Community Involvement	20
1.5	Others	20
<b>2</b>	<b>Evidence (100)</b>	
2.1	Monetary quantification	50
2.2	Non-monetary quantification	50
<b>GRAND TOTAL</b>		<b>200</b>

The study evaluated the combined CSR disclosure score value of the sample units based on CSR reporting with respect to the two primary indicators. Our assignment of score is based on attributes like comprehensiveness, clarity, relevance etc. Ultimately, to obtain Corporate Social Responsibility Disclosure Score (CSRDS), following formulae was applied:

$$\text{CSRDS} = \frac{\text{Score Obtained}}{\text{Maximum Achievable Score}} \times 100$$

## Social Reporting Practice of Indian Companies

### Extent of Social Reporting

The results of our analysis of the content of annual reports of 96 sample companies showed that 79.17 per cent of the companies made some form of CSR disclosure. Regarding

Indian practice of CSR the survey results show that there is scope of improvement. Organisations are not reporting material matters that reflect the concerns of stakeholders. Separate sustainability or corporate social report is not common barring a few companies. Of the various possible CSR disclosure themes, it was found that human resources accounted for 67 disclosures; the next highest number was community involvement (62) and products (58). Of lesser importance were environment and energy (33) and some other themes. Other reporting themes include safety management, total productive maintenance, welfare of women, corporate social responsibility, global compact, occupational health services, award and achievements, customers' view, new introductions in current year, etc. These results are reported in Table II.

**Table II. Types of Corporate Social Responsibility Disclosure**

Theme of Disclosure	Companies reporting	% of Total
Environment and Energy	33	34.38
Human resources	67	69.79
Products	58	60.42
Community involvement	62	64.58
Others	36	37.50
No disclosure	20	20.83

Note: Some companies reported more than one theme.

Source: Annual Reports (2008) of Select Companies. Results computed.

Table III outlines the results for the degree of quantification. Out of 96 sample companies, 76 companies quantified their disclosures, but none of the companies gave monetary disclosures alone, whilst 20.83 per cent gave some non-monetary quantification only. The reports giving both monetary and non-monetary quantification were limited to 58.34 per cent of 96 sample companies.

**Table III. Quantification of Social Responsibility Accounting Disclosure**

Quantification	No.	%
Both monetary and non-monetary quantification	56	58.34
Monetary quantification	0	0
Non-monetary quantification	20	20.83
No disclosure	20	20.83

Source: Annual Reports (2008) of Select Companies. Results computed.

Table IV indicates that human resources had the highest incidence of CSR disclosures to be located throughout the annual reports with 56.72 per cent used general body and 25.37 per cent used management discussion and analysis part of the annual report devoted to social responsibility disclosures. However, 16.42 per cent of companies disclosed this information in the separate section of the report, and only one sample company issued a separate booklet on socially related matters.

**Table IV. Location of Corporate Social Responsibility Disclosure**

Theme of Disclosure	Management Discussion and Analysis		Separate section of annual report devoted to CSR Disclosure		Other section		Separate booklet	
	No.	%	No.	%	No.	%	No.	%
Environment and Energy	7	21.21	8	24.24	17	51.52	1	3.03
Human resources	17	25.37	11	16.42	38	56.72	1	1.49
Products	4	6.90	12	20.69	41	70.69	1	1.72
Community involvement	13	20.97	12	19.35	36	58.07	1	1.61
Others	2	5.56	12	33.33	21	58.33	1	2.78

Note-Many companies made disclosure under more than one theme and disclosure in Director's Report has not been considered.

Source: Annual Reports (2008) of Select Companies. Results computed.

Table V indicates that in case of 20.83 per cent of the sample companies corporate social responsibility disclosure is absent, whereas less than 4 per cent of total pages of the annual report is devoted by 28.13 per cent of the companies for the purpose. On the contrary, only 21.87 per cent of the companies devote more than 10 per cent of total pages for CSR, out of which 6.25 per cent shows satisfactory result where more than 16 per cent of total pages are devoted for the purpose.

**Table V. Proportion of Page Devoted to CSR Disclosure**

Ratio of Pages (%)	No. of Companies	%
0	20	20.83
0-2	5	5.21
2-4	22	22.92
4-6	21	21.88
6-10	7	7.29
10-14	10	10.42
14-16	5	5.20
>16	6	6.25
Total	96	100.00

Source: Annual Reports (2008) of Select Companies. Results computed.

### CSR Disclosure Score of Sample Companies

The study evaluated the combined CSRDS value of the sample companies

“The scarcity of hard data that is publicly available on the business benefits of CSR poses a challenge for companies who are trying to calculate the extent of their investment in CSR. The hesitancy on the part of firms to collect or disclose data justifying CSR investments reflects the tensions between those, including many activists that view CSR as an ethical issue that should be removed from the realm of profit and those that understand CSR as a business imperative.”



based on performance with respect to two primary indicators – theme and evidence, as reported in Table VI. Analysis of the CSRDS value reveals that out of 96 sample companies, 20.83 per cent companies (20 companies) don't attain any score, as they have

not made any form of CSR disclosure. Out of rest 76 sample companies, that made some form of CSR disclosure, no sample company has attained 100 per cent score. The maximum score of CSR disclosure is high enough i.e. 91 per cent and the minimum score of CSR disclosure is very low i.e. 8.50 per cent with the mean and standard deviation of CSRDS being 46.91 per cent and 20.55 per cent respectively. 3.13 per cent companies (3 companies) have attained more than 80 per cent CSR disclosure score; on the contrary 31.25 per cent companies (30 companies) have attained less than 40 per cent CSR disclosure score. 18.75 per cent companies (18 companies) have attained 60-80 per cent CSR disclosure score, whereas 26.04 per cent companies (25 companies) have attained 40-60 per cent CSR disclosure score.

**Table VI. Overall Corporate Social Responsibility Disclosure Score**

Score (%)	No. of Sample Companies	% of Sample Companies
0	20	20.83
<40	30	31.25
40-60	25	26.04
60-80	18	18.75
>80	03	3.13
<b>Total</b>	<b>96</b>	<b>100.00</b>

Source: Annual Reports (2008) of Select Companies. Results computed.

### Summary and Conclusion

On an overall basis, there is scope of improvement in corporate social reporting practices of Indian companies. Although, a few companies have started to publish separate sustainability or corporate social report, there is lack of objective and informative reporting as demonstrated by this survey.

Multitude of directives regarding CSR reporting pose a challenge on having a simple and credible framework for analysing CSR initiatives of the reporting companies. It must also be

appreciated that given the diversity of industries it is unlikely that there could be a one-size-fits all structure. Social responsibility reports are a reflection of the reporting company and of its approach to a wide range of issues that may impact its stakeholders. They are unlikely ever to become fully comparable. It may be hoped that responsible company through its structured CSR reporting would clearly demonstrate its committed approach (as opposed to simply complying) and such a company will deliver more valuable report to its shareholders incorporating their expectations.

However, the scarcity of hard data that is publicly available on the business benefits of CSR poses a challenge for companies who are trying to calculate the extent of their investment in CSR. The hesitancy on the part of firms to collect or disclose data justifying CSR investments reflects the tensions between those, including many activists that view CSR as an ethical issue that should be removed from the realm of profit and those that understand CSR as a business imperative.

Among firms in developing countries, management performance indicators for CSR are often not even on their radar screen and they remain focused on trying to fulfill order, manage demand, and grapple with the many challenges associated with global competition. For the immediate future, given the nature of the intangible benefits associated with CSR, the business case is likely to remain vague. Despite the significant anecdotal evidence that exists today, more firms are unlikely to undertake CSR in the absence of a simple and credible framework for analysing the business case, and quantifying the costs and benefits of CSR. These significant issues require careful consideration by regulators and appropriate policy change may only induce the business organisations to report CSR performance. ■

## Nominee vis-à-vis Legal Heir

In the event of the death of a person holding any property, asset or estate, the successors by inheritance or those under an executed will are entitled to share such property, asset or estate. In India there are several Acts whereunder a nomination has to be done so that the property, asset or equity of a deceased person would be paid, handed over to the nominee to make a valid discharge under that Act. A legal heir can be a nominee but a nominee can not necessarily be a legal heir. One has to be alert and cautious while making nomination, considering the legal status of the nominee as per the Act/Scheme under which one is executing/availing a nomination facility. This article discusses the legal position of a nominee vis-à-vis legal heir.

The nomination is required to be done to make a valid discharge of obligation under the Indian Acts. However, the Supreme Court considers a 'nominee' as merely a trustee for the deceased's estate.

In *Smt. Sarbati Devi & Another v. Smt. Usha Devi* A.I.R. 1984 SC 346/(1984) 1 SCC 424, the assured of a life insurance policy nominated his wife as a nominee under Section 39 of the Insurance Act, 1938. The assured died intestate leaving behind him his mother, widow and a son. The mother, in the capacity of the nearest legal heir, claimed the share of the beneficial interest from the amount payable under the policy. The Supreme Court held that "A mere nomination made under Section 39 of the Insurance Act, 1938 does not have the effect of conferring on the nominee any beneficial interest in the amount payable under the LIC policy on the death of the insured. The nomination only indicates the hand which is authorised to receive the amount, on payment of which the insurer gets a valid discharge of its liability under the policy". Thus as per the Supreme Court's verdict, nomination under the Insurance Act does not operate as succession. This view was taken in respect of nomination under the other Acts/Schemes.

The Supreme Court in *Vishin N. Khanchandani & Another v. Vidya Lachmandas Khanchandani & Another* (2000) RD-SC 430/ (2000) 6 SCC 724 held that "The law laid down in *Smt. Sarbati Devi's* case holds the field and

*is equally applicable to the nominee becoming entitled to the payment of the amount on account of national savings certificates."*

In *Ramdas Shivram Sattur v. Rameshchandra Popatlal Shah*, the Bombay High Court, relying on *Sarbati's* Case (Supra), held that "the purpose of nomination under Section 30 of the Maharashtra Co-operative Societies Act 1960 is essentially to provide for the discharge of the societies' obligation and the nomination does not lay down any special rule of succession of properties of the deceased member overriding the general rule of inheritance prescribed by the personal law of the member of co-operative society."

Similarly, in *Arnab Kumar Sarkar v. Smt. Reba Mukherjee and Ors*, A.I.R. 2007 Cal 79/IV (2007) BC 134, the Calcutta High Court in respect of nomination under Section 45Z of the Banking Regulation Act held that "Just as Section 39 of the Insurance Act, 1938 is for discharge of insurer's obligations, the purpose of Section 45Z of the Banking Regulation Act, 1949 is to provide for the discharge of the Bank's obligation." Sections 45ZA & 45ZE of Banking Regulation Act relate to nomination for bank deposits & locker/safe deposit vaults respectively.

**Supreme Court considers a 'nominee' as merely a trustee for the deceased's monies/estate of the deceased.**



**CA. Manoj Deore**

(The author is a member of the Institute. He can be contacted at [camanojdeore@icai.org](mailto:camanojdeore@icai.org))

## “Nomination under the Insurance Act does not operate as succession.”

Thus, Courts intend to treat the 'Nominee' merely as trustee/custodian and the 'Legal Heirs' under the Law of Succession/Enforceable Will as absolute beneficial owner of the deceased's estate/asset. As per Reserve Bank of India (RBI) Guidelines, the nominee of the deceased would receive the money in the capacity of a trustee of legal heirs.

This view is again confirmed by the Supreme Court in *Shipra Sengupta v. Mridul Sengupta & Others* [Civil Appeal No. 809 of 2002, decided on 20<sup>th</sup> August, 2009], wherein it was held that *"In view of the legal position, it is abundantly clear that the amount in any head can be received by the nominee, but the amount can be claimed by the heirs of the deceased in accordance with the law of succession governing them"*. In this case the widow of the deceased claimed **her share** of the deceased's insurance, gratuity, PPF under Indian Succession Act, though the deceased had nominated his mother as nominee under these schemes before his marriage.

### Laws of Nomination

Several Acts / Schemes in India have certain rules for nomination. The nominee is entitled to receive and keep money under LIC/GIC policy, Provident Fund, PPF, Bank Accounts & Fix Deposits, Mutual Fund investment and other welfare laws in the event of death of their holder.

Under the Insurance Act, nominee is a person named in the proposal for the LIC/GIC policy and who, in the event of death of the assured, will receive money due under the policy as trustee for the benefit of legal heirs. Under the Employees Provident Fund Act, 1952 and Payment of Gratuity Act, 1972, in case of an employee

having no family, nomination made in favour of an outsider is permissible. Under PPF Act, 1968, the amount to the credit of the deceased member shall go to the nominee, whether a member of the family or not. Under the Banking Regulation Act, 1949, nominee is such a person to whom the amount of deposit may be returned or the contents of locker/safe deposit vault may be handed over in the event of the death of depositor/locker holder. Even after valid nomination, the heirs under will/ inheritance are entitled to own/ share the beneficial interest in the deceased's property.

### Contradictory Legislative Intent

The Companies Act, 1956 specifically intends to give a validly designated nominee of shares in a company, the exclusive right of ownership of shares after the death of the holder. Interpreting Section 109A of the Companies Act, 1956, the Bombay High Court in *Harsha Nitin Kokate V. Saraswat Co-Operative Bank Limited & others* [Suit No. 1972 of 2008, decided on 20<sup>th</sup> April, 2010] held that rights of the nominee to the shares of a company would override the rights of heirs whom property may be bequeathed. Thus if nomination of shares has been made in favour of a person other than heir, the nominee and not the heir will be entitled to the beneficial interest in the shares.

### Section 109A. Nomination of shares

- (1) Every holder of shares in, or holder of debentures of a company may, at any time, nominate, in the prescribed manner, a person to whom his shares in or debentures of, the company shall vest in the event of his death.
- (2).....
- (3) Notwithstanding anything contained in any other law for the time being in force or in any disposition,

whether testamentary or otherwise, in respect of such shares in, or debentures of, the company, where a nomination made in the prescribed manner purports to confer on any person the right to vest the shares in, or debentures of, the company, the nominee shall, on the death of the shareholder or holder of debentures of the company or, as the case may be, on the death of the joint holders become entitled to all the rights in the shares or debentures of the company or, as the case may be, all the joint holders, in relation to such shares in, or debentures of the company to the exclusion of all other persons, unless the nomination is varied or cancelled in the prescribed manner.

The same principle applies to the shares held in **Demat form** under the Depositories Act, 1996. The actual investor in shares in demat form is known as the **Beneficial Owner** and is entitled to all the benefits as security holder on the securities lying in his name with the depository. Section 9.11 of The Depositories Act, 1996 confers exclusive ownership right of shares on the last valid nominee of the deceased beneficial owner provided the nomination shall be dated and registered with the depository participant (Bank) as per business rule.

### Section 9.11 of The Depositories Act, 1996 reads as -

- 9.11.1.** In respect of every account, the Beneficial Owner(s)

“Courts intend to treat the 'Nominee' merely as trustee/custodian and the 'Legal Heirs' under the Law of Succession/Enforceable Will as absolute beneficial owner of the deceased's estate/asset.”

**As per Reserve Bank of India Guidelines, the nominee of the deceased would receive the money in the capacity of a trustee of legal heirs.**

("Nominating Person(s)") may nominate any Person ("Nominee") to whom his securities shall vest in the event of his death in the manner prescribed under the Business Rules from time to time.

**9.11.6.** A nominee shall on the death of the Nominating Person(s) be entitled to elect himself to be registered as a Beneficial Owner by delivering a notice in writing to the Depository, along with the certified true copy of the death certificate issued by the competent authority as prescribed under the Business Rules. Subject to scrutiny of such election, the securities in the Account shall be transmitted to the account of the Nominee held with any depository.

**9.11.7.** Notwithstanding anything contained in any other disposition and/or nominations made by the Nominating Person(s) under any other law for the time being in force, for the purposes of dealing with the securities lying to the credit of deceased Nominating Person(s) in any manner, the Depository shall rely upon the last nomination validly made prior to the demise of the Nominating Person(s). The Depository shall not be liable for any action taken in reliance upon and on the basis of nomination validly made by the Nominating Person(s).

The facts of the Harsha Nitin Kokate's case (Supra) were that the deceased person validly executed the nomination in respect of shares with the depository participant cell of the defendant bank held in **demat** form. The nomination was made in

favor of his nephew before his death and after his marriage with plaintiff. The nomination was as per business rule and registered with depository participant. The deceased's wife (plaintiff) claimed the shares as legal heir.

**The High Court denied her claim and held that:**

*"A reading of Section 109A of the Companies Act and 9.11 of the Depositories Act makes it abundantly clear that the intent of the nomination is to vest the property in the shares which includes the ownership rights thereunder in the nominee upon nomination validly made as per the procedure prescribed, as has been done in this case. These Sections are completely different from Section 39 of the Insurance Act which require a nomination merely for the payment of the amount under the Life Insurance Policy without confirming any ownership rights in the nominee or under Section 30 of the Maharashtra Cooperative Societies Act which allows the Society to transfer the shares of the member which would be valid against any demand made by any other person upon the Society. Hence these provisions are made merely to give a valid discharge to the Insurance Company or the Cooperative Society without vesting the ownership rights in the Insurance Policy or the membership rights in the Society upon such nominee".*

*"On the death of the shareholder, the nominee would become*

**Even after valid nomination, the heirs under will/ inheritance are entitled to own/ share the beneficial interest in the deceased's property.**

**If nomination of shares under Section 109A of the Companies Act, 1956 has been made in favour of a person other than heir, the nominee and not the heir will be entitled to the beneficial interest in the shares.**

*entitled to all rights in the shares to the exclusion of all other persons. Nomination under Section 109A of the Companies Act does not entail mere payment of shares but specifically vests property in the shares with the nominee in the event of death of the holder of shares".*

The meaning of 'vests' as per Black's Law Dictionary is –

- to confer ownership of (property) upon a person
- to give a person an immediate, full right of present or future enjoyment
- to put a person in the possession of land by the ceremony of investiture

### Conclusion

In spite of the nomination facility so as to make valid discharge of obligations under various Indian Acts (Excluding Companies Act), the heirs can claim the money, estate paid to the nominee. The nominee is mere a trustee while the heir enjoys title to the monies/ estate of the deceased. Exceptionally, under the Companies Act there is a specific legislative intension to confer beneficial rights of deceased's shares on the nominee and not the heirs. Hence, one has to be alert and cautious while making nomination, considering the legal status of the nominee as per the Act/Scheme under which one is executing/availing a nomination facility. ■

## Base Rate: A Pragmatic Shift in Banking Industry



Indian banking entered a new era on 1<sup>st</sup> July, 2010 when an improved method of pricing loans was finally activated. The move to a transparent Base Rate will act as a benchmark for the pricing of all loans, dished out by banks. This transition from the Benchmark Prime Lending Rate (BPLR) to the base rate system is targeted to increase transparency in lending rates and help small borrowers negotiate better rates with banks. Consequently, SMEs with healthy credit profiles will now be able to negotiate far better rates with banks. The new regime shall see an increased credit flow to small borrowers. Banks with competitive base rate and efficient treasury operations are well placed to benefit from the new scenario. Read on to know more about the concept.

Reserve Bank of India (RBI) had constituted a Working Group on Benchmark Prime Lending Rate to review the present benchmark prime lending rate (BPLR) system and suggest changes to make credit pricing more transparent.

The Working group has submitted its recommendation in the month of October 2009 to Reserve Bank of India. Based on the recommendation made by the Working group and the suggestions received from various banks operating in India, Reserve Bank of India has subsequently issued the guidelines on Base Rate on 9<sup>th</sup> April, 2010. As per the guidelines, all banks are required to introduce Base Rate with effect from 1<sup>st</sup> July, 2010, for pricing the borrowers. Subsequently on 14<sup>th</sup> May, 2010 there was a clarification from RBI that banks can have only one Base Rate.

- Base Rate system will replace the existing COBAR system with effect from 1<sup>st</sup> July 2010.
- Banks may choose any benchmark to arrive at the Base Rate that may be disclosed transparently.
- Banks are free to use any methodology as considered appropriate, provided it is consistent and is made available for review/scrutiny by RBI.
- Guidelines permit the Banks to change the benchmark and the methodology any time during the initial six months till end of December 2010 to stabilise the system of Base Rate calculation.
- The Actual lending rates charged may be transparent and consistent and be made available for supervisory review/scrutiny, as and when required.



**CA. (Dr.) R. K. Agrawal**

*(The author is a member of the Institute. He can be reached at [eboard@icai.org](mailto:eboard@icai.org))*

### Salient Features of the Guidelines

Salient features of the Base Rate guidelines are as under:

### Applicability of the Base Rate

Base Rate shall be applicable to all categories of Loans, except for DRI advances, Loans to Staff and Loans

against our own deposits, which could be priced without reference to the Base rate.

The Base Rate could also be a benchmark rate for floating rate loan products, apart from external market benchmark rates. The floating interest rate based on external benchmark should, however be equal to or above the base rate at the time of sanction or renewal.

Changes in the Base Rate shall be applicable in respect of all existing loans linked to Base Rate, in a transparent and non-discriminatory manner.

Since the Base Rate will be the minimum rate for all loans, banks are not permitted to resort to any lending below the Base Rate. Accordingly, the stipulation of BPLR as the ceiling rate for loans up to ₹2 lakh is withdrawn by RBI. In other words the loans up to ₹2 lakh sanctioned on or after 1<sup>st</sup> July, 2010 shall be with reference to the Base Rate. This move is expected to increase the flow of credit to small borrowers at reasonable rates.

Interest rates applicable for all tenors of rupee export credit advances with effect from 1<sup>st</sup> July, 2010 shall be at or above Base Rate.

### Review of Base Rate

Base Rate has to be reviewed at least once in a quarter, with the approval of the Board or the Asset Liability Management Committee (ALCO), as per the Bank's practice. Since transparency in the pricing of lending products has been a key objective, banks are required exhibit the information on their Base Rate at all branches and also on their websites. Banks are also required to provide information on the actual minimum and maximum lending rates to the RBI on a quarterly basis, as hitherto.

### Transitional Issues

The Base Rate system shall be applicable for all loans sanctioned on

or after 1<sup>st</sup> July, 2010. In respect of existing loans, Base Rate shall be applicable at the time of renewal. Existing loans based on the COBAR system shall run till their maturity. In case the existing borrowers want to switch to the new Base Rate system, before the expiry of the existing contracts, an option may be given to them on mutually agreed terms. Banks however, should not charge any fee for such switch over. Banks may announce their Base Rate after obtaining approval from the ALCO/BOARD.

### Methodology Used in Computing Base Rate

Based on the guidelines issued by the Reserve Bank of India on Base Rate implementation, banks arrive at the Base Rate on the basis of different benchmark rates so as to consider different options in loan pricing. Different benchmark rates reckoned while working out the Base rate are as under:

1. Average Cost of Deposits for 12 months ended on 31<sup>st</sup> March, 2010 (2009-10).
2. Average Cost of Funds for 12 months ended on 31<sup>st</sup> March, 2010 (2009-10).
3. Average Cost of Deposits for the quarter ended 31<sup>st</sup> March, 2010 (4<sup>th</sup> Quarter 09-10)
4. Average Cost of Funds for the quarter ended 31<sup>st</sup> March, 2010 (4<sup>th</sup> Quarter 09-10)

### Base Rate is computed taking into account the following

- Positive Spread on account of SB and Current account deposits
  - Negative carry for CRR and SLR
- a) Average Yield on Investments for the 12 months ended on 31<sup>st</sup> March, 2010
  - b) 364 Day Treasury Bills Rate
  - c) Average Yield on SLR Investments for the 12 months ended on 31<sup>st</sup>

**“The base rate system gives complete freedom to banks in their loan pricing decisions while ensuring transparency. Banks have unlimited access to public deposits and privileged access to the liquidity facility of the Reserve Bank. Hence there is a greater need for transparency and responsible lending practices for public purposes.”**

March, 2010

d) Average Yield on SLR Investments for the last quarter ended on 31<sup>st</sup> March, 2010

- Unallocatable overhead cost
- Average Return on Net worth

The illustrative methodology given by Reserve Bank of India while computing the Base Rate is followed. However, as regards average Return on Net Worth, it is taken the average for the last 3 years, to ensure stability.

To arrive at the negative carry for CRR/SLR, three different methods are considered which are as under:

- i) 364 days Treasury Bill Rate as per the illustration methodology annexed to the RBI circular.
- ii) Average Yield on SLR for 12 months is taken in the case of benchmark related to Average Cost of Deposits/Funds for the whole year 2009-10 and Average Yield on SLR for the fourth quarter of 2009-10 is taken in the case of benchmark related to the Average Cost of Deposits/Funds for the 4<sup>th</sup> Quarter of 2009-10.
- iii) Average Yield on Investments for 12 months is taken in the case of benchmark related to Average Cost of Deposits/Funds for the whole year 2009-10 and Average Yield on Investments for the 4<sup>th</sup> quarter of 2009-10 is taken in the case of benchmark related to the Average Cost of Deposits/Funds for the fourth Quarter of 2009-10.

Detailed workings in this regard are furnished here below.

Base Rate Calculations					
Return on SLR is proxied to 364 Days Treasury Bill Rate		Avg. Cost of Deposits for the immediately preceding 12 months ended on 31 <sup>st</sup> March 2010	Avg. Cost of Funds for the immediately preceding 12 months ended on 31 <sup>st</sup> March 2010	Avg. Cost of Deposits for the immediately preceding 3 months ended on 31 <sup>st</sup> March 2010	Avg. Cost of Funds for the immediately preceding 3 months ended on 31 <sup>st</sup> March 2010
A	Benchmark Rate	5.95%	5.54%	5.40%	5.01%
B	<b>Negative Carry on SLR / CRR</b>	<b>0.69%</b>	<b>0.51%</b>	<b>0.45%</b>	<b>0.27%</b>
C	Unallocatable Overhead Cost	0.66%	0.66%	0.66%	0.66%
D	Average Return on Net worth	1.68%	1.68%	1.68%	1.68%
E	<b>Base Rate [ ( A ) + ( B ) + ( C ) + ( D ) ]</b>	8.98%	8.39%	8.19%	7.62%
<b>Base Rate ( rounded off to the nearest multiples of 25)</b>		<b>9.00%</b>	<b>8.50%</b>	<b>8.25%</b>	<b>7.75%</b>
Return on SLR is proxied to Average yield on SLR for 12 months / latest quarter corresponding to Bench Mark					
A	Benchmark Rate	5.95%	5.54%	5.40%	5.01%
B	<b>Negative Carry on SLR / CRR</b>	<b>0.05%</b>	<b>0.00%</b>	<b>0.00%</b>	<b>0.00%</b>
C	Unallocatable Overhead Cost	0.66%	0.66%	0.66%	0.66%
D	Average Return on Net worth	1.68%	1.68%	1.68%	1.68%
E	<b>Base Rate [ ( A ) + ( B ) + ( C ) + ( D ) ]</b>	8.34%	7.88%	7.74%	7.35%
<b>Base Rate (rounded off to the nearest multiples of 25)</b>		<b>8.25%</b>	<b>8.00%</b>	<b>7.75%</b>	<b>7.25%</b>
Return on SLR is proxied to Average yield on Investments for 12 months / latest quarter corresponding to Bench Mark					
A	Benchmark Rate	5.95%	5.54%	5.40%	5.01%
B	<b>Negative Carry on SLR / CRR</b>	<b>0.23%</b>	<b>0.04%</b>	<b>0.00%</b>	<b>0.00%</b>
C	Unallocatable Overhead Cost	0.66%	0.66%	0.66%	0.66%
D	Average Return on Net worth	1.68%	1.68%	1.68%	1.68%
E	<b>Base Rate [ ( A ) + ( B ) + ( C ) + ( D ) ]</b>				
<b>Base Rate ( rounded off to the nearest multiples of 25)</b>		<b>8.50%</b>	<b>8.00%</b>	<b>7.75%</b>	<b>7.25%</b>

**“Deregulation of lending rates will promote financial inclusion with greater credit flow to agriculture and small business. This, together with other specific measures taken by the Reserve Bank for financial inclusion, will draw borrowers away from the informal financial sector to the formal financial sector and thus, facilitate credit penetration.”**

As per RBI guidelines, the banks may determine their actual lending rates on loans and advances with reference to the Base Rate and by including such other customer specific charges as considered appropriate.

The Base Rate shall apply to all loans sanctioned on or after 1<sup>st</sup> July, 2010.

Base Rate shall not apply to

1. DRI advances
2. Loans to Staff

3. Loans against our bank deposits

### Impact Analysis of Base Rate

1. A perusal of ultimate lending rates indicates that the small borrowers and MSME borrowers stand to benefit with introduction of base rate.
2. For Corporate Clients there could be a 100-150 basis point rise in the cost of borrowing eventually.

“Implementation of any such regulatory initiative could impact the profitability of mortgage lenders severely. According to the report, over 90 per cent of all mortgage loans are estimated to be at floating rates of interest. Therefore, the average yield on advances on the overall book should be closely linked to the interest rates offered to new borrowers. However, this is not the case, as the current system of Prime Lending Rate is non-transparent and somewhat inflexible in a scenario of declining interest rates. Therefore, an existing borrower with a clean track record and substantial equity build-up may end up paying a higher rate of interest (by 1.5-2 per cent) than a new borrower.”

3. Implementation of the new Base Rate system to calculate lending rates could bring in more transparency for new home loan borrowers.

But interest rates for old borrowers may still not get aligned to those offered to new borrowers.

4. Implementation of any such regulatory initiative could impact the profitability of mortgage lenders severely. According to the report, over 90 per cent of all mortgage loans are estimated to be at floating rates of interest. Therefore, the average yield on advances on the overall book should be closely linked to the interest rates offered to new borrowers. However, this is not the case, as the current system of Prime Lending Rate is non-transparent and somewhat inflexible in a scenario of declining interest rates. Therefore, an existing borrower with a clean track record and substantial

“Public sector banks will have an edge over private sector banks in offering a more competitive base rate as they have a larger deposit base, which gives them access to cheaper sources of stable financing. Public sector banks have access to the Government/ treasury funds and thereby their cost of fund works out to be lower than private sector banks.”

equity build-up may end up paying a higher rate of interest (by 1.5-2 per cent) than a new borrower.

5. Borrowers in the retail, priority and small and medium enterprise (SME) segments will most likely get loans at lower rates.

6. The introduction of the new lending regime would make raising money through banks costlier for highly

PRIVATE FINANCIAL TOOLS  
 FUNDS LOAN MUTUAL  
 ACCOUNT CREDIT CARD  
 MORTGAGE INSURANCE  
**BANKING**  
 PERSONAL BUSINESS  
 MANAGEMENT MONEY  
 SERVICE FINANCIAL  
 INVESTMENT



rated companies, the survey said they (corporates) might resort to other low-cost financing options such as commercial paper, qualified institutional placement, external commercial borrowing, and so on, and this, in turn, could result in lower credit offtake from banks.

7. Unlike the BPLR regime, whereby banks predominantly lent below the benchmark rate to India Inc, leading to distortion in monetary transmission, under the Base Rate regime, banks will not be able to lend below the benchmark.
8. There was high probability of a 'slight' upward bias as far as lending rates were concerned. If the monetary policy indicates further tightening, then there could be a squeeze on liquidity, which will have an upward bias on base rate.
9. While an upward pressure on interest rates for corporates, that have so far availed loans at ultra-

low rates, is imminent, the retail, priority and SME products will most likely be able to get loans at a relatively lower rate.

10. Borrowers with better credit rating will be able to negotiate a good deal for themselves.
11. Public sector banks will have an edge over private sector banks in offering a more competitive base rate as they have a larger deposit base, which gives them access to cheaper sources of stable financing. Public sector banks have access to the Government/ treasury funds and thereby their cost of fund works out to be lower than private sector banks.

### Conclusions

- The introduction of the base rate system along side removal of interest rate ceiling on small loans and freeing of rupee export credit interest rate brings to fruition over two decades of efforts to deregulate the lending rates of banks. This is expected to enhance the allocative efficiency of the financial intermediation process by banks.
- Deregulation of lending rates will promote financial inclusion with greater credit flow to agriculture and small business. This, together with other specific measures taken by the Reserve Bank for financial inclusion, will draw borrowers away from the informal financial sector

to the formal financial sector and thus, facilitate credit penetration.

- The base rate system gives complete freedom to banks in their loan pricing decisions while ensuring transparency. Banks have unlimited access to public deposits and privileged access to the liquidity facility of the Reserve Bank. Hence there is a greater need for transparency and responsible lending practices for public purposes.
- The base rates of banks will mirror their relative efficiency and cost structure. While lending rates tend to be sticky, it is expected that the base rate system will show greater flexibility and strengthen both the interest rate and credit channels of monetary transmission.
- The new system gives the freedom to banks to choose other market related benchmarks besides their base rates for pricing floating rate products. This could promote development of market benchmarks. It could also deepen the money market to facilitate short-term liquidity management by banks.
- There is some apprehension that the base rate system may raise the effective cost of borrowings. This is unlikely because corporates have access to multiple sources of funds and hence the effective borrowing rates will be determined by market competition. ■

“There is some apprehension that the base rate system may raise the effective cost of borrowings. This is unlikely because corporates have access to multiple sources of funds and hence the effective borrowing rates will be determined by market competition.”



rents them out to the very same users, then it would not be a case of a real estate business and would be treated as if it were a real estate development.

The term NRI would cover a Person of Indian Origin also. Thus, the following persons resident outside India are eligible for investment under this route:

- (a) Any person who at any time, held an Indian Passport
- (b) Any person who or either of whose parents/grand parents was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955
- (c) Any person who is a spouse of an Indian citizen or of any of the persons mentioned in (a) or (b) above.

FDI by NRIs under this route is allowed up to 100 per cent in a company engaged in the Housing and Real Estate activities. These include the following activities:

- (a) Development of serviced plots and construction of built-up residential premises
- (b) Investment in real estate covering construction of residential and commercial premises including business centres and offices
- (c) Development of townships
- (d) City and regional level urban infrastructure facilities, including both roads and bridges
- (e) Investment in manufacture of building materials
- (f) Investment in participatory ventures in (a) to (c) above
- (g) Investment in Housing Finance Institutions

This route is available only for NRIs and not for any other person resident outside India.

### FDI by Any Person Resident Outside India

Any person resident outside India, whether he is a foreign citizen, foreign company, foreign LLP, LLC, private

equity fund, etc., is eligible to make a Foreign Direct Investment in an Indian company engaged in real estate under the automatic route. However, the condition is that such FDI must comply with the conditions laid down under the Circular 1/2010 (or the erstwhile Press Note 2/2005) issued by the FIPB. FDI is not allowed for Real Estate Business or for trading in Transferable Development Rights.

FDI up to 100 per cent is allowed under the automatic route in townships, housing, built-up infrastructure and construction-development projects (which would include, but not be restricted to, housing, commercial premises, educational institutions, recreational facilities, city and regional level infrastructure).

#### Conditions under Circular 1/2010

Circular 1/2010 or the erstwhile Press Note 2/2005 and its conditions have been the subject matter of great debate. Let us analyse some of the contentious issues which this Note has thrown up.

**Minimum Area** – The minimum area to be developed under each project is:

- (a) In case of development of serviced housing plots, a minimum land area of 10 hectares (i.e., 1 lakh sq. mts. or 10.76 lakh sq. ft. or 25 acres or 1.2 lakh sq. yards)
- (b) In case of construction-development projects, a minimum built up area of 50,000 sq. mts. (i.e., 5.38 lakh sq. ft)
- (c) In case of a combination project, anyone of the above two conditions would suffice

The issue which arises here is that what is the meaning of the term 'built up area'? The Circular does not define this term. S.80-IB(10) of the Income-tax Act has defined the term to mean the inner measurements of the residential units at the floor level including projections and balconies as increased by the

**“ Any person resident outside India, whether he is a foreign citizen, foreign company, foreign LLP, LLC, private equity fund, etc., is eligible to make a Foreign Direct Investment in an Indian company engaged in real estate under the automatic route. However, the condition is that such FDI must comply with the conditions laid down under the Circular 1/2010 (or the erstwhile Press Note 2/2005) issued by the FIPB. FDI is not allowed for Real Estate Business or for trading in Transferable Development Rights. ”**

thickness of the walls but does not include the common areas shared with other units.

Would basement car parking/club house/recreational area /other facilities be covered within the definition? One of the conditions of the Note is that the project shall conform to the norms and standards, including land use requirements and provision of community amenities and common facilities, as laid down in the applicable building control regulations, by-laws, rules, and other regulations of the State Government/Municipal/Local Body concerned. Hence, it stands to reason that the definition of this term should be understood in the context of which it is approved by the Municipal /Local Authority which sanctions the building plans. E.g., land development in the city of Mumbai is regulated by the Development Control Regulations of 1991 and the Mumbai Municipal Corporation Act, 1881.

**Minimum Capitalisation** - US\$ 10 million for wholly owned subsidiaries and US\$ 5 million for joint ventures with Indian partners. The funds would have to be brought in within six months of commencement of business of the Company. Certain issues which arise in this respect are would only equity

shares be counted for the minimum capitalisation? Would preference shares/compulsorily convertible debentures be counted? What would be the position if the shares are issued at a premium? Further, is a minimum threshold investment by the Indian partner required for an entity to be treated as a joint venture? The FIPB has consistently refused any request for the relaxation of the minimum capitalisation norms. There has been one case where it accepted the request since the foreign investor was unable to bring in the balance funds for the construction activities and hence, the company wanted to disband the project and repatriate the money received.

What is meant by the commencement of the business? Is the six months' period counted from the time when the company acquires the land or is it from the time when it obtains the permission to commence construction? Various decisions under the Income-tax Act have taken different views as to when a business can be said to have commenced. For instance, in *Sarabhai Sons 90 ITR 318 (Guj)*, it was held that the new business could not be said to be ready to discharge the function for which it was established viz., manufacture of certain product unless the required machinery for manufacturing was installed. In the case of *Ralliwolf Ltd 121 ITR 262(Bom)*,

**“ Can a company which has FDI in an FDI compliant project make a downstream investment in a company which has a project which is not FDI compliant? As per the provisions of the erstwhile Press Note 2/2009, if the investor Indian company is a company owned and controlled by resident Indian citizens, then the downstream investment would be treated as domestic investment. ”**

the business of the assessee was in the nature of both manufacturing and trading activities of similar type of products. It was held by the Court that even when a mere purchase has taken place of goods which could either be used for manufacture or for sale, the assessee can be said to have commenced business. Based on these decisions can a view be taken that business commences from the time from which the stock-in-trade, i.e., land is acquired by the company.

**Lock-in** – The original investment cannot be repatriated before a period of three years from completion of minimum capitalisation. Does this lock-in apply only to the minimum capital or does it apply to the entire investment? Further, if the investment is made in tranches, does this apply to the entire investment or only to the first tranche of the investment?

**Completion** - At least 50 per cent of the project must be developed within a period of five years from the date of obtaining all statutory clearances. The investor is not permitted to sell undeveloped plots. The term “all statutory clearances” is very wide in its coverage. Does this mean that each and every permission required for developing a property is to be obtained and five years is to be counted from the last date such permissions? For instance, there are several buildings in Mumbai which have not obtained an Occupancy Certificate (OC) from the Municipal Corporation even though each and every flat in the building may have been sold. Would these be treated as projects which have not yet obtained all statutory clearances?

In case the company has FDI and non-FDI compliant projects, then it cannot get FDI. In the case of *M/s Vatika Limited* the FIPB did not permit infusion of FDI as some of the projects of the company were non-FDI compliant. It may also be noted that the Indian company cannot raise FDI

for acquiring agricultural lands with an intention of subsequently, making them Non Agricultural (NA) Lands. Recently, a large real estate developer was questioned by the Enforcement Directorate / RBI for using FDI money for buying agricultural lands.

It may be noted that Circular 1/2010 (erstwhile Press Note 2/2005) does not apply to FDI by an NRI. Further, it does not apply to FDI in a company engaged in development of hotels, hospitals, SEZs, IT parks, etc. The conditions for the same are explained below. The FIPB has clarified in the case of *M/s Supreme Infrastructure India Limited*, that there is no need of compliance with Press Note 2 of 2005 where the applicant is not a developer but only a service provider to developer.

#### **Instruments**

One of the questions to be addressed is the instrument which would be used for the investment. The instruments which are often considered for FDI:

- (a) Equity Shares
- (b) Compulsorily Convertible Preference Shares – Redeemable/Optionally Convertible Preference Shares are treated as External Commercial Borrowings and hence, not allowed. The maximum dividend permissible on CCPS is the Prime Lending Rate of the State Bank of India + 3 per cent.
- (c) Compulsorily Convertible Debentures–NonConvertible/Optionally Convertible Debentures are External Commercial Borrowings and hence, not allowed.
- (d) Warrants – However, this requires the prior permission of the FIPB. It may be noted that the second highest cases (10 in number) of compounding before the FIPB in 2009 pertained to the issue of warrants without the permission of FIPB. For instance, *M/s. Era Infra Engineering Ltd* applied to the FIPB for compounding for issue of warrants without approval.

However, Circular 1/2010 has now specified that such instruments cannot be issued to any non resident.

- (e) Partly Paid-up shares – This also requires the prior FIPB approval. E.g., M/s. Wire and Wireless India Ltd has obtained the prior FIPB permission for issuing partly paid-up shares to foreign persons. However, Circular 1/2010 has now specified that such instruments cannot be issued to any non resident.
- (f) Non-Voting Shares – This is permissible under the automatic route. However, if the issue is by a public company, then it needs to comply with the conditions specified u/s. 86 of the Companies Act, 1956.

In addition to the FEMA implications, one also needs to consider other factors while selecting an instrument, such as, stamp duty on issue, ease of capital repatriation, tax treatment of income and gains from the instrument, etc.

**Jurisdiction**

An important question to be addressed by a foreign investor desirous of investing in a real estate project is the jurisdiction from which he would invest from. Most FDIs are structured through tax havens / favourable tax jurisdictions, such as, Mauritius, Cyprus, Singapore, etc., because of the concessional tax treatment.

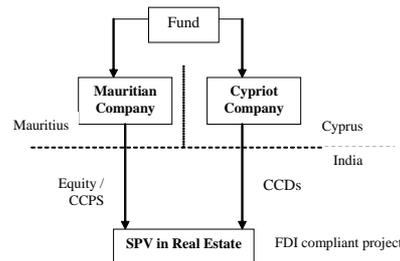
The jurisdiction also decides the instrument to an extent. Let us consider the tax treatment of an investor who is considering Mauritius, Cyprus or Singapore as a jurisdiction. Under India’s Double Tax Avoidance Agreement with each of these countries, capital gains tax is payable in the country of the residence of the Investor. None of these jurisdictions levy a capital gains tax. Hence, as regards, Equity or CCPS or CCDs, the investor would be tax neutral as to the capital gains aspect.

In the case of CCPS, the Indian company paying dividend would pay Dividend Distribution Tax. Hence, the investor would be tax neutral as to the income aspect on CCPS.

However, the position is different when one considers CCDs. The tax treatment of income and gains on CCDs in India under the DTAA of each of the 3 jurisdictions as well as under its domestic law is given below:

Jurisdiction	Tax on Interest Income on CCDs– Higher of Local Tax or Tax under DTAA (after credit for taxes in India)	Capital Gains Tax on Sale of CCDs in the country of the Investor
Singapore	17%	Nil
Mauritius	20%	Nil
Cyprus	10%	Nil

Thus, the above table shows that Cyprus is a more favoured destination when one structures investments via the CCD Route. Several offshore real funds use a combination of Equity/CCPS via Mauritius and CCDs via Cyprus as depicted in the following diagram:



**Exit Options**

The foreign investor is, normally, given an exit option from the company by one or more of the following modes:

- (a) IPO or Initial Public Offer of the shares of the company. Subsequently, the foreign investor may sell its shares on the floor of the exchange after the applicable lock-in period under SEBI (Issue and Disclosure of Capital Requirements) Regulations, 2009. However, an IPO may not be suitable if the company is a single

project SPV.

- (b) Buyback of the shares of the investor by the Company. A buyback is on the automatic route. However, the price cannot exceed the lower of two independent valuation reports. No valuation methodology has been prescribed for the same. Certain documentation (Form FC-TRS) and reporting requirements also need to be complied with by the parties.
- (c) Buyout of the foreign investor by the Indian partners, also known as a Put and Call Option by the Indian partners. A buyout is also on the automatic route of the RBI. The requirements are the same as explained above in the case of a buyback. The RBI has clarified that a Fixed Price Put and Call Option, without regard to the pricing guidelines, cannot be given to the foreign partner.
- (d) Voluntary Liquidation of the SPV – the SPV may be liquidated and the funds lying in the SPV may be distributed to the shareholders.

An exit mechanism should be structured having due regard to the Indian tax laws, applicable DTAA provisions, FEMA/Company Law provisions, etc.

**Downstream Investment**

Can a company which has FDI in an FDI

**Under Schedule 2 to the Foreign Exchange Management**

**(Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, a Foreign Institutional Investor (FII) can purchase the shares of an Indian listed company under the Portfolio Investment Scheme (PIS). PIS is not permitted in the shares of a company which is in the real estate business or construction of farm houses or trading in TDRs.**

compliant project make a downstream investment in a company which has a project which is not FDI compliant? As per the provisions of the erstwhile Press Note 2/2009, if the investor Indian company is a company owned and controlled by resident Indian citizens, then the downstream investment would be treated as domestic investment. The criteria for considering whether a company is owned and controlled by resident Indian citizens, is that the resident Indian citizens must own more than 50 per cent of the equity capital of that company and must have the power to appoint a majority of the directors on the board of that company. Thus, investment by such a company in another company is treated as if it is a domestic investment and not an indirect foreign investment. Accordingly, it is possible for such a company to invest in a non-FDI compliant project.

### FDI in SEZs, Hotels, IT Parks

FDI is allowed in an Indian company for development of Special Economic Zones, Hotels, Hospitals, IT Parks, etc. FDI under these projects is not subject to the restrictions imposed under Press Note 2/2005.

100 per cent FDI under the automatic route is permissible under

the projects mentioned below and the conditions for the same are also briefly explained below:

No.	Type of Project	Conditions for FDI
(a)	Hotels	The term hotels include restaurants, beach resorts, and other tourist complexes providing accommodation and/or catering and food facilities to tourists.
(b)	Hospitals	No conditions
(c)	SEZs / Free Trade Zones	<ul style="list-style-type: none"> <li>Conditions under the SEZ Act, 2005 and the SEZ Rules 2006 must be complied with</li> <li>To avail of a tax benefit u/s. 80-IAB of the Income-tax Act, 1961 the SEZ must comply with the conditions specified therein</li> </ul>
(d)	Software / IT Parks	<ul style="list-style-type: none"> <li>Press Note 2/2005 not applicable</li> <li>The Park should comprise a minimum of 10 units and no single unit shall occupy more than 50% of the allocable area</li> <li>Minimum percentage of the area to be allocated for industrial activity shall not be less than 66% of the total allocable area.</li> </ul>

premises, educational institutions, recreational facilities, city and regional level infrastructure, townships. Thus, a company which is in the land development business would be eligible for receiving PIS.

Under the PIS, FIIs can invest in a listed company which has FDI compliant as well as FDI non compliant projects. The only condition is that the total holding by each FII cannot exceed 10 per cent and the total holding of all FIIs, under the PIS may be raised up to the Sectoral cap, if any. Since there is no Sectoral cap for the real estate sector, in theory, the holding can go up to 100 per cent. For instance, the shareholding pattern of a few large listed real estate companies reveals the following FII holding as on 31<sup>st</sup> December, 2009:

Company	% FII holding
Ackruti City Ltd	6.00
DLF Universal Ltd	15.23
Mahindra Lifespace Developers Ltd	18.13
Phoenix Mills Ltd	19.41
Unitech Ltd	33.47
Indiabulls Real Estate Ltd	69.74

Source: [www.bseindia.com](http://www.bseindia.com)

Under this Scheme, FIIs can also acquire shares of real estate company making an IPO. The conditions of the erstwhile Press Note 2/2005 are not applicable to Portfolio Investment made by FIIs, including that made under the IPO of the Company. However, FII investments in any pre-IPO placement are treated on par with FDI and would be subject to all conditions of the erstwhile Press Note 2/2005.

Under Schedule 3 to the above-mentioned Regulations, NRIs can purchase the shares of an Indian listed company under the Portfolio Investment Scheme. There are no restrictions as to the nature of activities of the company or the sectors in which the investment can be made. NRIs can invest, under the PIS, in a listed company which has FDI compliant as well as FDI non compliant projects. The only condition

**“ECBs of External Commercial Borrowings are foreign loans and are prohibited for use in the real estate business. They are allowed only for a very limited use. ECBs may take the form of loans, Non Convertible Debentures, Redeemable Preference Shares, Optionally Convertible Debentures / Preference Shares. Foreign Currency Convertible Bonds or FCCBs are also ECBs and hence, need to comply with the end-use and other restrictions applicable to ECBs.”**

### Portfolio Investment in Listed Real Estate Companies

Under Schedule 2 to the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, a Foreign Institutional Investor (FII) can purchase the shares of an Indian listed company under the Portfolio Investment Scheme (PIS).

PIS is not permitted in the shares of a company which is in the real estate business or construction of farm houses or trading in TDRs. “Real estate business” does not include construction of housing / commercial



is that the total holding by each NRI cannot exceed 5 per cent and the total holding of all NRIs under the PIs may be raised up to 24 per cent

### ECBs in Real Estate Sector

ECBs of External Commercial Borrowings are foreign loans and are prohibited for use in the real estate business. They are allowed only for a very limited use. ECBs may take the form of loans, Non Convertible Debentures, Redeemable Preference Shares, Optionally Convertible Debentures/Preference Shares. Foreign Currency Convertible Bonds or FCCBs are also ECBs and hence, need to comply with the end-use and other restrictions applicable to ECBs.

Companies engaged in the development of integrated township, as defined in Press Note 3 (2002 Series) dated 4<sup>th</sup> January, 2002, issued by the Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce & Industry, Government of India are permitted to avail of ECB, under the approval route, until December 31, 2010. However, ECBs are not permissible for development of integrated township and commercial real estate within an SEZ.

Integrated township, as defined above, includes housing, commercial

premises, hotels, resorts, city and regional level urban infrastructure facilities such as roads and bridges, mass rapid transit systems and manufacture of building materials. Development of land and providing allied infrastructure forms an integrated part of township's development. The minimum area to be developed should be 100 acres for which norms and standards are to be followed as per local bye-laws/rules. In the absence of such bye-laws/rules, a *minimum of 2,000 dwelling units for about 10,000 population* will need to be developed.

Several other conditions were specified in that Press Note for the development of an integrated township. It is a moot point whether these also need to be complied for availing of ECBs. Some of these additional

**There are myriad issues and complexities involved in structuring foreign investment in the real estate sector. Considering that real estate is one of the prime sectors of the Indian economy which attracts FDI, it would be desirable that the Government/RBI clarifies all the issues raised in this article in greater depth.**

conditions include the following:

- (a) Land with assembled area for peripheral services such as police stations, milk booths will be handed over free of cost to the Government /local authority /agency as the case may be.
- (b) The Developer will retain the lands for community services such as (i) schools (ii) shopping complex (iii) community centres (iv) ration shop (v) hospital/dispensary. These services will be developed by developer himself and shall be made operational before the houses are occupied.
- (c) The developer, after properly developing playgrounds, park, will make it available to the local authorities free of cost.
- (d) The developer will ensure the norms and standards as applicable under local laws/rules.

### Epilogue

From the above discussion it would be evident that there are myriad issues and complexities involved in structuring foreign investment in the real estate sector. Considering that real estate is one of the prime sectors of the Indian economy which attracts FDI, it would be desirable that the Government/RBI clarifies these issues in greater depth. ■

### ■ ■ ■ Noose Tightens on Tax Haven Funds

The government is hard on the trail of money allegedly stashed away in secret bank accounts in tax havens. Finance minister Pranab Mukherjee told delegates recently at the Hindustan Times Leadership Summit that India has written to 78 countries to amend existing tax treaties, insisting on their adding on Article 26 of the Model Tax Convention of the Organisation for Economic Cooperation and Development (OECD). "We are renegotiating the double taxation avoidance agreements (DTAAs) with 78 countries," Mukherjee said. He said the government has also finalised tax information exchange agreements (TIEAs) with eight countries. "Once this is institutionalised, we can analyse how much the quantum (of black money is stashed away in secret accounts) would be," he added. "I would not know the actual estimation of black money or unaccounted money stored in other countries," he said. Global Financial Integrity, a Washington-based research group, says India is losing about US\$ 16 billion (₹72,496 crore) a year to outflows related to tax avoidance by wealthy individuals and companies, besides money lost to corruption. It has estimated that India has been drained of US\$ 462 billion (over ₹20 lakh crore) between 1948 and 2008 at current prices. This is nearly 40 per cent of India's gross domestic product. In August, India and Switzerland inked an amended tax pact.

(Source: <http://www.hindustantimes.com/>)

### ■ ■ ■ Survey: Economic Optimism Rose Significantly Among Indians in 2010

After being hit by the global recession, economic optimism rose significantly among Indians in 2010, so did their perception about their own standard of living, the latest Gallup poll said. Between 2007 and 2009, the percentage of Indians who believed their local economic conditions were getting better dropped from 52 per cent to 37 per cent, but rebounded to 45 per cent in 2010. The Gallup said Indians' perceptions about their own standard of living follow a similar pattern. This year, 44 per cent of Indians surveyed by Gallup said their standard of living is improving, up from 32 per cent last year. This year's figure is identical to the findings of July 2008, before the severity of the global downturn was fully apparent, it said. This rising optimism comes in tandem with the country regaining its high growth trajectory after the GDP increase rate saw a downturn in the recessionary years. India's prosperity, however, is spread unevenly. Large income disparities exist between urban and rural areas and across regions, Gallup said, adding that regional results indicate the recession's effects were more severe for some Indians than others.

(Source: <http://www.business-standard.com/>)

### ■ ■ ■ GST Regime Will Not Be Implemented From April 1, 2011: Finance Ministry

The Finance Ministry has admitted that the proposed Goods and Services Tax (GST) regime will not be implemented from 1<sup>st</sup> April, 2011 and said that no timeframe for the introduction of the new indirect tax system has been

set yet. Revenue secretary Sunil Mitra said it would be difficult to roll out GST without constitutional amendments, contrary to the suggestion made by some states. These amendments require time, Mitra said, adding that the Finance Ministry has not decided on new timeframe for introducing GST. Originally scheduled to be implemented from the beginning of this fiscal, the GST regime will subsume excise duty, service tax at the Centre's end and VAT on states front, besides some local levies surcharges and cesses. However, differences between states and the Centre over the structure of the new tax regime has led to delays in its implementation. Now, even the revised deadline will be missed. Constitution amendments are required because, under the current mechanism, the Centre cannot impose tax beyond manufacturing, and states cannot levy service tax.

(Source: <http://economictimes.indiatimes.com/>)

### ■ ■ ■ Indian Social Auditing Schemes Makes World Attention

If Brazil has its Bolsa Familia, and Mexico its Progresas schemes for alleviating poverty that have caught the fancy of international organisations something that India has done recently is making news internationally. India's system of social audits, that is, independent but local auditing of social programmes to fight poverty, like the Mahatma Gandhi National Rural Employment Guarantee Act (MNREGA), is attracting world attention. A 42-member delegation from 33 countries was in Rajasthan recently to study the unique way of auditing schemes through direct participation of people. The delegates represented countries as diverse as Ukraine, Saudi Arabia, Costa Rica and the Philippines. This programme is part of the international audit training conducted by the CAGs International Training Institute. Social audits like the hugely successful model in Andhra Pradesh, which has set up an independent and autonomous Society for Social Audit, Accountability and Transparency (SSAAT) to help ensure proper working of the MNREGA, have excited people in various countries, especially Africa. The problems of inherent corruption trouble countries in the third world.

(Source: <http://www.financialexpress.com/>)

### ■ ■ ■ Companies Can Use Legal Financial Structures to Save Tax: ITAT

In a ruling that will have a bearing on foreign companies operating in India, a Mumbai-based tax tribunal has held that tax-planning carried out within the provisions of law cannot be construed as a structured transaction carried out only for the purpose of evasion of taxes, even if the transaction helps the taxpaying company save taxes. In its November 10 order, a division bench of the Income-Tax Appellate Tribunal (ITAT), Mumbai, comprising NV Vasudevan and Pramod Kumar, held that the finance structure used by the taxpayer had to be specifically prohibited for it to be illegal. As long as the finance structure adopted by the taxpayer is not specifically prohibited by the applicable tax treaty provisions and as long as there are no specific anti-abuse provisions, the effect of the finance structure cannot be ignored. The

ITAT order was on an appeal filed by the Belgium company, Besix Kier Dabhol SA.

(Source: <http://beta.profit.ndtv.com/news>)

### ■ ■ ■ CDBT to Reopen Income-tax Returns of Entities

In one of the biggest tax recoveries to be made from blue-chip companies, the finance ministry has asked Central Board of Direct Taxes (CBDT) to reopen income-tax returns of entities found to have allegedly evaded taxes estimated at over ₹27,000 crore by wrongly claiming derivative losses. Sources said the huge tax liability has been estimated just for the two years of financial meltdown during 2008 and 2009. Derivative losses claimed by these entities were to the tune of ₹50,000 crore. Derivative trading is hedging of foreign exchange against any future risk.

(Source: <http://economictimes.indiatimes.com/>)

### ■ ■ ■ SC Gets Service Tax on Leasing Services

The Supreme Court has held that banks and financial institutions, including non-banking financial companies, are liable to pay service tax on transactions of leasing and hire purchase of moveable goods. While bringing such services within the service tax net, a Bench headed by Chief Justice SH Kapadia has upheld the levy of service tax on hire purchase and leasing transactions, notwithstanding that the same transactions are chargeable to the sales tax (now VAT). The decision in effect has upheld the double taxation of the same transaction of hire purchase and leasing to both the service tax as well as the VAT. These are services rendered to their customers, which comes within the meaning of the expression taxable services, the taxable event under the impugned law is the rendition of service. The impugned tax is not on material or sale. It is on activity/service rendered by the service provider to its customer, the court said. It further added that as far as the taxable value in case of financial leasing including equipment leasing and hire-purchase is concerned, the amount received as principal is not the consideration for services rendered. Such amount is credited to the capital account of the lessor/hire-purchase service provider. It is the interest/finance charge which is treated as income or revenue and which is credited to the revenue account. Such interest or finance charges together with the lease management fee/processing fee/documentation charges are treated as considerations for services rendered and accordingly they constitute the value of taxable services on which service tax is made payable, the judgement stated.

(Source: <http://www.financialexpress.com/>)

### ■ ■ ■ Custom Duty Not Liable to Pay by Aviation Firms for Imported Aircrafts

The Customs, Excise and Service Appellate Tribunal has ruled that companies that generate revenue from the use of the imported aircraft fall under the category of non-scheduled use and would, therefore, not be liable to pay customs duty. This ruling is likely to have a bearing on several cases that are either being investigated or are in litigation across the country. Importers will not have to pay customs duty on aircraft that are brought into the country for non scheduled

use, while private use operators will have to. The difference between non scheduled and private operations is that an aviation company charges clients for using non scheduled services, while private use means companies operating aircraft on their own expenses. Several companies that imported aircraft under the non schedule use permits, were initially exempted from having to pay customs duty, but were later served show cause notices for the same. The Customs Department issued the notices on the basis that the companies were using the aircraft for private purposes and were hence, not covered by any exemption under law.

(Source: <http://www.thehindubusinessline.com/>)

### ■ ■ ■ India to Relax Thresholds Regarding Mergers and Acquisitions

India proposes to relax thresholds regarding mergers and acquisitions (M&As) to be examined by the country's anti-trust body and mandate tighter deadlines for approvals, corporate affairs minister Salman Khursheed has said. We will soon be placing the amendments to the competition law in Parliament and hope that these are passed either in this session or the coming (budget) session, Khursheed said on the sidelines of a seminar recently. The minister added that provisions relating to prior approval of the Competition Commission of India (CCI) before any M&As above a certain size in terms of turnover or asset are executed will be notified soon. Norms relating to M&As, however, haven't yet been notified by the ministry largely because of extensive lobbying by industry, which says the process of clearing them will be time consuming and adversely affect the formation of combinations. The ministry has gone through the details of the competition law and has come to the conclusion that amendments to it (Competition Act) have to be industry friendly. There are some issues such as that of target entity where a minimum threshold needs to be set up and through the amendment we are addressing these issues, Khursheed said.

(Source: <http://www.cainindia.org>)

### ■ ■ ■ Merger and Acquisition Transactions Deal Tally Touches US\$ 42.76 bn

India Inc's shopping spree for October remained unabated with 46 merger and acquisition transactions (M&A) worth over US\$ 530 million taking place during the period and the year-to-date deal touching a whopping US\$ 42.76 billion in value terms. According to global consultancy firm Grant Thornton, there were 46 M&A deals worth US\$ 530 million in October 2010. So far this year corporate India has announced 546 M&A deals worth US\$ 42,759 million -- the highest in the last two years both in terms of value as well as number of deals. Outbound deals, wherein Indian companies acquired businesses outside India, were the flavour of the month as deals worth US\$ 390 million were struck in this space. The total value of inbound deals where foreign companies acquired Indian businesses amounted to US\$ 100 million. The total value of domestic deals in October 2010 was \$ 40 million.

(Source: <http://beta.profit.ndtv.com/news>)

# CAPITAL ADVANTAGE - Invest & Buy Mart

28<sup>th</sup>, 29<sup>th</sup>, 30<sup>th</sup> January, 2011 **Kolkata**

## Investment and Buying options for the discerning investor

An exhibition to showcase financial and investment products and services to Chartered Accountants, Corporate leaders and decision makers.

### WHY PARTICIPATE ?

Capital Advantage exhibition is organized as a part of the Corporate Forum, a platform where Chartered Accountants and Corporates from all over India would mark their presence. This would enable various organizations ranging from Banking, Insurance, Mutual Funds, Capital Markets, Real Estate, Information Technology products and services and other technological products to interact with Chartered Accountants, Investors, Finance Fraternity, and Corporate Decision Makers.

Chartered Accountants in today's Corporate scenario are the major financial advisors.

They have the complete understanding of the latest market trends as they have with them a thorough training blended with analytical approach and research of years.

Being at the event in the midst of all these key decision makers would provide your company with a big business opportunity as these Chartered Accountants play an important role in the decision making process with their vast knowledge of finance, accounting and market understanding.

### EXHIBITORS PROFILE

The participation is restricted to the first 50 companies from the following sectors

- **Banking**
- **Insurance**
- **Mutual Funds**
- **Capital Market**
- **Real Estate**
- **Information Technology**
- **Software development**

Invitations would be sent to over 1,50,000 Chartered Accountants in Industry or in practice as well as leading decision makers from the Corporate world.

### PARTICIPATION FEES

Rs. 2,00,000/- + 10.3% Service Tax for three days i.e. 28<sup>th</sup>, 29<sup>th</sup>, 30<sup>th</sup> January, 2011

### THE PACKAGE WOULD INCLUDE

- Fully furnished booth to each Company; 9 sq. mtr. (approx. 100 sq. ft.)
- Facilities: Fascia, table with 3 chairs, lighting, waste basket, plug point, carpet and lockable cabinet.
- Two Complimentary invitation to the ICAI Awards 2010 functions to be held in the evening of 30th January 2011.

**Payment Terms :** All payments accepted by way of Cheque / Demand Draft in favour of 'The Secretary, The Institute of Chartered Accountants of India' payable at New Delhi.

For details please visit : [www.icai.org/forum](http://www.icai.org/forum)



**Committee for Members in Industry**  
**The Institute of Chartered Accountants of India**  
(A statutory body established under an Act of Parliament)  
ICAI Bhawan, Indraprastha Marg, New Delhi - 110002  
[www.icai.org](http://www.icai.org), [www.cmii.icai.org](http://www.cmii.icai.org), <http://jobs4cas.icai.org>

### For Details Contact :

- **Chairman, CMII**  
Tel: +91 (11) 30110450/491 Email: [cmii@icai.org](mailto:cmii@icai.org)
- **Deputy Secretary, EIRC**  
Tel: +91 (33) 30211132 Email: [ircsecretary@icai.org](mailto:ircsecretary@icai.org) [ircsec@icai.org](mailto:ircsec@icai.org)
- **Secretary, CMII**  
Tel: (11) 30110545/491 Email: [cmii@icai.org](mailto:cmii@icai.org) [secretarycmii@icai.org](mailto:secretarycmii@icai.org)

# ICAI awARDS 2010

(For individual Chartered Accountant Members)



Invitations for Participation opens NOW!  
Last date for nomination  
Thursday, 23rd December 2010

Award Ceremony Sunday 30th January 2011  
at Science City, Kolkata

### Corporate CA Achievers' Acclaim

"The quality of a man's life is in direct proportion to his  
commitment to excellence, regardless of his chosen field of endeavor."

ICAI Awards would honour the exemplary work of Chartered Accountants in Industry by recognizing those who have demonstrated excellence in the professional life, personal life and are the role models for others in industry. These Corporate CA Achievers Acclaim Awards of ICAI also seek to acknowledge Chartered Accountants who have created value to their company's stakeholders on a sustainable basis.

For details please visit:  
[www.icai.org/forum](http://www.icai.org/forum)

For details contact:

Chairman, CMII

Tel: +91 (11) 3011 0555 / 0491 E-mail: [cmii@icai.org](mailto:cmii@icai.org)

Secretary, CMII

Tel: +91 (11) 3011 0491 E-mail: [cmii\\_events@icai.in](mailto:cmii_events@icai.in)

[secretarycmii@icai.in](mailto:secretarycmii@icai.in)

Deputy Secretary, EIRC

Tel: +91 (33) 3021 1132 E-mail: [nircerevents@icai.in](mailto:nircerevents@icai.in), [abasu@icai.in](mailto:abasu@icai.in)



Committee for Members in Industry,  
The Institute of Chartered Accountants of India

(A Statutory body established under an Act of Parliament)

ICAI Bhawan, P. O. Box No. 7100

Indraprastha Marg, New Delhi - 110 002

[www.icai.org](http://www.icai.org), [www.cmii.icai.org](http://www.cmii.icai.org), <http://jobs4cas.icai.org>

For Sponsorship opportunities please contact Secretary, CMII

### I ■ ■ ■ WCOA 2010 Discusses Present and Future of Accountancy Profession

18<sup>th</sup> World Congress of Accountants (WCOA) opened recently with the participation of 6,000 distinguished delegates from 134 countries, a record-breaking number. The Congress, which originated in 1904 and has been held regularly since 1977, was jointly organised by the Malaysian Institute of Accountants (MIA) and the International Federation of Accountants (IFAC). The Congress, themed "Accountants: Sustaining Value Creation," held in Malaysia for the first time, brought together 183 eminent speakers from over 40 countries. World-renowned speakers explored the issues related to key areas which affect the accountancy profession now and in the future and provided concrete solutions to overcome the challenges faced by the industry. The key issues that were discussed included accounting ethics, governance, standards, and development of the accounting profession. Issues such as International Financial Reporting Standards (IFRS) convergence will also be deliberated upon. The World Congress of Accountants, also dubbed "the Olympics of the accountancy profession," as the foremost international event for the accountancy profession. The Congress gathered influential communities, including leaders in accountancy, business, and regulation, to explore the latest issues and innovative ideas on a platform of international and regional interests.

Source: <http://press.ifac.org/news/>

### I ■ ■ ■ IASB Issues Additions to IFRS 9 for Financial Liability Accounting

The International Accounting Standards Board (IASB) recently issued requirements on the accounting for financial liabilities. These requirements will be added to IFRS 9 *Financial Instruments* to complete the classification and measurement phase of the IASB's project to replace IAS 39 *Financial Instruments: Recognition and Measurement*. They follow the IASB's November 2009 issue of IFRS 9, which prescribed the classification and measurement of financial assets. The new requirements address the problem of volatility in profit or loss (P&L) arising from an issuer choosing to measure its own debt at fair value. This is often referred to as the 'own credit' problem. In response to feedback received during its consultation process, the IASB decided to maintain the existing amortised cost measurement for most liabilities, limiting change to that required to address the own credit problem. With the new requirements, an entity choosing to measure a liability at fair value will present the portion of the change in its fair value due to changes in the entity's own credit risk in the other comprehensive income (OCI) section of the income statement, rather than within P&L. IFRS 9 applies to financial statements for annual periods beginning on or after 1<sup>st</sup> January, 2013. Entities are permitted to apply the new requirements in earlier periods, however, if they do, they must also apply the requirements in IFRS 9 that relate to financial assets. The second and third phases of IFRS 9 are concerned with accounting for the impairment of financial assets and hedge accounting. The IASB is aiming to complete those phases by 30<sup>th</sup> June, 2011, by adding the impairment and hedge accounting requirements to IFRS 9 and, therefore, replacing IAS 39 in its entirety.

Source: <http://www.ifrs.org/News>

### I ■ ■ ■ Interoperable Taxonomy Architecture Project Publishes Global Filing Manual for XBRL

The Interoperable Taxonomy Architecture (ITA) project published recently the first set of aligned XBRL (eXtensible Business Reporting Language) filing rules for global use, in the form of *The Global Filing Manual*. The manual contains a set of rules which provide guidance on the preparation, filing and validation of XBRL filings created using the IFRS Taxonomy, the EDINET (Electronic Disclosure for Investors' NETwork) Taxonomy or the U.S. GAAP Taxonomy. The ITA project is aiming at achieving the convergence of the XBRL frameworks (i.e. architectures) of the IFRS, EDINET and the U.S. GAAP Taxonomies. It is hoped that this architectural convergence will support the

analysis and comparison of financial data reported in XBRL format, by enabling software vendors to develop applications for IFRS, Japanese GAAP and U.S. GAAP reporting based on a single XBRL architecture. By creating a single set of filing rules for XBRL filings, *The Global Filing Manual* will further support this convergence, and thereby improve the provision and comparability of financial information for markets that currently represent major worldwide market capitalisation. It is also hoped that *The Global Filing Manual* will be adopted by other regulators and users of the IFRS Taxonomy and that the rules will be applied to all related XBRL filings.

Source: <http://www.ifrs.org/News/>

### I ■ ■ ■ IFRS Taxonomy 2010 Updated

The IFRS Foundation recently issued an interim release for the International Financial Reporting Standards (IFRS) Taxonomy 2010 reflecting *Disclosures - Transfers of Financial Assets* (Amendments to IFRS 7), which was published by the IASB in October 2010. The IFRS Taxonomy 2010 is a translation of IFRSs as issued at 1 January 2010 into XBRL (eXtensible Business Reporting Language). IFRS Taxonomy interim releases contain additional taxonomy items that reflect new IFRSs and improvements to IFRSs published by the IASB. From an XBRL technology perspective, these additional items are consistent with the XBRL architecture of the 2010 taxonomy. In 2010, the IFRS Foundation made the decision to issue interim releases to support the early adoption of IFRSs, by providing taxonomy items earlier for entities wishing to report electronically using the latest IFRSs. The issue of IFRS Taxonomy interim releases following the publication of new IFRSs also serves to further align the Foundation's XBRL activities with the activities of the IASB. Subsequent IFRSs and improvements that are issued in 2010 will not be published as interim releases. Instead, these standards and improvements will be incorporated into the development of the IFRS Taxonomy 2011. The public draft of the 2011 taxonomy is currently scheduled for release in January 2011.

Source: <http://www.ifrs.org/News/>

### I ■ ■ ■ IFRS Foundation Enhances Stakeholder Representation in IFRS XBRL Advisory Committees

The Trustees of the IFRS (International Financial Reporting Standards) Foundation announced recently the new membership of the Foundation's two IFRS XBRL (eXtensible Business Reporting Language) advisory committees—the XBRL Advisory Council (XAC) and the XBRL Quality Review Team (XQRT). The existing membership base of the two committees has been enhanced through increased representation from auditors and preparers, financial institutions, accounting bodies, standard-setters, regulators and software vendors from around the world. Inaugural members of the XAC and XQRT were first appointed in November 2007 and have provided vital stakeholder input to the Foundation's XBRL activities, and in particular to the development of the IFRS Taxonomy. A review of the membership of both committees was conducted in preparation for the expiry of members' terms on 31<sup>st</sup> December, 2010. The expiry of these inaugural terms presented the Foundation with an opportunity to enhance the composition of both committees by including a broader range of international stakeholders. The new membership of the XAC and XQRT is, therefore, intended to reflect changes in the financial reporting and XBRL landscape and the widening user base of IFRS and XBRL reporting around the world. The XAC provides strategic advice to the IFRS Foundation on the adoption and implementation of the IFRS Taxonomy throughout the world. The XQRT reviews developed taxonomies and provides input and practical recommendations on the usability of the IFRS Taxonomy from the perspectives both of XBRL technology and of financial reporting. Members of both committees are drawn from a broad geographical spread and from a range of professional backgrounds.

Source: <http://www.ifrs.org/News/XBRL>

### IAASB Addresses Compilation Engagements; Exposes Enhanced Standard

The International Auditing and Assurance Standards Board (IAASB) recently released for public exposure proposed International Standard on Related Services (ISRS) 4410, *Compilation Engagements*. The proposed standard is the first step in the IAASB's work to create robust standards for services that can be used by entities that are either not required or do not elect to be audited to meet their business reporting needs. Through a compilation engagement, practitioners can provide significant benefit by applying their expertise in accounting and financial reporting. This expertise is applied to assist the management of an entity in preparing and presenting historical financial information for use by the entity's internal or external stakeholders. Through the proposed ISRS 4410, as well as additional planned standards, the IAASB aims to address the growing international need for standards that support a range of services other than audit. The proposed ISRS 4410 will help practitioners around the world converge on the use of a globally accepted benchmark for performance of compilation engagements," noted IAASB Technical Director. Further, the International Standard on Related Services will help promote development of practice in jurisdictions that currently do not have national standards in this area, and also provide clarity for users about what is delivered in a compilation engagement.

Source: <http://press.ifac.org/news/>

### IFAC Addresses the Concept of the Public Interest

The International Federation of Accountants (IFAC), the global organisation for the accountancy profession, has released for public exposure *A Public Interest Framework for the Accountancy Profession* (IFAC Position Paper #4). In order to consider and address issues in the accountancy profession on a consistent and clearly articulated basis, IFAC has developed a principles-based framework of the public interest, which can be applied to standard-setting, governance processes, policy analysis, and regulatory issues. Although mainly designed for use by IFAC itself, it may also be useful to the accountancy profession as well as to policymakers, regulators, and business leaders. IFAC considers that the accountancy profession, in serving the public interest, should be evaluated against three criteria: 1) consideration of costs and benefits for society as a whole; 2) adherence to democratic principles and processes; and 3) respect for cultural and ethical diversity. These criteria enable IFAC to assess the extent to which any policy, action, process, or condition is in the public interest.

The primary purposes of this paper are to explain how we understand the public interest, and to be transparent about how we will use that understanding to shape our decisions and actions.

Source: <http://press.ifac.org/news/>

### CASB and IAASB Issue Joint Statement Regarding Convergence of International Standards

The Chinese Auditing Standards Board (CASB) and the International Auditing and Assurance Standards Board (IAASB) recently met to discuss convergence of international standards. China firmly supports the efforts of the International Federation of Accountants (IFAC) and the IAASB to promote international convergence of auditing standards. The fundamental principle of drafting the Chinese auditing standards is to continuously improve them, as well as achieve continuous and comprehensive convergence with international auditing standards in line with the development of Chinese market economy and the overall trend of economic globalisation and international convergence. In recent years, the IAASB has conducted the Clarity Project to enhance the clarity of International Standards on Auditing (ISAs), which involved the application of new drafting conventions to all ISAs and substantial revisions of a number of ISAs. In February 2009, the Clarity Project reached its completion with the approval of the Public Interest Oversight Board (PIOB). Auditors worldwide now have access to 36 newly updated and clarified ISAs and a clarified International

Standard on Quality Control (ISQC). In accordance with the principle of continuous and comprehensive convergence, the CASB has completed the revision of Chinese Standards of Audit (CSAs), and achieved full convergence with the clarified ISAs. The revised CSAs were officially released in early November 2010, and are effective for audits of financial statements for periods beginning on or after 1<sup>st</sup> January, 2011. During the process of international convergence, the CASB made limited additions it considered necessary and maintained some standards dealing with matters that are not specially covered in ISAs to reflect China's unique circumstances and business requirements, such as standards for the verification of capital contributions and communication between predecessor and successor auditors. The IAASB recognises that such additional requirements may be necessary and are acceptable where they do not conflict with ISAs.

Source: <http://press.ifac.org/news/>

### International Federation of Accountants Responds to Monitoring Group Report

The International Federation of Accountants (IFAC) commented recently on the Monitoring Group's *Review of the IFAC Reforms—Final Report*. In the report, the Monitoring Group states that virtually all of the changes called for by the IFAC Reforms have been implemented. It also acknowledges that the initial implementation of the IFAC Reforms has been a significant undertaking, and it recognises the numerous achievements with respect to their implementation. The concept of the IFAC Reforms originated in 2002, when IFAC and a group of six international financial institutions began a dialogue about the importance of high-quality audits of financial statements and the need to restore and enhance public confidence in financial reporting and auditing. The result of this dialogue was the IFAC Reforms. The IFAC Reforms changed the structure and processes for the auditing, ethics, and education standard-setting boards supported by IFAC. The Reforms called for the Monitoring Group to perform a five-year review of their implementation. In addition to recognising the successful breadth and depth of achievements of the IFAC Reforms, the Monitoring Group has identified a number of near-term actions for IFAC and the standard-setting boards it supports, focused on further enhancing diversity, transparency, and accountability.

Source: <http://press.ifac.org/news/>

### IASB and FASB Consult on Effective Dates for Convergence Accounting Standards

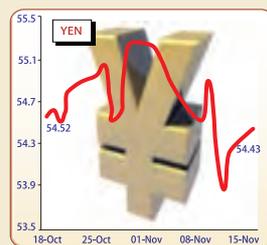
The International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) recently published documents seeking views on when new financial reporting standards resulting primarily from their work to improve and achieve convergence of International Financial Reporting Standards (IFRSs) and US generally accepted accounting principles (GAAP) should become effective. When finalising an IFRS, the IASB will identify a date from which entities will be required to start applying the new requirements (known as the effective date). This date is often 12 to 18 months after the date the IFRS is published, allowing time for entities to prepare for the change and for jurisdictions to implement the IFRS into their legal or regulatory regime. With a number of major projects planned to be completed in 2011, the boards are seeking views on whether or how to sequence effective dates in order to reduce the burden to interested parties. In deciding how to proceed, the IASB will consider the needs of jurisdictions already using IFRSs as well as those planning to do so. Feedback from the consultation will inform the boards as they jointly develop an implementation plan for those new standards that helps stakeholders to manage both the pace and cost of change. The projects covered by the request for views include the second and third phases of *Financial Instruments*, *Revenue from contracts with customers*, *Insurance contracts and Leases*. Comments are requested by 31<sup>st</sup> January, 2011.

Source: <http://www.ifrs.org/News/>

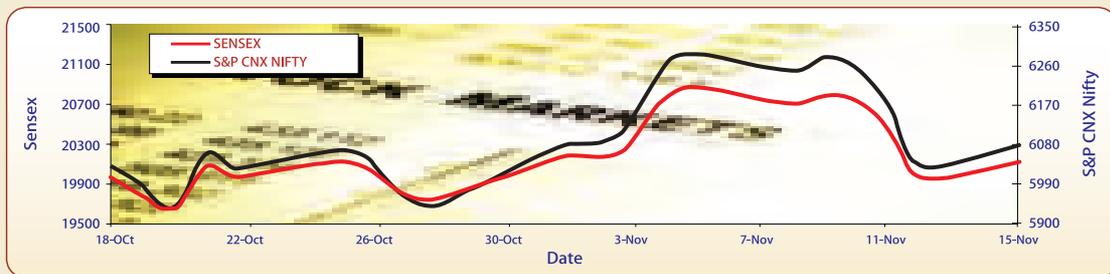
# Economic Indicators



## Indian Rupee vs. Major Foreign Currencies (October 16, 2010 to November 15, 2010)



## Stock Markets



## Selected Indicators

(per cent per annum)

Item	Unit/Base	2009	2010					
		Oct.30	Sep. 24	Oct.1	Oct.8	Oct.15	Oct.22	Oct.29
Cash Reserve Ratio <sup>(1)</sup>	Per cent	5.00	6.00	6.00	6.00	6.00	6.00	6.00
Bank Rate	Per cent per annum	6.00	6.00	6.00	6.00	6.00	6.00	6.00
Base Rate <sup>(2)</sup>	Per cent per annum	11.00-12.00	7.50-8.00	7.50-8.50	7.50-8.50	7.50-8.50	7.50-8.50	7.50-8.50
Deposit Rate <sup>(3)</sup>	Per cent per annum	6.25-7.50	6.75-7.75	7.00-8.00	7.00-8.00	7.00-8.00	7.00-8.00	7.00-8.00
Call Money Rate (Low/High)	Per cent per annum	2.00/3.35	4.00/6.40	4.00/7.40	3.25/6.60	3.25/6.75	3.50/7.15	2.75/12.00

Notes: (1) Cash Reserve Ratio relates to Scheduled Commercial Banks (excluding Regional Rural Banks).  
 (2) Base Rate relates to five major banks since July 1, 2010. Earlier figures relate to Benchmark Prime Lending Rate (BPLR).  
 (3) Deposit Rate relates to major banks for term deposits of more than one year maturity.

Readers are Invited to contribute write-ups or any relevant and interesting piece of information for this feature at [ebboard@icai.org](mailto:ebboard@icai.org).

# ACCOUNTANT'S BROWSER

'PROFESSIONAL NEWS & VIEWS PUBLISHED ELSEWHERE'

Index of some useful articles taken from Periodicals/Newspapers received during October-November 2010 for the reference of Faculty/Students & Members of the Institute.

## 1. ACCOUNTING

Accounting Choice & Earnings Quality: The Case of Software Development by Mustafa Ciftci. *European Accounting Review* Vol.19/3, pp. 429-459.

Accounting Standards: Gaps in Gaap – Accounting for Amalgamation by Dolphy D'Souza. *BCAJ*, October 2010, pp.87-90.

Business Reporting: How to Make Sure We Don't Tumble into Another Black Hole by Vincent Tophoff. *Accountancy Ireland*, October 2010, pp.22-23.

Cloud Computing: What Accountants Need to Know by Alexandra Defelice. *Journal of Accountancy*, October 2010, pp.50-52.

Decision Usefulness of Financial Accounting Measurement Concepts: Evidence From an Online Survey of Professional Investors & Their Advisors by Joachim Gassen & Kristina Schwedler. *European Accounting Review* Vol.19/3, pp. 495-509.

Fair Value or Cost Model? Drivers of Choice For IAS 40 in the Real Estate Industry by A. Quagli & F. Avallone. *European Accounting Review* Vol.19/3, pp. 461-493.

Measurement Issues in Financial Reporting by K. Schipper & M. Trombetta. *European Accounting Review* Vol.19/3, pp. 425-428.

Operating-Financing Distinction in Financial Reporting by Richard Barker. *Accounting & Business Research*, Vol.40/4, pp.391-403.

Transforming the Landscape (Environmental Reporting) by Rachel Fielding. *Accountancy*, October 2010, pp.38-39.

## 2. AUDITING

Effectiveness of External Audit: The Softer Side by Richard Sheath. *Accountancy Ireland*, October 2010, pp.18-20.

Internal Audit: Control Self Assessment in Retail Store Audits by Satish Shenoy. *BCAJ*, October 2010, pp.91-93.

## 3. ECONOMICS

Foreign Direct Investment & Economic Growth in China: Evidence From a Two Sector Model by Ping Yu, etc *Journal of Financial Management & Analysis*, Vol.23/1, 2010, pp. 1-9.

Microfinance in Asia: Need a Supportive & Effective Framework by Keerthi Parikh. *Hope Horizon*, September-November 2010, pp.22-25.

Microfinance Institutions an Investment Destination For Private equity by M.A. Shinod. *Hope Horizon*, September-November 2010, pp.4-5

Microfinance Regulations Aims to Protect the Interests of Customers by S. Iyengar. *Hope Horizon*, September-November 2010.

Microfinance Securitisation: Caterin to Immediate & Cost-Effective Funding by Shadab Rizvi. *Hope Horizon*, September-November 2010.

Micro View of Capital Profit & Issues Related to its Availability by Kevin Daftary. *Chartered Secretary*, October 2010, pp.1432-1434.

Perspectives on the Securitization of Assets: Spanish Economy in Perspective by Pilar Giraldez & Jose Luis Martin. *Journal of Financial Management & Analysis*, Vol.23/1, 2010, pp.40-59.

Some Explorations into India's Post-Independence Growth Process, 1950/51- 2002/03: The Demand Side by M. Mohanty & V.N. Reddy. *Eco.& Pol. Weekly*, October 9, 2010, pp.47-58.

## 4. EDUCATION

Communication & Presentation Skills: The Treasure of a

Teacher by Harish Kumar & C. Kujur. *University News*, October 18-24, 2010, pp.8-11.

Education System in India: Policy Review Needed to Reduce Inequality by Lincy Thomas. *Hope Horizon*, September-November 2010, pp.34-38.

## 5. INVESTMENT

Commodity Derivatives Market in India: Development Regulation & Future Prospects by Amit Kumar, etc. *Company Law Journal*, Vol. 4, 2010, pp.11-18.

Effect of Takeovers on the Fundamental Value of Acquirers by Paul M. Guest, etc *Accounting & Business Research*, Vol. 40/4, pp. 333-352.

Emerging Capital Market for Nonprofits by Robert S. Kaplan & A.S. Grossman. *Harvard Business Review*, October 2010, pp.111-118.

Takeovers & Standard of Conduct for Directors by Rajat Sharma. *Company Law Journal*, Vol.4, 2010, pp.44-48.

## 6. LAW

Compliance of Environmental Laws & Value Creation by T.V. Ganesan. *Chartered Secretary*, October 2010, pp.1405-1411.

## 7. MANAGEMENT

Broad Outline of the Environmental Management System & ISO -14001 Requirements by Delep Goswami. *Chartered Secretary*, October 2010, pp. 1416-1419.

Competing on Talent Analytics by Thomas H. Davenport, etc. *Harvard Business Review*, October 2010, pp.53-58.

Corporate Governance is Changing: Are You a Leader or a Laggard? by Marie – Josee Roy. *Strategic Finance*, October 2010, pp.31-37.

Deficits & Recession: Role of Subnational Governments by Archana R. Dholakia. *Eco. & Pol. Weekly*, October 16, 2010, pp.75-77.

Eastern & Western Management Skills: Comparing the Scores of Indians & Americans by Belal A. Kaifi. *Fortune Journal of International Management*, January-June 2010, pp.1-12.

Globalization & Governance for Sustainability by A. Martinelli & A. Middtun. *Corporate Governance*, Vol.10/1, 2010, pp.6-17.

Governance Arrangements for Sustainability: A Regional Perspective by Philippe C. Schmitter. *Corporate Governance*, Vol.10/1, 2010, pp.85-96.

Managing Sustainability Performance Through the Value-Chain by Fritz Balkau & G. Sonnemann. *Corporate Governance*, Vol.10/1, 2010, pp.46-58.

Measuring Corporate Governance by Sam Bradley. *Accountancy*, SA, October 2010, pp. 21-22.

Performance Measures & Short-Termism: An Exploratory Study by David Marginson, etc. *Accounting & Business Research*, Vol.40/4, 2010, pp.353-370.

Promise & Limitations of Partnered Governance: The Case of Sustainable Palm oil by Jordan Nikoloyuk etc. *Corporate Governance*, Vol.10/1, pp.59-72.

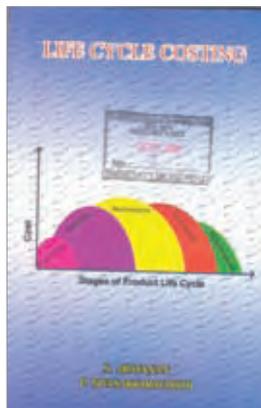
Understanding Costs Using the Value Chain A Ryanair Example by Tim McCormick. *Accountancy Ireland*, October 2010, pp. 28-30.

## 8. TAXATION & FINANCE

Exemption for Education Under EU VAT by Joep J.P. Swinkels. *International VAT Monitor*, September/October 2010, pp.340-345.

Full Texts of the above articles are available with the Central Council Library, ICAI, which can be referred on all working days. For further inquiries please contact on 011-23370154 or by e-mail at [library@icai.org](mailto:library@icai.org)

# A Useful Conceptual Analysis of Various Aspects of Life Cycle Costing\*



**Title :**  
Life Cycle Costing  
**Author :**  
S Aravanan and  
P Sivasakkaravarthi  
**Pages :**  
144  
**Price :**  
₹ 150  
**Publisher :**  
Vijay Pathippagam

The Life Cycle Costing (LCC) is “the design, construction, operation, maintenance and rehabilitation costs associated with a building over its actual service life.” The objective of LCC analysis is to choose the most cost effective approach from a series of alternatives to achieve the lowest long-term cost of ownership. LCC helps change provincial perspectives for business issues with emphasis on enhancing economic competitiveness by working for the lowest long term cost of ownership which is not an easy answer to obtain. LCC is a method to correctly consider long term business decisions which have advantages for profitability. LCC is not easy, but it is effective for building a sound business case for action.

This book is actually trying to set up an understanding on life cycle costing. The purpose of this book is to explain the meaning and application of life cycle costing. This book would be able to give ready material at hand to explain the basic concepts of LCC to readers and will be a good source of reference for gaining knowledge in this area. The work done in this book makes a conceptual analysis of the various aspects of life cycle costing and based on the analysis it attempts to give an overview about LCC. The book also present a very basic understanding of activity based costing and target costing.

The author has made an attempt to give an in-depth knowledge on the different aspect of LCC and made the Indian corporates realize about the importance of LCC. The author has given a detailed review of the existing literature on LCC and examined different models developed in life cycle costing. This author has evaluated the application of life cycle costing in the context of Indian corporates. Academicians and researchers doing work in this area would also find this book as a support for their further work and analysis. The limitation of the book is the use of hypothetical data in absence of primary data. ■

\* Reviewed by Dr. N.N. Sengupta, Asst-Director, Board of Studies of ICAI

## EVENTS

CPE

12  
Hours

### TWO DAYS NATIONAL CONFERENCE

Organised by: COMMITTEE FOR MEMBERS IN INDUSTRY OF ICAI

Hosted by: GUWAHATI BRANCH OF EIRC OF ICAI

Date & Time	Venue
17 <sup>th</sup> & 18 <sup>th</sup> December 2010	Pragyoti ITA Centre for Performing Arts, Machkhowa, Guwahati
<b>Day 1: 17<sup>th</sup> December, 2010</b>	
Timing of Sessions	Details
9.30 AM - 10.30 AM	Registration and Inaugural Session
<b>Technical Session I</b> 10:45 AM – 13:45 PM	IFRS and AS and AAS.
<b>Technical Session II</b> 14:45 PM – 17:45 PM	Corporate Laws
<b>Day 2: 18<sup>th</sup> December, 2010</b>	
Timing of Sessions	Details
<b>Technical Session III</b> 10:00 AM – 13:00 PM	Direct Taxation.
<b>Technical Session IV</b> 14:00 PM – 17:00 PM	Session on India Economy.
<b>Participation Fees</b>	CAs - ₹2,000/- ; CA Students – ₹700/- ; Others – ₹2,000/- Cheque (local)/draft in favour of “Guwahati Branch of EIRC of ICAI” payable at Guwahati and sent it to the address given below. <b>Limited Seats, Registration on First Come First Serve Basis.</b>
<b>Contact Details</b>	
<b>For Registration &amp; further details, please contact</b>	Guwahati Branch of EIRC of ICAI, ICAI Bhawan, 2nd Bye Lane, Manik Nagar, R G Baruah Road, Guwahati – 781005 ☎ : 0361-2207660 ✉ : <a href="mailto:icai.guwahati@gmail.com">icai.guwahati@gmail.com</a> ,

Chairman, CMII

## Discrepancies Noticed by the Peer Reviewers During Peer Review Process\*

Peer Review is directed towards maintenance and enhancement of quality of attestation services and to provide guidance to members to improve their performance and adhere to various statutory and other regulatory requirements. Essentially, through a review of attestation service engagement records, peer review identifies the areas where a practicing member may require guidance in improving the quality of his performance and adherence to various requirements as per applicable Standards. The main objective of Peer Review is to ensure that in carrying out their attestation service assignments; the Practice Unit should (a) comply with the Technical Standards, Ethical Standards and Professional Standards laid down by the Institute and (b) have in place proper systems including documentation systems, for maintaining the quality of the attestation services work they perform for their clients.

While reviewing, the work of Practice Unit the peer reviewers have noted discrepancies which may be non compliance of various Standard issued by ICAI (i) AAS3/SA 230 (Documentation) (ii)AAS 5/SA 500 (Audit Evidence) (iii)AAS 6/SA 315 (Risk Assessment and Internal Control) (iv)AAS 7/SA 610 (Relying upon the work of an Internal Auditor) (v)AAS 8/SA 300 (Audit Planning) (vi)AAS 14/SA 520 (Analytical Procedures) (vii)AAS 15/SA 530 (Audit Sampling) (viii)AAS 17/SA 220 (Quality Control of Audit Work) (ix)AAS 23/SA 550 (Related Parties) (x) AAS 29 (Auditing in a Computer Information System Environment). (xi) AAS 11/SA 580 (Representation by Management) (xii) AAS 10/SA 630 (using work of another Auditor).

It is also noted that the financial statements have not included all the disclosures required by the technical standards and PU does not have a practice obtaining representation from the management on matters material to the financial information, Non evidence for Articles Diaries/Statement are being maintained and verified by Partner/Incharge, Independence policies and procedure has been made available, however, the same is neither signed by the partner nor communicated to partner as well as the employees. Further working papers such as photo copies of office expenses, challans, TDS Certificate, Insurance, Payable Bills obtained without satisfactory attestation of parties. The review of the audit work performed by each audit assistant by the Seniors/ Partners is not being documented to show the evidence

of work conducted as per laid policies or performed in accordance with Audit Programme or no Management Representation letters are obtained and duly kept in record.

Other discrepancies include that the Practice Unit has not separately maintained the current and permanent files of working papers for attestation services Letter of Appointment of the Auditors was not obtained from their clients. Further Working papers not properly arranged as required by SA 230 (AAS 3) of Documentation and there is no proper system of Indexation and cross referencing and also there is no Audit plan and Audit Programme documented. No Practice of issuing engagement letter as required by SA 210 (AAS 26) terms of Audit Engagement and no policy & procedures found in place to ensure independence.

Keeping in view these discrepancies, the Practice Units may ensure such compliance by taking various corrective actions. A system of maintenance of permanent and current files where basic and fundamental documents form part of the permanent file and yearly routine/general working papers form part of current file which may be properly maintained in an organised manner. Proper documentation should be done with regard to audit programmes, and evidences/details on major issues obtained during the audit function are made part of the working papers. A checklist may be prepared before the commencement of the audit and most of the issues which have to be generally checked and items which have to be specifically checked for the clients may be clearly mentioned in the same. The audit Programs should be properly drafted with details of audit work, to be carried out along with audit Schedule and system of filing of important working papers. The staff and article must maintain diaries showing their daily work report and records of professional education being maintained. It should be ensured that there is a system of continuing professional education for staff and regular staff meeting is held in the offices to impart necessary training. Records of CPE Hrs and programmes attended by Qualified staff should be properly maintained

The Practice Units may ensure that the cited deficiencies may be kept in view to avoid deviations and shortfalls. Proactive approach in this regard would help in improving the quality of professional services being rendered to the clients by the Practice firms. ■

\* (Contributed by Peer Review Board of ICAI)

# Be Where It Matters Be a Part of the Fraternity Be a Contributor to CABF



A Fund set up by the members for the members

Life Subscription of the fund : **Rs. 2500**

Ordinary/Annual Subscription : **Rs. 500** per annum

payable in favour of Chartered Accountants Benevolent Fund at New Delhi

- Become life member of CABF, a fund registered under the Societies Registration Act 1860.
- The Fund provides financial assistance for maintenance/ medical needs of the members of the Institute and their families in distress. The Fund has provided generous financial assistance in past also as detailed below:-

Year	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010
<b>Beneficiary</b>	125	137	110	135	79	170
<b>Financial Assistance</b>	44,26,777	45,05,000	46,31,500	1,64,16,000	57,00,000	22,975,500

- Join today as a life member and be a part of the 97564 members of the Institute who have already joined CABF.
- Contribute voluntarily any sum over and above life contribution for the noble and pious cause.
  - Contributions are exempt from tax under section 80-G of Income Tax Act.
- The fund thanks all members who have contributed generously for the cause.



Chartered Accountants Benevolent Fund  
(Registered under the Societies Registration Act, 1860)  
**C/o The Institute of Chartered Accountants of India**  
ICAI Bhawan, Indraprastha Marg, New Delhi - 110002

Visit us at the link funds/award in members area on website [www.icai.org](http://www.icai.org), e-mail : [cabf@icai.in](mailto:cabf@icai.in)

## The Institute of Chartered Accountants of India duly acknowledges the following members for making generous contributions to the Chartered Accountants Benevolent Fund (CABF):

S.No.	M.No.	NAME OF FIRMS/ MEMBERS	AMOUNT (₹)
1	013753	CA. Narendra Kapoor	1,00,000.00
2	070601	CA. Sharad Shah	51,000.00
3	034769	CA. Rajkumar S. Adhukia	50,000.00
4	080737	CA. Paul Priti Saraf	25,000.00
5	007984	CA. Pradeep Seth	25,000.00
6		Borivali (Central) CPE Study Circle	23,953.00
7	008471	CA. M. H. Singhal	21,000.00
8	091043	CA. Rajender Narang	11,111.00
9	071213	CA. P. P. Pareek	11,000.00
10	082093	CA. Ram Babu Aggarwal	11,000.00
11	082526	CA. Suresh Kumar	11,000.00
12	082880	CA. Parmod Kumar	11,000.00
13	083695	CA. S. P. Goyal	11,000.00
14	087289	CA. Anil Aggarwal	11,000.00
15	087636	CA. J. P. Goyal	11,000.00
16	092333	CA. Murari Lal Garg	11,000.00
17	095361	CA. Janak Raj	11,000.00
18	080670	CA. Khera Kuldip	5,100.00
19	082058	CA. Bilash Chand Goyal	5,100.00
20	081949	CA. Mahabir Aggarwal	5,100.00
21	083237	CA. Satya Narain Singal	5,100.00
22	083320	CA. Charan Dass	5,100.00
23	083506	CA. Om Prakash	5,100.00
24	083947	CA. Ramesh Kumar	5,100.00
25	084289	CA. Bansal Naresh Kumar	5,100.00
26	085107	CA. Kamesh Bansal	5,100.00
27	085171	CA. Subhash Goyal	5,100.00
28	086471	CA. Mukesh Gupta	5,100.00
29	087481	CA. Rajesh Goyal	5,100.00
30	088037	CA. Anil Kumar	5,100.00
31	089071	CA. Rajesh Aggarwal	5,100.00
32	089499	CA. Sanjay Verma	5,100.00
33	090535	CA. Radhey Shyam	5,100.00



CA. Narendra Kapoor



CA. P. P. Pareek\*



CA. Sharad Shah



CA. Rajkumar S. Adhukia

34	092216	CA. Onkar Kedia	5,100.00
35	093128	CA. Arun Bansal	5,100.00
36	093455	CA. Teja Ram	5,100.00
37	094029	CA. Vijay Goyal	5,100.00
38	094251	CA. Sanjeev Gupta	5,100.00
39	096009	CA. Girish Gupta	5,100.00
40	096645	CA. Sanjeev Arora	5,100.00
41	096757	CA. Raj Kumar	5,100.00
42	096817	CA. Mehtani Sandeep	5,100.00
43	097013	CA. Sanjeev Garg	5,100.00
44	098414	CA. Deepak Chawla	5,100.00
45	500260	CA. Rupesh Kumar	5,100.00
46	500411	CA. Pardeep Jindal	5,100.00
47	500413	CA. Anoop Goyal	5,100.00
48	501877	CA. Vijay Bansal	5,100.00
49	504404	CA. Archana Goel	5,100.00
50	507002	CA. Ashanand Singla	5,100.00
51	507112	CA. Adish Jain	5,100.00
52	508314	CA. Gulshan Sardana	5,100.00
53	510258	CA. Akhil goyal	5,100.00
54	514440	CA. Manoj Kumar	5,100.00
55	084048	CA. S. C. Thakral	5,000.00
56	091914	CA. Vishsesh Chugh	5,000.00
57	094079	CA. Vinod Kumar	5,000.00
58	400927	CA. Sankalp Bhalla	5,000.00
59	094458	CA. Rajeev Kumar	5,000.00

\* The member has donated a total of ₹66,000 since June 2010

## INVITATION FOR ARTICLES

The Committee on Management Accounting (CMA) of ICAI invites research articles, case studies, write-ups and other similar materials in the areas of Management Accounting and Financial Management for publishing in its journal. The Institute proposes to publish a quarterly journal 'Management Accounting and Business Finance' with an object of spreading the advanced knowledge on Management Accounting and allied areas which are relevant for the members of the profession and others concerned. The Journal is to focus on practical articles for advanced and research oriented knowledge.

The articles submitted for consideration of publication should be of 4000-6000 words typed double spaced on A4 size paper with 1 inch margin all round. In order to facilitate the blind review process, the author should not mention his/her name on the body of the manuscript. Three hard copies of manuscript along with a soft copy (MS WORD) may be sent at the following address:

Secretary,  
Committee on Management Accounting (CMA),  
ICAI Bhawan

Second Floor,  
A-29, Sector-62,  
Noida – 201 309 (U.P.)  
Phone: 0120 – 3986910  
E-mail: [cma@icai.in](mailto:cma@icai.in); [zaidi@icai.org](mailto:zaidi@icai.org)

Authors may note that in appreciation of their contribution to the MABF Journal an honorarium of ₹5,000/- per article would be paid to them.

Detailed Guidelines for writing the articles are available on the website of Committee at [www.icai.org](http://www.icai.org)

The Editorial Board hopes that professionals and other experts will come forward to share their expertise and practical experience with our readers by preparing the papers in view of the specific requirements of the accounting profession.

Chairman,  
Committee on Management Accounting (CMA)  
ICAI, New Delhi

## Expert Advisory Committee of The Institute of Chartered Accountants of India

The fast changing and immensely competitive environment (of accounting), often calls upon organisations to enter into complex business deals and transactions where practice norms are not yet settled. In such situations, accounting for transactions and auditing thereof becomes a difficult task. This gives rise to the need for authoritative guidance on such matters. The Expert Advisory Committee (EAC) of the Institute of Chartered Accountants of India fits into the role of giving such authoritative guidance in the form of opinions, on matters relating to application and implementation of accounting and auditing standards and other pronouncements, comprising generally of accepted accounting and auditing principles under peculiar and intricate situations. Over a period of time, EAC's role has become widely acknowledged with members in practice and industry, alike, increasingly seeking the services of EAC to unravel wide array of issues and complex problems while discharging their duties, such as preparation and presentation of financial statements, reconciling the views of

auditors, management, various stakeholders and authorities, etc.

For the benefit of the members, EAC regularly releases Compendium of Opinions where the opinions finalised during the year are published in a volume of the Compendium. So far, EAC has released 28 volumes of the Compendium. A CD of 'Compendium of Opinions' containing more than 1128 opinions issued up to January 2009 has also been released by the Committee. These publications of the Committee are available at the Institute's head office in New Delhi and its regional council offices in Mumbai, Chennai, Kolkata and Kanpur.

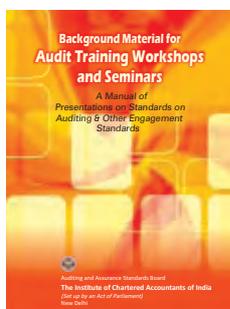
**Opinions can be obtained from the EAC as per its Advisory Service Rules which are available on the website of the ICAI, at its hyperlink, [http://www.icai.org/category.html?c\\_id=142](http://www.icai.org/category.html?c_id=142). The Rules, can also be obtained from the Institute's Head Office at New Delhi. For further information, Secretary, Expert Advisory Committee can be contacted through e-mail at [eac@icai.org](mailto:eac@icai.org).**

## New Publication from the Auditing and Assurance Standards Board

### Background Material for Audit Training Workshops and Seminars (A Manual of Presentations on Standards on Auditing & Other Engagement Standards)

#### Significant features of the Background Material are:

- Contains a snapshot of the recent developments in auditing.
- Contains the new structure and numbering pattern of the Standards.
- Contains simple and crisp power point slides to explain the Standards, accompanied by notes.
- Contains a compilation of the documentation requirements in various Standards on Auditing.
- Contains various technical posers and case studies on auditing to deal with practical situations.
- Helps the members to understand and implement the Standards in a simple and lucid manner.
- Makes a very useful one stop concise reference point for understanding the Standards.



- Makes an interesting reading even for lay readers.
- The Background Material is an important resource material for training programmes on auditing.
- The Background Material comes with a CD of the entire Background Material to provide ease of reference.

**Price:** ₹ 650/- (including CD)

#### Ordering Information

The Background Material can be purchased directly from the sales counters at the ICAI's regional offices or at its head office. To order by post, please send a demand draft for the price of the publication (plus postage charges as per the desired mode of delivery) in favour of "The Secretary, The Institute of Chartered Accountants of India, New Delhi", payable at New Delhi to the Postal Sales Department, The Institute of Chartered Accountants of India, ICAI Bhawan, A-29, Sector-62, NOIDA – 201 309, Uttar Pradesh.

Postal Charges:	
Courier (within NCR):	₹ 14 /-
Courier (rest of India):	₹ 63/-
Registered Post (all over India):	₹ 68/-
Unregistered Post (all over India):	₹ 51/-

## Office of The Comptroller and Auditor General of India 10, Bahadur Shah Zafar Marg, New Delhi – 110 124 Empanelment of Chartered Accountant firms for the year 2011-2012.

Applications are invited online from the firms of Chartered Accountants who intend to be empanelled with this office for the year 2011-2012 for appointment as auditors of Government Companies/Corporations. The format of application will be available on our website: [www.cag.gov.in](http://www.cag.gov.in) from 1<sup>st</sup> January, 2011. Chartered Accountant firms can apply/update the data showing the status of the firm as on 1<sup>st</sup> January, 2011 till 31<sup>st</sup> March, 2011 and generate online acknowledgement letter for the year. Only firms who have generated online acknowledgement letter for the year 2011-2012 will be considered for empanelment.

Any changes in the constitution of the firm occurring after the cutoff date of 1<sup>st</sup> January 2011, should continue to be updated by the CA firms in the website which will be available throughout the year. However, the changes in the firm occurring after 1<sup>st</sup> January, 2011 till the time of preparing the panel that will lead to a reduction in the rank of the applicant firm shall only be taken into account for ranking the CA firms.

Sd/-  
Director General (Commercial)

## Announcement from Committee on Management Accounting (CMA)

The Committee on Management Accounting of the Institute of Chartered Accountants of India - New Delhi has been conducting Post - Qualification Courses for the members of the Institute namely.

- (1) Management Accountancy Course
- (2) Corporate Management Course

The Broad Structure of the courses is as follows:

(1) Management Accountancy Course

Group – I Paper 1 Management Accounting and Decision Making

2 Financial Management

Group – II 3 Economic Environment and General Management

4 Systems Management

(2) Corporate Management Course

Group – I Paper 1 Organisational Behaviour and planning

2 Management Control and Management Audit

Group – II 3 Production and Productivity Management

4 Marketing Management

The Committee has decided to revise the syllabus of these courses. Members of ICAI and other persons, especially those who have joined/completed these courses are requested to provide their valuable inputs regarding revision of syllabus of these courses at [cma@icai.in](mailto:cma@icai.in), [zaidi@icai.org](mailto:zaidi@icai.org)

The address for Correspondence is

The Secretary,

Committee on Management Accounting

The Institute of Chartered Accountants of India

Second Floor,

A – 29, Sector 62,

Noida – 201309 (U.P.)

Ph. No: 0120 - 3986910

## Guidelines for Training of Articled Assistant Outside India

The Institute, while considering the difficulties being faced by overseas members in providing training to articled assistants has issued the revised guidelines and FAQs for training of articled assistants outside India. The same has been hosted on the Institute's website. For more details, please visit our website [www.icai.org](http://www.icai.org).

## Invitation for Faculty & Case Studies for Post Qualification Course on Information Systems Audit

The Committee on Information Technology of ICAI offers the highly popular Post Qualification Course (PQC) on Information Systems Audit (ISA) leading to the designation D.I.S.A. (ICAI) with an enrollment of over 31500 members.

The Committee is in the process of enhancing the ISA Faculty Bank on All India basis to organise sessions for the ISA Professional Training, which is generally organised on weekends and to contribute practical Case Studies, Questions, etc. to develop the profession in this area.

Chartered Accountants and experts specialising in this area are requested to send their detailed CV inter-alia covering their specialist qualifications in IS Audit, Educational & Professional Qualifications, Professional Experience in this field, Teaching Experience, Area of Specialisation, PPTs and Case Studies that they propose to cover, as a part of their deliberations to "The Secretary, Committee on Information Technology, The Institute of Chartered

Accountants of India, ICAI Bhawan, Plot Nos.52-54, Vishwas Nagar, Shahadra, Delhi - 110032. Phone: +91(11)-30210619/ 621, E-mail: [cit@icai.in](mailto:cit@icai.in)". The Committee pays honorarium @ ₹600/ 800/ 1000 per hour apart from reimbursing incidental expenses for outstation sessions, as per rules.

The Committee on IT also proposes to develop a Case Study Bank on Information Systems Audit to be used as a part of the course deliberations and a publication in due course. Each Case Study is expected to contain a brief description, objective, test data, processes/procedures to be followed, sample reports and their interpretation. The Committee would be paying honorarium and incidental expenses as per rules for Case Studies accepted. Proposals are invited in this regard also, at the aforementioned address.

Secretary  
Committee on Information Technology



## Invitation for Faculty & Case Studies for Certificate Course on Forensic Accounting & Fraud Detection using IT & CAATs

The Committee on Information Technology of ICAI has been offering Certificate Course on Forensic Accounting and Fraud Detection using IT & CAAT's. Further details of the course are available at [www.icai.org](http://www.icai.org) under certificate courses on the home page.

The Committee is developing a Faculty Database of experts on all India basis to offer the course at all Regional Councils, Branches and CPE Chapters. Chartered Accountants and experts specialising in this area are requested to send their detailed CV inter-alia covering their specialist qualifications in Forensic Accounting & Fraud Detection, Educational & Professional Qualifications, Professional Experience in this field, Teaching Experience, Area of Specialisation, PPTs and Case Studies that they propose to cover, as a part of their deliberations to The Secretary, Committee on Information Technology, The Institute of Chartered Accountants of India, ICAI Bhawan, Plot Nos.52-54, Vishwas Nagar, Shahadra, Delhi - 110032. Phone: +91 (11) 30210619/ 621, email: [cit@icai.in](mailto:cit@icai.in). The honorarium would be in the

range of at the rate of ₹1,000/ 1,500/ 2,000/- per hour depending on experience. Apart from honorarium incidental expenses for outstation sessions will paid at actual as per rules.

The Committee is also proposing to develop Case Study Bank on Forensic Accounting and Fraud Detection using IT & CAATs to be used as a part of the course deliberations and bring a publication in due course of time. Each Case Study is expected to contain a brief description, objective, test data, processes and procedures to be followed, sample reports and their interpretation. Attractive honorarium and incidental expenses at actual would be paid as per rules for Case Studies accepted by the committee. Proposals are also invited in this regard, at the above given address.

**Place:** New Delhi

**Date:** 18<sup>th</sup> November 2010

Secretary  
Committee on Information Technology



## Invitation for Participation



Corporate CA Achievers' Actiaim



Award Ceremony Sunday 30th January 2011 at Science City, Kolkata

### The Jury for the Awards-

- Shri. Adi Godrej (Jury Chairman) Chairman, Godrej Industries Ltd.
- Shri. Anil K. Agarwal Former President, ASSOCHAM
- Shri. A. M. Naik CMD, L&T Ltd.
- Smt. Chanda Kochhar MD & CEO, ICICI Bank Ltd.
- Shri. Deepak Parekh Chairman, HDFC Ltd.
- Shri. H.M Bangur MD, Shree Cement Ltd.
- Shri. J.J. Irani Director, TATA Sons Ltd.
- CA. Kamlesh S. Vikamsey Former President, ICAI
- Shri. Milind Murlid Deora Member of Parliament, Lok Sabha
- Shri. Nimesh N. Kampani Chairman, JM Financial Group
- Shri. Partha S. Bhattacharyya Chairman, Coal India Ltd.
- Shri. Prabhu Chawla Editor-in-Chief, India Today Group
- Shri. Raj Kumar Dhoot Member of Parliament, Rajya Sabha
- Shri. Rana Kapoor MD & CEO, Yes Bank
- Shri. Rashesh Shah Chairman, CEO & Founder, Edelweiss Capital Ltd.
- Shri. Rohinton Soli Screwvala CMD, UTV Software Communication Ltd.
- Shri. R.S. Sharma CMD, ONGC Ltd.
- Shri Sanjiv Goenka Vice Chairman, RPG Enterprises

There would be a Process Auditor.

To get details of nomination & application form visit [www.icai.org/forum](http://www.icai.org/forum)

Last date for nomination  
Thursday, 23rd December 2010

Applications can be made by-

1. The Chartered Accountant himself.
2. His / her employer.
3. Any other member of ICAI.



Committee for Members in Industry,  
The Institute of Chartered Accountants of India  
(A Statutory body established under an Act of Parliament)  
ICAI Bhawan, P. O. Box No. 7100  
Indraprastha Marg, New Delhi - 110 002  
[www.icai.org](http://www.icai.org), [www.cmii.icai.org](http://www.cmii.icai.org), <http://jobs4cas.icai.org>

Chairman, CMII  
Tel: +91 (11) 3011 0555 / 0491  
E-mail: [cmii@icai.org](mailto:cmii@icai.org)  
Secretary, CMII  
Tel: +91 (11) 3011 0491 / +91 93507 99916 / +91 93105 42605  
E-mail: [cmii\\_events@icai.in](mailto:cmii_events@icai.in) / [secretarycmii@icai.in](mailto:secretarycmii@icai.in)

For Sponsorship opportunities please contact Secretary, CMII

# Introduction To Multipurpose Empanelment Form (including Bank Branch Auditors' Empanelment)

Every year, Professional Development Committee of the Institute hosts the Multipurpose Empanelment Form (MEF) on [www.meficai.org](http://www.meficai.org). This year also, MEF 2010-11 was hosted on May 1, 2010. As per the decision of the Council of the Institute taken at its 235<sup>th</sup> meeting, financial documents were also called from 10 per cent applicants randomly selected by the computer.

As many enquiries were being received from members on various issues, the PDC felt it expedient to share some of the developments as well as relevant background details concerning the preparation of the Multipurpose Panel.

## *New Developments:*

Recently, the Council at its 299<sup>th</sup> Meeting held in October, 2010 has decided to call for financial documents from **all** the applicants of MEF for the year 2011-12. Further, several instances have come to notice where MEF application was submitted by unauthorized persons. As a result, the Professional Development Committee is contemplating that from next year onwards, digital signature may be required for submitting MEF application.

## *Status of the applicant:*

For preparation of the said panel, the data of the applicant appearing in the Institute's record as on 1<sup>st</sup> January of the respective year is considered. For e.g. for the preparation of panel for the year 2011-12, data as per ICAI's record as on 1<sup>st</sup> January, 2011 will be considered.

The Council of the Institute at its 242<sup>nd</sup> meeting held in April, 2004 had decided that there shall be a cut off date for condonation of cases for

empanelment purposes as on 1<sup>st</sup> January and the cases received beyond the cut off date will not be considered for condonation. In view of this, it has been decided inter alia as under:

"For the purposes of Empanelment in the C&AG Panel prepared by office of C&AG and Bank Branch Auditors' Panel prepared by ICAI (for which Constitution Certificates as on 1<sup>st</sup> January are issued every year); no condonation of delay in submission of Form no. 18 beyond 31<sup>st</sup> January preceding the financial year under audit (e.g. 31<sup>st</sup> January, 2011 for empanelment for the year 2011-12) will be done by the Institute."

In case the intimation of change in the constitution is given to the regional office after 31<sup>st</sup> January, the effect of the said change would not be given for preparation of PSU auditors' Panel and Bank Branch Auditors' panel; eg: if a firm has added 1 more partner before 1<sup>st</sup> January and the firm wants to apply for MEF, it should ensure that it submits all requisite documents to the Regional Office before 31<sup>st</sup> January of the year and changes are effected in Institute's database.

**Please note that MEF strictly picks data from Institute's database maintained by Regional Offices. PDC has no role in modifying the data of the applicant.**

## *Decision taken by the Council at its 241<sup>st</sup> meeting regarding part-time practitioners for Bank Panel 2005-06*

The Council at its 241<sup>st</sup> meeting decided that w.e.f. 1.4.2005, any member in part time practice (namely, holding Certificate of Practice and also engaging himself in any other business and/or occupation) will not be entitled

to perform attest function.

In view of the above decision, members may note the following for the purpose of Bank Branch Auditors' Empanelment for 2005-06 and onwards:-

Any firm which has Chartered Accountants whose main occupation is not practice, as partners, may apply for empanelment; however, no weightage will be given to the part-time partner(s).

## *Exclusivity of the proprietor or partners of the applicant firm*

As per the eligibility norms provided by RBI for preparation of the said panel, the Chartered Accountants associated with the applicant firm should be **"exclusively"** associated with the firm. Please note that in case of members who are partners/proprietors in two or more firms, their credit would not be given to any of the firms. **Furthermore, partner/proprietor of the firm also having their own sole practice would not be considered as exclusively associated with the firm.**

There seems to be a misunderstanding among the members that credit of common partners is given to applicant firm if only one of the firms in which he is a partner/proprietor applies for the said panel. This is not the case. It does not matter, whether one firm applies or both, in no case credit of common partner would be given to any of the firms.

**PN:** If as on 1<sup>st</sup> January of the relative year, a member is appearing as associated with more than 1 firm, credit of such partner is not given in any condition to any of the firms in preparation of Bank Branch Auditors' Panel.

Members may please note the application of the new empanelment norms as given in the examples below:

1. A & Co. is a partnership firm of 2 partners B & C. B has a proprietorship firm of his own, B & Co. A & Co. and B & Co. both apply – B & Co. will be rejected and A & Co. will be considered as a firm with only one exclusively associated partner and therefore treated at par with a proprietary firm.
2. Only A & Co. applies – A & Co. will still be treated as proprietorship firm with one exclusively associated partner.
3. ABC is a partnership firm of 3 partners A, B & C, and all 3 have proprietorship firms A & Co, B & Co. and C & Co. – All applications (ABC, A & Co., B & Co., C & Co. or any combination thereof, or of the individual firms) will be rejected.

Implication of the abovesaid norm is that members (both partners and C.A. employees) who are not exclusively associated with the applicant firm will not be given any weightage in Bank Branch Auditors' Panel e.g. if a partner P/C.A. employee E of firm F is also a partner/proprietor in any other firm and/or practicing in his individual name, or is employed elsewhere; then firm F will not get any credit for the partner P/C.A. employee E.

Further, in case, none of the partners are exclusively associated with the firm, (i.e. all partners are either practicing in their individual name/ have a sole proprietary concern or are associated as partner in another firm/ employed elsewhere also); then such firm will not be eligible for Bank Branch Auditors' Panel altogether.

Furthermore, a member who is also a partner in any firm besides practicing in his individual name or sole proprietary concern, will not be entitled to apply in his individual name/ sole proprietary concern also, e.g. the

partner P of the firm F in the example given hereinbefore will not be eligible to apply in his individual name/sole proprietary concern and the firm F in which he is a partner will also not get any credit for Partner P.

A member having more than 1 proprietorship is advised to keep only one of the proprietorships before 1<sup>st</sup> Jan, 2011 to maintain his exclusivity.

### **Unique Code Number (UCN) - Significance and due care**

UCN is a very important data which facilitates RBI in proper and correct recording of past Bank Audit experience of applicants. The Members/ Firms MUST quote their proper unique code number (if allotted, AT ANY TIME in the past) in the MEF to facilitate this. The MEF may show UCN field as "Not allotted" though it may have been allotted in past as the applicant might not have applied in the last years' empanelment. However, members must take utmost care to mention their UCN in Memorandum of Changes.

### **Professional Staff:**

The term "professional staff" as used in clause (ii) of para 1 of Annexure I to RBI's letter No. DBS.ARS.No. 650/08.91.008/2003-04 dated 1<sup>st</sup> March, 2004 containing the revised empanelment norms issued by the Reserve Bank of India (applicable from the year 2005-06 and hosted on the Institute's website) "also includes other audit staff having knowledge of book-keeping and accountancy and engaged in outdoor audit besides articulated clerks and audit clerks."

### **Memorandum of Changes**

In case applicant does not agree with the (static) data as appearing from the ICAI database in the online application form, the changes (as per the applicant) can be informed through MoC (Memorandum of Change).

### **Relaxation for - Chartered Accountants from North Eastern Region.**

RBI has relaxed the eligibility norm in respect of the number of years of professional standing required for individual members/proprietary firms from the North-Eastern Region (viz. the states of Assam, Meghalaya, Arunachal Pradesh, Manipur, Mizoram, Nagaland, Sikkim and Tripura) by reducing the period from 3 years to 1 year from the year 2008-09 and onwards.

### **MEF Complaint Centre:**

MEF was introduced to have a comprehensive data of Chartered Accountants/firms interested in empanelment of various authorities which call for panel from Institute. Every effort is made to facilitate Members to file MEF. One of such important step was introduction of Complaint Centre.

The MEF complaint centre was first time introduced in 2008. This complaint centre is dedicated to resolve the problems pertaining to MEF. It is a systematic and advanced version of grievance resolution. In case, an applicant faces any problem in accessing, operating or submission of MEF, complaint may be lodged by accessing complaint-centre link which is made available on [www.meficai.org](http://www.meficai.org). Applicants can lodge their complaint by using either MEF No./ M. No/ FRN. On successful lodging of complaint, complaint number is informed through e-mail. All complaints lodged by the applicant are looked into by the Committee. The applicants can view the status of their complaints by using MEF No./Complaint No./MRN/FRN.

After submission of online MEF, the applicant is required to send declaration duly signed by all the continuing Partners/Proprietor. Members shall ensure that the declaration reaches the designated address as mentioned in the advisory of the form within stipulated time. The declaration

is to be signed by all the partners/ proprietor of the applicant as on 1<sup>st</sup> January of the relative year continuing with the applicant till the date of signing of declaration. In case any partner resigns or retires from the firm after 1<sup>st</sup> January, the weightage of such members is not given to the applicant.

Advisory of MEF is basically a guide to help members in filling MEF. In short, it gives “do’s and don’ts” while filling MEF.

As the MEF Panel is used for submission of Panel to various authorities as per their respective requirements, the MEF may also include special sections for empanelment of CA firms to capture data as may be required by them. For e.g. next year there will be a separate section asking for additional data required by Commissioner of Cooperative Societies, Maharashtra

### State, for audit of Urban Cooperative Banks, Credit Cooperatives and other societies.

All members and firms are therefore requested to fill Multipurpose Empanelment Form to make it more broad based as the said panel may be used to provide list of Chartered Accountants/Firms to various authorities which request for the same as per their requirement.

### Important References:

- Please visit [http://www.rbi.org.in/Scripts/bs\\_viewcontent.aspx?id=946](http://www.rbi.org.in/Scripts/bs_viewcontent.aspx?id=946) for RBI road map on Guidelines for Appointment of Statutory Auditors in Public Sector Banks.
- Please visit [http://www.icai.org/post.html?post\\_id=725&c\\_id=91](http://www.icai.org/post.html?post_id=725&c_id=91) for Implementation of revised empanelment norms for

appointment of statutory auditors of public sector banks, select All India Financial Institutions and RBI.

- Please visit [http://www.icai.org/post.html?post\\_id=705&c\\_id=91](http://www.icai.org/post.html?post_id=705&c_id=91) for application of Revised Empanelment Norms for Bank Branch Auditors’ Panel.

### In case of Merger or Demerger

In case of any merger after 31<sup>st</sup> January, the firm which continues to be in existence will only be eligible to apply for MEF (with its constitution as on 1<sup>st</sup> January) likewise, in case of demerger after 31<sup>st</sup> January, the main firm (i.e. the merged entity) only will be eligible to apply however, only the partners since 1<sup>st</sup> January and continuing with the firm would be considered for determining eligibility of the firm in the panel. ■

## Shifting of Some Departments/Committees to Newly Constructed Building of ICAI at Sector-62, Noida

November 24, 2010.

We would like to inform you that some sections/committees which were housed in Institute’s Head Office, I.P. Marg, New Delhi and its rented premises at Sector-58, Noida have been shifted to its new premises at plot No A-29, Sector-62, Noida and are functional now. The details of Committees/Sections shifted and contact details are on the right hand side of this announcement.

The Address of the new location is under:

**The Institute of Chartered Accountants of India**  
**“ICAI Bhawan”**  
**Plot No- A- 29**  
**Sector- 62, NOIDA**  
**Dist: Gautam Budh Nagar**  
**Uttar Pradesh**  
**PIN- 201309**  
**Phone Number – 0120 – 3986900**

Sl.No.	Name of the Section/ Committee	Ph.No.	Sl.No.	Name of the Section/ Committee	Ph.No.
1	Board of Studies	0120 -3986902	9	Internal Audit Standards Board.	0120 -3986949
2	Auditing & Assurance Standards Boards	0120 -3986920	10	Committee on International Taxation	0120 -3986923
3	Committee for Capacity Building of CA Firms & Small and Medium Practitioners,	0120-3986952	11	BOS Store.	0120 -3986943
4	Continuing Professional Education Committee	0120 -3986957	12	Peer Review Board	
5	Direct Taxes Committee	0120-3986922	13	Regional Branch Affairs	
6	Committee on Financial Markets & Investor’s Protection	0120-3986915	14	HRD Administration	
7	Editorial Board	0120-3986926	15	Committee on Management Accounting, IFRS Group	0120 -3986910
8	Indirect Taxes Committee.	0120 -3986906	16	Committee on Public Finance & Govt. Accounting	

CPE

**12**  
Hours**NATIONAL CONFERENCE**

Organised : Jointly by Direct Taxes Committee and Committee for Members in Industry of ICAI  
Hosted by : The Ahmedabad branch of WIRC of ICAI

Date		Venue	
4 <sup>th</sup> December, 2010 and 5 <sup>th</sup> December, 2010		Sindhu Bhavan, Off. S.G.Road, Ahmedabad.	
Programme structure			
Date	Timing	TOPICS	Faculty
04/12/2010	10.00 AM to 11.00 AM	Inauguration	Chief Guests: Shri S. S. N. Moorthy, Chairman CBDT CA. Amarjeet Chopra, President of ICAI
	11.00 AM to 12.15 PM	CFC/GAAR/Place of effective management under DTC	CA. Pranav Sayta
	12.15 PM to 1.30 PM	Provision of Section 56(2)	CA. Rajesh Kadakia
	2.30 PM to 3.15 PM	Opportunities & Challenges for the profession	CA. Y. M. Kale* Past President of ICAI
	3.15 PM to 4.30 PM	Business Valuation (Including under FEMA)	CA. Sujal Shah
	4.30 PM to 5.45 PM	Penalties – Recent Trend	Shri Saurabh Soparkar Senior Advocate, Ahmedabad
05/12/2010	9.30 AM to 10.30 AM	Future of the Profession	CA. G. Ramaswami, Vice President of ICAI
	10.30 AM to 12.15 PM	IFRS Convergence in India - Challenges	CA. N. P. Sarda Past President of ICAI
	12.15 PM to 1.30 PM	Business Deductions including impact of Section 14A	CA. Padamchand Khincha
	2.30 PM to 3.00 PM	Speech by Industrialist	Eminent Industrialist
	3.00 PM to 4.15 PM	Import & Export of Services	CA. A. R. Krishnan
	4.15 PM to 5.30 PM	Transfer Pricing – Practical Perspective	CA. Vijay Iyer
*Subject to confirmation			
Registration Fees for Members – ₹1900/-. Registration restricted to 750 members on first served basis. Registration fee has to be paid by cheque/ DD in favour of "Ahmedabad Branch of WIRC of ICAI" payable at Ahmedabad. Members can download the registration form from the Website of the Branch i.e. <a href="http://www.ahd-icai.org">www.ahd-icai.org</a> , and send the registration form duly filled in along with the registration fees to the Branch at the address given below:			
For registration and further details, please contact			
Ahmedabad Branch of Western India Regional Council, The Institute of Chartered Accountants of India 'ICAI BHAWAN', 123, Sardar Patel Colony, Near Usmanpura Underbridge, Naranpura, Ahmedabad - 380 014 ☎: +91 (79) 39893989 / 27680537 ✉ : <a href="mailto:ahmedabad@icai.org">ahmedabad@icai.org</a>			

**Classifieds**

**4826** FCA DISA, 10 years professional, 15 years industry experience seeks professional assignment on contractual/permanent terms. Please mail to [mailme.chartered2010@rediffmail.com](mailto:mailme.chartered2010@rediffmail.com)

**4827** 35 years old firm having branches in metros and other cities, seeks merger/network offers from international/national firms/senior practising CAs, preferably with expertise in IFRS/SAP. Write with

details to [misraabhisek@rediffmail.com](mailto:misraabhisek@rediffmail.com) or contact : 09937620718

**4828** Kolkata based CA firm requires young CAs with DISA/ CISA and/or retired CAs (Preferably ex-banker) as Partner. Also interested for merger and networking. Please send your CV and proposals at: [apsnbe@yahoo.in](mailto:apsnbe@yahoo.in)

CPE  
**12**  
Hours

## Two Days National Conference on Excellence in Professional Approach

Organised by: Committee for Capacity Building of CA Firms & Small and Medium Practitioners, ICAI jointly with CPE Committee, ICAI  
Hosted by: AGRA Branch of CIRC of ICAI

Date & Time		Venue
24 <sup>th</sup> & 25 <sup>th</sup> December, 2010		Hotel Orient Taj, Fatehabad Road, Agra
24 <sup>th</sup> December, 2010- 8.30 a.m. to 9.30 a.m.		Registration of participants
24 <sup>th</sup> December, 2010- 9.30 a.m. to 11.00 a.m.		Inaugural session Chief Guest- CA. Amarjit Chopra, President, ICAI Guest of Honour- CA. G. Ramaswamy, Vice-President, ICAI
<b>Day 1: 24<sup>th</sup> December, 2010</b>		
Timing of Sessions	Topics to be discussed	Speaker
<b>Session-I</b> 11.00 AM to 1.00 PM	Session Chairman : CA Sunil Goyal, Past President, ICAI	
	Strategic Planning for Development of Small and Medium Firms	CA. Sanjeev Maheshwari Central Council Member & Chairman-CCBCAF&SMP
	Covergence to IFRS	CA. Manoj Fadnis, Central Council Member
<b>Session-II</b> 1.45 p.m. to 3.45 PM	Session Chairman : CA N.D.Gupta, Past President, ICAI	
	Direct Tax Code – Changes in conceptual approach	Dr. Girish Ahuja, New Delhi
	Business Deduction with impact to Sec. 14A of the Income-tax Act, 1961	CA. Dhinal Ashvinbhai Shah Central Council Member
<b>Session-III</b> 3.45 PM to 5.45 PM	Session Chairman : CA T.N. Manoharan, Past President, ICAI	
	Technology in the Profession	CA. S. Santhanakrishnan Central Council Member
	Disclosure in Financial Statements	CA. Akshay Gupta, Kanpur
<b>Day 2: 25<sup>th</sup> December, 2010</b>		
<b>Session-IV</b> 9.30 AM to 11.30 AM	Chairman: CA V. Murali, Central Council Member	
	Key Note Address	Dr. Rakesh Gupta
	Technicalities of Right to Information Act	Shri ShyamLal Yadav, Associate Editor, India Today
<b>Session-V</b> 11.30 AM to 1.30 PM	Chairman: CA Manoj Fadnis, Central Council Member	
	Business Rationale of LLP	CA. Ved Jain, Past President, ICAI
	Reassessment Proceedings u/s 148	CA. Kapil Goel
<b>Session-VI</b> 2.15 PM to 4.15 PM	Chairman: CA Praveen Bansal, ITAT Member	
	Interpretation of Law, Deed and Document	CA. Ravindra Holani, Central Council Member
	Re Structuring in Listed Companies	CA. Pawan Vijay
<b>Session-VII</b> 4.15 PM to 5.30 PM	Chairperson: CA Kemisha Soni, Chairperson, CIRC of ICAI	
	Presentation on KDOC and eSecretary Software – An Initiative by Committee for Capacity Building of CA Firms and Small & Medium Practitioners	By Hazel Infotech Ltd, Mumbai
5.30 PM to 6.00 PM	Valedictory Session	
Conference Fees – ₹2,000/- (If received upto 15.12.2010) ₹2,250/- ( If received after 15.12.2010)		
<b>Payment may be made by Cheque / Demand Draft in favour of 'AGRA Branch of CIRC of ICAI'.</b>		
<b>For Registration &amp; further details, please contact</b>	Agra Branch of CIRC of ICAI, 77/8, M.K. Tower, Sanjay Place, Agra- 282 002 ☎: 0562- 4040598, 2856598,4012537 / 09760006665, 09319108585 ✉ :agra@icai.org, icaiagra@gmail.com	

CPE

6

Hours

**Seminar on Social Audit at New Delhi**

Organised by: Internal Audit Standards Board

Hosted by: NIRC of the ICAI

Date & Time	Venue	
December 8, 2010, Wednesday, 9:30 AM to 5:30 PM	Casurina Hall, India Habitat Centre, Lodhi Road, New Delhi	
<b>Theme</b>		
<ul style="list-style-type: none"> <li>To understand the concept and process of Social Audit.</li> <li>To understand the tools and mechanisms involved in the process of Social Audit.</li> <li>To gain an understanding of the need and relevance of Social Audit in the context of Corporate Social Responsibility (CSR).</li> <li>To gather knowledge on the role of Chartered Accountants in the process of Social Audit.</li> </ul>		
<b>Topics to be Discussed</b>		
1. Social Audit - Genesis and Evolution		
2. Process and Methodology of Social Audit – Panel Discussion		
3. CSR and Social Audit		
4. Role of Chartered Accountants in the Process of Social Audit		
<b>Fees: ₹1,000 per Member</b>		
<b>For Registration and Further Details:</b>		
Chairman, Internal Audit Standards Board ✉ : <a href="mailto:cia@icai.org">cia@icai.org</a> ☎ : (0120) 3986949	Vice Chairman, Internal Audit Standards Board ✉ : <a href="mailto:auditing@icai.org">auditing@icai.org</a> ☎ : ((0120) 3986949	Chairman, NIRC of ICAI ✉ : <a href="mailto:nirc_seminar@icai.in">nirc_seminar@icai.in</a> <a href="mailto:nirc@icai.in">nirc@icai.in</a> <a href="mailto:chairmannirc@icai.in">chairmannirc@icai.in</a> ☎ : (011) 30100507, 30100524
For further details, please visit website of the Institute at <a href="http://220.227.161.86/20769announ11682.pdf">http://220.227.161.86/20769announ11682.pdf</a>		

CPE

12

Hours

**National Conference on Direct Tax at New Delhi**

Organised by: Direct Tax Committee of ICAI

Hosted by: Northern India Regional Council of ICAI

Date and Time	Venue	
10 <sup>th</sup> and 11 <sup>th</sup> December, 2010 From 9:00 AM to 5:30 PM	NCUI Auditorium, NCUI Convention Centre 3, Khel Gaon Marg, New Delhi	
<b>Day 1: 10<sup>th</sup> December, 2010 (Friday) 9.00 AM to 5.30 PM</b>		
<b>Topics</b>	<b>Speakers</b>	
Issues on Taxation of Capital Gains	Dr. Girish Ahuja	
<ul style="list-style-type: none"> <li>Schemes and Incentives (Non Tax) under Special Tax Friendly Zones</li> <li>Issues in taxation of SEZ &amp; Tax Friendly Zone</li> <li>Issues in Taxation of SEZ Developers</li> </ul>	CA. Ashvin Bhai Dhinal Shah	
Direct Tax Code	Dr. Rakesh Gupta	
<b>Day 2: 11<sup>th</sup> December, 2010 (Saturday) 9.00 AM to 5.30 PM</b>		
Concept of Capital, Revenue & Deferred Revenue Expenditure	CA. Ved Jain	
<ul style="list-style-type: none"> <li>Issues in Section 14A of Income-tax Act</li> <li>Issues on Allowability of Depreciation under Income-tax Act.</li> </ul>	CA. Ajay Wadhwa	
Issues on Cash Credit under Section 68 of Income-tax Act	CA. Ashwani Taneja	
Issues on Assessment under Section 148 of Income-tax Act	CA. Milin Mehta	
Issues on Assessment in case of Search/Requisition under Section 153A of Income-tax Act	CA. Sanjay Kumar Agarwal	

<b>Participation Fee:</b> Members : ₹1200/- (Registration before 30.11.10) Non-Members (Corporate Delegates) : ₹2000/- (Registration before 30.11.10) On-spot Registration for Members: ₹1500/- On-spot Registration for Non-Members (Corporate Delegates ₹2500/-) No Participation Fee for All Study Group Members of NIRC of ICAI
<b>For Registration and Further Details</b>
Members may enrol/register themselves by writing a simple application on plain paper identifying their name, membership No., mobile No., e-mail id and address of communication or download the registration form from <a href="http://www.nirc-icai.org">www.nirc-icai.org</a> and forward the same alongwith the participation fee through Cheque/DD, payable at New Delhi in favour of "NIRC of ICAI" at the following address:  Northern India Regional Council of The Institute of Chartered Accountants of India ICAI Bhawan, NIRC, 5 <sup>th</sup> Floor, Annexe Building, Indraprastha Marg New Delhi 110 002 ✉: <a href="mailto:nirc_conference@icai.in">nirc_conference@icai.in</a> ☎: +91-11-3010 0500, 3010 0507, 3010 0524, 98910 44010

CPE

10

Hours

## National Conference : CA Profession – Challenges and Opportunities

Organised by: CPE Committee of ICAI  
 Hosted by: Jaipur Branch of CIRC of ICAI

Date & Time	Venue	
Date : December 30 & 31 Time : 2.00 PM – 7.00 PM on 30.12.2010 9.30 AM – 4.30 PM on 31.12.2010	Birla Auditorium, Jaipur	
<b>Day 1: 30<sup>th</sup> December, 2010</b>		
Technical Sessions	Topics to be discussed	Speakers
2.00 PM – 7.30 PM I Technical Session – Accounting and Reporting	Emerging Issues	CA. Yagnesh Desai, Mumbai
	Auditing and Assurance Standards	CA. P. Rajendra Kumar, Chennai
<b>Day 2: 31<sup>st</sup> December, 2010</b>		
9.30 AM – 12.30 PM II Technical Session – Taxation	Direct Tax	CA Padam Khincha, Bangalore#
	Indirect Tax	CA. Madhukar Narayan Hiregange, Bangalore
1.30 PM – 4.30 PM III Technical Session – Personal Development & IT	Alternate dispute Resolution	CA. Pawan Sharma, Guwahati (Past Council Member)
	e-environment	CA. B C Chechani, Mumbai CEO, Hazel Infotech Ltd. (K.Doc)
#Consent Awaited		
<b>For Registration and further details visit <a href="http://www.icaijaipur.org">www. icaijaipur.org</a> :</b>		
ICAI Bhawan, D-1 Institutional Area, Jhalana Doongri, Jaipur (Rajasthan) ☎: 0141-3044200 / 214 / 3989398 ☎: 9667555213, 9667555220, 9667555215, 9667555211 Fax No. 3044215 Website : <a href="http://icaijaipur.org">icaijaipur.org</a> ; ✉ : <a href="mailto:jaipur@icai.org">jaipur@icai.org</a> ; <a href="mailto:jaipur@icai.in">jaipur@icai.in</a>		

## Non-Receipt of Journal

This is for the information of Members/students/subscribers who fail to receive The Chartered Accountant journal despatched to them either due to unanticipated change of address or postal problems. Please inform the respective Regional Office immediately after you change

the address to ensure regular and timely delivery of journals to you. Other queries and complaints in this regard can also be sent by email at [journal@icai.org](mailto:journal@icai.org) (for members), [eb@icai.org](mailto:eb@icai.org) (for students) or contact at 0120-3986921.

**6 CPE  
Hours**

## NATIONAL SUMMIT ON NETWORKING & CAPACITY BUILDING OF CA FIRMS

**Organised by :**  
Committee for Capacity Building of  
CA Firms & Small and Medium Practitioners

**Hosted by:**  
Western India Regional Council of ICAI

**Do you desire to expand the size of your practice..... ?**

**Are you planning to strengthen the capacity of your Firm.....?**

**Are you looking at expanding your reach to business clients across the Country....?**

If yes, then Networking could be the solution. The expectations of today's users are that of – *'Expertise, Experience & Efficiency'*. Networking enables professionals to provide Multi-location services through a 'Single Window', which is the need of the hour. Networking can expand your business opportunities exponentially and take you to the next orbit of professional practice.

In order to facilitate members to meet, interact & identify partners for forming Networks, the Committee for Capacity Building of CA Firms and Small & Medium Practitioners (CCBCAF&SMP) has organized this unique Networking Summit where like-minded peers may initiate collaborative approach to expand their professional opportunities. It will provide visionary keynote sessions on the practical aspects of capacity building measures and foster a productive networking environment for interested members. Do not miss this opportunity to network, establish connections, exchange ideas and gain knowledge.

### TOPICS OF THE SUMMIT

- ◆ **Need for Capacity Building**
  - Scope, Objective, Deliverables, Advantages, Disadvantages, Opportunities.
- ◆ **Practical aspects of Networking**
  - Scope, Objective, Experience, Success Stories, Do's & Don'ts, Advantages, Disadvantages.
- ◆ **Practical aspects of Merger & Corporate Form of Practice**
  - Scope, Objective, Experience, Success Stories, Do's & Don'ts, Advantages, Disadvantages.
- ◆ **Open Networking Session**
  - Face to Face interaction amongst Members/Firms for Networking & Merger

<b>Day &amp; Date</b>	: Saturday, 22 <sup>nd</sup> January, 2011.
<b>Time</b>	: 9:30A.M. to 5:30P.M.
<b>Venue</b>	: Mumbai
<b>Fees</b>	: Rs. 1000/- per participant.
<b>Program Director</b>	: Chairman, CCBCAF&SMP, ICAI
<b>Program Coordinator</b>	: Secretary-CCBCAF&SMP, ICAI, New Delhi Mobile No.-09350799922 Tel: 0120-3986945-952 E-mail: shivam@icai.in,ccbcaf@icai.org

**\*Participants may visit [www.caconnect.co.in](http://www.caconnect.co.in) to identify firms & members for Networking. Tablespace will be provided in the Summit for one to one meetings among the members.**

CPE  
**6**  
Hours

## Workshop on Capacity Building Measures for CA Firms and New Professional Avenues

Organised by: Committee for Capacity Building of CA Firms and Small & Medium Practitioners  
Hosted by: Baroda Branch of WIRC of ICAI

Date & Time	Venue	
25 <sup>th</sup> December, 2010 8:30 a.m. to 5:30 p.m.	The Auditorium, ICAI Bhawan, Kalali Tandalja Road, Atladra, Baroda 390 012	
<b>Theme:</b>		
With advent of globalization and challenges posed by the liberalization process taking place worldwide, a need is felt for strengthening competencies of CA firms and small practitioners. ICAI's initiative is to enlarge visibility of CA profession and to rejuvenate practice portfolio of Small and Medium Practitioners. ICAI has formed CCBCAF&SMP Committee for popularizing effective union of CA firms by facilitating consolidation through Networking, Mergers and setting up Management Consultancy Services etc. Committee's focus is on enriching SMPs through Capacity Building measures for bringing up world class competency and brand image. This seminar will concentrate on issues & impediments related to capacity building as well as highlight emergent issues of profession.		
<b>Registration of Participants</b>		8:30 AM to 9:30 AM
<b>First Session</b>	Capacity Building Measures-Networking, Merger and Corporate Form of Practice	9:30 AM to 11:00 AM
<b>Second Session</b>	Emerging Areas: <ul style="list-style-type: none"> <li>Compliance on Foreign Corrupt Practice Act (USA) and its impact on Business in India</li> <li>Compliance Laws Safe Harbour Laws viz-viz Indian Cyber Act</li> </ul>	11:30 AM to 1:00 PM
<b>Third Session</b>	Practice Management	2:00 PM to 3:00 PM
<b>Fourth Session</b>	Presentation on K-DOC software supplied by Committee for Capacity Building of CA Firms and Small & Medium Practitioners	3:00 PM to 4:00 PM
<b>Fifth Session</b>	Presentation on e-Secretary software supplied by Committee for Capacity Building of CA Firms and Small & Medium Practitioners	4:30 PM to 5:30 PM
<b>Registration Fees:</b>	Members: ₹550/-, Non-Members: ₹650/-	
<b>For registration and further details, please contact:</b>		
Baroda Branch of WIRC of ICAI, ICAI BHAWAN, Kalali-Tandalja Road, Atladra, BARODA-390012(Gujrat), ☎: (0265) 2680594, Fax: (0265) 2351151, ✉: baroda@icai.org Payment may be made by Cheque / Demand Draft in favour of 'Baroda Branch of WIRC of ICAI'.		

CPE  
**12**  
Hours

## Two Days Workshop on Excellence in Service Tax

Organised by: Committee for Members in Industry of ICAI  
Hosted by: Mathura Branch of CIRC of ICAI

Date & Time	Venue	
17 <sup>th</sup> & 18 <sup>th</sup> December, 2010	Hotel Brijwasi Royal, Mathura	
<b>Day 1: 17<sup>th</sup> December, 2010</b>		
<b>Timing of Sessions</b>	<b>Details</b>	
9:00 AM - 10:00 AM	Registration and Inaugural Session	
<b>Technical Session I</b> 10:00 AM – 12:00 PM	Service Tax: How to decide taxability & classifications.	
<b>Technical Session II</b> 12:00 PM – 13:30 PM	Service Tax: Key Issues on Real Estate Transaction.	
<b>Technical Session III</b> 14:30 PM – 16:00 PM	Other key services.	
<b>Technical Session IV</b> 16:00 PM – 18:00 PM	Exemption Notification – How to decide the scope.	
<b>Day 2: 18<sup>th</sup> December, 2010</b>		
<b>Timing of Sessions</b>	<b>Details</b>	
<b>Technical Session V</b> 10:00 AM – 12:00 PM	How to handle departmental proceedings—Search, Seizure, assessments, ad-judication & appeals proceedings.	
<b>Technical Session VI</b> 12:00 PM – 13:30 PM	Valuation of taxable services.	
<b>Technical Session VII</b> 14:15 PM – 16:45 PM	CENVAT Credit	
16:45 PM – 17:45 PM	Open House and Valedictory Session	
<b>Participation Fees</b>	₹1500/- Cheque (local)/draft in favour of "Mathura branch of CIRC of ICAI" payable at Mathura and sent it to the address given below. <b>Limited Seats, Registration on First Come First Serve Basis.</b>	
<b>Contact Details</b>		
<b>For Registration &amp; further details, please contact</b>	Bohre Ji Ka Bada, Near K. R. Degree College, Bhens Bahora, MATHURA - 281 001 (U. P.) ✉ : mathura@icai.org, ☎: [+91] (565) 2501	

Chairman, CMII

## All About Stress



The word **STRESS** has become a major buzzword in today's fast moving world. Stress is an inevitable part of everyday life for all of us. Anything that causes a change in life gives us stress – Be it good or a bad change. Over the recent years the individual life stress has increased thanks to new technology world. Today, 60 per cent of all work absences are related to stress. Stress has grown to be the most common cause of ill-health in our society. The varied responses to stress are of considerable interest in psychology as well as in everyday life.



**CA. R. S. Sivaraman**

*(The author is a member of the Institute. He can be reached at [eboard@icai.org](mailto:eboard@icai.org))*

### What is stress?

Although we all talk about stress, it often is not clear what stress is really about. Many people consider stress to be something that happens to them, an event such as an injury or a promotion. Others think that stress is what happens to our bodies, minds and behaviours in response to an event, e.g. heart pounding, anxiety, or nail biting. While stress does involve events and our

responses to them, these are not the most important factors. Our thoughts about the situations in which we find ourselves are the critical factors.

### Meaning and Definition

Stress is an individual's physical and mental reaction to environmental demands or pressures. Stress can be defined as the sum of physical and mental responses to an unacceptable disparity between real or imagined

personal experience and personal expectations. In short, *stress is physical or mental pressure*.

### Understanding Stress

To understand stress, we need to look at the events that occur, our thoughts about them, and the way we respond. There are many major events that occur in our lives: moving, leaving school, changing jobs, and experiencing losses. These “life events” can be stress-provoking. We also face many “daily hassles”. These are events that occur routinely. They also contribute to the levels of stress that we experience. Daily hassles include events such as being stuck in traffic, deadlines, conflicts with family members, and dealing with busy city life. Between life events and day-to-day hassles, we are faced with many stress-provoking situations each day. Our attitude towards these situations determines our response.

### Types of Stress

Stress is usually thought of in negative terms. But, there are two types of stress inducers one of which is positive and the other is negative.

**Eustress:** The results of positive events is called as eustress, which is brought about in the event of positive and challenging experiences of success followed by higher expectations. We all need a certain amount of stress to function well (healthy tension). As a positive influence, stress can help compel us to action; it can result in a new awareness and an exciting new perspective.

**Distress:** The results of negative events is called as distress. One gets distressed by disappointments, failures, anger, depression and other negative experiences, which in turn can lead to health problems. Distress becomes harmful when it is too much or when it occurs too often.

Despite the type, stress is additive. If your pet dies and you win in lottery,

**“To understand stress, we need to look at the events that occur, our thoughts about them, and the way we respond. There are many major events that occur in our lives, e.g. moving, leaving school, changing jobs, and experiencing losses. These “life events” can be stress-provoking. We also face many “daily hassles”. These are events that occur routinely. They also contribute to the levels of stress that we experience.”**

one does not cancel the other, both are stressful events.

### Top Negative Stressful Life Events

1. Death of spouse/ close family member
2. Divorce
3. Jail term
4. Personal injury or illness
5. Conflict with family Members
6. Financial Problems
7. Termination of job/unemployment

### Stages of Stress

In response to stressful events, you can experience one, two or all of the following stages:

#### Stage 1: Mobilisation of Energy:

All bodily activity is increased in response to a stressor that is frightening, such as a near road accident. This starts the body’s “fight-flight” reaction, causing the release of adrenalin. You feel your heart pounding and your palms feel sweaty. This is called primary stress.

It can also be the result of a situation where you choose to put yourself under stress, e.g. the night before your wedding. This is called secondary stress.

#### Stage 2: Exhaustion or Consuming Energy:

If there is no escape from Stage 1, the body will begin to release stored

sugars and fats, using up its bodily resources.

#### Stage 3: Draining Energy Stores:

If the stressful situation is not resolved, you may become chronically stressed, e.g. the body’s need for energy resources exceeds its ability to produce them.

### Early Symptoms of Stress

#### (a) Physical Symptoms

- Headaches.
- Blurry eye sights.
- Increase/decrease in appetite.
- Disruption of sleep patterns – Insomnia.
- Stomach disorders.
- Skin rashes.
- Heart palpitations (increased heart rate).
- Muscle tensions.
- Sweating.
- Increased blood pressure.

#### (b) Emotional Symptoms

- Irritability/anger.
- Crying spells/outburst of crying.
- Inability to cope.
- Early awakenings.

#### (c) Psycho-Social Symptoms

- Oppressive loneliness.
- Extreme sensitivity to opinions.
- Dysfunctional relationships.

### Stress Management and Coping with Stress

Stress management encompasses techniques intended to equip a person with effective coping mechanisms for dealing with psychological stress. In the market, there are a lot of books that tell us how to cope with stress. Each of these books offers its own perspective on stress along with various coping techniques. To make the most of the information on coping skills, you need to understand what coping is all about.

Coping is simply a way of short-circuiting the stress cycle: stopping the stress response.



“Stress management encompasses techniques intended to equip a person with effective coping mechanisms for dealing with psychological stress. In the market, there are a lot of books that tell us how to cope with stress. Each of these books offers its own perspective on stress along with various coping techniques. To make the most of the information on coping skills, you need to understand what coping is all about.”

There is no single right way of coping with a given situation. Each of us must figure out what works best for us. What works best will depend, in part, on your coping style.

#### Coping Styles:

There are three main styles in coping stress. None of these styles is better than the other and some people use a mixture of them.

1. **Task-oriented:** Feeling comfort to analyse the situation and taking action to deal directly with the situation.
2. **Emotion-oriented:** Prefer to deal with own feelings and find social supports.
3. **Distraction-oriented:** Use activities or work to take mind off the situation.

#### Ten Ways to Beat Stress

1. **Acknowledgement of stress:** Recognise the presence of stress

in your life. This is the first step towards prevention.

2. **Minor change in life style:** Analyse your life style pattern and make small changes in your work situation or family situation or your routine.
3. **Effective time management:** Use check list and plan your work. Do important work firstly and prioritise the rest of the work.
4. **Use relaxation techniques/methods:** Do Yoga – it makes both body and mind under control.
  - a) Do meditation such as prayer.
  - b) Deep breathing/slow breathing Such as *Pranayama*.
  - c) Getting massage – it will relieve mental and emotional stress.
5. **Proper diet:** Take balanced diet containing fruits, vegetable, whole grains and food containing high proteins and low fats. Avoid

alcohol, tobacco, caffeine, sugar and fat items.

6. **Rest:** Get enough rest and sleep to recharge your batteries.
7. **Self renewal:** Make time for self rejuvenation, viz., sports, dance, music, painting or hobby or vocation.
8. **Exercise everyday:** Go for brisk walk and do exercise regularly. Physical activity is a terrific stress remedy.
9. **Good relationships:** Maintaining good relationships with spouse, family and society.
10. **Fun and laughing:** Make your surrounding fun. Find little things that make you smile and keep them around your home and office. Have some laugh and be with people you enjoy.

#### Professional Help

If stress becomes a chronic pattern, reaching out for help, viz., a doctor or a qualified mental health professional.

#### Prevention

Finally, complete prevention of stress is neither possible nor desirable because stress is an important stimulus of human growth and creativity, as well as an inevitable part of life. In addition, specific strategies for stress prevention vary widely from person to person, depending on the nature and number of the stressors in an individual's life, and the amount of control he or she has over these factors. ■

“Finally, complete prevention of stress is neither possible nor desirable because stress is an important stimulus of human growth and creativity, as well as an inevitable part of life. In addition, specific strategies for stress prevention vary widely from person to person, depending on the nature and number of the stressors in an individual's life, and the amount of control he or she has over these factors.”

# CROSS

## WORD | 054

**ACROSS**

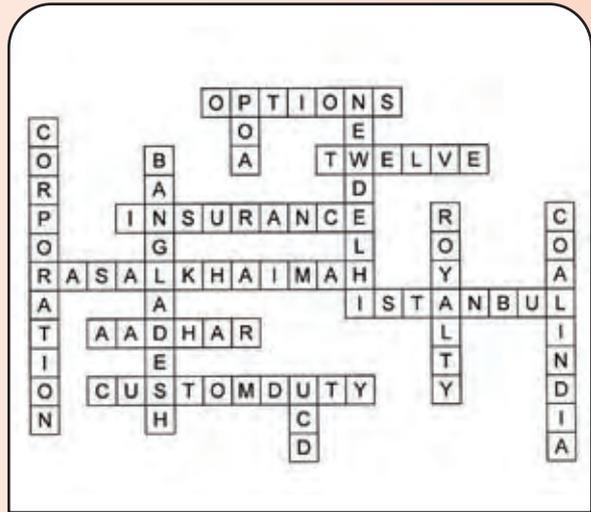
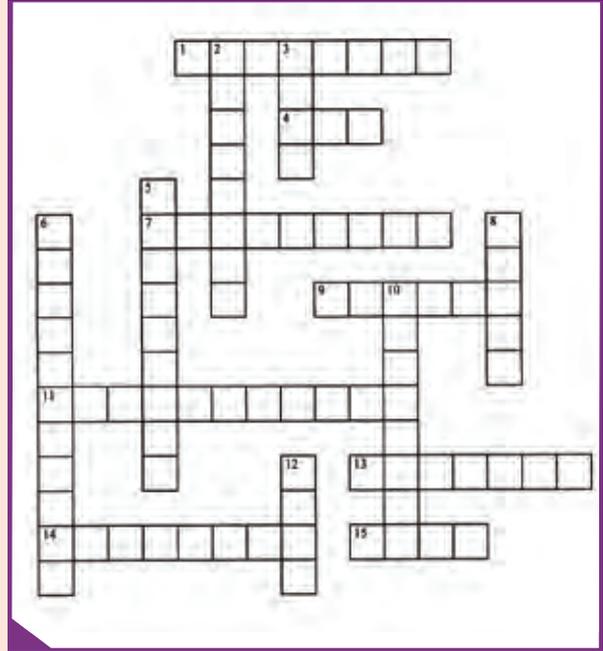
1. A firm, private company or \_\_\_\_\_ company is allowed to convert itself into LLP. (8)
4. The Central Board of Direct Taxes has clarified that the \_\_\_\_\_ are not eligible for deduction under Section 80P of the Income-tax Act, 1961 from the A.Y. 2007-08 onwards.
7. Details of LLP \_\_\_\_\_ are required to be filed within 30 days of the incorporation of LLP. (10)
9. One of the various registrars appointed for the UIDAI project is \_\_\_\_\_ bank. (6)
11. A working group on IAS 41, \_\_\_\_\_ was formed at a recently concluded meeting of the AOSSG held at Tokyo which will be led by ICAI. (11)
13. \_\_\_\_\_ accounting includes the computation of gross wages (hours worked times hourly pay rate) and other compensation such as salaries, employee commissions, and bonuses.
14. ICAI's International Conference on *Accountancy Profession: Catalyst to Sustained Economic Growth* is scheduled to be held on 4<sup>th</sup>-6<sup>th</sup> January, 2011 at \_\_\_\_\_. (3,5)
15. Current limit of FII investment in Government Securities has been increased by US\$ 5 billion and incremental limit may be invested in securities with residual maturity of over \_\_\_\_\_ years. (4)

**DOWN**

2. As per SA 570, negative \_\_\_\_\_ is one of the indicators wherein the 'Going Concern' is at risk. (3,5)
3. The process of implementation of \_\_\_\_\_ converged IND-AS is scheduled to start in India from April 1, 2011.
5. Persons \_\_\_\_\_ the lottery tickets, other than the authorised distributors or selling agents, are exempted from the service tax if the distributor or selling agent avails of optional composition scheme. (9)
6. The \_\_\_\_\_ balance reflected in the accounts is considered as impaired when it is expected that all contractual cash flows would not be recovered.
8. As per IFRIC-13 an entity shall apply paragraph 13 of IAS-18 and account for \_\_\_\_\_ credit as a *separately identifiable component* of the sales transaction(s) in which they are granted. (5)
10. Chairman of Unique Identification Authority of India (UIDAI) is Mr. Nandan \_\_\_\_\_. (8)
12. Every designated partner of a LLP shall obtain a \_\_\_\_\_ by filling Form 7 online.

*Note:*

Members can claim one hour – CPE Credit – Unstructured Learning for attempting this crossword by filling the details in the self-declaration form to be submitted to your regional office annually to avail CPE hours credit for Unstructured learning activities under the activity 'Providing solutions to questionnaires/puzzles available on Web/Professional Journals'. There is no need to individually send this crossword in hard copy or email.



### SOLUTION Crossword 053



**1** A young accountant was interviewed by the owner of a small business, who had built it up from scratch. He said "I need someone with an accounting degree, but mainly I'm looking for someone to do my worrying for me." "What do you mean?" says the accountant. "I have lots of things to worry about, but I want someone else to worry about money matters." "OK," says the accountant. "How much are you offering?" "You can start on seventy-five thousand" says the owner. Seventy-five thousand Rupees! How can a business like this afford me to pay so much? "That," says the man "is your first worry."