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SET UP BY AN ACT OF PARLIAMENT

THE CHARTERED ACCOUNTANT JOURNAL

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

VOLUME 59 | No. 11 | MAY 2011 THE CHARTERED ACCOUNTANT ₹ 100

"The fast increasing tempo of the industrial and economic development of the country makes it imperative that every Chartered Accountant should realise that he belongs to a profession which provides the first line of defence to the unwary public against money grabbers and opportunists. Your responsibility in this matter becomes all the greater because of the autonomy, which your profession enjoys."

First President of India, Dr. Rajendra Prasad, at the inauguration of ICAI headquarters, 1954

The Changing Face of Internal Audit World Over

Internal Auditing has gained so much importance that conducting it has been made mandatory by regulators for listed and other specified companies.

Internal Audit began in modest manner during the Second World War when organisations found it difficult to maintain operational efficiency and control. Companies appointed special staff (i.e. present day internal auditors) to review operations and report to them .The task assigned to internal auditors varied from routine check on finance and operations to appraisal of financial & operational activities.

Earlier, internal audit was largely voluntary and management appointed internal auditors only when they felt the need. With increased complexities in business, frauds and scams, internal audit has become essential for most organisations. Be it SEC in United States or SEBI in India, regulators are prescribing mandatory internal audits. The range of activities undertaken by internal audit teams has increased. They cover a whole gamut of operations ranging from review of finance & operations to providing assurance and consulting services.

Internal Audit is slowly shifting its focus from control-centred approach to a risk-centric approach. A risk-centric approach in addition to catering to the requirements of risk management also provides effective assurance.

In India, Banks, Manufacturing Companies, Depository Participants, Stock Brokers, Insurance companies, Credit Rating Companies, Mutual Funds, Custodians, Registrars and Share Transfer Agents require Internal Audit under regulations governing them.

The IASB of ICAI has issued 17 Standards on Internal Audit that are recommendatory in nature in the initial period. Internal audit to remain a strong source of support to the organisation should in addition to governing compliance with law and standards issued in this regard should redefine its fundamental value proposition.

With organisations' evolving need and rising expectations of management and audit committees, the internal audit teams should cater beyond the fundamental risk and control arena, widening its scope beyond the traditional responsibility of assurance over controls.

Redefinition of the fundamental value proposition of the Internal Audit Function basically depends on various influential factors like globalisation of business opportunities, newly emerging risk factors, increasing expectations from internal auditor, technological advancement in mode of conducting business and growing professional competition among members of the internal audit community in offering better and quality deliverables.

As rightly indicated globalisation of business opportunities opens up newer roles to internal audit professionals. Growth in professional opportunities has gone past geographical boundaries with talented professionals being called for world over.

Given that our world economies are faced with turbulent times, fast changing business models and increasing corporate wrong doings, the internal audit function should become far more effective and efficient to keep the frauds and collusions under check.

An internal audit function is based on three basic parameters namely the scope, need and cost. The audit today should be approached under the premise that the management cannot be expected to be honest. Hence, the auditor, be it internal or external should not be a part of the management, as critical analysis and audit procedures cannot be followed, and that will benefit the organisation as a whole.

A strong internal audit function is about having an efficient and an effective leader who has both in-depth financial knowledge and rounded business experience. The success of any internal audit function lies with ease with which the internal audit team is able to work effectively with others in the organisation, especially the audit committee. It is also important for the audit team to see the issues through to resolution

Traditionally speaking, the functions of risk and internal audit are two different functions, which are conveniently merged posing a clear case of challenge to the Internal Audit leadership skill. A complete transformation is the most effective way of handling the increasing expectations and practical challenges.

One of the greatest challenges for any head of internal audit is attracting the best talent into a function that has not been the preferred destination for aspiring finance professionals. Encouraging highly talented finance executives to participate in internal audit is difficult if you cannot demonstrate that the function commands respect and is a stepping stone to a successful career ahead.

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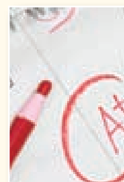

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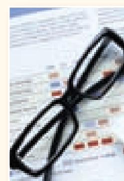

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From the President

Dear friends,

It is heartening and satisfying to observe that we have always ranked *integrity* as one of the most fundamental requirements of our profession. All stakeholders of the profession abide by this fundamental principle. I find it quite apt to recall the example of our first President of India, Bharat Ratna Dr. Rajendra Prasad, also fondly known as *Deshratna,* who had called upon our profession to realise the role of the *first line of defence to the unwary public against money grabbers and opportunists* and asked us to have greater share of responsibilities when he was in ICAI in 1954. That holds importance for us even today. Academically brilliant, a throughout first-class-first, and personally very simple and straightforward, he was often called a common man's President. It is cited that he voluntarily declined to accept his complete monthly salary of ten thousand rupees with a sumptuous allowance of two thousand five hundred rupees, as he found it quite high. He finally brought this down to an acceptable salary of two thousand five hundred rupees. We really need to learn from his simplicity. In fact, Mahatma Gandhi saw his own reflections in him and said: *There is at least one man who would not hesitate to take a cup of poison from my hands.* Mahatma later acknowledged in his autobiography: (Dr. Rajendra Prasad's) *devotion made it impossible for me to take a single step without…*(his)*…help.* Even Jawaharlal Nehru described him as *'Bharat',* and exclaimed once on his strengths: *We often commit mistakes. Our steps falter, our tongues falter and slip. But here is a man who never makes a mistake, whose steps do not falter, whose tongue does not falter or slip and who has no occasion to withdraw what he once said or was undone what he once did.*

Dr. Rajendra Prasad always believed in the purity of means: *In attaining our ideals, our means should be as pure as the end.* I am sure, our members and students will find his instance quite encouraging and inspiring. Let us have faith in his way of attaining ideals. Let us believe in his simplicity.

Let us observe some of the recent significant developments that have a merit to transcend our expectations, and a strength to bring us closer to the high ideals of our profession.

International Initiatives

SAFA Events in Pakistan: I wish to inform that I alongwith the ICAI Vice-President CA. Jaydeep N. Shah, immediate past-President CA. Amarjit Chopra, ICAI Secretary Shri T. Karthikeyan, and Central Council colleagues CA. Sumantra Guha, CA. Pankaj Tyagee, CA. Devaraja Reddy and CA. Abhijit Bandyopadhyay visited Karachi recently to attend the SAFA meetings and ICMAP (Institute of Cost & Management Accountants of Pakistan) International Conference on 'Corporate Finance & Economic Challenges'. CA. Bandyopadhyay presented a paper titled *Corporate Governance – The Foundation for Corporate Citizenship & Sustainable Business at* Conference. We attended various Committee meetings of SAFA. I being the Chairman of the SAFA SMP Committee highlighted some of the important capacity-building measures taken by our Institute for SMPs and offered our complete support to SAFA members in this regard. CA. Jaydeep N. Shah chaired the SAFA Committee on Education, Training and CPD wherein we apprised of various certificate and post-qualification courses offered by the ICAI to its members. We also offered our support to SAFA members in launching such certificate courses in their respective countries. A proposal of an MoU with other accounting bodies of the SAFA region was also discussed.

At the SAFA Board meeting, various committee reports were presented and an emphasis was laid on the byelaws and rules of the SAFA Board, which would be finalised by July 2011. Recognising an increase in number of women in accounting profession, a proposal to establish a women's forum of SAFA was also discussed.

Proposal for MRA with AIA (UK): As you know, we had signed a joint declaration with Association of International Accountants (AIA), established in the UK in 1928 and recognised by its Government for statutory auditors under the Companies Act, 2006. As per one of the clauses contained in the declaration, our Council has recently approved the proposal for entering into a mutual recognition agreement (MRA) with the AIA paving the way for a mutual recognition of qualifications. Since, AIA is a Recognised Qualified Body (RQB) in UK, it has been proposed that our members can benefit if we have a reciprocity arrangements with AIA. As per the MRA, training at both ends shall be recognised fully. While we have stipulated that AIA members will have to pass our five papers, our members are not required to pass any paper of AIA.

Meetings with Government Officials

Meeting with RBI Deputy Governor: I, along with my Central Council colleague CA. Manoj Fadnis, met Shri Anand Sinha, Deputy Governor, RBI, recently to discuss the amortisation of impact of additional pension liability due to wage revision under the 9th Bipartite settlement. We informed him that we would endeavour to take a positive view, when the regulator acted in the light of financial stability and saw how it fitted in overall framework of the Accounting Standards. We also informed that we were working on an announcement regarding the circular already issued by the RBI permitting amortisation of pension liability to new optees in banks to cater to the needs of statutory auditors in this regard and that the proposed treatment would be to consider the regulatory dispensation as a matter of emphasis than as a full-fledged qualification.

Interactive Session with Ministry of Home Affairs: An interactive session with the Joint Secretary, Ministry of Home Affairs, Government of India, was held recently on their invitation. The objectives of interaction were to sensitise chartered accountants about common irregularities/ discrepancies with reference to implementation of Foreign Contribution (Regulation) Act, and about financial, accounting and auditing issues of the not-for-profit organisations (NPO) sector. We made a presentation on

the basics of accounting for the NPO sector to follow, which was appreciated by all.

Developments in IFRS Convergence

Our Central Council colleague and Chairman Accounting Standards Board CA. Manoj Fadnis attended the National Standard Setters (NSS) meeting along with Secretary, Accounting Standards Board, Dr. Avinash Chander, in New York recently, where issues regarding the IAS 41 on *Agriculture* were discussed. India explained the current status of the Working Group of AOSSG on Agriculture. An approach (revision) paper on IAS 41, *Agriculture* is ready for comments. A meeting has already been scheduled at Mahatma Phule Krishi Vidyapeeth, Rahuri. Issue regarding rate-regulated activities was also raised, as the Ministry of Corporate Affairs, Government of India, had requested us to prepare a guidance note on Accounting for Rate Regulated Entities. In a separate discussion, the Indian concerns were discussed with representatives from Canada and the concerned IASB officials whereat it was agreed to share our attempt to issue the Guidance.

In the recently-held Foreign Exchange Working Group meeting, revision of the IAS 21, *The Effects of Changes in Foreign Exchange Rates,* was considered, and current Indian accounting requirement of deferring exchange differences on translating long term monetary items at current exchange rate was also discussed.

Groups Formed to Identify Issues and Formulate FAQs: A Group has been constituted to identify indirect taxes issues arising out of implementation of Indian Accounting Standards converged with IFRS (Ind ASs). Study Groups were also constituted to formulate Frequently Asked Questions (FAQs) on 12 Indian Accounting Standards to help our members and other stakeholder in the convergence process. Till date, draft FAQs have been received on two Indian Accounting Standards, namely, Ind AS 101, *First-time Adoption of Indian Accounting Standards, and Ind AS 1, Presentation of Financial Statements,* which will be finalised shortly.

Initiatives for Government

Uniform Accounting/Auditing Framework for Political Parties: Towards our initiative to help our Government, we had prepared a report on *Uniform Accounting & Auditing Framework for Political Parties* covering, *inter alia,* applicability of Accounting Standards, and uniform formats of financial statements and applicability of Standards on Auditing, issued by the ICAI to the political parties, etc. After a discussion with the Election Commission of India, the revised draft, based on its suggestions, has been recently approved by our Council.

Special Group on MPLAD Scheme: I wish to inform all of you that a special group had been reconstituted recently under the convenorship of our Central Council colleague CA. Jayant Gokhale to study the Guidelines of Members of Parliament Local Area Development (MPLAD) Scheme of the Central Government. The purpose of this constitution is to recommend areas for improvement with regard to

accounts and audit part in the scheme. The Group has finalised its recommendations which would be likely to be discussed in the *Rajya Sabha* Secretariat in a meeting scheduled to take place in the last week of April.

Technical Guide for Telecom Operators: A project to provide guidance on some complex accounting issues arising out of recognition of revenue of Telecom Operators by means of bringing out a *Technical Guide on Revenue Recognition of Telecom Operators* has been undertaken as part of our research initiative. An exposure draft of the above mentioned Technical Guide was hosted on the Institute website as well as sent to major telecom companies for comments. Ministry of Telecommunication while sending its comments on the draft, has expressed its wish to associate itself in the formulation of the Guide citing concerns from the regulatory point of view.

Accordingly, on invitation of the Department of Telecommunication (DoT), an ICAI group had discussions with Ms. Sadhna Dikshit, Advisor (Finance), and Shri Saurabh Kumar Tiwari, Deputy Director General (Licensing & Finance-II), and other officials of the DoT, on the concerns of the DoT and how to address the issues requiring guidance in the proposed Guide. It was decided that the DoT would send us their additional comments after further internal discussions by April 2011. Thereafter, the revised draft of the Guide will again be discussed with the DoT.

Suggestions to Ministry of Home Affairs: Our comments/suggestions on the Draft Foreign Contribution (Regulation) Rules, 2011 have been submitted to the Ministry of Home Affairs, Government of India, as the Ministry had invited our comments/suggestions on the Draft from the general public and stakeholders.

Submission of Post-Budget Memoranda, 2011: This is to inform all that Post-Budget Memoranda, 2011 on Direct Taxes and Indirect Taxes have been finalised and submitted to the Ministry of Finance, Government of India. It is a matter of pleasure that that two of our suggestions contained in Post-Budget memorandum relating to direct taxes have been accepted. The suggestions so considered and accepted have been hosted on the Institute website. Similarly, on Indirect Taxes, important suggestions have been accepted by the Government. The most significant of which was with respect to Point of Taxation Rules, 2011 where chartered accountants have been allowed to pay service tax on receipt basis as per our suggestions. To apprise the profession with this development, a note carrying all significant changes made in service tax, particularly Point of Taxation Rules, 2011, was prepared and hosted on the Institute website. It has also been sent to the registrants of *IDT Net*, a networking portal for members practising in indirect taxes.

Professional Opportunities

Filing Statements in XBRL and Implications: As you may be aware that the Ministry of Corporate Affairs has released a circular mandating certain class of companies in phase one for filing financial statements for the year ending 31st March, 2011, in XBRL formats, creating a new professional opportunity for all members, as we can help our clients in tagging the financial statements with the taxonomy and filing the instance documents so created with the MCA. Though the circular covers only a small class of companies, it is expected that some more will be covered in the next phase and eventually all companies will come under it, thereby giving an opportunity to professionals for XBRL filings for all its clients. Training programmes for the purpose shall be organised by the Institute, where XBRL India will provide the technical inputs, and the training schedule will be hosted on the Institute website. I am sure that our members will take the circular in right spirit and prepare themselves for such opportunities.

DISA Holder to Conduct System Audit: I am pleased to inform all members of the profession that the RBI vide its recent circular relating to submission of system audit reports has allowed a holder of a *Diploma in Information System Audit* (DISA) of the ICAI to conduct system audit of Authorised Payment System Operators and Entities, apart from a Certified Information Systems Auditor (CISA) and registered with Information Systems Audit and Control Association (ISACA).

"Partnership" in the CA Act, 1949, CWA Act, 1959 and CS Act, 1980: I wish to inform members of the profession that the Ministry of Corporate Affairs has issued a general circular dated 4th April, 2011, clarifying that the word "partnership" wherever occurring in the Chartered Accountants Act, 1949, the Cost and Works Accountants Act, 1959 and the Company Secretaries Act, 1980 shall *mutatis mutandis* be construed as including those limited liability partnerships (LLPs) where all the other partners are natural persons (individuals) and that the word "partner" shall also be construed accordingly. The matter was considered by the Council recently and, you will be pleased to note that it has been decided to allow all existing CA firms to convert themselves into LLPs, which would enable CA firms to grow bigger and increase their capacity. A much-awaited proposal, it has also been decided that, upon conversion, firms will be permitted to retain their seniority and all benefits of merger, networking, etc., will be available to the LLPs. We will soon bring out a format for making an application for conversion to an LLP. Thus, small and medium firms may enhance their capacities by including personnel with multidisciplinary competency, and grow big.

ICAI-CBEC MoU: As you are aware that, in the year 2010, we have entered into an MoU with the CBEC to facilitate setting up of the certified facilitation centres (CFC) by the chartered accountants in practice under the ACES Project of CBEC, which can upload returns and other documents for central excise and service tax assessees. I am pleased to inform you that the scheme has been renewed through an extension agreement for a further period of two years. Till recently, more than 600 CFCs have been registered under the ACES project. A list of our CFCs registered with ACES has been hosted on our website.

Capacity Building Measures

Portals for SMPs would be a Reality: I am happy to acknowledge before the members of our profession that necessary steps have been taken to create a website where small and medium practitioners may create their portals as per the norms laid down by the Council of the Institute. Thus, all CA firms will be able to upload details of their firms on the proposed website from their end and it shall also provide them an opportunity to reach out to the international practitioners. It has also been initiated to arrange for e-library, knowledge portal (including blogs, discussion forums, etc.), CA net-book facility, downloadable resources for reference including software for office management for members and firms. I sincerely hope that this would be helpful in enhancing the knowledge base of the members in practice.

Recommended Fee Structure on Professional Assignments: I am pleased to inform you that the Council has considered the Minimum Recommended Scale of Fees for professional assignments done by our members, which is about the fee as per the work performed for various professional assignments and the amount quoted under respective heads of professional work. The fee has been recommended separately for metros and non-metros. I am sure that the prescribed fee will enhance the productivity and capacity-building of practitioners and CA firms and benefit largely the SMP segment.

Benevolent Measures for the Profession: To strengthen the competence of members and firms, we have initiated IT measures to empower them by providing tax-solution software with initial license free of cost for two years. Such a technological empowerment will eventually

help our members in efficient documentation and knowledge and contact management and enable them in strengthening their practices in the field of taxation and audit.

Other Important Initiatives

Members in Industry Outreach Programme: I am pleased to inform the profession that the first Members in Industry Outreach Programme was organised at the GMR Group Corporate Office in Bangalore, where I, along with my Central Council colleague CA. K. Raghu, had the opportunity to interact with our members on issues concerning the profession. We also met the Chairman of GMR Group, Shri G. Mallikarjuna Rao, and discussed with him about the Institute and its initiatives. This programme was held to bring our members in industry closer to the Institute by enhancing interactions between the Institute and those members on matters of professional interest and by encouraging senior members to renew their membership and newly-qualified professionals to apply for membership. Such outreach programmes will also help us in understanding the expectations of the members in industry. At least, 25 such programmes would be conducted across the country. Corporates having more than 50 chartered accountants will be picked out and requested to conduct these programmes.

Launch of ICAI Web TV: It is a matter of pride and happiness for me to launch the ICAI Web TV, which will host educational videos to enable our members in industry as well as others to watch lectures of eminent speakers on their computers and mobile phones at their convenience. The idea behind this exercise is to help those members, who usually find it difficult to participate in professional programmes of the Institute due to their professional pressure and commitments. It will also cast important events of the Institute live including *webinars,* i.e. web-seminars, and enable those members in participation.

Successful Campus Placement (February-March 2011): I am really happy to inform all our students and newly-qualified chartered accountants that the response to campus placement programme during February-March 2011 has been excellent. Sort of history was created, as against the registration of more than 5,000 candidates, 1,863 candidates, i.e. more than one third of the registered, got the offer. A record number of 223 interview teams participated. Banking industry was the largest recruiter this year and ICICI Bank topped the list of recruiters by appointing 337 candidates.

Directives to POUs regarding CPE Programme: Continuing Professional Education (CPE) programmes, conducted by the Institute, are an integral part of chartered accountants' lifelong learning required to maintain standards of excellence in their professional services. Our Institute has been providing continual inputs to its members through seminars, lectures, workshops, background material, etc., with the help of all its Branches and Regional Councils. Recently, a communication has been sent to all programme organising units (POUs) as well as to all Non-Standing Committees with a request to follow the set of existing CPE guidelines in letter and spirit, that includes adherence of CPE programmes to the announced schedule, starting the programmes with technical sessions instead of introductions, presenting mementos in the form of technical/professional books, hosting of details on CPE programmes at least three days in advance and so on. CPE calendar for 2011-2012 has been hosted on the Institute website for the information of members and POUs.

Vision 2030 Document: A group has been constituted for the project of preparation and development of *Vision 2030* and action plan for the next two years, as desired by the Ministry of Corporate Affairs. Another group was constituted to study various reports and key regulatory developments for formulating our strategy to promote the interest of profession, which could be a part of Vision document.

Interactive Meeting with Chairmen and Heads of ICAI Regional Councils: Recently a meeting of the Chairmen of all Regional Councils and Heads of all Regional Offices of the ICAI was held with the ICAI leaders, i.e. President and Vice-President, at the ICAI headquarters in New Delhi. Issues such as CPE programmes, XBRL, infrastructure, services to our members and students, branch accounts reconciliation, other pending matters etc., were discussed in the meeting. There was also a presentation on vision for the year ahead for collecting inputs from other participants. All the participants gave assurance to cooperate in all endeavour of the Institute.

Appellate Authority is Functional: As all members of the profession are aware, the Appellate Authority under Section 22A(1) of the Chartered Accountants Act, 1949 was constituted by the Central Government in March, 2009, but the same was not functional, as the Chairperson of the Authority had not taken charge. Recently, Justice Shri S. N. Dhingra (Retd.) has been appointed by the Government as the Chairperson. I had the opportunity to call on him recently. At this meeting, we discussed the action plan to operationalise the Appellate Authority, and infrastructure requirements for the same. Shri Dhingra along with the representatives of all the three Instiutes would meet the MCA Secretary where it would be, *inter-alia,* proposed to request for an office space for the Appellate Authority that is currently housed in the ICAI headquarters in New Delhi.

C&AG Consideration of Criteria in Empanelment: As our profession is aware, the Office of C&AG has notified new norms of empanelment this year. Despite our efforts, the C&AG Office informed that it was not possible to defer the present empanelment norms this year. However, it has agreed to have a re-look at the criteria in respect of compensation payable to a partner either on percentage or on an absolute basis. I am pleased to inform you that the C&AG Office has extended the date for filing of documents to 30th April 30 from 25th April, 2011.

From the President

ICAI Nominates on RBI's Working Group on Concurrent Audit System: Recently, the Reserve Bank of India has constituted the *Working Group on Concurrent Audit System in Commercial Banks.* On a request received from the RBI, we have sent our nomination to the RBI on the Group on Concurrent Audit.

Certificate Course on Internal Audit: Despite being given to work in multi disciplinary internal audit teams, chartered accountants have created a *niche* of their own in that area. To maintain the niche in the area of internal audit, a core competence area of chartered accountants, they would require to periodically assess their skills and upgradation requirements. Considering this, a certificate course on Internal Audit has been launched, which will aim at disseminating technical developments among our members and providing practical implementation guidance to them. Further, to provide more focus on the area, three articles have been published on internal audit in this issue.

On Disciplinary Cases: There are around 125 cases pending for enquiry by the Disciplinary Committee under the unamended Act. As of now two hearings by the Disciplinary Committee under Section 21-D have been conducted in New Delhi wherein in 13 cases, Disciplinary Committee has concluded its hearing out of 46 cases fixed for hearing. This month, during the meetings of the Board of Discipline and Disciplinary Committee (under Section 21B), hearing of nine cases were concluded. Besides the above, 23 cases have been disposed off by the Board of Discipline till prima facie stage. Most recently, notices have been issued in 32 reports for consideration before the Council. On the Satyam matter, recently, an order has been passed by the PCAOB and SEC against the audit firm of the company on 5th April, 2011. We have forwarded this order to our Disciplinary Directorate for taking necessary action arising due to this order.

Initiatives for Students

Entry Requirement for CA Course: A Group, under the convenorship of the our Central Council colleague CA. Abhijit Bandyopadhyay has been formed recently with other Central Council colleagues CA. Vinod Jain, CA. Manoj Fadnis, CA. Charanjot Singh Nanda, CA. J. Venkateswarlu, CA. Naveen N.D. Gupta, CA. Nilesh S. Vikamsey, CA. M. Devaraja Reddy, CA. Atul C. Bheda and CA. Mahesh P. Sarda as members to review the *entry requirement* for Chartered Accountancy course and submit its recommendations within a stipulated time to be considered by the Council. I am really pleased to inform you that, after two meetings, draft recommendations on the matter are ready for comments of other competent members of the profession, after which, the recommendations will be brought to the Council for approval.

15-Minute Reading Time allowance CA Students in Examination: In order to bring down stress and anxiety in our students, the Council has taken a decision to allow 15 minutes of reading time to all students during examinations commencing from May 2011 examinations, i.e. students will be given question papers 15 minutes before the scheduled time of commencement of examination to facilitate them with time to go through question papers thoroughly and strategise their answers. All the students will surely benefit from this decision.

Setting up CA Students' Associations: The Council has decided to allow setting up of Chartered Accountants Students' Association at all its branches. Though students association exists at many places, it is the endeavour of the Council to ensure that students' association comes up at all its 126 branches so that the students' activities can go up.

Workshops for Resource Persons Organised regarding Examinations: Two workshops for the resource persons associated with the Institute have been organised with a view to sensitise them for enhancing the quality of valuation of answer books, maintaining timeliness, seeking newer ideas and methodologies for improving the quality of testing process and taking our exams with international benchmark levels. While there were about 350 participants in the workshop for the Northern Region, there were about 550 participants for the Central Region.

Let me take this opportunity to extend my sincere wishes and congratulations to all our stakeholders a great May Day, also known as *International Worker's Day,* as it is a celebration of the spirit, rights and solidarity of workers and employees. Recently while attending a gathering of employees of the Institute, I found their spirit quite inspiring and overwhelming. Instinctively, I felt a presence of tremendous power, which was the result of this unity. It can bring progress to the Institute, as together we can create wonders. I would like to see all stakeholders of the Institute smile, cherish and prosper in unison, as I understand, ultimately this happiness will reflect and bear upon the quality of services to be offered to our members and students, and other associates of the profession.

Poet-reformer, nationalist and iconoclast, *Mahakavi* Subramania Bharathi, is of the opinion: *We shall not look at caste or religion; all human beings in this land - whether they be those who preach the Vedas or who belong to other castes – are one.* Let us believe in the oneness of mankind and its divinity. Such a unity will bring us peace, happiness and prosperity.

Best wishes

CA. G. Ramaswamy
President, ICAI

April 23, 2011

MCA Secretary DK Mittal Stresses Discipline, Globalisation of Indian Accountancy Profession

Secretary, Ministry of Corporate Affairs Mr. D. K. Mittal addressed the Council of ICAI at ICAI Headquarters on 23rd March, 2011. He praised the endeavours and steps that the Indian Accountancy profession and ICAI have taken and the positive role played by them in nation building. He stressed Professional Discipline and the need for Indian accountancy profession to go global and asked the Institute to look to African countries for new opportunities. He hoped that the Institute will continue to contribute in the national and economic growth. During the course of interaction, he agreed that the revised Scheduled VI should be made applicable to all companies whose financial year commences on or after 1st April, 2011. Following are the excerpts of the address of Mr. D. K. Mittal.

"I feel proud and privileged to be here this afternoon to address the Council, the best body, in terms of Corporate Affairs. But when we say best, that is the end of us. Lot of changes and reforms are taking place which pose newer and newer challenges. We need a good number of very able members (Indian CAs) to deal with them independently for the larger good of the nation. If we do not do that, we cannot progress. What we need is an effective framework for growth of the profession. We have to read the time properly and amend ourselves accordingly. And we can of course do it. Just making suggestions and giving ideas is not enough. We have to go deeper into the relevant issues to understand.

We have to always ensure that Indian accountancy profession never compromises on quality. For this the accountancy examination system has be up-to-date and very effective. Indian accountants will have to be highly competent not just in India but also globally. Indian accountancy profession should go global and specifically look towards neighbouring countries, SAARC countries and African countries for newer opportunities. Ministry of Corporate Affairs will be there to support you in that endeavour. But the Council has to decide upon a definite plan in this regard. The moment you decide, you are the Leader, you will be the Leader. Why should we copy the Whites, why should we be so much obsessed with Whites. We want to lead.

You are hearing scams, more and more, some directly or indirectly involving members. My humble submission is that we should have some mechanism to see what is happening; we need to anticipate what is happening and how we can get the information about it. Find the root cause of the problems. Ministry is there to support you.

Discipline is another aspect which is of high importance for your profession. Discipline requires a quick and prompt action. You will have to evolve a mechanism to take prompt action. You will have to meet the requirements of having higher ethics and in the way how you have oversight.

We are all part and parcel of the whole, I mean the Government and the Council. In a democratic set up we should agree on some point and differ on another. If you have an issue, on which final call is to be taken by the Ministry, it should be referred to the Ministry. The finality is always a thing which goes to the Ministry.

The Council must be having a strategy. Then you can always have a two year rolling plan and keep on evolving it. That will give a lot of stability. My submission would be that you are a pioneering organisation and you have huge potential in every sense. We are ready to fight for you. We are standing behind you. ■

Inauguration of Hardyal Library

ICAI President CA. G. Ramaswamy inaugurates Hardyal Library at Mayur Vihar Phase I in New Delhi in presence of ICAI Central Council Member CA. Vinod Jain, NIRC Chairman CA. Rajesh Sharma and other dignitaries. (March 18, 2011)

Meeting with Appellate Tribunal Chairman

ICAI President CA. G. Ramaswamy at a meeting with Justice S.N. Dhingra, Chairman, Appellate Tribunal constituted under the CA Act, 1949 in New Delhi. (March 9, 2011)

Meeting with Secretary, Ministry of Steel

ICAI President CA. G. Ramaswamy with Shri P.K. Mishra, Secretary, Ministry of Steel, during a meeting at New Delhi. (April 1, 2011)

Meeting with Secretary Ministry of Textiles

ICAI President CA. G. Ramaswamy and ICAI Vice President CA. Jaydeep N. Shah in a meeting with Secretary, Ministry of Textiles Ms. Rita Menon at New Delhi. (April 5, 2011)

Seminar on Bank Audit

ICAI President CA. G. Ramaswamy along with ICAI Central Council member CA. K. Raghu and other dignitaries at the seminar on Bank Audit organised in Bangalore. (March 19, 2011)

Outreach Programme

ICAI President CA. G. Ramaswamy and Central Council Member CA. K Raghu with Shri G. M. Rao, Chairman, GMR Group during the Outreach Programme organised at Bangalore. (March 26, 2011)

Member Coordination Meet

ICAI President CA. G. Ramaswamy with the Office Bearers and Members of Coimbatore Branch at the Member Coordination Meet organised by Coimbatore Branch of the ICAI. (March 27, 2011)

Meeting of Society of Auditors

ICAI President CA. G Ramaswamy and ICAI Vice President CA. Jaydeep N. Shah at a meeting organised by Society of Auditors at Chennai. (February 24, 2011)

Programme in Trichur

ICAI President CA. G. Ramaswamy and ICAI Vice President CA. Jaydeep N. Shah with SIRC Chairman CA. K. Shanmukha Sundaram at a felicitation programme organised in Trichur. (April 11, 2011)

Meeting with Chairmen of Regional Councils

ICAI President CA. G. Ramaswamy, ICAI Vice President CA. Jaydeep N. Shah and ICAI Secretary Shri T. Karthikeyan with Chairmen of Regional Councils and Heads of Regional Offices of ICAI during an interactive meeting at ICAI Headquarters in New Delhi. (April 21, 2011)

Felicitation Programme at Jaipur

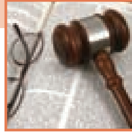
ICAI President CA. G. Ramaswamy with ICAI Central Council Member CA. Vijay Garg and other dignitaries during a felicitation programme in Jaipur. (April 14, 2011)

Visit to Surat Branch

CA. G.Ramasway, President ICAI and CA. Jaydeep N. Shah during their visit to Surat branch. Also seen in the photograph are Central Council members CA. Mahesh P. Sarda and CA. Dhinal Ashwinbhai Shah, and Surat branch Chairman CA.H. Tosniwal. (April 22, 2011)

LEGAL DECISIONS[1]

DIRECT TAXES



Section 2(15) read with Section 12A/12AA of the Income-tax Act, 1961 – Charitable purpose

Activities of promoting micro finance services as permitted from time to time by the Reserve Bank of India, exclusively to large number of poor persons in their villages, towns, etc., for income-generation and thus, to help them and their family to rise out of poverty, not with motive of profit, can be considered to be charitable purpose within meaning of section 2(15)

Disha India Micro Credit v. CIT, January 28, 2011 (ITAT-DEL)

On perusal of the meaning of "relief of the poor" as occurring in section 2(15), it is clear that it encompasses a wide range of objects for the welfare of the economically and socially disadvantaged or needy people. It would include within its ambit, purposes such as relief to destitute, orphans or the handicapped, disadvantaged women or children, small and marginal farmers, indigent artisans or senior citizens in need of aid. Entities who have these objects will continue to be eligible for exemption even if they incidentally carry on a commercial activity, subject, however, to the conditions stipulated under section 11(4A) or the seventh proviso to section 10(23C).

Further, it is not necessary that in order to do public charity, any one association is to be registered as a society or a trust. Therefore, in the present case before us, merely because association is registered as company under section 25 of the Companies Act, that by itself cannot be a ground to refuse registration under sec. 12A/12AA.

The assessee was engaged in activities of promoting micro finance services as permitted from time to time by the Reserve Bank of India, exclusively to large number of poor persons in their villages, towns, etc., for income-generation and thus, to help them and their family to rise out of poverty. The assessee was not providing finance to a particular section of the society. It was providing loan to individual beneficiaries not directly but through some mediator. It was charging minimum rate of interest. Thus, the assessee was providing micro-financial services as per the guidelines given by the Reserve Bank of India. Further, the assesee had made application for financial assistance under micro scheme to Small Industries Development Bank of India, who sanctioned to the assessee a loan not exceeding ₹200 lakh only for financing the project under micro credit scheme with certain conditions and stipulations which had been duly complied with by the assessee. As per the conditions, the loan was to be disbursed in need based instalments and on recommendation of Project Advisory Committee.

It is well settled that when a profit is used towards the achievement of the charitable objects of the trust, it would be considered to be incidental to the achievements of the objects of the trust notwithstanding the profit and gain involved therein. Merely, because there was a surplus from the activity of micro financing, that by itself, could not be a ground to say that the assessee did not exist for charitable purpose particularly when under the Memorandum of Association and Articles of Association, it has been clearly provided that the profit would not be distributed amongst the members but shall be utilised towards its objects, and in the case of dissolution, any property remaining after meeting out the liability would be transferred to the association having similar object. Therefore, the rejection of the registration of trust on this score was also unjustified.

As profit or surplus remaining with the assessee was used for carrying out the objects of the assessee association and it was neither distributed as profit or dividend amongst the members nor accumulated as profits for distribution, it could not be said that the assessee was established with profit motive so as to deny registration under section 12A/12AA.

Section 28(va) of the Income-tax Act, 1961- Business and Professional Income – Sum received/receivable under an agreement

Prior to 1-4-2003, payment under an agreement not to compete, (i.e., negative covenant agreement) was a capital receipt and not a revenue receipt; with effect from 1.4.2003 that said capital receipt is now made taxable

Guffic Chem (P.) Ltd. v. CIT, March 16, 2011 (SC)

The position in law is clear and well settled. There is a dichotomy between receipt of compensation by an assessee for the loss of agency and receipt of compensation attributable to the negative/restrictive covenant. The compensation received for the loss of agency is a revenue receipt whereas the compensation attributable to a negative/restrictive covenant is a capital receipt.

Payment received as non-competition fee under a negative covenant was always treated as a capital receipt till the assessment year 2003-04. It is only vide Finance Act, 2002 with effect from 1.4.2003 that the said capital receipt is now made taxable [*See*: section 28(va)]. The Finance Act, 2002 itself indicates that during period prior to 1-4-2003 compensation received by the assessee under non- competition agreement was a capital receipt, not taxable under the 1961 Act. It became taxable only with effect from 1-4-2003. It is well settled that a liability cannot be created retrospectively. In the present case, compensation received under Non-Competition Agreement became taxable as a capital receipt and not as a revenue receipt by specific legislative mandate vide section 28(va) and that too with effect from 1-4-2003. Hence, the said section 28(va) is amendatory and not clarificatory. Lastly, in *Commissioner of*

[1] *Readers are invited to send their comments on the selection of cases and their utility at eboard@icai.org.*

Income-Tax, Nagpur v. Rai Bahadur Jairam Valji reported in 35 ITR 148 it was held by this Court that if a contract is entered into in the ordinary course of business, any compensation received for its termination (loss of agency) would be a revenue receipt.

Where the agreement entered into by the assessee with one Ranbaxy led to loss of source of business of the assessee; and the payment was received under the negative covenant and, therefore, the receipt of ₹50 lakhs by the assessee from Ranbaxy was in the nature of capital receipt. The Supreme Court held that in fact, in order to put an end to the litigation, Parliament stepped into specifically tax such receipts under non-competition agreement with effect from 1-4-2003. Prior to 1-4-2003, payment under an agreement not to compete (negative covenant agreement) is a capital receipt and not a revenue receipt.

Section 40A(3) read with section 158BH of the Income-tax Act, 1961 and Rule 6DD of the Income-tax Rules, 1962 – Expenses Disallowed – Payment in excess of prescribed limits by cash

Where assessee has not been able to cover its case under Rule 6DD, disallowance under Section 40A(3) can be made in block assessment

CIT v. Sai Metal Works, March 10, 2011 (P&H)

Chapter XIV-B was inserted in the Act by the Finance Act,1995 providing special procedure for undisclosed income found during the search for the block period. The said Chapter lays down special procedure for the assessment and provides for special rate of tax. Section 158BH provides that unless otherwise provided in the said Chapter, all the provisions of the Act are applicable to the assessment under the Chapter. No doubt, the said Chapter contained certain special provisions such as making assessment for block period instead of assessment year, it prescribes higher rate of tax and lays down separate procedure for issuing notice etc. for assessment of undisclosed income as a result of search, section 158BH provides that except the said special provisions all other provisions of the Act apply to assessment under this Chapter. None can accept the agreement in view of section 158BH, this Chapter is a complete Code by itself and except the provisions which are specifically mentioned for their application to the assessment under this Chapter, no other provision could be invoked. In *Commissioner of Income-tax v. Suresh N. Gupta* (2008) 297 ITR 322 (SC), the Supreme Court while considering the said issue in the context of applicability of provision for surcharge to assessment under Chapter XIV-B held that the concept of a charge on the "total income" of the previous year under the 1961 Act is retained even under Chapter XIV-B. Therefore, section 158BB which deals with computation of undisclosed income of the block period has to be read with computation of total income under Chapter IV of the 1961 Act.

If the expenditures which are legally not permissible has been taken into account, the same can certainly be disallowed. Rule 6DD of the Rules allows cash expenditure to be taken into account if circumstances in which the expenditure is incurred can reasonably explained. Where, the assessee has not been able to cover its case under Rule 6DD, the Assessing Officer would be justified in disallowing expenditures incurred in contravention of section 40A(3).

Section 45, read with section 29 of the Income-tax Act, 1961 – Capital Gains – Chargeable as

Merely because shares had been purchased from borrowed funds obtained on high rate of interest would not change nature of transaction from investment to one in nature of an "adventure in nature of trade" [Assessment Year 2001-02]

CIT v. Niraj Amidhar Surti, October 21, 2010 (GUJ)

The assessee, a Chartered Accountant showed professional income as well as income from purchase and sale of shares. Both the Tribunal as well as Commissioner (Appeals) have recorded concurrent findings of fact to the effect that the assessee had disposed of most of the shares held by him after more than a year or two. The assessee had not shown the shares in question as stock in trade. After the shares in question were sold, the assessee made investments under the provisions of section 54BC in the Bonds of NABARD. The profit of purchase and sale of shares or investment in mutual fund was always shown on capital account, that is, capital gains either short term. The same was accepted as such in earlier years.

The Assessing Officer held that the transaction in question was an "adventure in the nature of trade" and not an investment since for the purpose of purchasing the shares in question, the assessee had obtained loan from an investment company on interest at the rate of 30 per cent, which according to the Assessing Officer, was an exorbitant rate.

Another reason for holding that the transaction in question was an "adventure in the nature of trade or business" was that the shares in question were held by an investment company till the entire loan was paid and were initially purchased in the name of an investment company in terms of the agreement between the assessee and an investment company. According to the Assessing Officer, since the assessee had not obtained physical possession of the shares in question at the relevant time, the assessee was not the owner of the shares in question.

The Gujarat High Court held that merely because the shares had been purchased from borrowed funds obtained on high rate of interest would not change the nature of the transaction from investment to one in the nature of an

"adventure in the nature of trade". Where the assessee had held the shares in question for fourteen months, which is a long period for the purpose of long term capital gain and the intention of the assessee had always been that of making investment in shares and not dealing in shares, which was also apparent from the fact that the shares had not been treated as stock in trade by the assessee. Even after the sale of shares, the assessee had made investment in bonds of NABARD, indicating that he had treated the same as long term capital gain; as well as the fact that the assessee had not split the shares in lots but had sold the same in one lot; it was not possible to agree with the contention that the transaction in question was an "adventure in the nature of trade" and therefore, the income derived by the assessee from the said transaction was a business income and could not be treated as capital gain.

Insofar as the second ground for holding the transaction in question to be an adventure in the nature of trade, viz., that the assessee was not the legal owner of the shares and was not having physical possession thereof, was concerned, if the said ground were to be accepted, then, as had been rightly contended on behalf of the assessee, there was no transaction in the hands of the assessee and as such, there was no question of taxing the said transaction merely on the ground that the assessee had offered the same as capital gain. It was nobody's case that delivery of shares allotted was not taken at all. The shares were held by the creditor company as security towards loan advanced to the assessee indicating that the assessee was the owner of shares which were offered and held as security.

It was apparent that both the appellate authorities had recorded concurrent findings of fact which indicated that the relevant factors and circumstances proved therein determine the character of the transaction in question to be one of capital gain and not an adventure in the nature of business or trade. The said findings required no interference.

Section 80HHC read with Section 115JB of the Income-tax Act, 1961 – Deductions – Profits from Export Business

Assessee whose gross total income after setting off business loss and depreciation carried forward from previous years is NIL, is entitled to deduction under section 80HHC in computation of book profit under section 115JB(2)(iv)

CIT v. Packworth Udyog Ltd, November 30, 2010 (KER) (FB)

Assessees are entitled to deduction under section 80HHC computed in accordance with sub-section (3) and (3A) of section 80HHC because it is expressly so provided under clause (iv) of section 115JB(2). The ceiling contained in section 80HHC(1B) is not applicable for the purpose of granting deduction under clause (iv) in the computation of book profit. In the computation of book profit, the eligible deduction of export profit under clause (iv) can not be computed in any other manner other than what is provided in sub-section (3) and (3A) of section 80HHC. What is clearly stated in clause (iv) is that deduction of export profit in the computation of book profit is the same 'amount of profit eligible for deduction under section 80HHC' computed under clause (a) or clause (b) or clause (c) of sub-section (3) or sub-section (3A) of the said section. So much so, computation of export profit has to be done only in accordance with the method provided under section 80HHC which is in fact done in the computation of business profit if the assessment was on the total income computed under the other provisions of Act. MAT assessment is only an alternative scheme of assessment under section 115JB assessee is entitled to deduction of export profit under section 80HHC. In other words, export profit eligible for deduction under section 80HHC is allowable under both the scheme of assessment. So much so, assessees are certainly entitled to deduction under section 80HHC but it is only by following the method provided under sub-section (3) and (3A) of section 80HHC. The restriction contained in section 80AB or section 80B(5) could not be applied inasmuch as carry forward of business loss or depreciation should not be first set-off leaving gross total income nil, which disentitles the assessee for deduction under other provisions of Chapter VIA-C which includes section 80HHC also. The export profit cannot be computed with reference to the Profit and Loss Account prepared under the Companies Act because there is no such provision in section 80HHC to determine export profit with reference to Profit and Loss Account maintained under the Companies Act. Finally, it was to be held that the assessees are entitled to deduction of export profit under section 80HHC and the relief is to be granted in terms of sub-section (3) and (3A).

Section 80HHE read with Section 90 of the Income-tax Act, 1961 – Deductions – Profits from export of Computer Software, etc

A non-resident is entitled to deduction under section 80HHE on same footing as it is available to a resident person in India [Assessments Years 2002-03 too 2004-05]

Shri Rajeev Sureshbhai Gajwani v. Assistant CIT, March 4, 2011 (ITAT-AHD) (SB)

The assessee was a non-resident engaged in export of software and had a permanent establishment in India. The assessee claimed deduction under section 80HHE. The Assessing Officer as well as the Commissioner (Appeals) were of the opinion that deduction available to an Indian company or Indian resident, under section 80HHE, in

respect of export of software out of India, is not available to the non-resident assessee in the light of the express language employed in section 80 HHE which speaks of an Indian company or a person "resident in India".

Section 90(2) provides that where the Central Government has entered into an agreement with the Government of any Country outside India or specified territory outside India for grant of relief of tax or avoidance of double taxation, then in relation to the person to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to the person. In a nutshell, this provision makes it obligatory in respect of a person to whom DTAA applies that the assessment shall be made in accordance to the DTAA, but if any provision of the Act is more beneficial to the person, then he shall be granted benefit under the Act. In common parlance this principle is known as "Treaty Override". What it means is that the assessment of such person shall be made in accordance with the provision contained in the DTAA. However, if any provisions of the Act are found to be more beneficial, then the assessment shall be made in accordance with the provisions contained in the Act. Article 26(2) of the DTAA with USA provides that except where the provisions of Paragraph (3) of Article 7 (business profits) apply, the taxation of a PE of an enterprise of a contracting State in the other contracting State shall not be less favorably levied in that other State contracting than the tax levied on enterprises of that other contracting State carrying on the same activities. The paragraph contains some more provisions regarding deduction on account of civil status etc., which are not relevant to the facts of this case. While interpreting this Paragraph, it is also necessary to examine the contents of Paragraph (3) of Article 7. This paragraph deals with deduction of expenses incurred for the purpose of the business of the PE, including a reasonable allocation of executive and general administrative expenses, research & development expenses, interest and other expenses incurred for the purpose of the enterprise as a whole. On consideration, it is seen that these provisions are not material in so far the facts of our case are concerned because there is no dispute about the computation of income which includes deduction of expenses from the income earned by the PE. In simple language and taking into account the facts of the case, the language employed in the provisions means that taxation of a PE of the USA shall not be less favorable than the taxation of resident enterprise carrying on the same activities.

The wording of Article 26(2) is to the effect that if a US enterprise is carrying on a business in India, it shall not be treated less favorably than an Indian enterprise carrying on the same business for the purpose of taxation. It follows automatically that exemptions and deductions available

to Indian enterprises would also be granted to the US enterprises if they are carrying on the same activities.

The case of the assessee was that the provision contained in section 80HHE is industry specific and the assessee was not precluded in any manner from conducting this business in India. This view is correct as no debate seems to be feasible in this regard. Therefore, it was to be held that the assessee was carrying on the activities of export of software. An Indian Company or any other resident person carrying on the business of export out of India of computer software or its transmission from India to a place outside India by any means is entitled to deduction under section 80HHE. Therefore, the deduction admissible to an Indian company or a person resident in India would be allowable to the assessee also.

Therefore, the assessee is entitled to deduction under section 80 HHE on the same footing as it is available to a resident person in India.

Section 195, read with section 40(a)(i) of the Income-tax Act, 1961 – Deduction of tax at source – Payments to Non-resident

Interest payment made by Indian branch of Dutch Bank to its head office abroad was to be allowed as a deduction in computing profits of branch in India; and in making payment of interest to head office abroad, Indian branch was not required to deduct tax at source under section 195

ABN AMRO Bank, N.V. v. CIT, December 23, 2010 (CAL)

If one is to make an interpretation of the word "assessee" in section 2(7) read with the definition of "person" in Section 2(31), a branch of a company not being an artificial juridical person is not to be taken as a separate assessee/entity. But under Article 5(2) of the convention or agreement defining "permanent establishment" a branch is to be taken as a permanent establishment and if it is further read with Article 7, this permanent establishment or branch is to be treated as a separate unit. Article 7(2) specifically states that it is to be considered as a distinct and separate enterprise and its profits are to be so computed, as profit properly attributable to such a permanent establishment. In the calculation of such profit by banking enterprise interest paid can be taken as a deduction by virtue of Article 7(3), read with Article 11(7).

As far as the remittance of interest is concerned, it cannot be said that the branch or permanent establishment and the head office are one entity. Neither can the permanent establishment nor the branch, and the head office be treated as one entity for the purpose of deduction of tax under section 195(1).

The permanent establishment of the foreign company in India is to be treated as if it were an assessee. The permanent establishment is to be taken as an assessee and the foreign company or the head office is not to be treated as such assessee and the income to be computed accordingly on the above principles of proportionality, in as much as, the above agreement is applied with the Act the foreign company cannot be an assessee. Its assessable income is the assessable income of the branch and the other income or expense which it receives or makes is to be computed separately as attributable to the foreign company, not being such permanent establishment.

Under article 7 read with definition of article 5, the permanent establishment is to be taken as an assessee for the purpose of computation of business profits. Further, under sub-article 3(b) of Article 7, payment of interest can be claimed as a deduction.

Section 195(1) says that, if any interest is paid by a person to a foreign company, which interest is chargeable under the provisions of this Act tax should be deducted at source. The word "chargeable" is not to be taken as qualifying only the phrase "any other sum" only but it qualifies the word "interest" also. This interpretation is supported by the phrase in parenthesis, namely, not being income chargeable under the head "salaries". Therefore, the meaning of section 195(1) is that such interest must be chargeable under the provisions of this Act. To simplify the matter, this interest must be accounted for or credited in the account of some person who is chargeable under the Act. In other words, this remittance of interest must result in an income which is chargeable under the Act. In such circumstances tax may be deducted at source. But where this interest is not so chargeable, no tax is deducted. In this case, by virtue of the above convention, the head office of the appellant was not liable to pay any tax under the Act. Therefore, there was no obligation on the part of the appellant's said branch to deduct tax while making interest remittance to its head office or any other foreign branch.

The permanent establishment and the head office had to be taken as separate entities for all purposes. Therefore, if no tax was deductible under section 195(1)/section 40(a)(i) would not come in the way of the appellant claiming such deduction as from its income. Therefore, in the circumstances the appellant would be entitled to deduct such interest paid, as permitted by the convention or agreement, in the computation of its income.

Section 260A of the Income-tax Act, 1961 – High Court – Appeal to

CIT v. Delhi Race Club Ltd, March 3, 2011 (DEL)

As per the recent guidelines of the CBDT, appeal in those cases where the tax effect is less than Rs. 10 lacs, are not to be entertained and such circular would also apply to pending cases.

Section 260A read with section 208A of the Income-tax Act, 1961 – High Court – Appeal to

Monetary limit laid down vide circular dated 15-5-2008 will apply only to filing of appeals. Appeals already filed and pending prior thereto will be governed by monetary limit laid down at time of filing these appeals prior to date of said circular

CIT v. Varindera Construction Co. Baghapurana, February 4, 2011 (P&H)(FB)

Circular laying down monetary limit controls the filing of the appeals and not their hearing. Appeals filed as per applicable limit at the time of filing cannot be governed by circular applicable at the time of hearing. The object of circular under section 268A is only to govern monetary limit for filing of the appeals. There is no scope for reading the circular as being applicable to pending appeals.

Accordingly, monetary limit laid down vide circular dated 15-5-2008 will apply only to filing of appeals. Appeals already filed and pending prior thereto will be governed by monetary limit laid down at the time of filing.

OTHER ACTS

Companies Act

Section 391/394 read with Section 209A of the Companies Act, 1956 – Power to compromise or make arrangements with creditors and members

Pendency of investigations against a company cannot come in the way of amalgamation in as much as even if the allegations are found to be true, the same will lead only to a report under section 241 and ultimately a prosecution, which would not dilute or affect the scheme of amalgamation

Sesa Industries Ltd. v. Krishna H. Bajaj & Ors, February 10, 2011 (SC)

The Board of the appellant, Sesa Industries Limited (SIL) passed a resolution seeking to amalgamate SIL with Sesa Goa Limited (SGL) and accordingly filed company applications in the High Court seeking permission for convening a general body meeting for the purpose. Krishna Bajaj (KB), holder of 0.29% of the shares in SIL, intervened in these petitions objecting to the amalgamation on the ground that an inspection report under Section 209A, where some alleged malpractices, including siphoning of funds, were highlighted. The Single Judge rejected the objections, and allowed SIL and SGL to convene a general body meeting. The Judge also directed a disclosure to be made to the meeting in respect of the Inspection Report.

Following this, a general body meeting was held, and 99 per cent of the shareholders consented to the scheme. SIL and SGL approached the High Court for sanctioning of the scheme. The Registrar of Companies, Goa, filed an

affidavit stating that he had no objections, subject to the fact that the scheme should not result in any dilution of legal action on the basis of the Inspection Report. The Official Liquidator (OL) also filed a Report [(as required under the second Proviso to Section 394(1)] that the affairs of the company were not being carried out prejudicial to the interest of the members/public.

The Company Judge sanctioned the scheme of amalgamation between SGL and SIL. In his decision, he gave detailed reasons after appreciation of the facts as to why the objections were being rejected, covering inter alia (i) since inspection proceedings under Section 209A of the Act are different from an investigation carried out in terms of Section 235 of the Act, they are not required to be disclosed under the proviso to Section 391 of the Act; (ii) in any event, SIL and SGL have not suppressed any material facts as the letter dated 17th February, 2006 was made part of the individual notices sent to the shareholders; (iii) inspections carried out under Section 209A of the Act cannot come in the way of sanctioning of amalgamation, as they can only result in criminal prosecution of those responsible for contravention of various Sections of the Act; (iv) three years have elapsed since the inspections but the Central Government has not taken any further actions in terms of the inspection reports, which shows that investigations or action in terms of Section 401 of the Act was not in the offing; (v) the Central Government has, through the Regional Director, clarified that the merger would not come in the way of any action to be taken pursuant to the two inspection reports, (vi) non-disclosure of pending criminal complaints is also not fatal to sanctioning of the scheme as the Objector did not raise this contention earlier; pendency of criminal complaints cannot be equated to "material facts" in terms of the proviso to Section 391 of the Act and the merger will have no effect on the criminal complaints; (vii) merely because the Registrar has failed to perform his duties, it cannot be said that the scheme of amalgamation, which has been approved by a majority of the shareholders, should be rejected. The learned Judge also clarified that the sanctioning of the scheme will not come in the way of either civil or criminal proceedings which may be initiated pursuant to the inspection reports as well as further progress of criminal complaints filed by the objector.

This decision was reversed by a Division Bench of Bombay High Court *inter alia* on the grounds that a scheme should not be sanctioned when there was a pending investigation u/s 209A.

Further, the Court stated that there was no affidavit by the Registrar that the affairs of the company were not being carried out in a manner prejudicial to the interests of the members/public; and consequently, the first Proviso to Section 394(1) was not complied with. It held that the OL's report was vitiated, and consequently the second Proviso was not complied with either.

The issue before the Supreme Court was:

> "Whether existence of an investigation report under section 209A or the pendency of an investigation under section 235 was not sufficient grounds for refusing to sanction a scheme which was approved by the general body."

Before the Supreme Court, it was urged by the Appellants that the first Proviso to Section 394(1) applied only to the amalgamation of a company which was being wound up, and not to cases where the prayer in the amalgamation petition was for "dissolution without winding up".

Contrary to this, the Respondents urged that Chapter V of Part VI of the Act was intended to introduce "a system of checks and balances to promote the interests of shareholders, creditors and society at large so as to promote a healthy corporate governance culture, and the Courts should adopt an interpretation that advances this object."

Decision

Pendency of investigations against a company cannot come in the way of amalgamation in as much as even if the allegations are found to be true, the same will lead only to a report under section 241 and ultimately a prosecution, which would not dilute or affect the scheme of amalgamation. A just and equitable scheme of amalgamation cannot be rejected merely because the Official Liquidator had failed in his duty to place the correct position before the Court.

The Court, before whom the scheme is placed, is not expected to put its seal of approval on the scheme merely because the majority of the shareholders have voted in favour of the scheme as it would be binding on the dissenting minority shareholders or creditors also. The

approved scheme of amalgamation will not come in the way of any civil or criminal proceedings which may arise pursuant to the action initiated under Sections 209A or 235 of the Act, or any criminal proceedings.

Reasons

The Supreme Court observed that the court would not act as a court of appeal and sit in judgment over the informed view of the concerned parties to the scheme, as the same is best left to the corporate and commercial wisdom of the parties concerned, yet it is clearly discernible from a conjoint reading of the aforesaid provisions that the Court before whom the scheme is placed, is not expected to put its seal of approval on the scheme merely because the majority of the shareholders have voted in favour of the scheme.

Since the scheme which gets sanctioned by the court would be binding on the dissenting minority shareholders or creditors, the court is obliged to examine the scheme in its proper perspective together with its various manifestations and ramifications with a view to finding out whether the scheme is fair, just and reasonable to the concerned members and is not contrary to any law or public policy.

The Court has to see that the provisions of the Act have been duly complied with; the statutory majority has been acting bona fide and in good faith and are not coercing the minority in order to promote any interest adverse to that of the latter comprising the same class whom they purport to represent and the scheme as a whole is just, fair and reasonable from the point of view of a prudent and reasonable businessman taking a commercial decision.

Subsequently, the Supreme Court confirmed the finding that the OL's report was vitiated.

However, the Supreme Court then considered the issue of whether a lapse by the OL would be sufficient to refuse to sanction a scheme. This – the Court held – was a matter which was to be seen by the Company Judge.

The Court refused to lay down an absolute rule that the vitiation of the OL's report u/s 394(1) would result in vitiation of a scheme of amalgamation. The effect of misdemeanour on the part of the official liquidator on the scheme as such would depend on the facts obtaining in each case and ordinarily the Company Judge should be the final arbiter on that issue.

In the instant case, indubitably, the findings in the report under Section 209A of the Act were placed before the Company Judge, and he had considered the same while sanctioning the scheme of amalgamation. Therefore, in the facts and circumstances of the present case, the Company Judge had, before him, all material facts which had a direct bearing on the sanction of the amalgamation scheme.

On this basis, the Court allowed the appeal, and the order of the Single Judge sanctioning the scheme was restored.

Securities Laws

Regulations 7 and 11 of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 – Acquisition of Five per cent and more shares or voting rights of a company

Where appellants-promoters of company pledged their shares in company with banks as collateral security when a group company availed loan facilities and on default in repayment of loans, pledges were invoked by banks and shares were transferred from demat accounts of appellants to demat accounts of banks and banks were registered as beneficial owners in records of depository and when loan account was settled, banks transferred back shares to appellants by executing DIS but appellants failed in making public announcement to acquire shares of target company, appellants were guilty of violating Regulations 7 and 11(1)

Liquid Holdings Private Limited v. Securities and Exchange Board of India, March 11, 2011 (SAT-MUM)

The appellants-promoters of the company pledged their shares in company with the two banks as collateral security when a group company Morepen availed the loan facilities. When Morepen made default in repayment of the loans, the pledges were invoked by the banks and the shares were transferred from the demat accounts of the appellants to the demat accounts of the banks. Upon the shares being so transferred, the names of the banks came to be recorded as the beneficial owners of those shares in the records of the depository. In the records of the target company as well, the names of the two banks as members of that company were reflected. After acquiring the shares by invoking the pledge, the banks disclosed to all the stock exchanges where the shares of the target company were listed, the aggregate of its shareholding/voting rights in the target company. When the loan account was settled, the banks transferred back the shares to the appellants by executing DIS but appellants failed in making public announcement to acquire shares of target company. The Securities and Exchange Board of India (for short the Board) was of the view that the appellants on acquiring the shares from the two banks ought to have complied with this regulation by making a public announcement to acquire shares of the target company in accordance with the takeover code and not having done so, had violated this provision. The Adjudicating Officer held the appellants guilty of violating Regulations 7 and 11(1) of the Takeovers Regulations and imposed a monetary penalty of ₹3 lacs on each of them.

It was argued by the appellants that the shares throughout remained under pledge even when they were transferred in the name of the banks on the invocation of the pledge and that the banks did not acquire those shares. The argument was that the appellants throughout remained the beneficial owners of the shares and that when

they were transferred back to them by the banks there was no acquisition by them so as to attract the provisions of Regulations 7 and 11 of the takeover code.

The Securities Appellate Tribunal held that as long as the shares remained under pledge, the peldgors (the appellants) were their beneficial owners and the only effect of the pledge was that the shares under pledge could not be transferred any further or dealt with in the market without the concurrence of the pledgees i.e. the banks. The pledge by itself did not bring about any change in the beneficial ownership of the shares pledged and there was no question of the provisions of the takeover code being attracted. On the default being committed in the repayment of the loans, the banks invoked the pledges and got the shares transferred. Upon the banks being recorded as beneficial owners of the shares in the records of the depository, they became members of the target company and they acquired not only the shares but also the voting rights attached thereto. But for the exemption granted to them under Regulation 3(1)(f)(iv) of the takeover code, they would have been required to comply with the provisions of Regulation 11(1) by making a public announcement to acquire further shares of the target company as envisaged therein. The shares acquired by the banks ceased to be the security for the loans as the banks had become the beneficial owners thereof. When Morepen paid the entire loan amounts to the banks and settled the loan accounts and the banks executed DIS requiring their participants to debit their accounts and transfer the shares in the names of the appellants and, accordingly, the shares got transferred from the demat accounts of the banks to the demat accounts of the appellants in the records of the depository, the appellants acquired the shares and became their beneficial owners as their names were entered in the records of the depository. Admittedly, the shares which the appellants acquired after settlement were in excess of the threshold limit(s) prescribed by Regulation 11(1) of the takeover code and, therefore, the said regulation got triggered. The appellants were required to come out with a public announcement to acquire further shares of the target company as envisaged in this Regulation. This was not done. Not only this, the appellants having acquired the shares from the banks were also required to make the necessary disclosures in terms of Regulation 7 of the takeover code to the target company and the stock exchanges where the shares were listed. This, too, was not done. Therefore, the provisions of Regulations 7 and 11(1) stood violated and the adjudicating officer was right in recording a finding to this effect. No fault could, thus, be found with the impugned order, in this regard.

The Depositories Act, 1996 provides for only two categories of owners viz. 'registered owner' who has necessarily to be a depository and a 'beneficial owner' in whom all the rights vest. Once the beneficial ownership

stands transferred to the banks the parties cannot circumvent the legal provisions by entering into an agreement to make a declaration otherwise. The law also prescribes a mode for the creation and revocation of a pledge. The parties cannot agree to create a pledge contrary to the provisions of Regulation 58.

The present was, indeed, a case where the shares had been pledged to secure the loan and on default being made in its repayment, the pledge was invoked. Even the Contract Act entitles the pledgee to invoke the pledge when a default occurs. In the case of shares held in demat form, the Depositories Act and the Regulations framed thereunder provide the manner in which the pledge is to be created and invoked and that procedure was duly followed in the present case. As already noticed, when the pledge was invoked, the banks became the beneficial owners of the shares and thereafter on repayment of the loan the shares were transferred back to the appellants on the basis of an agreement between the parties. The appellants did not get back the shares by redeeming the pledge. If that had been the case, the matter would have been different. There was no merit in the contention that the banks might have become beneficial owners of the shares when they were transferred in their demat account but they had not become the real owners of the shares and they could not have gained title to the said shares in the absence of any consideration. Further, no sale of shares was involved in the present case and, therefore, the Sale of Goods Act would not apply. The Contract Act entitles a pledgee to invoke the pledge in case of default which was what the banks did. Thus, there was no conflict in the provisions of these statutes. Resultantly, there was no merit in the appeal and the same was dismissed.■

CIRCULARS/NOTIFICATIONS

Given below are the important Circulars and Notifications issued by the CBDT, CBEC, MCA, RBI and SEBI during the last month for information and use of members. Readers may use the citation/website or weblink to access the full text of desired circular/notification. You are requested to please submit your feedback and suggestions on the column at eboard@icai.org

DIRECT TAXES

I. Notifications

1. CBDT Notification No.15/2011 dated 18th March 2011

The President of India has, vide this Notification, approved the creation of the Directorate of Income Tax (Expenditure Budget), Central Board of Direct Taxes, Department of Revenue, Ministry of Finance, with immediate effect. The Directorate of Income Tax (Expenditure Budget) will act as the Nodal Authority in respect of all Budget matters for the Grant No.42-Direct Taxes and will perform all work related to the management of Expenditure Budget under this grant.

2. Notification No. 16/2011 dated 29th March, 2011

The Central Board of Direct Taxes, has, through this notification, notified Income-tax (Second Amendment) Rules, 2011 which has come into effect from 1st April, 2011. Through this notification, the following changes have been made:

A. Rule 28AA which deals with *"Certificate of deduction at lower rates or no deduction of tax from income other than dividends"* has been substituted by new Rule 28AA. The provisions of new Rule 28AA are as follows:-

(1) Where the Assessing Officer, on an application made by a person under rule 28(1), of rule is satisfied that existing and estimated tax liability of a person justifies the deduction of tax at lower rate or no deduction of tax, as the case may be, the Assessing Officer shall issue a certificate in accordance with the provisions of sub-section 197(1) for deduction of tax at such lower rate or no deduction of tax.

(2) The Assessing Officer shall determine the existing and estimated liability after taking into consideration the following:-
 (i) tax payable on estimated income of the previous year relevant to the assessment year;
 (ii) tax payable on the assessed or returned income, as the case may be, of the last three previous years;
 (iii) existing liability under the Income-tax Act,1961 and Wealth-tax Act,1957;
 (iv) advance tax payment for the assessment year relevant to the previous year till the date of making application under sub-rule (1) of rule 28;
 (v) tax deducted at source for the assessment year relevant to the previous year till the date of making application under sub-rule (1) of rule 28; and
 (vi) tax collected at source for the assessment year relevant to the previous year till the date of making application under sub-rule (1) of rule 28.

(3) The certificate shall be valid for such period of the previous year as may be specified in the certificate, unless it is cancelled by the Assessing Officer at any time before the expiry of the specified period.

(4) The certificate shall be valid only with regard to the person responsible for deducting the tax and named therein.

(5) The certificate shall be issued direct to the person responsible for deducting the tax under advice to the person who made an application for issue of such certificate."

B. In Rule 31A,which deals with *"Statement of deduction of tax under section sub-section (3) of Section 200"* in sub-rule (4), after clause (iv), the clauses (v) and (vi) have been inserted requiring the deductor to furnish the following particulars at the time of preparing statements of tax deducted at source:-

(i) Particulars of amount paid or credited on which tax was not deducted in view of the issue of certificate of no deduction of tax under section 197 by the Assessing Officer of the payee;

(ii) Particulars of amount paid or credited on which tax was not deducted in view of the compliance of provisions of sub-section (6) of Section 194C by the payee."

C. In Appendix-II, for Form No.13, the new Form No. 13 has been substituted.

3. Notification No. 18/2011 dated 5th April, 2011

The Central Board of Direct Taxes, has, through this notification, notified Income-tax (3rd Amendment) Rules, 2011 which has come into effect from 1st April, 2011.

Through this notification, the CBDT has notified the new return forms for the Assessment year 2011-12. Further, Rule 12 of the Income-tax Rules,1962 has also been amended in respect of the following :-

a. Reference to return of fringe benefits has been deleted.

b. Form Saral-II has been substituted by the Form "SAHAJ"

c. The return of income in case of a person being an individual and HUF deriving business income and such income is computed on presumptive basis under section 44AD and section 44AE to be in Form SUGAM (ITR-4S) and be verified in the manner indicated therein.

The Central Board of Direct Taxes also issued the list of specifications for printing of the SAHAJ and SUGAM Forms.

The complete details of the text of the above-mentioned notifications can be downloaded from the following link: http://law.incometaxindia.gov.in/DIT/Notifications.aspx

II. Circulars

1. Circular No. 1/2011 dated 6th April, 2011

The Central Board of Direct Taxes has through this circular given Explanatory notes to the provisions of the Finance Act, 2010.

The complete details of the text of the circular can be downloaded from the following link http://law.incometaxindia.gov.in/DIT/Circulars.aspx

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

INDIRECT TAXES

A. SERVICE TAX

I. Notifications:

1. **Notification No. 19-21/2011 ST dated 30.03.2011:** Service tax levy on transport of goods by the Government railways and transport of goods by rail otherwise than in containers would be applicable from July 1, 2011 instead of April 1, 2011. Consequently, exemption for transport of notified goods like defence military equipments, railways equipment/materials, postal mail bags by rail etc. and abatement of 70% of the gross amount charged for transport of goods by the Government railways and transport of goods by rail otherwise than in containers would also be effective from July 1, 2011.
2. **Notification No. 22-23/2011 ST dated 31.03.2011:** Second proviso to rule 3(1)(ii) of the Export of Services Rules, 2005 lays down that where management, maintenance or repair service, technical testing and analysis agency's service and technical inspection and certification service provided in relation to any goods or material or any immovable property, as the case may be, situated outside India at the time of provision of service, through internet or an electronic network including a computer network or any other means, then such taxable service, whether or not performed outside India, would be treated as the taxable service performed outside India.

   The said proviso has been amended so as to exclude the technical testing and analysis agency's service from the purview of the said proviso.

   Similarly, the technical testing and analysis agency's service has also been removed from the purview of second proviso to rule 3(ii) of the Taxation of Services (Provided From Outside India and Received in India) Rules, 2006.

3. **Notification No. 24/2011 ST dated 31.03.2011:** Rule 2B of the Service Tax (Determination of Value) Rules, 2006 has been amended to substitute the words "reference rate for that currency for that day" with the words "reference rate for that currency at that time".
4. **Notification No. 25/2011 ST dated 31.03.2011 & Notification No. 28/2011 ST dated 01.04.2011:** Significant amendments have been made in the Point of Taxation Rules, 2011. The major amendments are:

   (I) While the rules shall come into force from 01.04.2011, an option has been given in rule 9 to pay tax on payment basis, as at present, till 30.06.2011.

   (II) Rule 3 has been amended to provide that the point of taxation would be as under:

   (a) Date of invoice or payment, whichever is earlier, if the invoice is issued within the prescribed period of 14 days from the date of completion of the provision of service.

   (b) Date of completion of the provision of service or payment, if the invoice is not issued within the prescribed period as above.

   (III) Date of receipt or payment of consideration would be the point of taxation in the following cases:-

   (a) Services listed in rule 3(1) of the Export of Service Rules, 2005 if the amount is realised within the period prescribed by RBI. However, if the amount is not realised within the specified period, then general rule of completion of service or date of issue of invoice, whichever is earlier would be applicable. If advance is received, to that extent, the date of receipt of advance would become taxable.

   (b) Person liable to pay service tax under reverse charge mechanism (Goods Transport Agency's services, sponsorship services and import of service) provided the payment has been made within a period of 6 months from the date of invoice. However, if the payment is not made within six months from the date of invoice, the general rule as explained above would be applicable. In case of import of services by associated enterprises, date of credit in the books of accounts of the person receiving the service or the date of making payment whichever is earlier would be the point of taxation.

   (c) Individual/proprietor/firms providing the following service:

   (i) Architect's Services
   (ii) Interior Decorator's Services
   (iii) Practicing Chartered Accountant's Services
   (iv) Practicing Cost Accountant's Services
   (v) Practicing Company Secretary's Services
   (vi) Scientific or Technical Consultancy Services
   (vii) Legal Consultancy Services

   (IV) The provision of following services shall be treated as continuous supply of service for the purpose of the Point of Taxation Rules, 2011:-

   (a) Construction in respect of Commercial or Industrial Buildings or Civil Structures

(b) Construction Services of Residential Complexes
(c) Telecommunication Services
(d) Internet Telecommunication Services
(e) Works Contract Services

5. **Notification No. 26/2011 ST dated 31.03.2011:** Service Tax Rules, 1994 have been amended as under:
   (i) The obligation to issue invoice shall be within 14 days of completion of service and not provision of service.
   (ii) If the amount of invoice is renegotiated due to deficient provision or, in any other way is changed in terms of conditions of the contract (e.g. contingent on the happening or non-happening of a future event), the tax will be payable on the revised amount provided the excess amount is either refunded or a suitable credit note is issued to the service receiver. However, concession is not available for bad debts.
   (iii) The composition rate in relation to purchase or sale of foreign currency, including money changing, which was reduced from 0.25% to 0.10% vide *Notification No. 03/2011-ST dated 01.03.2011*, has been changed as follows:-
      (a) 0.1 % of the gross amount of currency exchanged for an amount upto ₹100,000, subject to the minimum amount of ₹25; and
      (b) ₹100 and 0.05 % of the gross amount of currency exchanged for an amount exceeding ₹100,000 and upto ₹10,00,000; and
      (c) ₹550 and 0.01 % of the gross amount of currency exchanged for an amount exceeding ₹10,00,000, subject to maximum amount of ₹5000.

6. **Notification No. 27/2011 ST dated 31.03.2011:** *Notification No 19/2009 ST dated 07.07.2009* exempted the banking and financial services provided to a Scheduled bank, by any other Scheduled bank, in relation to inter-bank transactions of purchase and sale of foreign currency. *Notification No. 27/2011 ST dated 31.03.2011* has amended the said notification so as to exempt such services provided to any bank, including a bank located outside India, or money changer, by any other bank or money changer.

II. Circulars

1. **Circular No. 134 /3 / 2011 – ST dated 08.04.2011:** It has been clarified that where 'whole of service tax' is exempted by virtue of a notification i.e. where service tax is NIL, education cess and secondary and higher education cess would also be Nil.

B. CENTRAL EXCISE

I. Notifications:

1. **Notification No. 08-09/2011-CE (NT) dated 24.03.2011:** Fifth proviso inserted to rule 12(i) of the Central Excise Rules, 2002 provides that where an assessee is availing the exemption under *Notification No. 01/2011-CE dated 01.03.2011* and does not

manufacture any other excisable goods, he shall file a quarterly return of production and removal of goods and other relevant particulars, within ten days after the close of the quarter to which the return relates.
   Further, following provisions, which were earlier applicable to the jewellery falling under heading 7113, have been extended to jewellery or other articles of precious metals falling under heading 7113 or 7114:-
   (i) Rule 12AA(1) of the Central Excise Rules, 2002
   (ii) Definition of manufacturer/producer under rule 2(naa) of the CENVAT Credit Rules, 2004
   (iii) First proviso to rule 4(1) of the CENVAT Credit Rules, 2004

2. **Notification No. 10/2011-CE (NT) dated 24.03.2011:** Every mine engaged in the production/manufacture of goods falling under chapter heading 2701, 2702, 2703, 2704 and 2706 is exempt from obtaining registration where the producer or manufacturer of such goods has a centralised billing or accounting system in respect of such goods produced by different mines and opts for registering only the premises or office from where such centralised billing or accounting is done.

3. **Notification No. 13/2011-CE (NT) dated 24.03.2011:** CENVAT Credit Rules, 2004 have been amended as follows:-
   (i) The CENVAT credit on input services can be availed on receipt of invoice. However, the payment has to be made within three months. This is effective from 01.04.2011 irrespective of the fact that the service provider may continue to pay service tax on receipt basis.
   (ii) In case of service tax paid by the recipient of service on reverse charge basis, the credit can be taken on making payment of the value of service to the service provider and service tax to the Government.
   (iii) If the payment is not made within three months, then the credit availed has to be reversed/paid. However, the same can be taken back as credit on making payment.
   (iv) If subsequent to payment made or invoice received, an amount is received back or credit note is received, when the value of service is renegotiated or altered for any reason the credit availed to that extent is required to be reversed/paid.

(v) Credit on the invoices issued prior to 01.04.2011 by the service provider would continue to be eligible only on payment basis and not on receipt of invoice.

(vi) Supplementary invoice, bill or challan issued by a provider of output service, which should be in terms of the Service Tax Rules, 1994 is also added as one of the documents on which credit can be availed. However, if such invoice is raised by the service provider in cases where such additional amount of tax became payable by him on account of fraud or collusion or wilful mis-statement or suppression of facts or contravention of any of the provisions of the Finance Act or of the rules made thereunder with the intent to evade payment of service tax, then it would not be considered as eligible document for credit.

(vii) As regards to computation of proportionate credit or payment of 5% pertaining to trading goods, the rules have been amended to provide that the value of exempted service will be difference between the sale price and the cost of goods sold (determined as per the generally accepted accounting principles without including the expenses incurred towards their purchase) or 10% of the cost of goods sold, whichever is more.

4. **Notification No. 28/2011-CE dated 24.03.2011:** *Notification No. 8/2003-CE dated 01.03.2003* has been amended to insert an explanation thereby clarifying that "packing material" includes labels.

The complete text of the above-mentioned notifications and circulars can be downloaded from the following link: http://www.cbec.gov.in

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

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FEMA

1. Annual return on Foreign Liabilities and Assets reporting by Indian Companies

RBI/2010-11/427 A.P. (DIR Series) Circular No. 45 dated March 15, 2011

In order to capture the statistics relating to Foreign Direct Investment (FDI), both inward and outward, in a more comprehensive manner the RBI has notified a revised procedure for reporting of all Foreign Direct Investment (FDI), both inward and outward. Accordingly RBI has replaced Part B of the Form FC-GPR (annual filing by Indian companies for foreign investment) by a separate 'Annual Return on Foreign Liabilities and Assets'.

This return should be submitted by all the Indian companies which have received FDI and/or made FDI abroad (i.e. overseas investment) in the previous year(s) including the current year by July 15 of every year along with a copy of audited Balance Sheet for the reporting year. In case accounts are not audited, information should be submitted based on un-audited figures. On completion of audit, if there are major differences in the reported figures, revised return may be submitted along with a copy of audited balance sheet.

For the purposes of this return, the RBI has provided detailed methodology for valuation of foreign liabilities and foreign assets which can be referred in the circular. Details of Foreign Liabilities and Foreign Assets shall be provided separately under separate sections and blocks mentioned in the form. The form is broadly divided into three sections viz. Section I: "Identification Particulars", Section II: "Foreign Liabilities" and Section III: "Foreign Asset".

In case the reporting company is a Group company, a consolidated return covering all the Branches/Offices in India is required to be furnished. RBI has also explained the concepts and definitions useful in filling the Annual Return on Foreign Liabilities and Assets.

The above circular is available on RBI website at http://www.rbi.org.in/scripts/BS_CircularIndexDisplay.aspx?Id=6286

2. Remittance of winding up proceeds of a branch/office

Notification No. G.S.R. 199(E) [NO. FEMA217/2011-RB] January 19, 2011

Presently, the application for remittance of winding up proceeds of a branch/office (other than Project office) in India is required to be made directly to the RBI.

RBI has now amended the Foreign Exchange Management (Remittance of Assets) Regulations, 2000 retrospectively from February 1, 2010 to provide that application for remittance of winding up proceeds of a branch / office (other than Project office) in India supported by the prescribed documents can be made to the concerned Authorised Dealers.

3. Establishing a branch or liaison office in India

Notification No. G.S.R. 200(E) [NO. FEMA218/2011-RB] January 19, 2011

Presently, a person resident outside India desiring to establish a branch or liaison office in India is required to apply to the RBI in Form FNC 1.

RBI has now amended the Foreign Exchange Management (Establishment in India of Branch or Office or other Place of Business) Regulations, 2000 retrospectively from February 1, 2010. It has now been provided that a person resident outside India desiring to establish a branch or liaison office in India shall apply to the RBI through an Authorised Dealer in the prescribed form (Form FNC as

against Form FNC 1). Further application for extension of the validity period of approval shall also be made to the concerned Authorised Dealer.

4. Export of Goods and Software – Realisation and Repatriation of export proceeds – Liberalisation

RBI/2010-11/ 457 A.P. (DIR Series) Circular No. 47 dated March 31, 2011

In consultation with the Government of India, RBI has extended the enhanced period of 12 months for realisation and repatriation to India of the amount representing the full export value of goods or software exported upto September 30, 2011. Accordingly, the enhanced period for realisation of export proceeds will be available in respect of export made till September 30, 2011.

However, the provisions with regard to period of realisation and repatriation to India of the full export value of goods or software exported by a unit situated in a Special Economic Zone (SEZ) as well as exports made to warehouses established outside India remains unchanged.

[Ref: A.P. (DIR Series) Circular No.70 dated June 30, 2009 and A.P. (DIR Series) Circular No.57 dated June 29, 2009]

5. Acquisition of credit card/debit card transactions in India by overseas banks - payments for airline tickets

RBI/2010-11/ 460 A.P. (DIR Series) Circular No. 48 dated April 05, 2011

Airline companies incorporated outside India are permitted to repatriate the surplus arising from sale of air tickets through their agents in India after payment of the local expenses and applicable taxes in India.

However, where the payment for the tickets are made by the residents using credit /debit card, Card Companies have been providing arrangements to the foreign airlines operating in India to select the country and currency of their choice, in respect of transactions arising from the sale of the air tickets in India in Indian Rupees (INR). In such transactions, the overseas bank as the acquiring bank receives the funds from Card Issuing Company in its Vostro account maintained with an Authorised Dealer bank in India or in its foreign currency account maintained abroad and makes the payment in foreign currency overseas to the foreign airline. This practice adopted by foreign airlines is not in conformity with the extant provisions of the Foreign Exchange Management Act, 1999.

Accordingly, RBI has advised the foreign airlines to discontinue immediately the practice of using overseas banks for settlement of INR transactions on account of sale of air tickets in India.

6. Money changing activities

RBI/2010-11/468 & 470 A.P. (DIR Series) Circular No. 49 & 51 A.P. (FL/RL Series) Circular No. 11 & 13 dated April 06, 2011

RBI has vide circular A.P. (DIR Series) Circular No.17 {A.P. (FL/RL Series) Circular No.4} dated November 27, 2009 advised Authorised Persons (APs) to take into account risks arising from the deficiencies in AML/CFT regime of certain jurisdictions, as identified in the Financial Action Task Force (FATF) Statement (www.fatf-gafi.org), issued from time to time.

FATF has issued a further Statement on October 22, 2010 on the captioned subject calling upon jurisdictions listed in the statement to complete the implementation of their action plan within the timeframe and called upon its members to consider the information given in the Statement. The statement divides the strategic AML/CFT deficient jurisdictions into two groups as under:

(a) Jurisdictions subject to FATF call on its members and other jurisdictions to apply countermeasures to protect the international financial system from the ongoing and substantial money laundering and terrorist financing (ML/FT) risks emanating from the jurisdiction : Iran

(b) Jurisdictions with strategic AML/CFT deficiencies that have not committed to an action plan developed with the FATF to address key deficiencies as of October 2010. The FATF calls on its members to consider the risks arising from the deficiencies associated with each jurisdiction: Democratic People's Republic of Korea (DPRK).

Accordingly, APs are advised to take into account risks arising from the deficiencies in AML/CFT regime of these countries, while entering into business relationships and transactions with persons (including legal persons and other financial institutions) from or in these countries/ jurisdictions and are advised to consider the information contained in the above statement.

7. Cross Border Inward Remittance under Money Transfer Service Scheme

RBI/2010-11/469 & 471 A.P. (DIR Series) Circular No. 50 & 52 and A.P. (FL/RL Series) Circular No. 12 & 14 dated April 06, 2011

RBI has vide circular A.P. (DIR Series) Circular No.18 {A.P. (FL/RL Series) Circular No.5} dated November 27, 2009 advised Authorised Persons who are Indian Agents under Money Transfer Service Scheme (APs) to take into account risks arising from the deficiencies in AML/CFT regime of certain jurisdictions, as identified in the Financial Action Task Force (FATF) Statement (www.fatf-gafi.org), issued from time to time.

FATF has issued a further Statement on October 22, 2010 on the captioned subject calling upon jurisdictions

listed in the statement to complete the implementation of their action plan within the timeframe and called upon its members to consider the information given in the Statement. The statement divides the strategic AML/CFT deficient jurisdictions are divided into two groups as under:

(a) Jurisdictions subject to FATF call on its members and other jurisdictions to apply countermeasures to protect the international financial system from the ongoing and substantial money laundering and terrorist financing (ML/FT) risks emanating from the jurisdiction : Iran
(b) Jurisdictions with strategic AML/CFT deficiencies that have not committed to an action plan developed with the FATF to address key deficiencies as of October 2010. The FATF calls on its members to consider the risks arising from the deficiencies associated with each jurisdiction: Democratic People's Republic of Korea (DPRK).

Accordingly, APs are advised to take into account risks arising from the deficiencies in AML/CFT regime of these countries, while entering into business relationships and transactions with persons (including legal persons and other financial institutions) from or in these countries/ jurisdictions and are advised to consider the information contained in the above statement.

8. Overseas forex trading through electronic / internet trading portals

RBI/2010-11/472 A.P. (DIR Series) Circular No. 53 dated April 06, 2011

RBI has observed that overseas foreign exchange trading has been introduced on a number of internet / electronic trading portals luring the residents with offers of guaranteed high returns based on such forex trading. The advertisements by these internet / online portals exhort people to trade in forex by way of paying the initial investment amount in Indian Rupees. Some companies have reportedly engaged agents who personally contact people to undertake forex trading/ investment schemes and entice them with promises of disproportionate / exorbitant returns. Most of the forex trading through these portals are done on a margining basis with huge leverage or on an investment basis, where the returns are based on forex trading. The public is being asked to make the margin payments for such online forex trading transactions through credit cards / deposits in various accounts maintained with banks in India. It is also observed that accounts are being opened in the name of individuals or proprietary concerns at different bank branches for collecting the margin money, investment money, etc.

Accordingly, RBI had clarified vide Press Release 2010-2011/1196 dated February 21, 2011 that remittance in any form towards overseas foreign exchange trading through electronic/internet trading portals is not permitted under the Foreign Exchange Management Act, 1999 (FEMA). It is also clarified that the existing regulations under FEMA do not permit residents to trade in foreign exchange in domestic / overseas markets. Residents are, however, permitted to trade in currency futures and options contracts, traded on the stock exchanges recognised by the Securities and Exchange Board of India in India, subject to the conditions specified by the Reserve Bank from time to time.

RBI has, now, advised Authorised Dealers (ADs) to exercise due caution and be extra vigilant in respect of the above transactions. It is clarified that any person resident in India collecting and effecting / remitting such payments directly / indirectly outside India would make himself/ herself liable to be proceeded against with for contravention of FEMA besides being liable for violation of regulations relating to KYC norms / AML standards.

(Matter on FEMA has been contributed by CA. Manoj Shah and CA. Hinesh Doshi)

CORPORATE LAWS

1. Directions under section 212 for attaching subsidiaries' financial statements – year of applicability

www.mca.gov.in

The MCA has issued General Circular No. 3/2011 dated 21.02.2011 clarifying that the MCA Circular No. 2/2011 dated 08.02.2011 shall be effective in respect of balance sheet and profit and loss accounts prepared regarding the financial year ending on or after March 31, 2011. One may refer to the above website for further details.

2. CRAR requirements for NBFCs

www.rbi.org.in

The RBI has issued Notification No. DNBS.224/CGM (US) - 2011 dated 17.02.2011 stating that under the current dispensation, every deposit taking NBFC shall maintain a minimum capital ratio consisting of Tier I and Tier II capital, which shall not be less than 12% of its aggregate risk weighted assets on balance sheet and of risk adjusted value of off-balance sheet items. However, in terms of paragraph 16 of Non Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank)

Directions, 2007, dated 22.02.2007, every systemically important non-deposit taking NBFC (NBFC-ND-SI) has to maintain a minimum capital ratio consisting of Tier I and Tier II capital, which shall not be less than 15% of its aggregate risk weighted assets on balance sheet and of risk adjusted value of off-balance sheet items by 31.03.2011. The RBI has now decided to align the minimum capital ratio of all deposit taking as well as systemically important non-deposit taking NBFCs to 15%, and hence, all deposit taking NBFCs shall maintain a minimum capital ratio consisting of Tier I and Tier II capital, which shall not be less than 15% of its aggregate risk weighted assets on balance sheet and risk adjusted value of off-balance sheet items w.e.f. 31.03.2012. One may refer to the above website for further details.

3. Companies name availability rules

www.mca.gov.in

The MCA has issued the Companies (Name Availability) Rules, 2011 superseding all previous Circulars and Instructions and has laid down the principles for deciding cases for availability of names. The rules also give an illustrative list of names considered to be undesirable within the meaning of Section 20 of the Companies Act, 1956 has also been given in an Appendix. Regarding minimum authorised capital requirement, the following tabulated dispensation is required to be observed:

S. No.	Key Words	Required authorised capital (in R)
1	Corporation, corp, corpn, corp.	25 crore
2	International, Globe, Global, World, Overseas, Universe, Universal, Continent, Continental, Inter Continental, Asiatic, Asia, Asian being the first word of the name	5 crore
3	If any of the words at (2) above is used within the name (with or without brackets)	2 crore
4	Hindustan, India, Indo, Indian, Bharat, Bharatvarsh, Bhartiya or any other country's name being first word of the name	2 crore
5	If any of the words at (4) above is used within the name (with or without brackets)	25 lakh
6	Industries/ Udyog	5 crore
7	Enterprises, Products, Business, Manufacturing, Venture.	50 lakh

The MCA has evolved the guiding principles for deciding on availability of names and a name which falls within the categories mentioned in the rules will not be generally made available. One may refer to the above website for further details and the format of the annual return.

4. Certification of e-forms under the Companies Act, 1956 by the practicing professionals

www.mca.gov.in

The MCA has issued General Circular No. 14/2011 dated 08.04.2011 in relation to the MCA's steady progress towards total electronic filing and approval regime with the objective of doing away with human intervention in MCA approvals to the maximum extent possible. The MCA states that for this purpose, it has entrusted practicing professionals registered as members of the professional bodies namely, ICAI, ICSI and ICWAI, with the responsibility of ensuring integrity of documents filed by them with MCA in electronic mode. Professionals are now to be responsible for submitting/ certifying documents (to be signed digitally by them) and system would accept most of these documents online without approval by Registrar of Companies or other officers of the Ministry. Hence, to ensure that the data integrity is maintained at all times, there will be checking of such submissions to guard against fraudulent filing. In addition to the penal actions against the companies and their officers in default for furnishing incorrect or false information in the documents as provided under the Companies Act, 1956, action would also be taken on receipt of any complaint, anonymous or otherwise, against such professionals. In case of alleged wrong submissions, a quick enquiry will be conducted by the concerned Regional Director who will be assessing prima facie cases of wrong doing by the professionals and the concerned professionals will be given time for furnishing explanation before conveying to a cancellation. This report will be submitted to e-Governance Cell of MCA which will inform in the concerned professional Institute to initiate an enquiry and complete the same within a month's time. Simultaneously, the concerned professional shall be debarred and shall not be allowed to enter to submit any document on the MCA Portal. This debarment will be for a period of 30 days or till the final enquiry report is received from the respective professional Institute. The MCA will take a final decision after considering the report so received. One may refer to the above citation and website for further details.

5. Director's Relatives (Office or Place of Profit) Amendment Rules, 2011

www.mca.gov.in

The MCA has issued Notification No. F.No.17/75/2011-C.L.V dated 06.04.2011 and enhanced the current limit of ₹50,000/- per month contained in Rule 3 of the Director's Relative (Office or Place of Profit) Rules, 2003 to ₹2,50,000/- per month for payment remuneration to relatives or partners of the directors of the company covered by section 314(1B) of the Companies Act, 1956. Now, companies would be required to obtain prior consent of the company by a special resolution and approval of the Central Government under section 314(1B) of the Companies Act 1956 read with Director's Relative (Office or Place of Profit) Amendment Rules, 2011, for appointment of:

- Partner or relative of a director or manager ; or
- A firm in which such director or manager, or relative of either is a partner; or
- Private company of which such director or manager or relative of either is a director or a member,

to any office or place of profit which carries a monthly remuneration exceeding ₹2,50,000/- per month. The constitution of the selection committee is also redefined under Rule 7 of the Director's Relative (Office or Place of Profit) Amendment Rules, 2011 for the purpose of

appointment of persons mentioned under Section 314 (1B) of the Companies Act, 1956 for listed companies, unlisted public companies and private companies. The selection committee is defined to mean: (a) for listed public companies- a committee, the majority of which consist of independent directors and an expert in the respective field from outside the company, (b) for unlisted public companies- independent directors are not necessary but outside experts must be there, and, (c) for private limited companies- independent directors and outside experts are not necessary to be there. This implies that henceforth, even private limited companies would be required to form selection committee for appointment of persons covered by Section 314 of the Companies Act, 1956. One may refer to the above citation and website for further details.

6. Limitation period for filing an arbitration reference under SEBI regulations

www.sebi.gov.in

The SEBI has issued Circular No. CIR/MRD/DP/04/2011 dated 07.04.2011 and referred to its earlier directions to stock exchanges on limitation period for filing an arbitration reference. To streamline the provisions in depositories on the subject, it is decided that the limitation period for filing an arbitration reference shall be governed by the law of limitation, i.e., The Limitation Act, 1963. The modified limitation period shall also be applicable to cover *inter alia* the following cases:

- where the limitation period (in terms of the Limitation Act, 1963) have not yet elapsed and the parties have not filed for arbitration with the depository, or,
- where the arbitration application was filed but was rejected solely on the ground of delay in filing within the earlier limitation period; and the limitation period (in terms of the Limitation Act, 1963) have not yet elapsed.

One may refer to the above citation and website for further details.

7. Clarification on Easy Exit Scheme (EES)

www.mca.gov.in

The MCA has issued General Circular No. 12/2011 dated 08.04.2011 pursuant to certain proposals received by it for simplification in the procedure of the Easy Exit Scheme (EES), 2011. The proposals have been examined in the Ministry and the revised simplified procedures for dealing with applications under Easy Exit Scheme (EES), 2011 are as under:

REVISED PROCEDURE FOR EASY EXIT SCHEME/ STRIKE OFF U/S.560 OF THE COMPANIES ACT, 1956

Sr. No.	Issue raised in Existing Procedure	Revised procedures to be followed by ROCs
1.	Prosecution if pending has to be compounded or disposed by Court.	If the pending prosecutions are only for non-filing of Annual Returns U/s 159 and Balance Sheets U/s 220 of the Companies Act, 1956 and the company is actually a defunct one as reflected in the Statement of Accounts submitted along with their application under EES Scheme, such application may be accepted., provided the applicants have already filed compounding application or has furnished an undertaking that the compounding application will be filed before closing of EES Scheme. Steps for final strike of the name of the company should be taken only after disposal of compounding application by the competent authority.
2.	How to deal with Companies having assets and liabilities is not specifically discussed in the scheme.	Ministry cannot advise directors and shareholders for waiver of their liabilities and distribution of assets, to the shareholder other then the process provided in the Act. It is for the management of the company to take action, as permissible under law of the land.
3.	Directors should be as per database.	Application with certificates from practicing Chartered Accountants, Cost Accountants and Company Secretaries giving their membership number and certifying that the applicants are present Directors of company can be considered. In such cases, the applicants shall not be asked to file Form 32.
4.	As per the procedure signatories details are checked from the database and sometimes it does not match and needs clarification /documentary evidence in this regard.	Application with certificates from practicing Chartered Accountants, Cost Accountants and Company Secretaries giving their membership number and certifying that the applicants are present Directors of company can be considered.
5.	Indemnity Bond and affidavit needs to be furnished by the directors	Foreign nationals and NRIs have to get their Indemnity Bond and Affidavit notarised as per their respective country's law.

One may refer to the above citation and website for further details.

8. PAN Mandatory for Allotment of Director Identification Number (DIN)

www.mca.gov.in

The MCA has issued General Circular No. 11/2011 dated 08.04.2011 and has stated that it has already simplified the process for obtaining DIN online, if the DIN-1 eform has been digitally signed by the practicing Chartered Accountant, Company Secretary or Cost Accountant, verifying the particulars of the applicants given in the application. However, in other cases, where the DIN form is digitally singed by the applicant only, the applications are being disposed off with in one or two days after examination by the Central Government. Now, as another step towards simplification in allotment of DIN, the Ministry is considering allotting all DIN applications online. To examine the DIN-4

eform through the system, it has been decided that the following fields in the DIN-1 eform will be mandatory :

- Name of Applicant
- Father's name of the Applicant
- Date of Birth
- Income Tax Permanent Account Number (PAN) in case of all Indian Nationals
- Passport in case of all Foreign Nationals.

Currently, the PAN of applicant is not a mandatory field in DIN eform-1. In order to examine DIN-4 eform through the system and to avoid duplicate DIN, it has been decided that all existing DIN holders who have not furnished their PAN earlier at the time of obtaining DIN, are required to furnish their PAN by filing DIN-4 eform by May 31, 2011. One may refer to the above citation and website for further details.

9. Filing of Balance Sheet and Profit and Loss Account in XBRL mode

www.mca.gov.in

The MCA has issued General Circular No. 9/2011 dated 31.03.2011 and has stated that it has decided to mandate certain class of companies to file balance sheets and profit and loss account for the year 2010-11 onwards by using eXtensible Business Reporting Language (XBRL) taxonomy. The financial statements required to be filed in XBRL format would be based upon the taxonomy on XBRL developed for the existing Schedule VI, as per the existing (non converged) Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006. This taxonomy is being hosted on the website of the Ministry at www.mca.gov.in shortly. The Frequently Asked Questions (FAQs) about XBRL have been framed by the Ministry and they are being annexed as Annexure I with the above referred circular for the information and easy understanding of the stakeholders.

All companies that are part of coverage in Phase I would be the following class of companies which will be required to file the financial statements in XBRL form only from the year 2010-2011 :

- All companies listed in India and their subsidiaries, including overseas subsidiaries;
- All companies having a paid up capital of ₹5 crore and above or a turnover of ₹100 crore or above.

All companies covered by Phase-I would be permitted to file upto 30-09-2011 without any additional filing fee.

The MCA has taken care of training requirement for the purpose and has stated that stakeholders desirous to have training on the XBRL or on taxonomy related issues, may contact the persons as mentioned in Annexure II annexed to the above circular. One may refer to the above citation and website for further details.

10. Interpretation of the word "Partnership" for CA / CS / ICWA Act

www.mca.gov.in

The MCA has issued General Circular No. 10/2011 (file No. 17/71/2011-CL-V) dated 04.04.2011 interpreting of the expression "partnership" for the purpose of Chartered Accountants Act,1949, Cost and Works Accountants Act, 1959 and Company Secretaries Act, 1980. In all the three Acts, there is a provision for a member to be in practice when he is inpartnership with certain others. In the case of Chartered Accountants and Cost & Works Accountants, such persons must be member of the same Institute, while in the case of Company Secretaries, it is provided that the partnership could also be with members of such other recognised professions as may be prescribed. It is expressed that at the time of enactment of the three Acts governing the professional Institutes, only one form of partnership existed in India, namely partnerships under Indian Partnership Act, 1932. Subsequently, the Parliament has enacted the Limited Liability Partnerships (LLP) Act, 2008. Though LLPs are bodies corporate under section 3(i) of the LLP Act, though LLPs are basically partnerships may be seen from the definition in section 2(i)(n), ie, "LLP means a partnership formed and registered under this Act". Section 2(i)(q) of the LLP Act defines a 'partner' as "any person who becomes a partner in the LLP in accordance with the LLP Agreement". Hence, LLP is also a partnership and its members are also partners. The MCA has examined this matter and stated that the Acts governing these professionals were passed at a time when LLP did not exist. It is also clear from the definitions in the LLP Act that such entities are also partnerships and their members are also partners. In the context of section 2 of the Acts governing the professional Institutes, this interpretation is also not repugnant to the context. Accordingly, the MCA now clarifies that the expression 'partnership' wherever occurring in the Chartered Accountants Act, 1949, the Cost and Works Accountants Act, 1959 and the Company Secretaries Act, 1980 shall mutatis mutandis be construed as including those LLPs where all the other partners are natural persons (i.e., individuals). The expression 'partner' shall also be construed accordingly. This clarification shall apply only to these three Acts and not to any other enactment where the expression 'partnership' occurs. One may refer to the above citation and website for further details.

11. Submission of system audit reports

www.rbi.org.in

The RBI has earlier issued circulars DPSS. AD.No./1206/02.27.005/2009-2010 dated December 7, 2009 and DPSS.1444/ 06.11.001/ 2010-2011 dated December 27, 2010 on the captioned subject. In partial modification of the instructions contained therein, the RBI vide circular No. DPSS.CO.OSD. No. 2374 /06.11.001/ 2010-2011 dated April 15, 2011 has advised that the system audit may be conducted by

(a) Certified Information Systems Auditor (CISA) and registered with Information Systems Audit and Control Association (ISACA) or

(b) by a holder of a Diploma in Information System Audit (DISA) qualification of the Institute of Chartered Accountants of India (ICAI).

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

■

Revenue recognition where sale value in foreign currency is covered by a forward contract.

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 Limited is a manufacturing company and is listed in Bombay Stock Exchange and National Stock Exchange as a public listed company. The company has domestic sales as well as export sales (physical exports) and the company has the following forex hedging strategy for currency risk:
   (a) The hedged exposures/forecasted cash flows are highly probable because these are always based on signed contracts, sales orders and purchase orders (and not on budgets, intentions, etc.).
   (b) The *hedge documentation* (such as, the forex policy/ procedure, the documentation for each individual hedge, selection of the hedge instruments, etc.) is in place.
   (c) There is always a *one-to-one relation* between the hedged exposure and the hedge instrument (no netting, no clubbing together of hedged items).
   (d) The relation of hedged item versus hedge instrument is *100 per cent effective* and can be measured accordingly.

(Emphasis supplied by the querist.)

2. After entering into an export order, the company takes forward cover for the full amount of the sales invoice which is receivable in US Dollars normally after sixty days. The forward cover is also taken for sixty days.

B. Query

3. In the light of the above, the querist has sought the opinion of the Expert Advisory Committee regarding revenue recognition on the following issues:

(i) The rate at which the sales should be accounted:
   (a) Whether it is the rate on the date of bill of lading, on which date the property in the goods has passed on to the customer as per the contract.
   (b) Whether it is correct to apply the forward contract rate and account the sales at that rate as finally, the company will be realising from the customer at the forward rate on the due date.

(ii) It is assumed that the customer will not fail on the due date for the purpose of the above. If customer fails to pay on the due date what will be the opinion of the Committee.

(iii) Will the company be complying with following accounting standards, if it follows accounting for revenue (sales) at the forward contract rate:
   (a) Accounting Standard (AS) 9, 'Revenue Recognition',
   (b) Accounting Standard (AS) 11, 'Effects of Changes in Foreign Exchange Rates', and
   (c) Accounting Standard (AS) 30, 'Financial Instruments: Recognition and Measurement', AS 31, 'Financial Instruments: Presentation' and AS 32, 'Financial Instruments: Disclosure' dealing with hedge accounting.

C.Points considered by the Committee

4. The Committee notes from the Facts of the Case that the basic issues raised in the query relates to the rate at which sales should be recognised and the treatment to be followed if the customer fails to pay on due date. The Committee has, therefore, considered only these issues and has not touched upon any other issue that may arise from the Facts of the Case, such as, accounting treatment of forward exchange contract taken to hedge the foreign exchange exposure of the sale amount, treatment of changes in foreign exchange rates after initial recognition, etc.

5. The Committee notes paragraph 9 of Accounting Standard (AS) 11, 'The Effects of Changes in Foreign Exchange Rates', which provides as follows:

> ***"9. A foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction."***

From the above, the Committee is of the view that the sales in the instant case should be recorded by applying the exchange rate at the date of the transaction. The transaction

date for the purposes of recognition of revenue would be the date on which the significant risks and rewards of ownership of goods are transferred to the buyer. In this regard, the Committee notes paragraph 6.1 of Accounting Standard (AS) 9, 'Revenue Recognition':

> "6.1 A key criterion for determining when to recognise revenue from a transaction involving the sale of goods is that the seller has transferred the property in the goods to the buyer for a consideration. The transfer of property in goods, in most cases, results in or coincides with the transfer of significant risks and rewards of ownership to the buyer. However, there may be situations where transfer of property in goods does not coincide with the transfer of significant risks and rewards of ownership. Revenue in such situations is recognised at the time of transfer of significant risks and rewards of ownership to the buyer. Such cases may arise where delivery has been delayed through the fault of either the buyer or the seller and the goods are at the risk of the party at fault as regards any loss which might not have occurred but for such fault. Further, sometimes the parties may agree that the risk will pass at a time different from the time when ownership passes."

6. The Committee further notes paragraphs 9.1 to 9.3 of AS 9, which provide as follows:

> "9.1 Recognition of revenue requires that revenue is measurable and that at the time of sale or the rendering of the service it would not be unreasonable to expect ultimate collection.
>
> 9.2 Where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, e.g., for escalation of price, export incentives, interest etc., revenue recognition is postponed to the extent of uncertainty involved. In such cases, it may be appropriate to recognise revenue only when it is reasonably certain that the ultimate collection will be made. Where there is no uncertainty as to ultimate collection, revenue is recognised at the time of sale or rendering of service even though payments are made by instalments.
>
> 9.3 When the uncertainty relating to collectability arises subsequent to the time of sale or the rendering of the service, it is more appropriate to make a separate provision to reflect the uncertainty rather than to adjust the amount of revenue originally recorded."

From the above, the Committee is of the view that revenue should not be recognised unless it is reasonably certain that the ultimate collection of the revenue will be made. However, if the uncertainty relating to collectability arises subsequent to recognition of revenue, a separate provision for the uncertainty should be recognised. In this context, the Committee notes that the impairment of receivables is covered by Accounting Standard (AS) 4, 'Contingencies and Events Occurring After the Balance Sheet Date', which, inter alia, provides as follows:

> ***"10. The amount of a contingent loss should be provided for by a charge in the statement of profit and loss if:***
> ***(a) it is probable that future events will confirm that, after taking into account any related probable recovery, an asset has been impaired or a liability has been incurred as at the balance sheet date, and***
> ***(b) a reasonable estimate of the amount of the resulting loss can be made."***

The Committee notes that an event is regarded as 'probable' if the event is more likely than not to occur, i.e., the probability that the event will occur is greater than the probability that it will not. Thus in case, at the balance sheet date, it is probable that the receivables would not be recovered in future, a provision in that respect should be made as per the provisions of AS 4.

7. As regards the question raised by the querist relating to compliance with AS 9, AS 11, AS 30, AS 31 and AS 32 in case the company records revenue at the forward contract rate, the Committee clarifies that for accounting purposes, the issue of recognition of revenue is independent of the accounting for foreign exchange transactions including hedging. Accounting for sale, i.e., recognition of revenue in the present case would be governed by the provisions of AS 9 as stated in paragraphs 5 and 6 above. Accounting for foreign exchange transactions including hedging is governed by AS 11 and/or AS 30 depending upon the nature of transaction. In the instant case, since the transactions undertaken by the company have been stated by the querist to be highly probable forecast transactions, forward exchange contracts in respect of these transactions can be accounted for as a cash flow hedge considering the provisions of AS 30 as AS 11 does not deal with accounting for forward contracts for such transactions. AS 31 is not relevant in the present case. In case of highly probable forecast transactions, where forward exchange contract is considered as cash flow hedge, the company should make disclosures as per the requirements of AS 32.

D. Opinion

8. On the basis of the above, the Committee is of the following opinion on the issues raised in paragraph 3 above:

(i) The sales should be recognised at the rate on the date of the transaction, i.e., the date on which the significant risks and rewards of ownership of goods have been transferred to the buyer and not at the rate of forward exchange contract, as discussed in paragraph 5 above.

(ii) The revenue should not be recognised unless it is reasonably certain that the ultimate collection of the revenue will be made. However, if the uncertainty relating to collectability arises subsequent to recognition of revenue, a separate provision for the uncertainty should be recognised. Refer to paragraph 6 above.

(iii) If the company accounts for revenue (sales) at forward contract rate, it will not be complying with the requirements of AS 9, AS 11, AS 30 and AS 32. AS 31 is not relevant in the present case. Refer to paragraph 7 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 eac@icai.org .

Know Your Ethics*

Ethical Issues in Question-Answer Form

Q. Can a chartered accountant in practice agree to select and recruit personnel, conduct training programmes and work studies for and on behalf of client?

A. Yes, the 'Management Consultancy and other Services' as specified by the Council includes both, personnel recruitment and conduct of training programmes and work studies. As such, the same are permitted for a chartered accountant in practice.

Q. Whether a member can act as insurance agent and arrange business for the Insurance Companies?

A. No, a member is not permitted to render Insurance Financial Advisory Services. It is not permissible to a member to do any kind of marketing and business procurement for any insurance company. Their services are limited to professional services in the form of advisory and consultancy services.

Q. Can a chartered accountant in practice allow any person to practice in his name as a chartered accountant?

A. No, a chartered accountant in practice is prohibited to allow any person to practice in his name as a chartered accountant unless such person is also a chartered accountant in practice and is in partnership with or employed by him.

Q. Can a chartered accountant in practice secure any professional business through the services of a person who is not his employee or partner?

A. No, the CA Act , 1949 does not permit a practicing chartered accountant from securing, either through the services of a person who is not an employee of such chartered accountant or who is not his partner, any professional business.

Q. Whether a member in practice is permitted to have his name published in Telephone Directory?

A. Yes, a member in practice is permitted to have his name published in the Telephone Directory subject to certain conditions :-

1. The entry should appear in the section/ category of "Chartered Accountants".
2. The member/firm should belong to the town/city in respect of which the directory is being published.
3. The entry should be in normal type of letters. Entry in bolder type or abnormal type of letters or in a box is not permissible.
4. The order of the entries should be alphabetical and logical.
5. The entry should not appear in a manner giving the impression of publicity/advertisement. Entry should not be given in a manner which gives prominence to it as compared to other entries.
6. The payment, if any, for the entry should not be unreasonable.
7. The entries should not be restricted and should be open to all the chartered accountants/firms of chartered accountants in the particular city/town in respect whereof the directory is published.
8. Subject to the above conditions, the members can also include their names in trade directories which are published and/or otherwise available such as electronic media e.g. Internet, telephone services like "Ask Me Services"

Q. Can a member in practice indicate in a book or an article, authored /contributed/published by him, his association with any firm of Chartered Accountants?

A. No, as per CA Act, 1949, a member is not permitted to indicate in a book or an article, authored/contributed/ published by him, his association with any firm of Chartered Accountants.

Q. Can a Chartered Accountant in practice seek professional work from his professional colleagues?

A. Yes, as per CA Act, 1949 a member is permitted to apply or request for, or to invite, or to secure professional work from another Chartered Accountant in practice.

Q. Can a Chartered Accountant in practice accept original professional work emanating from the client introduced to him by another member?

A. No, a Chartered Accountant in practice should not accept the original professional work emanating from a client introduced to him by another member. If any professional work of such client comes to him directly, it should be his duty to ask the client that he should come through the other member dealing generally with his original work.

Q. Can a chartered accountant accept the appointment as Superior Authority by Certifying Authority for processing Digital Signature?

A. Yes, a chartered accountant may accept the appointment as Superior Authority by Certifying Authority for processing Digital Signature.

Q. Whether Code of Ethics will be applicable outside India?

A. The Code of Ethics of the Institute is applicable to all its members even outside India. ■

* Contributed by the Ethical Standards Board of the ICAI

Use of Risk-Based Internal Audit as a Tool for Good Governance of Public Sector Undertakings

The efficiency of every organisation depends on how effectively it is managing the risks and ensuring a competitive return on capital. For this, it is essential to have in place effective risk management and internal control systems, which are crucial to the conduct of business. The internal audit function plays an important role in contributing to the effectiveness of the internal control systems and governance of Public Sector Undertakings (PSUs). The terms good governance and corporate governance are commonly used today. The 1992 World Bank report on "Governance and Development" identified certain aspects of 'Good governance', which became an important criterion for consideration while funding projects. Good governance has been described as an ideal which can be understood as a set of eight characteristics namely, participation, rule of law, transparency, responsiveness, consensus orientation, equity and inclusiveness, effectiveness and efficiency, and accountability. An effective internal audit function is a fundamental component of good governance. Read on to know more.

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The internal auditor should provide the management with accurate information on the effectiveness of the risk management system and the internal controls including regulatory compliance by the company. At present, there are various types of internal audits, which basically adopt the methodology of transaction testing, testing of accuracy and reliability of accounting records and financial reports, integrity, reliability and timeliness of control reports, and adherence to legal and regulatory requirements. However, all these do not provide any opinion on the qualitative dimension of business management including risk management. As such, there is a need for redefining and redirecting the scope of audit so as to

ensure the adoption of modern tools of risk management, adequacy and effectiveness of such tools, as well as to assist the PSUs in mitigating the risks. The paradigm shift in the focus of internal audit can be achieved by modifying the approach towards risk-based audit.

What is Risk Based Internal Audit?

Risk based internal auditing (RBIA) is the methodology which provides assurance that risks are being managed within the organisation's risk appetite. The internal audit function has a major role in risk management and assists in identifying the potential risks, assessing the risk intensity and risk exposure of the organisation, and also provides an objective and independent opinion on the effect of risk response measures, key controls and checking whether the risks of the organisation are managed at tolerable levels or not. In this continuous process of risk management, the Institute of Chartered Accountants of India and the Institute of Internal auditors have issued standards and guidelines regarding the functions of the internal auditor and that of the management. The role and responsibility of RBIA in the risk management of an organisation depends on the risk maturity of the organisation. The risk maturity of an organisation is broadly categorised in five ways depending on its preparedness to deal with the inherent Risks:

- *Risk Enabled*: Wherein the risk management and internal control is fully embedded into the operations.
- *Risk Managed*: Where an enterprise-wide approach to risk management is developed and communicated.
- *Risk Defined*: Where strategies and policies are in place and communicated.
- *Risk Aware*: These are organisations with an unstructured approach to risk management.
- *Risk Naive*: These are the organisations with no formal approach developed for risk management.

In all organisations other than the risk enabled organisations, the internal auditor has to undertake the task of risk assessment. Since the internal auditor has a major role to perform in risk assessment, risk estimation, risk evaluation and risk reporting, the core essentials of RBIA are elaborated further.

a. *Risk Assessment*: The first and foremost requirement in risk management is to identify the potential risks and assess the risk exposure of the organisation. While in risk enabled, mature organisations, these tasks are duly carried out by the management, in most of the other organisations RBIA is entrusted the task of identifying the potential risks and assessing the risk exposure of the organisation. The risk identification should be approached in a methodical way to ensure that all significant activities within the organisation have been identified and all the risks flowing from these activities defined. The process based approach to identify the risks is considered to be very efficient and relatively easy. Under this approach, since the objective of the organisation is delivered through various processes, all processes involved in achieving the organisation's primary objective are identified. Since each process in turn will have a sub-objective, the process and primary objective of the entity is bifurcated into sub-objectives and sub-processes. Under each process, the sub-objective of that process and the corresponding risks, both internal and external which may affect that sub-objective are identified and catalogued. Each risk so identified has to be aligned with the corresponding process and the objective is to facilitate formulation of auditable units and audit plans subsequently.

b. *Risk Register*: In order to manage risk, an organisation needs to know what risks it faces, and to evaluate them. Identifying risks is the first step in building the organisation's risk profile. There is no single right way to document an organisation's risk profile, but documentation is critical to effective management of risk. Though there is no standard format for the risk register, it should contain all the potential risks of an organisation with reference to each process, its perceived impact on the achievement of the objectives and its probability of occurrence. The risk register will be useful for the internal auditors to prioritise

"In an ideal risk management system in PSUs, the organisation should have a risk management strategy designed to achieve the objectives of the organisation and manage the risks. The role and responsibilities of RBIA in the organisation's risk management should be enshrined in the organisation strategy. The application of that strategy should be embedded into the organisation's business processes, systems and policy setting, to ensure that risk management is an intrinsic part of the way business is conducted. Successful implementation of RBIA in PSUs in India is a challenging task and fraught with certain organisational, functional and cultural impediments."

the potential risks with reference to its consequence, impact and the probability of its occurrence and prepare their audit plans accordingly.

c. *Risk & Audit Universe (RAU)*: Grouping the risks and corresponding processes into audit units is called the Risk Audit Universe (RAU). The RAU contains the risks that the management and internal auditors have identified, their score, the auditable entities with reference to the risk and process, the owner of the risk, details of the audit that is responsible for providing an opinion on the management of each risk, details of the previous and subsequent audits, details of controls managing the risk etc. The RAU provides a macro picture of the issues and activities involved and will help in drafting the audit plans.

d. *Audit Plan*: It provides a broad outline of the objectives of audit, its scope, detailed activity plan, constitution of the audit teams, its composition, period and time of audit, allocation of resources and also decides on the risks to be included in the scope of audit. As the active co-operation of the management would be necessary at every stage, it would be advisable to prepare the annual audit plans in consultation with the audit committee and senior management of the company.

e. *Audit Reporting*: As per the audit plan the individual audits are carried out to evaluate risks at each process and the impact of available key controls and residual risks. Compilation and alignment of these audit reports with reference to the organisation's main objectives and risks, the efficiency and effectiveness of the controls will provide the comprehensive audit assurance to the management on effectiveness of the key controls in managing the risks at tolerable levels, residual risks and the final risk exposure of the organisation. The reports are submitted to the audit committee for appropriate action. Depending on the feedback, the risk register and RAU are updated from time to time.

The above five stages or core components of RBIA are neither mutually exclusive nor exhaustive. These five stages are interdependent, mutually supportive and facilitate organising risk based internal audit work more systematically and methodically.

RBIA and Good Governance of PSUs

Good governance means responsiveness, effectiveness and efficiency in ensuring that processes and institutions produce results that meet the needs of society while making the best use of resources at their disposal. It necessitates accountability which means that PSUs will be accountable to the public, and to all those who are affected by their decisions. The Fiscal Responsibility and Budget Management (FRBM) Act seeks to put in place stringent fiscal controls and the Right to Information Act seeks to bring about transparency and accountability in the functioning of the government. In this scenario internal audit can act as a powerful tool to improve accountability, it can give the required inputs which can be fed into the planning process, inputs that can be utilised to monitor implementation. The audit function has traditionally been seen as being part of the financial management function of the Government and increasingly as a way for improving the performance of the PSUs. It has provided assurance that public funds received and spent are in compliance with the relevant laws, and that the reported use of funds is a fair and accurate representation of the financial position of the organisation. Beyond this, audit in many countries has evolved to take a more comprehensive view of the economic and social implications of the operations of the Government or performance audit. In recent years, the demand for greater transparency and accountability in PSUs, has resulted in a move to strengthen the internal audit function. It is necessary to bring out the differences that exist between the conduct of internal audits in the Government sector and in the private sector.

“Risk-based internal auditing (RBIA) is the methodology which provides assurance that risks are being managed within the organisation's risk appetite. The internal audit function has a major role in risk management and assists in identifying the potential risks, assessing the risk intensity and risk exposure of the organisation, and also provides an objective and independent opinion on the effect of risk response measures, key controls and checking whether the risks of the organisation are managed at tolerable levels or not.”

- The environment of the audited PSU is vastly different from what exists in the private sector. The

PSU audit is carried out in an environment determined by legal rules and a great deal of importance is attached to lawful and rightful conduct.

- In the public sector, the auditor's opinion serves the interest of the public in general and is not confined to only providing a full and fair view to the stakeholders as is the case with the private sector audit.
- It is also a fact that the decision making process in a PSU is much more complex when compared to the private sector.
- In respect of PSUs, success cannot be translated in terms of the bottom line of income and expenditure account but rather needs other criteria as a measure of performance.
- Financial reporting in the public sector is also different from that in the private sector because the laws and regulations regarding financial reporting in the public sector are different on account of the need for transparency on the part of the government regarding the Government's plans and the resource allocations.
- Furthermore, as far as the Government is concerned, its primary goal is not to earn a profit over and above the cost of production as is the case with private entities. Rather the goal of government is to realise the maximal possible usefulness for society from a limited amount of resources and the performance indicators are also different since the success of government entities is not expressed only in financial terms.

For a PSU, the internal control systems are of key importance as a pre-condition for better performance because the system of internal control is often the only instrument available, unlike in the private sector where the market signals act as warning signals.

Challenges for Implementing RBIA in PSUs

In an ideal risk management system in PSUs, the organisation should have a risk management strategy designed to achieve the objectives of the organisation and manage the risks. The role and responsibilities of RBIA in the organisation's risk management should be enshrined in the organisation strategy. The application of that strategy should be embedded into the organisation's business processes, systems and policy setting, to ensure that risk management is an intrinsic part of the way business is conducted. Successful implementation of RBIA in PSUs in India is a challenging task and fraught with certain organisational, functional and cultural impediments. Some of the risks which may impact the successful implementation of Risk based internal audit in PSUs in India are briefly discussed below:

- **Role of Internal Audit**: The internal auditors are viewed with suspicion and considered at all levels as an unavoidable evil. Unless the mindset of the senior management and staff at all levels change, and the internal audit is given its due status as a supportive management tool, it will be difficult for the internal auditor to make any substantive contribution in the financial management or risk management of any organisation. In India, the internal audit function is yet to get its due importance.
- **Lack of ownership and accountability**: In PSUs, the major problem is lack of accountability. While there will be several claimants to share the achievements, it will be almost impossible to fix responsibility for the failure of the PSUs. The public sector employee is in general averse to taking any risks and does not own the responsibility of objectives or risks of the organisation. Unless the senior management is made responsible and accountable for achieving the objectives and they own the corresponding risks and also understand the benefits of risk management, there cannot be effective risk management systems nor risk based internal audit systems in PSUs.
- **Lack of trained manpower**: The Risk management and Risk based Internal audit is an emerging discipline and the internal auditors of PSUs in India need sufficient training to hone their skills in the subject.
- **Corruption in public places**: India does not fare very well in the corruption perception index of Transparency International. The corrupt officials and practices perpetuate inefficiency in service delivery and thrive on leakages and poor management of valuable public resources. Unless this evil is dealt with effectively and sincerely, the public sector system and service delivery cannot be improved even by introducing Risk based internal audit.

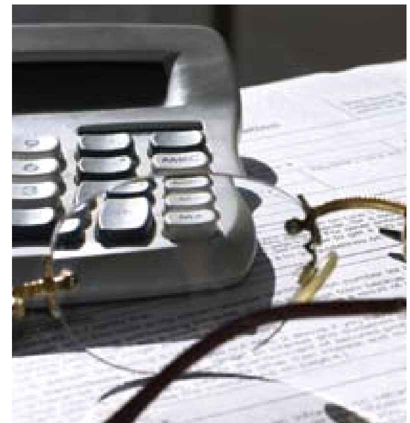
> **"Internal Auditors of PSUs talk about an appropriate "tone at the top" as being a key component of the internal control structure of the organisation. Best practice emphasises the responsibility of the Board/CEO to establish an appropriate 'corporate' culture, including code of ethics and standards of conduct to enhance the organisation's reputation for fair and responsible transactions and to help maintain high standards of behaviour throughout the organisation."**

Internal Auditors of PSUs talk about an appropriate "tone at the top" as being a key component of the internal control structure of the organisation. Best practice emphasises the responsibility of the Board/CEO to establish an appropriate 'corporate' culture, including code of ethics and standards of conduct to enhance the organisation's reputation for fair and responsible transactions and to help maintain high standards of behaviour throughout the organisation.

Implementing RBIA Best Practices in PSUs

Designing effective internal control procedures which provide reasonable assurance regarding the achievement of the organisation's objectives is important to a Best Practice Framework. The identification of the functions performed by the organisation in the achievement of its strategic objectives, and the breaking down into individual tasks and related risks and the control procedures built in to mitigate these risks are important. Best practice therefore requires the preparation of a Risk Management Plan which will provide the framework for monitoring the risk management activities. Once the whole array of risks is identified, the next step is to rank the risks and draw up an audit plan accordingly. One way to effectively prioritise the processes for audit purposes is to look at the matrix of probability of occurrence versus severity of loss for each of the processes and develop a risk based audit plan according to this classification. It is also desirable if the audit plan is devised with a holistic view as to the nature and significance of the risks facing the organisation/activity rather than focusing only on the financial reporting risks. In the process of identifying these risks the audit team may use intelligence gathered by other functions within the organisation. However, in devising the audit plan, the internal auditors should have an independent view on risks. Best practices also demand timely and comprehensive coverage by audit across a spectrum of risks. While we grade risks using simple ranking as high, medium and low risk, timeliness of the audit as per this categorisation is important, with high risk areas being covered annually and so on. This does not imply that there should be slippage in covering the low risk areas because even these can create problems. In fact internal auditors consider it advisable to annually re-assess the organisations' risk profile. Given that the risks to the organisation/activity would change over time, with new risks emerging, revisiting the risk based plan is imperative to an effective audit function. The effectiveness of audit is dependent on its ability to not only spot problem areas or areas where improvements can be suggested, but also on its ability to ensure speedy remedial action after audit has been completed. This in turn is dependent on timely completion and submission of the audit report. Any delay in this would defeat the very purpose and function of internal audit. The Institute of Internal Auditors (IIA) has identified key elements of an effective PSU audit which can serve as a starting point to developing best practices for internal audit in the public sector.

"Risk-based internal audit is expected to be an aid to the risk management in PSUs by providing necessary checks and balances in the system. IIA's professional guidance document on the Role of Auditing in Public Sector Governance, states that "Internal Auditors perform an especially important function in those aspects of good governance that are crucial in the public sector for promoting credibility, equity, and appropriate behaviour of government officials, while reducing the risk of public corruption"."



Conclusion

Risk-based internal audit is expected to be an aid to the risk management in PSUs by providing necessary checks and balances in the system. IIA's professional guidance document on the Role of Auditing in Public Sector Governance, states that "Internal Auditors perform an especially important function in those aspects of good governance that are crucial in the public sector for promoting credibility, equity, and appropriate behaviour of government officials, while reducing the risk of public corruption". Hence, it would be appropriate to conclude that Risk Based Internal Audit is a very important measure to ensure the efficiency of internal control systems and this is the key factor for providing good governance in Public Sector Undertakings.

References:

"Risk Based Internal Audit-An Introduction" By Mr. David Griffiths

"An approach to implementing Risk Based Internal Audit" By IIA

"Best Practices in Internal audits" By Ms. Sonali Singh

"RBIA-Indian Perspective" By Mr. P. Sudhir Kumar.

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Internal Audit Report Writing

"The ill and unfit choice of words wonderfully obstructs the understanding." **-Francis Bacon**

This quote aptly describes the need for sensible writing. This applies to every kind of writing, especially to reports prepared by auditors for they have the power of changing the fate of an organisation. Writing too much or too little is not the focus; it is about delivering your opinion on the real state of happenings using the appropriate set of words. "A well-written audit report is the actionable hallmark of a value-adding audit function." The audit report is used to communicate to the audience the purpose, the scope and the results of the work performed. Results are usually reported on an exception basis (findings, implications, and recommendations). Reporting may be more informal depending on the purpose and goals to the internal audit activities. Reports may also highlight or acknowledge a job well done. This article discusses various aspects of writing an internal audit report.

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Internal Audit Report Format

Guidelines on Report Writing aim at helping audit teams choose the most appropriate and effective format for a report, whether it be an audit report, a quality assurance review, or other project report.

Writing a report involves three aspects. The suggested report format should meet the:

- Expectations,
- Reporting standards, and
- Cost

Certain guidelines created at the

beginning of the project or process should be reviewed in detail prior to formatting the final report. This will identify any agreed upon format, content and issuance procedures. It also becomes important to communicate certain significant findings, subprocess and specify the nature of finding, namely:

- o Effective Information Management
- o Integrity of Assets
- o Compliance with laws and regulations
- o Economical, efficient and effective business processes

Structure of an Audit Report

Audit reports may include some or all of the following sections:

- Objective
- Scope
- Conclusion
- Summary of results
- Detailed results
- Background information
- Appendices or exhibits

Layering an Audit Report

A report can be layered so that the needs of the highest level readers are addressed in the first few pages of the report. The rest of the report can include greater detail. The following is an example of layered sequence:

- Cover sheet
- Table of contents (optional)
- Objective
- Scope
- Conclusion
- Summary of results
- Results of work
- Background information
- Detailed scope (if needed)
- Appendices or exhibits

Organising the report in the following format will put the objective, scope, and conclusion on the first page. This section, which may even be separated from the body of the report for distribution to senior management, can become the executive summary. This section provides the succinct, conclusive overview desired by top managers and board members.

Different Formats in Internal Audit Reporting

There are several different formats which are commonly used for deliverables on individual audits:

- **Presentation Format**
  Presentation Format is the preferred format for communicating audit findings, recommendations and management responses (if applicable) on a high level. Utilise presentation style formats to facilitate efficiency, brevity, clarity and readability of the audit report. (Presentation style reports lend themselves well to business process reviews.) The presentation style uses bullet points and key phrases to communicate the important points in a succinct, yet understandable, way.
- **Table Format**
  This format uses columns for findings, recommendations and management responses (if applicable.) Additional columns can be added for action plan, expected timing of implementation and status updates. This format can be used as a real-time tracking tool to monitor and report on the implementation status of the agreed upon recommendations.
- **Text Format**
  This format uses narrative text to communicate findings, recommendations and management responses (if applicable.) This is the most detailed format and the most difficult to read. If using text based reports, address the needs for the highest-level readers in the first pages.

Report Writing – A Process

The following guidelines provide the audit team with ideas for streamlining the report writing process and for producing timely, effective, final reports.

Organise the findings and recommendations. Findings can be categorised by:

- Significance
- Subprocess
- Type of finding

Steps in Report Writing Process

1. Develop a tentative conclusion about the data, and start selecting the key pieces of information supporting that idea.
2. Think of ideas for the final report as the work paper review is being conducted.
3. These ideas should be recorded immediately so they can be incorporated as the report is being composed.
4. Summarise the major findings. The purpose of the summary is to provide the reader with an awareness of the significant issues without having to read the details of the report. This summary can take the form of a brief narrative, a list, or a table of contents.

> **“Despite the tools and technologies we have today for audit tracking and reporting, internal audit teams are still confronted with the challenge of figuring out what to say and how to say it. It is important that these audit teams effectively communicate with their clients and build stronger customer relationships through proper internal audit reporting. Poor internal audit reporting can marginalise quality work and inhibit management’s willingness to take action. Clear, effective reporting, in contrast, leads to action and improvement.”**

Before drafting any business document, consider the objective. What do you wish to accomplish? Is your purpose to inform the audience or to persuade them to action? Approaches will differ depending upon the goal or the prescribed format. Be sure your language, purpose, and descriptions are clear and easy to understand. Avoid using technical language that confuses the audience. Ask yourself, would someone outside the accounting and audit field comprehend?

5. Draw a conclusion or render an opinion when appropriate. If management is expecting a conclusion or opinion as a result of the audit, the audit team should include this in the final report.
6. Put together a rough draft of the entire report, concentrating on the content. After the content is in place, go back through the report and focus on the format, the level of detail, and the readability.
7. Format the report so that it flows smoothly and is easily read.
8. Strategic use of headings and graphics enhance the effectiveness and readability of a report. Try to avoid lengthy paragraphs, excessive detail, and cumbersome sections of straight narrative.
9. Allow some time away before finalising the draft report. This will make the final review more objective.

Content/Style of Internal Audit Report

The following is a list of guidelines related to report content and style. The final report should be

- Appropriate
- Target writing to the interest of the readers
- Emphasise key ideas
- Persuasive
- Provide enough support to convince readers
- Describe the effects of conditions presented
- Describe the benefits of the recommendations
- Quantify the impact of findings
- Constructive
- Use an objective and constructive tone
- Identify causes of problems
- Express ideas positively
- Balance report with strengths and mitigating circumstances
- Include only the necessary information
- Describe the condition and its impact rather than using general adjectives
- Results-Oriented
- Indicate management action taken on findings
- Request specific action on unresolved items
- Direct
- State your key message directly
- Make your ideas clear at first reading
- Use informative and descriptive headings
- Generate interest and hold the reader's attention
- Succinct
- Choose the right amount of supporting detail
- Write concisely
- Put action in sentences
- Select an effective style
- Provide variety in words and sentences
- Inviting
- Summarise the report in an opening paragraph
- Format your report for easy reading
- Use headings, tables, and layout to guide the reader
- Timely
- Get started quickly and write an acceptable first draft efficiently
- Correct
- Use correct grammar and punctuation

Best Practices for Internal Audit Reporting

The Challenge:

Despite the tools and technologies we have today for audit tracking and reporting, internal audit teams are still confronted with the challenge of figuring out what to say and how to say it. It is important that these audit teams effectively communicate with their clients and build stronger customer relationships through proper internal audit reporting. Poor internal audit reporting can marginalise quality work and inhibit management's willingness to take action. Clear, effective reporting, in contrast, leads to action and improvement.

Drafting the Report:

The internal audit report is the most important deliverable of an audit cycle. Proper internal audit reporting can help clarify important issues and establish a cooperative tone focused upon management action. The content of internal audit reports should be carefully reviewed and substantiated during the drafting process.

Audit Report – A Communication Channel

The audit report is used to communicate to the audience the purpose, the scope and the results of the work performed. Results are usually reported on an exception basis (findings, implications, and recommendations). Reporting may be more informal depending on the purpose and goals to the internal audit activities. Reports may also highlight or acknowledge a job well done.

Internal audit reporting and communications strive to increase risk awareness, minimise expectation gaps, and facilitate actions that will improve

internal controls or effectiveness. Points of interest for management and the Audit Committee include the status of the risk and control environment, as well as the effectiveness of operations.

Listing the ten core reporting practices that will help staff, at all levels, to avoid common pitfalls and improve overall internal audit services. These practices help in effective report writing that will also assist in the development or review of any audit communication.

1. Determining the purpose of Audit. Communicate it clearly and succinctly:

Before drafting any business document, consider the objective. What do you wish to accomplish? Is your purpose to inform the audience or to persuade them to action? Approaches will differ depending upon the goal or the prescribed format. Be sure your language, purpose, and descriptions are clear and easy to understand. Avoid using technical language that confuses the audience. Ask yourself, would someone outside the accounting and audit field comprehend?

2. Establish the practical business impact:

Provide a strong case to support your recommendations, whether it is a way to achieve cost savings or to improve a control. Include support for your conclusions and incorporate quantitative results. The facts in your report will convey the degree of importance and will assist with influencing the audience to act.

3. Propose a workable solution:

Identifying control or process optimisation issues is only half of the effort. The overall goal is to positively improve the organisation. Once the goal is established, management may need assistance in designing a workable solution. Finally, the steps must be taken to realise change. Although it is the management's responsibility to act on report findings, the internal auditor may be well positioned to assist in creating a practical solution.

4. "A picture is worth 1000 words"

Consider how you will present the information. The reporting format is often based upon the preceding activities. Depending upon your intended impact, the content may be best presented using charts, matrices, and graphs. Graphs can communicate a point more effectively than using words alone. They will often allow you to make your case more effectively or persuasively, particularly when presenting financial data or descriptions of processes. Be prepared to provide additional detail or supporting analysis if requested.

5. Executive summary and format:

Consider writing an executive summary for those only interested in high-level results. Some organisations routinely use the executive summary for certain levels of management and provide the full report only to the subject matter management and related executive sponsors.

The body of the document should be divided into distinct and clearly labeled sections (ex. Significant Findings, Analysis, and Potential Risks). This will make it easier for the reader to locate specific information.

Effective communication requires organisation. Develop a list of main points before drafting the report. This exercise will especially help in conveying a complex message. Well-developed outlines will enable you to stay on topic and address all relevant issues. The outline can also be circulated to the other IAs and to IA management. By doing this, you will confirm inclusion of appropriate elements and scope. This is also a good practice tool to gain input and identify additional elements of inclusion. Using the outline in this way may minimise subsequent review and editorial efforts.

Place non-essential but supporting material in the appendix. This is a separate section at the end of the report containing details such as

> **Consider how you will present the information. The reporting format is often based upon the preceding activities. Depending upon your intended impact, the content may be best presented using charts, matrices, and graphs. Graphs can communicate a point more effectively than using words alone. They will often allow you to make your case more effectively or persuasively, particularly when presenting financial data or descriptions of processes. Be prepared to provide additional detail or supporting analysis if requested.**

"The little things can make a huge difference. Always proofread carefully. Spelling and grammatical errors reflect poorly on your attention to detail (one of the primary qualifications of an audit or accounting professional). It is useful to run spell-check; however it will not catch incorrect word usage or omitted phrases. Take time to personally review the reports."

statistics, figures, and explanations of calculations. Each piece of data should be labeled separately so it can be easily referenced within the body of the document.

If the report is lengthy due to project scope or findings, consider writing an executive summary for each section of the report. The summary should include and explain the purpose, data, and conclusions. Re-reading the report sections often clarifies which information should go in the summary.

6. Tailor message to the audience:

Tailor the information to your audience. Use plain English whenever possible and avoid buzzwords or acronyms unless they are understood by everyone who will review your findings. Keep in mind that not all your readers will have the same background or familiarity with audit or accounting terminology.

Attempt to understand the following:

- The audience – strike an appropriate tone and depth of detail
- Report usage – determine how the report will be utilised and for what purpose
- "So what" – assess the relevance of all data elements and conclusions

Your audience primarily will be concerned with the bottom line. Provide background information in your report but avoid going overboard

with the historical perspective. One recommended aspect of report introductions includes an area dedicated to placing the report scope or results in proper perspective. The information in the report will be scrutinised during both the development process and the readership receipt.

It may be helpful to cite business unit relationships, per cent of revenues, and the purpose or function of report subject matter in relation to the organisation at large or position of the reader. These basic considerations will ensure adequate perspective of report contents, which is an important characteristic of understandability.

Explain terminology and expand acronyms for readers, especially when the content includes technical or organisational terms unfamiliar to the audience. Consider a glossary of terms if the report is filled with acronyms or technical terminology. This approach may prevent disrupting report flow with definitions.

7. Pay attention to details:

The little things can make a huge difference. Always proofread carefully. Spelling and grammatical errors reflect poorly on your attention to detail (one of the primary qualifications of an audit or accounting professional). It is useful to run spell-check; however it will not catch incorrect word usage or omitted phrases. Take time to personally review the reports.

8. Minimise expectation gaps:

All findings prior to reporting, obtain the auditee's agreement with substantiated conclusions with recommendations should be previously communicated with subject matter management.

9. Timeliness of escalation:

Communicate results during and after fieldwork completion, especially if they are significant findings or if immediate action is required. If necessary, both the executive management and the Audit Committee should be notified prior to press coverage, etc.

10. Balance presentation:

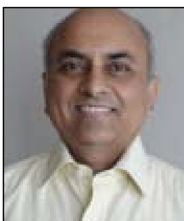
Present a balanced perspective and include management's responses with related findings. Point out areas where your colleagues excel to balance the report and maintain cooperative relationships. The most controversial aspect of the internal audit report is language (relative meaning and the tone). Use positive and constructive words. Avoid language that condemns such as "did not perform" or "failed to control." Instead, incorporate phrases with action: "We identified where internal controls need improvement" or "identified opportunities for improvement."

Audit reporting is designed to raise awareness and affect positive change, rather than generate unnecessary consternation and political warfare. Internal auditors must strive to find balance in presenting. ■

Changing Role of Internal Auditor

"Some cause happiness wherever they go; others, whenever they go" - *Oscar Wilde*

This summarises the general perception of the Internal Auditor in the corporate world. Several organisations in the past (and some even today) use Internal Audit department to accommodate non-performing employees. Similarly, most professionals shunned careers in Internal Audit and at best used it as a stepping stone for the more "glamorous" roles within Finance or Business stream. However, the last few years have witnessed a sea change in the role and expectations from the Internal Auditor. New demand from board, senior organisational leaders, and regulators are requiring internal audit to understand and manage business risks, prioritise goals and activities, promote behavioral change, improve processes, reduce costs, eliminate complexity and redundancy. This article highlights the fast changing role of the Internal Auditor.



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The Traditional Internal Audit – Value Protectors

Internal Audit started as a document verification exercise, assisting organisations for safeguarding of assets and enforcing corporate policies to preserve value. It would examine whether a control was being performed or procedure was being followed and report either a "yes" or "no", thus focusing more in detecting control deviations. The audit was largely a 'rule' or 'checklist' based audit which ensured the then objective of protecting values for the organisation.

The Change Triggers

Gradually, organisations world over are realising the value addition that internal audit can provide, going beyond the typical role of policeman to a more dynamic role of a business support function. This transition has occurred on account of certain triggers in the business environment, which highlighted the importance and relevance of internal audit.

1) ***Corporate Failures***

   The spate of large scale corporate failures, internationally as well as in India (Enron, Worldcom, Parmalet, Lehman, Satyam, etc.) demonstrated that the largest risks for the businesses were from the unscrupulous Management itself. The traditional internal audit "for" the Management (compliances with policies, procedures and decisions) was considered inadequate as the need was felt for audit "of" the Management Decision Processes.

2) ***Corporate Governance and Business Needs***

   Boards are increasingly being held accountable for risk, while

executive managements are being measured in the market place by their ability to manage both returns and risks. Mounting pressure from stakeholders and regulators as well as strong correlation between better Governance and value creation/perception in the last few years are driving businesses to identify, prioritise and manage risks in an enterprise-wide manner. These changes have opened the floodgates for better governance practices that include greater independence and expectations from Internal Audit.

3) Regulatory Environment

Repetitive business failures have alerted Regulators to become proactive and establish framework to minimise and mitigate the possibility of such failures in the future. Introduction of Sarbanes Oxley Act in the USA, Basel III norms and clause 49 of Listing Requirement for Indian listed companies together with several recommendatory practices on Corporate Governance highlighted the importance and relevance of internal audit.

Evolving Role of Internal Audit – Value Creator

To a significant extent, the traditional purposes for internal auditing have become virtually obsolete in these new environments. New rationales and responsibilities for internal auditing are emerging. The Pyramid illustrates how Internal Audit is changing.

Transactional Audit is losing relevance as volumes and size of businesses increase thus limiting

The expanding list of expectations has also led to a raging debate on whether Internal Audit function should be outsourced or kept in house. Amongst other, the Outsourced model offers greater independence and wider knowledge pool while in house model allows better business understanding. Though consensus is yet to be reached on either of the models as opinion is divided amongst the different committees formed for review of Corporate Governance, there is no disagreement on the need for independence of the Internal Audit function.

the ability to conduct transactional audit to cover meaningful number of transactions. Moreover, basic controls are increasing in-built into transaction through software and systems. Examples of system controls include pricing, discounts, credit check, etc. in the sales cycle.

Operations Audit is gaining importance from the Executive Management as it is intended to assess the extent to which a function or a unit is achieving the goals set by the Management. Operation Audit has several sub-types as briefly described below.

a) *Organisation Audit* to determine effectiveness of the structure of the Company and covers reporting procedures, intra departmental chains of command, inter department co-ordination, conflicts of responsibilities etc.
b) *System Audit* is designed to assess effective implementation of policies and procedures instituted by a company.
c) *Function Audit* examines the extent of which a department or individuals within a department perform the work as expected and believed by the top management.
d) *Programme Audit* reviews the effects of implementation of a specific policy or procedures after it is implemented.

Two key elements of Operations Audits are the application of judgment by the Internal Auditor and suggesting improvement steps.

Risk and Controls Audit: This has gained tremendous relevance in the last five years as businesses increasing adopt Enterprise Risk Management at Company and at function/unit level. The key controls that mitigate major risks across the organisation needs to be validated on a periodical basis to avoid surprises. Internal audit can move ahead from its monitoring role to help influence and improve how risks are managed before they become challenges.

Management Decision Process Audit encompasses audit 'of' the Management and its decision process to establish its soundness, transparency and sustainability. This is an area of high attention arising from Corporate Frauds caused by Management actions.

The paradigm shift is illustrated from the following changes in approach to Internal Audit:

TRADITIONAL: Value Protectors	MODERN: Value Creators
Reactive	Proactive
Transaction Based	Risk and Process Based
Focus on people (who has done what and how)	Focus on Opportunities (what and how can it be done and by whom)
Detect and Correct	Prevent and Monitor
Inspect quality of Controls	Build Quality of Controls

New demand from board, senior organisational leaders, and regulators are requiring internal audit to

"The internal audit function is now expanding into additional roles aligned to its primary role of providing assurance on Governance, Controls and Compliance. Internal auditors are no longer required to focus solely on financial audits. They increasingly need to be able to provide value adding support to management across all areas of operation e.g. IT, Marketing, Project Management, etc. They are coaches, internal and external stakeholders' advocates, facilitators of risk management, control experts, efficiency specialists and problem solving partners."

understand and manage business risks, prioritise goals and activities, promote behavioral change, improve processes, reduce costs, eliminate complexity and redundancy.

Changing Expectations from Internal Audit

As business organisations become larger and complex, demands on the time the Board of Directors and the Management are larger. The following are commonly expected by the Board of Directors and the Management from the Internal Audit function:

- Greater emphasis on Governance and Policy Matters instead of Procedures and Transactions.
- Develop deep understanding of business and risks.
- Align Internal Audit Plans with Enterprise Risk management Framework.
- Concentrate on High Risk and Impact issues and material weaknesses.
- Assess Management Decision Processes (but not the judgments).
- Conduct substantive tests instead of limiting to process walk through.
- Offer practical solutions in the form of actionable dashboards with timelines and responsibility.
- Focus on sustainable improvements instead of past failures.
- Monitor, participate and report on Action Taken and its timeliness.
- Establish Continuous Controls Monitoring – providing a "real-time" overview of the internal control environment.

The expanding list of expectations has also led to a raging debate on whether Internal Audit function should be outsourced or kept in house. Amongst other, the Outsourced model offers greater independence and wider knowledge pool while in house model allows better business understanding. Though consensus is yet to be reached on either of the models as opinion is divided amongst the different committees formed for review of Corporate Governance, there is no disagreement on the need for independence of the Internal Audit function.

Regulations mandate that the Chief Internal Auditor (CIA) reports directly to the Audit Committee. However, it is not uncommon in several good companies that CIA in effect reports to the Management and several times to the Chief Financial Officer. In the recent past this trend is changing and to create independence of the function, several progressive companies have introduced Board Approved Internal Audit Charter that defines the role, responsibility and authority of the CIA. A beginning is also made of one on one meeting of the CIA with the Audit Committee sans the executive management.

Opportunities for Internal Auditors

The internal audit function is now expanding into additional roles aligned to its primary role of providing assurance on Governance, Controls and Compliance. Internal auditors are no longer required to focus solely on financial audits. They increasingly need to be able to provide value adding support to management across all areas of operation e.g. IT, Marketing, Project Management, etc. They are coaches, internal and external stakeholders' advocates, facilitators of risk management, control experts, efficiency specialists and problem solving partners. The expanding avenues and opportunities for Internal Auditors include the following:

1) *Supporting Corporate Goals:* The Board and Management need an assurance that organisation's strategic objectives are well communicated, understood and implemented across the organisation. Internal audit can play a key role in ensuring that several levels down from leadership, the organisational resources are being effectively channelised in pursuit of management agenda.
2) *Assessment, implementation and assurance on Enterprise Risk Management systems (ERM):* With knowledge of organisation's key risks, ability to have an enterprise wide view and expertise in best practices and controls across different organisations, Internal Auditor can play a key role in risk identification, prioritisation and mitigation as well as its periodical reviews. Internal auditor is a contributor to the ERM process and also an effective user/consumer of ERM. Internal audit is therefore in a unique position to help drive the ERM process for many organisations and can provide assurance to the Board that the organisation's key business risks are being managed and mitigated appropriately.
3) *Support Compliance Function* that could include Sarbanes Oxley Act

requirements like periodical testing of financial reporting controls, Regulatory Framework, Clause 49, adherence to Code of Business Conduct.

4) *Fraud Monitoring:* Internal Audit can create fraud awareness across the organisation as well as initiate steps for fraud prevention, detection and investigation. It would also include review of complaints under the Whistle Blower Policy or similar other processes laid out.
5) *Identifying Improvement Opportunities:* Internal Audit is one of the few functions which has cross functional exposure within an organisation and is, therefore, is in a position to assess implication of an action or inaction across different activities. Internal Auditor is thus well suited to suggest opportunities for cost reduction, revenue maximisation, elimination of non-value adding activities and optimising utilisation of organisational resources.
6) *Review of non-Financial Processes:* Internal Audit now encompasses non-financial processes in HR, QA, R&D, Production, Regulatory Compliances, Information Technology as they become increasing relevant for achieving business objectives and goals. For example in a BPO, Recruitment and Training are extremely business critical function while for a chemical manufacturing business, adherence to Environment, Health and Safety requirements is critical. These functions/activities are key to survival and growth but involve limited financial activities.

With the expanding role, Internal Audit now offers tremendous scope for learning and contributing to organisations goals making it a professionally challenging and satisfying career option.

“The key challenge faced by an internal auditor is to strike a balance between the internal needs of Board and management, external needs of stakeholders and the requirements of regulatory authorities. The expectation to ‘add-value’ rather than ‘protect-value’ keeps pushing the auditor beyond process compliance to process design and efficiency/ productivity objectives. This expectation has now graduated to an even higher level of ‘create-value’, where the auditor is expected to recommend ways to help management exploit opportunities (and not just mange risks).”

Emerging Challenges

The key challenge faced by an internal auditor is to strike a balance between the internal needs of Board and management, external needs of stakeholders and the requirements of regulatory authorities. The expectation to ‘add-value’ rather than ‘protect-value’ keeps pushing the auditor beyond process compliance to process design and efficiency/productivity objectives. This expectation has now graduated to an even higher level of ‘create-value’, where the auditor is expected to recommend ways to help management exploit opportunities (and not just mange risks). These developments certainly present an immense challenge for the internal audit community. This transition would necessitate Internal Auditor to be equipped with certain skill set as enlisted below:-

1) Industry knowledge and functional expertise.
2) Expertise in risk understanding, management and evaluation.
3) Improved interpersonal skills – for effective communication with process owners and line managers, convincing them towards the required change in design or process,
4) Fraud skills.
5) Automation of internal control environment (IT).

Internal Audit needs strategic thinkers who understand business issues, perceive risks in achievement of business objectives, evaluate control implications and communicate them effectively to senior management.

Conclusion

To keep up to the challenge of the new role and responsibility the Internal Auditor will need to sharpen his existing skill set. The Internal Auditor will need to be equipped to obtain business understanding, risk mapping, effective interpersonal skills, abreast with developments in IT and automation tools, fraud detection, etc.

Internal Audit has the potential to be one of the most influential and value-adding services available to a company’s senior management and board of directors. The role of the Internal Audit function can take on different appearances, going from an independent assurance function to a real management advisor. Internal Audit will need to find equilibrium between both roles, catering to expectations from the different stakeholders. Independently of which role is selected, the ability to have impact within the organisation will be a KPI for every future Internal Audit function. Executive Management will request more advisory involvement of Internal Audit, including performing reality checks on key management decisions. The establishment of internal audit function can become an integral part of the overall strategy and assist in achieving corporate objectives. Internal audit is best positioned not only to keep the company “out of trouble” but also help “make the business better”. ■

IFRS – Convergence in India

Never in the history has there been a time when we were closer to the ideal where companies around the globe all use the same accounting standards in their financial reporting. International Financial Reporting Standards (IFRSs) are now accepted in over 120 countries, and the number is expected to grow to 150 countries in the next few years. India is all set to implement Indian Accounting standards converged with IFRSs. The Institute of Chartered Accountants of India (ICAI), the premier accounting body of the country has been entrusted with the responsibility of formulating the converged accounting standards and ensure smooth convergence. The ICAI has so far formulated 35 Indian Accounting Standards (IND AS) converged with IFRS which are in line with corresponding IAS/IFRS, adoptable under the conditions prevailing in the country and the same have also been notified by Ministry of Corporate Affairs on 25th February, 2011 on the recommendation of NACAS. To make the convergence process smooth and timely it is imperative to make Indian laws and regulations consistent with IFRS requirements. Changes are required in the existing Companies Act, SEBI Rules & Regulations, Banking Regulation Act, Insurance laws & Income Tax Act. A globally accepted accounting and reporting standard will facilitate easier comparison of financial statement and will be helpful to the investor in making informed decisions. Read on to know more.

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International Financial Reporting Standards (IFRSs) issued by the International Accounting Standard Board (IASB) headquartered at London has assumed the status of Globally Accepted Accounting Standards. It is an independent standard setting body which is appointed and overseen by a geographically and professionally diverse group of trustees. Earlier the standard setting body was known as International Accounting Standard Committee (IASC) and the standard issued by IASC was known as International Accounting Standard (IAS). Since 1st April, 2001, IASB took over IASC and adopted the existing IAS and started developing the standards with the name IFRS.

As per the notification issued by Ministry of Corporate Affairs (MCA) two separate set of accounting standards will prevail in India. The first set would comprise Indian Accounting Sandards converged with IFRS applicable for specified class of companies and second set would comprise notified accounting standards applicable for companies not required to follow convergence. The MCA vide Notification dated 28th February, 2011 has revised the Schedule VI of Companies Act, 1956 in compliance with IFRS converged accounting standards which will be effective from accounting period commencing on or after 1st April 2011.

Government of India has decided to implement the IFRS Converged Accounting Standards issued by Institute of Chartered Accountants of India (ICAI) and notified by NACAS and not to adopt IFRSs issued by IASB in totality. The ICAI, the premier accounting body of the country has been entrusted with the responsibility of formulating the converged accounting standards and ensure smooth convergence. ICAI has formulated Indian Accounting Standards converged with IFRS which are in line with corresponding IAS/IFRS adoptable under the condition prevailing in the country. But for IFRS to allow comparability and reliability of financial reporting, we must make full compliance with IFRS without any dilution through local adjustments. The ICAI has so far formulated 35 Indian Accounting Standards (IND AS) converged with IFRS and the same have also been notified by Ministry of Corporate Affairs on 25th February, 2011 on the recommendation of NACAS. ICAI has adhered to the timeline given for formulation of IFRS converged Indian Accounting Standards. Ministry of Corporate Affairs (MCA) had prepared the road map for implementation of IFRS- Converged standards in India in a phase wise manner beginning from accounting periods commencing on or after 1st April, 2011.

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To make the convergence process smooth and timely, it is imperative to make Indian laws and regulations consistent with IFRS requirements. Changes are required in the existing Companies Act, SEBI Rules & Regulations, Banking Regulation Act, Insurance laws & Income Tax Act. The Government is expected to amend these acts shortly.

What is IFRS?

International Financial Reporting Standards (IFRSs) are standards and interpretations adopted by the International Accounting Standard Board (IASB).

IFRSs Comprise:

a) International Accounting Standards (IAS), 1 to 41 (12 out of this have since been omitted)
b) IFRSs (1 to 9)
c) Interpretation developed by the IFRIC or the former Standing Interpretation Committee (SICs).

Presently, there are Nine (09) IFRSs, Twenty Nine (29) IASs, Fifteen (15) IFRIC interpretations and Eleven (11) SIC interpretation.

Components of Financial Statement Under IFRS:

A complete set of financial statements under IFRS comprise:

1) A Statement of Financial Position as at the end of the year (i.e. Balance Sheet)
2) A Statement of Comprehensive Income for the period (i.e. P&L Account)
3) A Statement of Changes in Equity for the period
4) A Statement of Cash Flows for the period
5) Notes comprising a summary of significant accounting policies and

other explanatory information.

Status of preparation of IFRS Converged standards corresponding to IAS / IFRS by ICAI:

Sl. No.	Standards	Status
01	Cleared by Council & recommended by NACAS for notification by Government	35
02	Not required to be notified at present	02 (IFRS 9: Financial Instruments & IAS 26: Accounting & Reporting by Retirement benefit plan)
03	To be redrafted	01 (IAS 41 : Agriculture)

Why IFRS?

A single system of financial reporting would benefit a host of constituents. With quality standards consistently applied, investor understanding and confidence rises. That translates to strong, stable, liquid markets. With quality reporting, investors would not need to compensate for a lack of understanding by demanding a risk premium. Never in the history has there been a time when we were closer to the ideal where companies around the globe all use the same accounting standards in their financial reporting. International Financial Reporting Standards (IFRSs) are now accepted in over 120 countries, and the number is expected to grow to 150 countries in the next few years. Canada, Japan and India will be migrating to IFRS in 2011 while US is planning to move to IFRS by 2013.

With over 120 countries requiring or accepting International Financial Reporting Standards, the likelihood of companies around the globe using the same accounting standards is in view.

A key moment in the move to IAS/ IFRS came on 6th June, 2002 when the European Council of Ministers approved the regulation that would require all EU companies listed on a regulated market to prepare accounts in accordance with International Accounting Standards for accounting periods beginning on or after 1st January, 2005.

“In the existing set up Multinational Companies (MNCs) are required to prepare financial statements under different set of accounting rules. First, under the local GAAP to meet statutory and regulatory requirements, and secondly, under a different GAAP based on accounting where its headquarters are located or securities are listed, which require extra efforts and cost. This problem will be overcome under IFRS regime.”

Convergence of accounting standards has played a major role in the growing acceptance of IFRSs. As the differences narrow between IFRSs and other widely-accepted accounting systems, resistance to IFRS is beginning to fall away.

Benefit of Convergence or Adoption of IFRS

Implementation of IFRS-converged standards would help in bringing excellence in financial reporting, easy for comparison, globally understand-ability, transparent and will be helpful for investor to take informed decisions.

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A globally accepted accounting & reporting standards will facilitate easier comparison of financial statements and will be helpful to the investor in making informed decisions.

In the current free trade economy there is increased mobility of funds and resources. Capital markets are getting integrated. IFRS will facilitate cross border listing of securities thereby attracting more foreign investment.

Under IFRS, financial statements will be prepared by applying a common set of consistent standards. This will improve quality of reporting, facilitate easy comparability with global peers and enhance the image of the companies.

With consistent application and the resulting comparability investors and analysts will have an easier time knowing how to best allocate capital.

Having one financial reporting language reduces preparation time and audit costs.

The emergence of global financial reporting language will open up new business opportunities for many. Now it will be possible for developed nations to outsource their finance function fully.

No longer is there a need to learn different standards, or keep current in them, at the expense of more fruitful pursuits. Regulation can be easier if properly coordinated. Education and training will become easier and more focused.

Roadmap for Application of Converged Accounting Standards in India

Category 1: For companies other than Banking companies, Insurance Companies and NBFCs:

As per the MCA roadmap, converged accounting standards were to be applied in India in following phases:

Phase I	Type of Companies
Conversion of opening Balance Sheet as at 1st April, 2011 for financial year commencing on or after 1st April, 2011	Companies forming part of NSE -Nifty 50
	Companies forming part of BSE - Sensex 30
	Companies whose share or securities are listed in stock exchanges outside India.
	Listed or Non-listed companies having Net Worth in excess of ₹1000 Crores.
Phase II	
Conversion of opening Balance Sheet as at 1st April, 2013 for financial year commencing on or after 1st April , 2013	Listed or Non-listed companies with a Net Worth exceeding ₹500 Crores but not exceeding ₹1000 Crores.
Phase III	
Conversion of opening Balance Sheet as at 1st April 2014, for financial year commencing on or after 1st April 2014.	Listed companies with a Net Worth of ₹500 Crores or less.

Note 1: Companies covered under phase I were to prepare their financial statements for the FY 2011-2012 in accordance with converged accounting standards. However previous year figure of 2010-2011 were to be as per non-converged accounting standards.

Note 2: However, the entity were to have the option to add an additional column to indicate what these figures could have been if the first set of Accounting Standards (i.e. converged accounting standards) had been applied in that previous year. Companies which make this additional disclosure were, for this purpose, to convert their opening balance sheet as at the date on which this previous year commences and, in that case, a further conversion of the opening balance sheet for the year for which the financial statements are prepared were not to be necessary.

Note 3 : Non listed company with a Net Worth of ₹500 crore or less as on 31-03-2009 and whose share/securities were not listed in any stock exchanges outside the country and Small & Medium Companies (SMCs) have been given exemption from adoption of IFRS converged accounting standards (though they can voluntarily adopt). However, they need to follow only the notified accounting standards which are not converged with IFRS.

Category II: For Banking Companies, Insurance Companies and NBFCs:

Converged accounting standards were to be applied in India in following phases:

Date of convergence of opening Balance Sheet in compliance with converge accounting standards	Type of Companies
1st April 2012	All Insurance Companies
1st April 2013	All Schedule Commercial Banks & Urban Co-operative Banks (UCB) with Net Worth exceeding ₹300 Crores.
1st April 2014	Urban co-operative bank (UCB) with Net Worth in excess of ₹200 crores but ₹300 Crores or less
1st April 2013	NBFC Part of NSE-Nifty 50
	NBFC Part of BSE-Sensex 30
	NBFC whether listed or not having Net Worth in excess of ₹1000 Crores.
1st April 2014	All listed & unlisted NBFC not falling in above categories and which have Net Worth in excess of ₹500 Crores.

"The emergence of global financial reporting language will open up new business opportunities for many. Now it will be possible for developed nations to outsource their finance function fully. No longer is there a need to learn different standards, or keep current in them, at the expense of more fruitful pursuits. Regulation can be easier if properly coordinated. Education and training will become easier and more focused."

Note 1: Urban Co-operative Bank with Net Worth not exceeding ₹200 crore and the Regional Rural Banks (RRBs) are exempted from applying converged accounting standards. However, they can voluntarily adopt.

Note 2: Unlisted NBFCs with net worth of ₹500 crore or less are also exempted from applying converged accounting standards.

Cut-off dates for calculation of Net Worth:

1) The cut off date for calculation of Net Worth in case of companies is audited balance sheet as on 31st March 2009.
2) For companies not in existence as on 31st March 2009, the net worth will be calculated on the basis of first balance sheet ending after that date.
3) Once a company prepare financial statement under IFRS converged accounting standards it will be mandatory to prepare subsequent financial statements under IFRS converged accounting standards even if it does not meet the eligibility criteria.
4) Where a parent company covered in any of the above three phases, all of its subsidiaries, joint venture and associates will have to follow converged accounting standards. ■

Accounting for MAT Credit

The concept of Minimum Alternate Tax (MAT) was introduced in the Income-tax Act, 1961 vide Section 115JB. The Income-tax Act, 1961 provides for numerous exemptions, deductions and incentives to companies. As a result of this, some companies, although having huge profits as per Profit and Loss Account, did not pay any taxes. The main idea behind insertion of Section 115JB was to bring such companies into the tax net. MAT is payable by a company when the normal income tax payable is less than 18 per cent per cent of its book profit. Such a company is liable to pay tax at the rate of 18 per cent of its book profit plus surcharge and education cess making effective tax rate of 19.93 per cent. Read on to know more.

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CA. Prashraya Prabhudesai
(The authors are members of the Institute. They can be reached at eboard@icai.org)

ICAI Guidance Note

ICAI has issued a Guidance Note in March 2006 on accounting for MAT credit entitlement. The salient features of MAT credit are as follows:

(a) A company, which has paid MAT, would be allowed credit in respect thereof.

(b) The amount of MAT credit would be equal to the excess of MAT over normal income tax for the assessment year for which MAT is paid.

(c) No interest is allowable on such credit.

(d) The MAT credit so determined can be carried forward for set-off for ten succeeding assessment years from the year in which MAT credit becomes allowable.

(e) The amount of MAT credit can be set-off only in the year in which the company is liable to pay tax as per the normal provisions of the Act and such tax is in excess of MAT for that year.

(f) The amount of set-off would be to the extent of excess of normal income-tax over the amount of MAT calculated as if Section

115JB has been applied for that assessment year for which set-off is being allowed.

MAT Credit: Whether Deferred Tax Asset?

The guidance note also discusses whether MAT credit can be considered as a deferred tax asset within the meaning of AS-22, *Accounting for Taxes on Income* issued by the ICAI. According to AS-22, "Timing Differences are the differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods." From this definition it is noted that payment of MAT, does not by itself, result in any timing difference since it does not give rise to any difference between the accounting income and the taxable income which are arrived at before adjusting the tax expense, namely, MAT. Thus, deferred tax assets and deferred tax liabilities do not arise on account of the amount of tax expense itself. In view of this it is not appropriate to consider MAT credit as a deferred tax asset for the purposes of AS-22.

MAT Credit: Whether an "asset"?

After stating that MAT credit is not a deferred tax asset under AS-22, the Guidance Note further goes on to answer the following questions regarding the accounting treatment of MAT credit

i) Whether MAT credit can be considered as an asset?

ii) In case it can be considered an asset, whether it should be so recognised in the financial statements?

In the Framework for the Preparation and Presentation of Financial Statements, the term "asset" is defined as follows:

"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 the enterprise"

Accordingly,

- MAT paid in a year in respect of which credit is allowed in the specified period is a resource controlled by the company.
- It is a result of the past event, namely, the payment of MAT.
- MAT credit has expected future benefits in the form of its adjustment against the discharge of the normal tax liability if the same arises during the specified period.

Thus, MAT credit is an **"asset"**.

According to the Framework, once an item meets the definition of the term "asset' it has to meet the criteria for recognition of an asset so that it may be recognised as such in the financial statements.

"An asset is recognised in the balance sheet when it is probable that the future economic benefits associated with the asset will flow to the enterprise and the asset has a cost or value that can be measured reliably"

In view of this, MAT credit should be recognised as an asset only when and to the extent there is convincing evidence that the company will pay normal income tax during the specified period.

"Payment of MAT, does not by itself, result in any timing difference since it does not give rise to any difference between the accounting income and the taxable income which are arrived at before adjusting the tax expense, namely, MAT. Thus, deferred tax assets and deferred tax liabilities do not arise on account of the amount of tax expense itself. In view of this it is not appropriate to consider MAT credit as a deferred tax asset for the purposes of AS-22."

Relevance of MAT Provisions in Current Scenario

The financial year 2008-2009 was the year in which the impact of recession and foreign exchange fluctuations was seen in the financial statements and many companies, especially large trading houses, reported huge losses. This decline in profitability was occasioned as much by extrinsic factors and general economic slowdown as by intrinsic factors, if not more. A reversal of the slowdown started in the year 2009-2010. The exchange rates not only stabilised but showed a favourable movement. Many companies showed improved results and profits in their books. However, the carried forward losses of the previous year resulted in a negligible or even negative figure under the head "Profits and Gains of Business and Profession" and consequently MAT liability arose. In the current financial year, i.e.2010-2011, presuming a further reversal of recessionary trends, the need to claim the benefit of the MAT credit entitlement may also arise. Hence, a better understanding of the utilisation of MAT credit entitlement and presentation in financial statements is necessary.

Presentation of MAT Credit in Financial Statements

Balance Sheet: Where a company recognises MAT credit as an asset on the basis of the considerations stated above, the same may be reflected as 'MAT credit entitlement' under the head 'Loans and Advances'.

In the year of setoff of credit, the amount of credit availed should be shown as a deduction from the 'Provision for Taxation' on the liabilities side of the balance sheet. The

unavailed amount of MAT credit entitlement, if any, should continue to be presented under the head 'Loans and Advances'

Profit and Loss Account: MAT being a current tax, the tax expense arising on account of payment of MAT should be charged at the gross amount in the normal way, to the Profit and Loss Account in the year of payment of MAT.

In the year in which the MAT credit becomes eligible to be recognised as an asset in accordance with the recommendations contained in the Guidance Note, the said asset should be created by way of a credit to the profit and loss account and presented as a separate line item therein.

Case Study

A. Y. 2009-2010

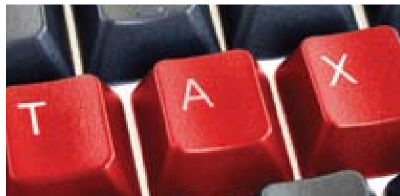
XYZ Limited has reported the following for the year ended 31st March , 2009 (A.Y. 2009-10)

a.	Loss before Depreciation:	₹900.00 lakh
b.	Depreciation as per Companies Act (Books):	₹15.00 lakh
c.	Depreciation as per Income Tax Act:	₹10.00 lakh

A. Y. 2010-2011

The relevant figures for the year ended 31st March, 2010 (A.Y. 2010-2011) are:

a.	Profit as per Profit & Loss Account:	₹1100.00 lakh
b.	Depreciation as per Companies Act (Books):	₹11.00 lakh
c.	Depreciation as per Income Tax Act:	₹8.00 lakh



Computation of income as per MAT

Profit as per Profit & Loss Account	₹1100.00 lakh
Less: B/f loss before depreciation OR Unabsorbed Depreciation as per books, whichever is less	₹15.00 lakh
Income subject to MAT	**₹1085.00 lakh**
MAT @ 16.995 per cent	**₹184.40 lakh**

Computation of income as per normal provisions

Profit as per Profit & Loss Account	₹1100.00 lakh
Add: Depreciaton as per books	₹11.00 lakh
Less: Depreciation as per Income Tax Act	₹8.00 lakh
	₹1103.00 lakh
Less: B/f business loss u/s. 72	₹900.00 lakh
	₹203.00 lakh
Less: Unabsorbed Depreciation u/s. 32(2)	₹10.00 lakh
Taxable Income	**₹193.00 lakh**
Tax @ 33.99 per cent	**₹65.60 lakh**

Hence, MAT credit entitlement to be recognised as per Guidance Note - ₹118.80 lakh. (i.e. ₹184.40 lakh (-) ₹65.60 lakh)

The accounting entry to be passed on 31st March, 2010

MAT Credit entitlement	Dr. 118.80	
To Profit & Loss Account		118.80

A. Y. 2011-2012

Let us assume the position for the financial year 2010-2011 (A.Y. 2011-2012) as follows-

a.	Profit as per Profit & Loss Account:	₹300.00 lakh
b.	Depreciation as per Companies Act (Books):	₹10.00 lakh
c.	Depreciation as per Income Tax Act:	₹7.00 lakh

" Where a company recognises MAT credit as an asset on the basis of the considerations stated above, the same may be reflected as 'MAT credit entitlement' under the head 'Loans and Advances'. In the year of setoff of credit, the amount of credit availed should be shown as a deduction from the 'Provision for Taxation' on the liabilities side of the balance sheet. "

Computation of income as per MAT

Profit as per Profit & Loss Account	₹300.00 lakh
Less: B/f loss before depreciation OR Unabsorbed Depreciation **as per books**, whichever is less	₹0.00 lakh
Income subject to MAT	**₹300.00 lakh**
MAT @ 19.93 per cent	**₹59.79 lakh**

Note- For A.Y. 2011-12 MAT rate has been increased to 18 per cent plus surcharge @ 7.5 per cent and education cess @ 3 per cent, making effective rate as 19.93 per cent

Computation of income as per normal provisions

Profit as per Profit & Loss Account	₹300.00 lakh
Add: Depreciaton as per books	₹10.00 lakh
Less: Depreciation as per Income Tax Act	₹7.00 lakh
	₹303.00 lakh
Less: B/f business loss u/s. 72	₹0.00 lakh
	₹303.00 lakh
Less: Unabsorbed Depreciation u/s. 32(2)	₹0.00 lakh
Taxable Income	**₹303.00 lakh**
Tax @ 33.22 per cent	**₹100.66 lakh**

Since the tax liability as per normal provisions exceeds the liability under MAT, the company is allowed to utilise the credit to the extent of ₹40.87 lakh and balance ₹59.79 lakh shall be actually payable.

The accounting entries to be passed on 31st March, 2011 shall be

Profit & Loss Account	Dr.	100.66
To Provision for taxation (A.Y. 2011-2012)		100.66

Provision for taxation (A.Y. 2011-2012)	Dr.	40.87
To MAT Credit entitlement		40.87

(Excess of normal tax liability over liability under MAT i.e. ₹100.66 lakh (-) ₹59.79 lakh)

Balance of MAT credit Entitlement in the Balance Sheet of 31st March, 2011 shall continue to be shown under Loans & Advances to the extent of ₹77.93 lakh (₹118.80 lakh (–) ₹40.87 lakh)

On expiry of ten years, the unutilised balance in the MAT credit entitlement account, if any, will be written off to Profit & Loss Account.

Disclosure in Financial Statements

If the company decides to follow the treatment of MAT Credit as per Guidance Note, it is advisable to make the disclosure in Accounting Policies or notes to accounts. MAT credit is not a regular feature of a business and hence disclosure in only notes to accounts may be sufficient.

Section 10A/10B Companies

The profits derived by an undertaking covered by Sections 10A and 10B, though eligible for exemption under normal provisions, are subject to MAT under Section115JB.

The deduction under 10A and 10B is not allowed with effect from Assessment Year 2012-2013. Thus the financial year ended 31st March, 2011 shall be the last financial year for availing deductions under these sections. Since these companies are profit making, the utilisation of MAT credit is virtually certain. Hence, compliance of Guidance Note by such companies shall be more appropriate.

Position Under New Direct Tax Code

The first draft of Direct Tax Code provided for MAT as follows-

(i) In the case of banking companies, the rate of MAT will be 0.25 per cent of the value of gross assets while in case of all other companies it will be 2 per cent of the total value of gross assets.

(ii) The MAT will be a final tax, and as such, the same cannot be carried forward to subsequent years for the purpose of claiming tax credit.

However, the revised draft of DTC, released recently, states-

'Some of the issues raised by stakeholders (such as MAT credit) can be addressed by making appropriate changes in the proposed scheme of the asset based MAT. However, there may be practical difficulties and unintended consequences, particularly in the case of loss making companies and companies having a long gestation period. It is, therefore, proposed to compute MAT with reference to book profit.'

"The revised draft of DTC, released recently, states: 'Some of the issues raised by stakeholders (such as MAT credit) can be addressed by making appropriate changes in the proposed scheme of the asset based MAT. However, there may be practical difficulties and unintended consequences, particularly in the case of loss making companies and companies having a long gestation period. It is, therefore, proposed to compute MAT with reference to book profit.'"

Other Effects of MAT Credit

1. Creation of asset by crediting Profit and Loss Account would result in increase of net worth of the company
2. MAT credit, to the extent of utilisation, can be taken into consideration for determining advance tax installments
3. Although it may not be a prudent financial practice, legally a company can declare dividend out of its credit balance in Profit and Loss Account

Authority of Guidance Note

The ICAI has clearly laid down the authority attached to Guidance Notes issued by it.

The broad principles to be noted with regard to Guidance Notes, their applicability and the authority attached to them are:

a) Guidance Notes are recommendatory in nature;
b) Guidance Notes are primarily designed to guide members of the Institute and assist members in resolving issues which may pose difficulty;
c) A member should ordinarily follow the recommendations in the Guidance Notes relating to auditing matters. If an accounting matter has not been followed, the auditor shall consider whether a disclosure is required in his report.

This Guidance Note is not a part of 'Mandatory Guidance Notes' specified by ICAI. However, it is an important Guidance Note, the adherence to which can result in true and fair view of company's financial position. ■

Intangible Assets and Market Capitalisation - A Case Study of FMCG Companies in India

Market capitalisation has been popular among the Indian companies for last two decades to support and enhance the value creation for the shareholders. It is calculated by outstanding shares multiplied by market value per share at the end of the financial year. It plays an important role for determination of the value of intangible assets. Their are various methods for the valuation of intangible assets such as, Direct Intellectual Capital method, Market Capitalisation method, Return on Assets method (ROA), Scorecard method/indicators method and Knowledge Capital Earnings, etc. Out of all these methods, market capitalisation method (MCM) has been taken up by the author to analyse creation of intangible assets by the FMCG companies in India. MCM method is useful in dealings of merger & acquisition situations and for stock market valuations. It can also be used for comparisons between companies within the same industry and it is good for demonstrating the financial value of intangible assets. This article highlights the valuation of intangible assets by market capitalisation method especially for FMCG industry because they have been claiming higher intangible assets (90.14 per cent of the market capitalisation) over the last five years.

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Market capitalisation method is one of the best valuation methods which indicate intangible assets by market capitalisation over the net worth of the company. In the last few years, more and more firms have shown keen interest about the valuation and reporting for intangible assets due to difference between market value and book value of the shares of the firms. When there is a wide difference between firm's market value and book value, the difference will be treated as Intangible Assets. This 'intangible assets' is equal to a sum of its human capital (talent), structural capital (intellectual property, methodologies, software, documents and other knowledge), and customers capital (clients relationship). Intellectual capital is the ability to transform knowledge and intangible assets into wealth creating resources by multiplying human capital with structural capital.

Market Capitalisation

Market capitalisation is a measurement of the size of a business enterprise equal to the share price times the number of shares outstanding of a public company. Market capitalisation is popular in the area of financial management especially over the last two decades. It is one of the measures of the strength of company related with demand of the share at national as well as global market. Market capitalisation is calculated by outstanding shares multiplied by market value per share at the end of the financial year. Market capitalisation is a market estimate of a company's value, based on perceived future prospects, economic and monetary conditions. Stock prices can also be moved by speculation about changes in expectations about profits or about mergers and acquisitions.

Net worth: At the time of calculation of intangible assets under market capitalisation method, net worth is a significant indicator. Net worth is the total assets minus external liabilities of an individual or a company. For a company, this is called shareholders' equity and may be referred to as book value. Net worth is stated for a particular point in time. Net worth is generally based on the value of all assets and liabilities at the carrying value, that is, the value as expressed on the financial statements. To the extent that items on the balance sheet do not express their true ("market") value, the net worth will also be inaccurate. Normally net worth is equal to paid up capital, plus reserves and funds minus fictitious assets.

Intangible assets: Under the market capitalisation method, intangible assets are taken as difference between market capitalisation for particular time (normally at the end of the financial year) and net worth. To find out the value of intangible assets, market capitalisation method (MCM) is one of the popular valuation methods. Under this method initially market capitalisation is calculated by multiplying the market value per share with number of outstanding shares, then deducted from the stockholders equity value, difference will be treated as the value of intangible assets. This 'intangible assets' is commonly represented by the value for Human capital[1], Relationship capital[2] and Organisational (Structural) Capital[3].

At global level, India is the third largest country having higher intangible assets in the market capitalisation among the European Union, G8, Organisation of Economic Co-operation & Development countries and even the BRIC grouping. India Inc is having most 'intangible assets' among Asian economies, but is number three economy in the world with the highest intangible component as a percentage of the total enterprise value (TEV), value of disclosed and undisclosed tangible and intangible assets. With an estimated intangible assets component of 74 per cent (as proportion of TEV), India is just behind US (75 per cent) and Switzerland (74 per cent), according to Global Intangible Tracker 2007 (GIT), the most extensive global study ever on intangibles assets by the London-based Brand Finance Institute. Global intangibles to TEV average is around 65 per cent.

Market Capitalisation and Indian Companies

Market capitalisation is one of the bases for the shareholders value creation. In long term perspective higher market capitalisation indicates higher demand for the shares in the open market due to higher earning/profitability and higher market share in the business operations. Similarly it also depends on the long term strategy of the company as to how are they utilising their resources such as manpower, their knowledge, competence and skills to enhance the earning for the shareholders. At global level, India is the third largest country having higher intangible assets in the market capitalisation among the European Union, G8, Organisation of Economic Co-operation & Development countries and even the BRIC grouping. India Inc is having most 'intangible assets' amongst Asian economies, but is number three economy in the world with the highest intangible component as a percentage of the total enterprise value (TEV), value of disclosed and undisclosed tangible and intangible assets. With an estimated intangible assets component of 74 per cent (as proportion of TEV), India is just behind US (75 per cent) and Switzerland (74 per cent), according to Global Intangible Tracker 2007 (GIT), the most extensive global study ever on intangibles assets by the London-based Brand Finance Institute[4].Global intangibles to TEV average is around 65 per cent.

[1] Human capital refers to Capability of a company to benefit from knowledge, skills and experience of employees, which imminently pertain to the latter, such as capability for innovations, creativity, know-how and experience, ability to work in a team, motivation, learning capability, educational and professional level and loyalty, etc.

[2] Relationship Capital refers to capability of a company to benefit from resources connected with the company's external relations (with customer, suppliers, and other counteragents) such as brands, suppliers, loyalty of the customers, distribution channels, business cooperation, alliances and partnerships, licensing agreements, franchising agreements, etc.

[3] Organisational (Structural) Capital means capability of a company to benefit from attainments remaining inside the company such as Intellectual Property patents, trademarks, service marks, name of origin of goods, copyright, etc. *Infrastructural Assets* corporate culture, internal administration of the workflow, information systems, management philosophy, decision-making system, etc.

[4] GIT 2007, exclusive global break with ET, covered over 5,000 companies in 32 countries. For India, GIT considered the top 50 companies (by market cap) on the Bombay Stock Exchange.

As far as Indian companies are concerned Exhibit I indicates the market capitalisation by top 20 Indian companies in the year 2009. Reliance Industries Ltd. is top among the 20 companies with a market capitalisation of ₹337998 crore in the year 2009 then followed by ONGC (₹255415 crore), NTPC (₹175452 crore) and so on. When we analyse the nature of industry and market capitalisation to know which industry contributed more among the top 20 companies, we find that Infrastructure companies were the leader in the market capitalisation process in the year 2009. Five companies were from infrastructure sector such as NTPC, BHEL, L&T, SAIL and Sterlite industry as they contributed significantly in market capitalisation. Four companies belonged to Oil and Gas sector (RIL, ONGC, Indian Oil, and GAIL), four companies from banking & finance sector (SBI, ICICI bank, HDFC bank and HDFC), while three companies belonged to information technology and computer software industry (Infosys, TCS, and WIPRO), two companies belonged to FMCG (ITC and HUL) and two companies from Telecommunication sector (Bharti Airtel and Reliance communication). In summary we can say that in the year 2009 higher market capitalisation secured by the Oil and Gas, Power, Banking and Telecommunication sectors.

Exhibit I

Top 20 Indian Companies based on the Market Capitalisation-2009

Top 20 Rank	Company	Industry type	Market Capitalisation 2009 (₹ in crore).
1.	Reliance Industries ltd	Oil & Gas	337998
2.	ONGC	Oil & Gas	255415
3.	NTPC	Power	175452
4.	SBI	Banking	143211
5.	Bharti Airtel	Telecom	128968
6.	Infosys Technologies	InfoTech	128085
7.	TCS	Computer	120000
8.	BHEL	Capital Goods	117729
9.	ICICI bank	Banking	100003
10.	L&T	Capital Goods	96073
11.	ITC	FMCG	95204
12.	WIPRO	InfoTech	86264
13.	Indian oil	Oil & Gas	79043
14.	HDFC	Housing Finance	77860
15.	SAIL	Infrastructure/Steel	73009
16.	HDFC bank	Banking	71238
17.	Sterlite industries	Copper Product	67275
18.	HUL	FMCG	61342
19.	Reliance communication	Telecom	49019
20.	GAIL	Petroleum Gas	46589

Source: http://money.rediff.com/companies/market-capitalisation

Market Capitalisation and Intangible Assets

Over last two decades, especially after globalisation, many financial expert and management gurus are of the opinion that the most important assets for both old as well as new economy businesses are not the tangible assets conventionally reported on the company balance sheet, but the intangible, Intellectual Capital Assets, which are not reported in any financial statements due to lack of recognition under AS 26 and other laws.

“Even after the global slowdown/economic crisis over the last two and one half years, the market capitalisation of top 50 Indian companies exceeds their book value by two, three or even four to one. This means that for every Rupee of value contributed by tangible assets, two to four Rupees more are being contributed to enterprise value by the intangibles. This is a true feature of the old economy as well as the new economy companies. This means that the value being contributed by their intangible Intellectual Capital Assets is significantly greater than the value contributed by their largely acquired physical assets. Consequently, knowledge and service sector industries are allocating/spending more funds for the creation and maintenance of intangible assets.”

Market capitalisation plays an important role in the determination of the value of intangible assets in the current knowledge environment. Intangible assets play an important role in the valuation of enterprises. In the 1980 the share of intangible assets as part of a company’s market value was 40 per cent which increased up to 80 per cent by the end of 1990 and in certain companies (such as IT sector) up to 90 per cent till 2007. In the global economy, intangible assets play an increasingly important role, and consequently, inability of financial statements to adequately report intangible assets on a company’s Balance sheet results in a declining value of financial statements for users of financial information.

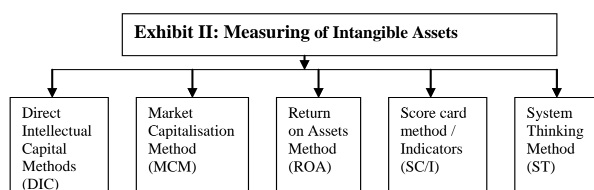
Even after the global slowdown/economic crisis over the last two and one half years, the market capitalisation of top 50 Indian companies exceeds their book value by two, three or even four to one. This means that for every Rupee of value contributed by tangible assets, two to four Rupees more are being contributed to enterprise value by the intangibles. This is a true feature of the old economy as well as the new economy companies. This means that the value being contributed by their intangible Intellectual Capital Assets is significantly greater than the value contributed by their largely acquired physical assets. Consequently, knowledge and service sector industries are allocating/spending more funds for the creation and maintenance of intangible assets.

Analysis of the corporate valuation depends upon the market capitalisation which is divided into two parts, one is tangible assets evaluating as book value and reported on the balance-sheet by every company and second is intangible assets which are largely not reported by the companies in

the balance sheet which represent the rest of the market capitalisation. Now the question arises if a company wants to enhance the corporate value, how can they use intangible assets and tangible assets? The simple answer is that corporate valuation can be enhanced by leveraging enterprise assets to create value and drive growth through the efficient leveraging of the tangible assets comprising book value, and the strategic leveraging of the intangible Intellectual Capital Assets. Therefore, we can actually steer and enhance the corporate valuation by optimising and leveraging both the tangible and the intangible assets within the enterprise. To find out the value or real contribution of Intangible Assets in the growth and development, market capitalisation is the best technique in contemporary environment.

Measuring and Valuation of Intangible Assets

The idea that corporations must manage their employees, customer relations, and other Intangible Assets is not new. The new thing is the increased attention the corporates are paying to intangible assets. Baruch Lev[5] puts forward the unique combination of two related economic forces as the reason for the recent surge of interest in Intangible Assets; intensified business competition brought about by the globalisation of trade and deregulation in key economic sectors, and the advent of information technologies. Together, they have dramatically changed the structure of corporations and have projected Intangible Assets into the role of the major value drivers. According to Karl Erik Sveiby[6], the following are the approaches for the measuring of intangible assets.



- *Direct Intellectual Capital Method (DIC)*: Under this method monetary value of intangible assets are estimated by identifying its various components. Once these various components are identified then they can be evaluated directly.
- *Market Capitalisation Method (MCM)*: Under this method first of all market capitalisation is calculated by multiplying the market value per share with number of outstanding shares, then deducted from the stockholders equity value, difference will be treated as the value of Intangible Assets.
- *Return on Assets Method (ROA)*: This method is one of the simple methods for the calculation of value of intangible assets. Under this method average pre tax earnings of the company is divided by the average tangible assets of the company and then the ROA is compared with the industry average. If any excess difference will be multiplied by the average tangible assets of the company and it is the average earning/ value for the Intangible Assets.
- *Score card Method/Indicators method*: Under this method various components of Intangible Assets or intellectual capital of the firm are identified and indicators and indices are generated and reported in scorecard/graph. There are similarities in the DIC and SC method except that the estimated value is made in currency value.
- *Knowledge Capital Earnings (KCE)*: This method was proposed by Baruch Lev (2001). First, one needs to normalise earnings three years before and the forecast for three years after. Subtracting the income caused by intangibles from the normalised earnings gives a portion of non-accounted earnings. This amount represents knowledge capital earnings and can be used for different ratios such as intellectual capital margin KCE/ sales, and operative knowledge capital margin KCE/net income.

Out of all these methods, market capitalisation method (MCM) has been taken up by the author to analyse the creation of intangible assets by the FMCG companies in India. MCM method is useful in dealings of merger & acquisition situations and for stock market valuations. It can also be used for comparisons between companies within the same industry and it is good for demonstrating the financial value of Intangible assets.

Market Capitalisation & FMCG Industry

FMCG industry is one of the popular and strong customer base industries in India for many years. Under this category firms such as Dabur, HUL, Colgate Palmolive, Britannia, ITC, Nestle, Marico, and Godrej are the major FMCG companies as they are contributing a major part in India FMCG market. For calculation of market capitalisation, average of the Higher and lower market value for the month of March every year at Bombay stock exchange (BSE) is taken for the last five years (2004-2005 to 2008-2009). When we analyse the market capitalisation and role of intangible assets, FMCG companies are leader among all industries (refer Exhibit III). In the process of market capitalisation, ITC is having strong market capitalisation with an average of ₹62148

[5] **Lev, B. (2001)** *"Intangibles: Management, Measurement, and Reporting"*, Washington, D C: The Bookings Institution.
[6] See Kari-Erik Sveiby (www.sveiby.com.au)

When we analyse the market capitalisation and role of intangible assets, FMCG companies are leader among all industries. In the process of market capitalisation, ITC is having strong market capitalisation with an average of ₹62148 crore during the last five years and similarly, they have also created huge intangible assets on an average ₹51511 crore in the same period. Second largest market capitalisation in the same period was created by HUL with ₹44278 crore and they have also generated intangible assets worth ₹42103 crore. These are followed by Nestle, Godrej, Dabur, Colgate Palmolive and Britannia respectively.

crore during the last five years and similarly, they have also created huge intangible assets on an average ₹51511 crore in the same period. Second largest market capitalisation in the same period was created by HUL with ₹44278 crore and they have also generated intangible assets worth ₹42103 crore. These are followed by Nestle, Godrej, Dabur, Colgate Palmolive and Britannia respectively.

Exhibit III

Market Capitalisation and Intangible Assets - FMCG Industry

(In crore ₹)

Companies	Total market capitalisation*	Net worth*	Intangible assets**	per cent of intangible assets with total market capitalisation	Market capitalisation/ Net worth (In times)	Rank
DABUR	6540	555	5985	91.52 per cent	11.78	IV
HUL	44278	2125	42103	95.20 per cent	20.84	II
COLGATE	4894	236	4650	95.18 per cent	20.74	III
BRITANNIA	3099	638	2461	79.42 per cent	4.86	VIII
ITC	62148	10637	51511	82.88 per cent	5.84	VII
NESTLE	11016	443	10573	95.98 per cent	24.87	I
GODREJ	6614	641	5973	90.31 per cent	10.32	VI
MIRCO	3068	288	2780	90.62 per cent	10.65	V

Source: calculated and complied from the annual reports from 2004-2005 to 2008-2009.
*Average of the last five years. ** Intangible assets = Market capitalisation – Net worth

When we compare Intangible Assets with market capitalisation to know the contribution of intangible assets in the overall market capitalisation and creation of intangible assets, the scenario is found to be entirely different. Nestlé is the company in which contribution of intangible assets are 95.98 per cent of market capitalisation and it is leading among the FMCG companies. The second and third places are secured by HUL (95.20 per cent) and Colgate (95.18 per cent) of their market capitalisation respectively, and then followed by Dabur (91.52 per cent), Marico (90.62 per cent), Godrej (90.31 per cent), ITC (82.88 per cent) and Britannia with 79.42 per cent.

When market capitalisation is compared with net worth to know the impact of intangibles on the shareholder value creation, again Nestlé is the leader— their market capitalisation is 24.87 times the net worth, which indicates that intangible assets are having a greater role in the shareholder value creation. Nestle is followed by HUL (20.84), Colgate (20.74) Dabur (11.78), Marico (10.65), Godrej (10.32) ITC (5.84) and Britannia with 4.86 times of their market capitalisation. In FMCG industry intangible assets are in the form of Goodwill, Trade Marks & Patent, Computer Software, Copyrights and Design, Business and Commercial Rights, Technical Know-how and Strong customer base, and distribution channels, etc.

Many important but hidden or not disclosed or non-reported intangible assets are also related with FMCG companies. One of the important intangible assets is Brand of the FMCG companies which attract and retain many customers and result in higher market share, higher turnover and profitability. According to top 50 brands in the year 2009 as reported by ET[7], ITC was having 9th position with the brand value of ₹11271 crore, and Dabur India was having 25th position with ₹3045 crore, but these values are not a part of financial statement (self generated intangible assets) due to lack of recognition. Another important intangible asset is strong customer base and distribution network. But due to the lack of their recognition under AS-26, companies cannot disclose and incorporate the value of these intangible assets in financial statements.

Over all creation of intangibles assets has been 90.14 per cent for the FMCG industry in the last five years.

Conclusion

FMCG industry is one of the oldest customer based industry for more then two centuries. Their main intangible assets are their bands and strong customer base which directly support them to enhance the shareholder value creation. As contribution of service oriented industries increase in our economy, intangible assets are having a greater importance in earning as well as wealth creation for the shareholders. But unfortunately current accounting and reporting practices do not cover all the intangible assets in annual reporting statements. For instance Britannia may not be the most admired company but its strong brand continuously earns more money for it. The most valuable intangible assets for HUL are its brand and channel partners (both form the external structure). However, gradually as per the need of the hour and international practices some leading Indian firms are reporting the valuation of intangible assets, Brand valuation and market capitalisation in their reporting practices, which is very useful for the various stakeholders to take appropriate decisions regarding investment and ownership about the company in competitive environment. ■

[7] *The Economic Times dated November 21, 2009*

Taxation of Non-Profit Organisations

The Finance Minister introduced the Direct Taxes Code Bill, 2010 (DTC) in the Parliament on 27-8-2010. This Bill contained 319 Sections divided into 20 Chapters. There are 22 Schedules annexed to this Bill which explain the details about computation of income, procedure to be followed, rates of taxes, rates of depreciation, etc. Sections 90 to 103 and Schedule 7 provide for taxation of Non-Profit Organisations. In the DTC the term "Non-Profit Organisation" (NPO) is used for a Charitable Trust. The provisions for taxation of NPO in DTC are very harsh as compared to the existing provisions in the Income-tax Act, 1961 granting exemption to Charitable Trusts under Sections 11 to 13. This article discusses the provisions of DTC relating to Non-Profit Organisations.

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The Finance Minister introduced the Direct Taxes Code Bill, 2010 (DTC) in the Parliament on 27-8-2010. This Bill contained 319 Sections divided into 20 Chapters. There are 22 Schedules annexed to this Bill which explain the details about computation of income, procedure to be followed, rates of taxes, rates of depreciation, etc. Under the existing Income-tax Act, 1961 the rates of taxes are announced every year through the Finance Bill introduced with the Budget every year. Now, DTC gives Rates of Taxes in the first four schedules. At present, there are two separate Acts for levying Income tax and Wealth tax. DTC now provides for levy of Income tax and Wealth tax and rates for both these taxes are given in Schedules 1 and 2. DTC provides that, after Parliament enacts this legislation, it will be effective from 1-4-2012.

Sections 90 to 103 and Schedule 7 provide for taxation of Non-Profit Organisations. In the DTC the term "Non-Profit Organisation" (NPO) is used for a Charitable Trust. The provisions for taxation of NPO in DTC are very harsh as compared to the existing provisions in the Income-tax Act, 1961 granting exemption to Charitable Trusts under Sections 11 to 13.

What is a Non-Profit Organisation?

The term "Non-profit Organisation" (NPO) is defined in Section 314 (169) to include any organisation or a trust if -

(i) It is not established for the benefit of or does not provide any benefit to any particular caste or religious community.

(ii) It is established for carrying on Charitable activities or activities for the benefit of general public, scheduled caste, scheduled tribes, backward classes, women or children.

(iii) It actually carries on the charitable activities during the financial year.

(iv) It is not for the benefit of any of its members.

(v) The actual beneficiaries of its activities are the members of general public, scheduled caste, scheduled tribes, backward classes, women or children.

(vi) It is registered as NPO by CIT under Section 98 of DTC or under Section 12 A/12 AA of Income-tax Act,1961 (ITA). It appears that item (iv) above will mean that chambers of commerce, trade associations, etc. may not be considered as NPOs.

Some Definitions Relating to NPO

The following terms are defined in Section 103 as under.

(i) "Charitable Activity" means (a) Relief of the poor, (b) Advancement of Education, (c) Medical Relief, (d) Preservation of Environment, Monuments, Plaques or objects of artistic or historic interest, (e) Advancement of any other object of general public utility, not involving the carrying on of any activity in the nature of trade, commerce, business or any activity of rendering any service in relation thereto for any cess, fee or any consideration and where the gross receipts from such activity in a F.Y. exceeds ₹10 lakh. It may be noted that in the Finance Bill, 2011, this limit is proposed to be increased to ₹25 lakh. Therefore, corresponding limit in DTC is likely to be increased to ₹25 lakh.

(ii) "Business incidental to charitable activity" means a business carried on in the course of the actual carrying out of any charitable activity.

(iii) "General Public" means the body of people, at large, sufficiently defined by some common quality of public or impersonal nature.

"The definition of Non-Profit Organisation does not include an institution or trust for religious purposes. At present, Section 11 of ITA grants exemption to an institution established for religious purposes complying with certain conditions. Section 90 (3) of DTC specifically provides that Sections 90 to 94, 96 and 100 dealing with special provisions for computation of total income of the NPO will not apply to public religious trust or institution."

(iv) "Interested Person" means (a) the Settler, Founder, Manager or Trustee of the organisation or trust, (b) Any relative of the persons stated in (a), (c) Any person whose total contribution or donation to the NPO exceeds ₹50,000/- in the F.Y. (d) Any member of HUF, if the settler/founder is HUF or (e) Any concern in which any of the persons stated above has a substantial interest.

(v) Section 314 (185) defines the expression "person having a substantial interest in a concern" to mean -

(a) A person who, along with one or more relatives, has a beneficial ownership of equity shares carrying 20 per cent or more of the voting power in a company, at any time, during the F.Y. Here, the word "company" will include an Indian or Foreign company, whether closely held or widely held.

(b) A person who, along with one or more relatives, is entitled to 20 per cent or more of the income in a HUF, Firm, LLP, AoP, BoI, etc.

(vi) Section 314 (214) defines the word "Relative" in relation to an Individual to mean (a) Spouse, Brother, Sister or any lineal ascendant or descendant of the Individual, (b) Brother, Sister or any lineal ascendant or descendent of the spouse of the Individual, (c) Brother or Sister of either of the parents of the individual, (d) Spouse of the persons referred to (a), (b) or (c), (e) Any lineal descendant of the Brother or sister of the Individual or Spouse of the Individual. It may be noted that the spouse of the nephew or niece is not considered as a relative.

Religious Trusts

From the above, it is evident that the definition of NPO does not include an institution or trust for religious purposes. At present, Section 11 of ITA grants exemption to an institution established for religious purposes complying with certain conditions. Section 90 (3) of DTC specifically provides that Sections 90 to 94, 96 and 100 dealing with special provisions for computation of total income of the NPO will not apply to public religious trust or institution. However, it may be noted that the following powers to grant exemption

to certain Institutions or Trusts are given to the Central Government.

(i) Under Section 90 (2) the Central Government may notify a person as NPO of public importance which will be entitled to exemption from Income tax and Wealth tax. This exemption will be available subject to such conditions as may be notified by the Government.

(ii) Under Item No.39 of Schedule 7 it is provided that a public Religious Trust or Institution will not be liable to pay any Income tax if the following conditions are complied with.

  (a) It is registered under any State Act, if any, and is also registered under Section 98 of DTC.

  (b) It is established for the benefit of the General Public and applies its income for Public Religious purposes.

  (c) It maintains books of account and obtains audit report from a Chartered Accountant if its gross receipts exceed ₹5 lakh in any F.Y.

  (d) Its funds or assets are invested or held, at any time during the F.Y., in the modes specified in Section 95 of DTC, and

  (e) Its funds or assets are not used or applied, directly or indirectly, for the benefit of any interested person.

It may be noted that the provisions of Section 100 of DTC dealing with Anonymous Donations do not apply to a Public Religious Trust or Institution. Similarly, the restriction on accumulation of income and utilisation of such income within specified period will also not apply to such a Religious Trust or Institution.

Other Trusts

At present, Sections 10 (23 A) and 10 (23 C) of ITA grants exemption to certain notified institutions established for regulation of profession of law, accountancy, medicine, engineering, etc. and certain recognised universities, colleagues, schools, hospitals etc. subject to certain conditions. No such separate provision is made in DTC. Therefore, such institutions will now be governed by the provisions of Sections 90 to 103 and Schedule 7 of DTC.

Computation of Income of NPO

Section 92 provides that the total income of NPO in relation to any charitable activity shall be computed on cash basis of accounting by deducting the outgoings specified in under Section 94 out of the gross receipts specified under Section 93. However, in the case of NPO which is a company registered under Section 25 of the Companies Act, 1956 such computation shall be made on the basis of mercantile system of accounting.

The "gross receipts" of NPO shall be the aggregate of various receipts as provided in Section 93. Briefly stated this will include –

(i) The amount of voluntary contributions received during the financial year;

(ii) Any rent from property and income from business which is incidental to any charitable activities of NPO;

(iii) Capital Gains computed under Sections 46 to 54 of DTC on transfer of asset not used for charitable activity or business incidental to such activity;

(iv) Full value of the consideration received from the transfer of any asset other than the asset referred to in (iii) above;

(v) The amount of any income received from any investment of its funds or assets and all other incomings, realisations, proceeds, or subscriptions received from any source;

(vi) Any amount received in the month of March of the F.Y. will be considered as income of the subsequent F.Y. if it is not deposited in a specified deposit account as per the scheme prescribed by CBDT during the subsequent F.Y.

However, the gross receipts shall not include –

(a) Any loan taken in the F.Y.

(b) Donations received with specific direction that it shall form part of the corpus of NPO.

Briefly stated, the amount of "outgoings" referred to above as provided in Section 94 are as under:

(i) The amount paid during the F.Y. for any expenditure (other than capital expenditure) incurred wholly and exclusively for earning or obtaining gross receipts stated in Section 93.

(ii) The amount paid for any expenditure incurred for the purpose of carrying out charitable activity. It appears that the above expenditure will include capital expenditure.

(iii) Any capital expenditure for the purpose of business which is incidental to the charitable activity of the NPO. As the entire capital expenditure is allowed as deduction no depreciation can be claimed separately.

(iv) Any amount applied outside India by NPO, notified by the Government, for an activity which promotes international welfare in which India is interested.

"Section 92 provides that the total income of NPO in relation to any charitable activity shall be computed on cash basis of accounting by deducting the outgoings specified in under Section 94 out of the gross receipts specified under Section 93. However, in the case of NPO which is a company registered under Section 25 of the Companies Act, 1956 such computation shall be made on the basis of mercantile system of accounting."

Section 100 provides that if the NPO receives any anonymous donation of an amount aggregating to 5 per cent of total donations in any F.Y. or Rs.1 lakh, whichever is higher, then Income tax at the rate of 30 per cent on such excess amount shall be payable by the NPO. No deduction will be allowed in respect of any outgoings in respect of this type of donation. This tax is payable even if the anonymous donation is with a direction that it shall form part of the corpus of the trust. For this purpose, an anonymous donation shall mean any voluntary contribution in respect of which no record about identity of the donor, his address and such particulars as may be prescribed by CBDT are maintained by the NPO.

(v) Any amount accumulated or set apart for carrying on any charitable activity to the extent of 15 per cent of total income or 10 per cent of the gross receipts whichever is more. Further, the above accumulated amount should be invested or deposited in the specified modes as provided in Section 95 for a maximum period not exceeding three years from the end of the F.Y.

Accumulation of Income by NPO

Section 96 provides that the amount accumulated, as stated above, shall be deemed to be the income of NPO if the said accumulated amount is not utilised for the purpose for which it is accumulated or set apart within the above period of 3 years or ceases to be invested or deposited as provided in Section 95. In view of such a short period of accumulation, restricted to 15 per cent of total income or 10 per cent of gross receipts, whichever is higher, it will be difficult for any NPO to build up a corpus for investment in any large project for the benefit of general public.

Tax Payable by the NPO

(i) From the above, it is evident that NPO cannot accumulate more than 15 per cent of total income as computed after deducting from the gross receipts specified in Section 93 the outgoings specified in Section 94 or 10 per cent of such gross receipts, whichever is more. If such accumulation is more than the above permitted amount the same will be taxable at the rate provided in paragraph "C" of Schedule 1. This rate is as under.

(a)	First ₹1 lakh	Nil
(b)	Balance of total income	15 per cent

(ii) Section 100 provides that if the NPO receives any anonymous donation of an amount aggregating to 5 per cent of total donations in any F.Y. or ₹1 lakh, whichever is higher, then Income tax at the rate of 30 per cent on such excess amount shall be payable by the NPO. No deduction will be allowed in respect of any outgoings in respect of this type of donation. This tax is payable even if the anonymous donation is with a direction that it shall form part of the corpus of the trust. For this purpose, an anonymous donation shall mean any voluntary contribution in respect of which no record about identity of the donor, his address and such particulars as may be prescribed by CBDT are maintained by the NPO.

(iii) Section 112 provides that no Wealth tax shall be payable by any NPO.

(iv) The NPO shall be liable to pay income tax at the rate of 30 per cent in respect of its net worth if -

(a) It converts into any form of organisation which does not qualify as NPO;

(b) It merges with any organisation which is not NPO;

(c) It fails to transfer, upon its dissolution, all its assets to any other NPO within three months from the end of the month in which it is dissolved.

"Net worth" for this purpose means aggregate value of assets less liabilities as computed by Rules to be prescribed by CBDT.

Investment of Funds of the NPO

Section 95 provides for modes of investing or depositing the surplus money with NPO. The permitted list of such investments or deposits is as under:

(i) Deposit in any Post Office Savings Bank, Schedule Bank or any other public sector company.

(ii) Investment in any Central or State Government securities, any debentures of any company/corporation guaranteed by Central/State Government or any public sector company.

(iii) Investment in any immovable property, or

(iv) Any other mode of investment or deposit as may be prescribed by CBDT.

From the above list it is evident that this list is restrictive as compared to modes of investments or deposits permitted in Section 11(5) of ITA.

Section 97 provides that the funds or assets of the NPO shall not be used or applied, directly or indirectly, for the benefit of an interested person. Section 97(2) provides for a deeming fiction when the funds, assets or income of NPO shall be deemed to have been used for the benefit of an interested person. The term interested person is defined in Section 103 as stated in para 3 above. It may be noted that Section 97 is more or less similar to existing Section 13 of ITA.

Accounts and Audit

Section 99 provides that the NPO should keep and maintain

such books as may be prescribed by CBDT. Separate books of accounts should be maintained for the Business, incidental to the charitable activity, carried on by the NPO. The NPO should obtain, before the due date for filing the Return, a report from a Chartered Accountant if the specified gross receipts, exceed Rs. 5 lakh.

Registration of NPO

(i) It will be mandatory for every NPO to register with the income-tax Department, by making an application to the Commissioner of Income tax, as provided in Section 98. The Commissioner, after calling for such information as he may deem fit, has to pass an order within six months from the end of the month in which the application is received. If the registration is refused, the applicant shall have the right to appeal before the Income tax Appellate Tribunal under Section 183. This procedure is similar to that provided in Sections 12 A and 12 AA of ITA.

(ii) If a trust or institution is already registered under Section 12 A/12 AA of ITA prior to 1-4-2012, it will not be required to get registration under Section 98 of DTC. Such registration will be valid till it is withdrawn.

(iii) The registration, once granted, shall be valid from the financial year in which the application is made till it is withdrawn.

(iv) The donations made to a recognised NPO will be eligible for deduction in the hands of the donor at the appropriate rates as provided in Schedule 16. This provision is similar to Section 80 G of ITA.

Provisions Relating to NPO Not to Apply to Certain Organisations

Section 102 provides that the above provisions shall not apply to any organisation which -

(i) holds any business under trust, notwithstanding a specific direction that the business shall form part of the corpus of such person or a specific direction that the income from the business shall be applied only for a charitable activity ;

(ii) carries on a business which is not incidental to the charitable activity;

(iii) ceases to be NPO at any time during the financial year;

(iv) fails to comply with the provisions of Section 97 referred to above.

Principle of Mutuality

It may be noted that the above provisions relating to NPO will not affect the principle of Mutuality. As stated earlier, the definition of NPO does not cover any organisation which is for the benefit of any of its members. Therefore, the tax authorities are likely to take the stand that chambers of

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commerce, professional associations, clubs, co-operative societies, etc. will not be covered by the definition of NPO. In such cases, it will be possible to take the view that, in view of the principle of mutuality, income from subscriptions, receipts from members for common services, etc. will not be taxable. It may be noted that the principle of mutuality has been accepted in various judicial pronouncements. Some of them are

(i) *CIT v/s Banikpur Club Ltd. 226 ITR 97 (SC)*, (ii) *CIT v/s Willingdon Sports Club 302 ITR 279 (Bom)*, (iii) *CIT v/s Cement Association & Co-ordinating organisation 236 ITR 553 (Bom)*, (iv) *CIT v/s Cochin Oil Merchants' Association 168 ITR 240 (Kerala)*, (v) *Walkeshwar Triveni Co-op. Housing Society Ltd. v/s ITO 88 ITD 159 (Mum) (SB)*, (vi) CBDT Circular No.11/2008 of 19.12.2008 clarifies that under the principle of mutuality, if trading takes between persons who are associated together to contribute to a common fund for financing some venture or object and in this respect have no dealings or relations with any outside body, then any surplus arising to such association is not chargeable to tax. In such cases, there must be complete identity between the contributors and the participants.

Exemption to Political Parties

(i) The term "Political Party" is defined in Section 314 (194) to mean a political party registered and recognised under the Representation of the People Act, 1951. The term "Electoral Trust" is defined in Section 314 (87) to mean a trust so approved by CBDT in accordance with the scheme made by the Central Government.

(ii) Schedule 6 (Item No. 22) provides that the following income of a political party shall not be included in the total income of the party subject to certain conditions.

 (a) Income from House property, Capital gains or Residuary sources.

 (b) Income by way of voluntary contribution received from any person if the following conditions are complied with -

  - Proper books of Accounts from which income can be computed are maintained and are audited by a Chartered Accountant.
  - Records of such contributions with names and

- addresses of such persons where contribution exceeds ₹20,000/- are maintained.
- The Treasurer of such party submits the prescribed report to the authorities.

The above provisions are similar to Section 13 A of ITA.

(iii) Item No.22 of Schedule 7 provides that an Electoral Trust is not liable to pay any income tax under DTC if 95 per cent of the aggregate of all voluntary contributions received by it during the F.Y. and the surplus, if any, brought forward from any preceding year is distributed to political parties. This provision is similar to Section 13 B of ITA.

(iv) Any contribution to a recognised Political Party or a recognised Electoral Trust is allowable as deduction in the computation of income as provided in Section 81. The deduction is restricted to 5 per cent of the average net profit for the three preceding F.Y. in the case of a company or 5 per cent of gross total income from ordinary sources in other cases.

Some Issues

From the analysis of the above provisions relating to taxation of NPO it appears that some of the concessions which are enjoyed by Charitable Trusts, Religious Trusts, Chamber of Commerce, Trade Bodies, Professional Institutions and other similar Organisations at present under the provisions in ITA will not now be available if DTC is enacted in its present form. Some of the important issues are as under:

(i) Religious Trusts and other similar Trusts created for the benefit of a particular caste before 1-4-1961 will not be treated as NPO and, therefore, the exemption enjoyed by them at present will not be available.

(ii) Chambers of Commerce, Trade Bodies, Professional Institutions, etc. which render service to their members may not be considered as NPO. Therefore, exemption from tax available under Section 10 (23 A) or 11 to 13 of ITA will not be available to them. As stated above, they will be able to claim limited exemption on the principle of mutuality.

(iii) Since the provisions of Sections 93 and 94 of DTC for computation of total income of NPO are not applicable to religious trusts and other institutions which are not considered as NPOs, they will have to compute income on the basis of commercial principles. It is not clear whether expenses incurred on the objects of such trusts and institutions will be allowed and under which head of income their income will be taxable.

(iv) The scope for investment of funds by NPO under Section 95 is very much restricted. Under Section 11 (5) of ITA public trusts are allowed to invest in many more instruments. If any NPO has invested in instruments permitted under Section 11 (5) of ITA but not permitted under Section 95 of DTC, no time limit for regularising such investments is provided in DTC.

(v) The period of accumulation and quantum of such income of NPO is now drastically reduced. Therefore, no NPO will be able to build up corpus out of its income for construction of Hospital, School, College etc. or for any major project for which NPO is established.

(vi) If the outgoings in the case of any NPO is more than its gross receipts in any F.Y. , there is no clarity whether the deficit will be allowed to be adjusted against the gross receipts of the subsequent F.Y. Similarly, there is no clarity whether the accumulated deficit upto 31-3-2012 will be allowed to be adjusted against the gross receipts of subsequent years under DTC.

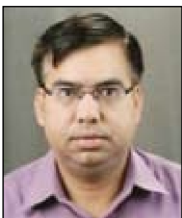
(vii) Under Section 11 of ITA there is a concept of "Computation" of income and "Application" of income to the objects of the trust. This concept is abolished in DTC. Therefore, the controversy about computation of amount to be accumulated upto 15 per cent with reference to gross receipts or net receipts, allowance of depreciation on assets whose capital cost is treated as application of income, etc. will not now arise.

(viii) It will be noticed from the above provisions that the existing exemptions to political parties under ITA is to be continued under DTC. Therefore, there is no logic in denying the existing exemption enjoyed by Charitable Trusts and Religious Trusts under DTC.

The DTC Bill has been referred to the Finance Committee of the Parliament. After receipt of this Committee's Report, the Bill will be modified on the basis of the report and the revised Bill will be discussed in the Parliament and enacted into law. From the above provisions relating to NPO, it is evident that they are very harsh. Those who desire to help the poor and needy persons and carry out Charitable objectives like relief of poor, medical relief, education, general public utility etc. will now have to part with a portion of the funds generated for this noble cause for payment of taxes to the Government. It appears that the exemption so far enjoyed by the Charitable Trusts for the last over 100 years since the Income tax was introduced in our Country will no more be available after the DTC comes into force. Majority of NPOs will have to pay tax at 15 per cent which may be enhanced after some years. Similarly, most of the Religious Trusts, Chambers of Commerce, Clubs etc. which were enjoying exemption from tax upto now will have to pay tax at the normal rate. Trustees of Charitable Trusts will have to make a strong representation before the Government for restoration of the existing exemption, before DTC is enacted into law, so that more funds are available to them for charitable objects of the Trust. ■

How to Use RTI for Income Tax Refund?

In a democratic country like India, Right to Information Act 2005 is a wonderful tool to get the Income Tax refund which may be pending for so many years. Well said by Mahatma Gandhi that "if you will not ask, you will not get" and "real swaraj will come not by the acquisition of authority by a few, but by the acquisition of the capacity by all to resist authority when abused". After computerisation and online facility of filing the income tax returns, it was expected that working of Income Tax Department will improve and assessee will be able to get their Income Tax refunds faster but situation remains different. The assessees are waiting for their refund for more than one assessment years and it is a helpless and hopeless situation for all the citizens of this country, whose refunds are due from Income Tax Department. Now RTI Act 2005 is the only hope for the assessees who are desperate for their income tax refund. It is a remarkable and most effective tool to get your income-tax refunds soon, if they have been due since long. However, you have to be careful in framing the questions you have asked for seeking information, so that you can get your refund faster.



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As all of us are aware that lot of assesses are desperately waiting for their income tax refunds which are pending since last three or more assessment years. On 19th April 2007, the Central Board of Direct Taxes stated in its press release that "It has been reported in some sections of the media that a large number of taxpayers are awaiting refunds from the income-tax department for up to three years. These reports are factually incorrect and based on incomplete appraisal of facts". As per the statement made by Minister of State for Finance, there have been instructions to issue refunds within four months from the date of receipt of return and dispatched within 30 days from the date of signing the refund order.

Continuous rise in pendency of refund claims, cost the exchequer interest of a whopping ₹5,785 crore during financial year 2008-2009, as per the report of the Comptroller and Auditor General of India.

"It took a decade for computerisation by the Income Tax department, but the pendency rate of refund claims is on

rise…we recommend that the department identify the gaps in automation," CAG said in a report on Income Tax Refunds tabled in Parliament.

During the four years from 2005-2006 to 2008-2009 reviewed by CAG for income tax refunds processed, the apex auditor said that it found procedural irregularities in refunds aggregating ₹5,803.5 crore, the tax effect of erroneous refunds being ₹135.8 crore.

The CAG also found that the time taken in processing of refunds is much longer than international standards, which range from 24 days to 6 weeks. "Our analysis showed that the average time taken for processing of refund claims, leading to issue of refund vouchers is 10 month. The average time taken for the assessee to receive the refund voucher after its issue is 40 days," CAG said.

However, the ground situation is contrary to the press release of CBDT dated 19th April, 2007. You may not have received refunds for one or more earlier years despite many reminders, personal visits, and grievance-cell applications.

What is RTI?

The Right to Information (RTI) Act came into effect from 12th October, 2005 and is applicable on the whole of India, except Jammu and Kashmir. The Act helps many citizens to obtain information, which earlier was not available to the citizens of the country, from various Government, Semi Government, Corporations, Committees, and other organisations like PSUs, Indian Railways, Universities, Banks, Reserve Bank of India and so on. Information can be accessed by making an application under the RTI Act 2005. It is very simple, least time consuming, and most inexpensive tool for getting the income tax refund as soon as possible.

Who Can Make an Application

It is important to note that only assessee can make an application for knowing the status of his/her income tax refund. As per RTI Act 2005, you can't ask the information related to another person. Even a Chartered Accountant or a Lawyer is not authorised to seek information from Income Tax on behalf of his client under RTI Act. However, the assessee can take help of some expert while drafting the application for Income Tax Refund. In case of company, firms, AOP, Society and HUF, application can be made by an officer or director of the company, partner of the firm, member of AOP or Society, Karta of HUF can also file RTI on letter head but sign the same in his individual capacity, stating clearly that the address provided is for communication purpose only.

How RTI Helps in Getting Income Tax Refund

For example, in spite of many reminders, if you have not

"It is important to note that only assessee can make an application for knowing the status of his/her Income Tax refund. As per RTI Act 2005, you can't ask the information related to another person. Even a Chartered Accountant or a Lawyer is not authorised to seek information from Income Tax on behalf of his client under RTI Act. However, the assessee can take help of some expert while drafting the application for Income Tax refund."

received Income Tax refunds for Assessment Year 2007-2008, of ₹10,000/- and for Assessment Year 2008-2009 of ₹15,000/- and for Assessment Year 2009-2010 of ₹20,000/-, you can make the application to the concerned assessing officer, where you have filed Income Tax Returns for each Assessment Year (preferably separately). The fee for an RTI application to a Central Government authority is ₹10 for each application, which can be paid in the form of demand draft/Bankers Cheque/Indian Postal Order.

You can make an application to the "Central Public Information Officer" (Your Assessing Officer) of Income Tax department personally or through registered post or Registered A.D. or Speed Post. RTI application should be addressed to the Central Public Information Officer (CPIO)/Assessing Officer, Income Tax Department and their complete address.

HOW TO MAKE RTI APPLICATION

To: Date:

The CPIO under the RTI Act 2005
ITO/ Assessing Officer
Income Tax Ward/Circle No. --------
Address------------------------------

From:
Name :
Address :
Mobile No. :
Email :

Dear Sir/Madam,

Application for information under Section 6(1) of the RTI Act 2005

I, -----------------------------------, a law abiding Citizen of India and seek some information related to my income tax refund under the RTI Act 2005:

Brief Details of the Matter

Enclosed is a photocopy of my Income Tax Return for the Financial Year ------------ (A.Y: ---------) submitted on ------------------vide acknowledgement No.--------------------------- (or Ward/Circle No. if filed manually) and My PAN is ------------------

In the mentioned Income Tax Return, I had claimed a refund of ₹ ------------------ till date, I have not received the said refund order along with the detailed calculation of the refund and the interest payable thereon and nor has it been credited to my Bank A/C No. ------------------------- with ------- --------------------------------------

In this connection, please provide me the following information under the **RTI Act 2005:**

Information Sought:

1. A certified copy, of the recent Circular/Notification/ Citizens Charter issued by Income Tax Department for making the payment of Income Tax Refund.
2. As per the Circular/Notification/Citizens Charter, in how many days the Income Tax Department supposed to refund the excess income tax paid by the assessee and claimed in his/her Income Tax return?
3. Names, Designations, Office Address and Office Telephone Number of **ALL** the officers of the Income Tax department who have seen my Income Tax return and are supposed to process the refund claimed there in.
4. Name, Designation, Office Address and Office Telephone Number of the Officer with whom my Income Tax refund matter is presently pending along with reasons of pendency.
5. The date since which the file/matter is pending with the Officer as identified in point no. 4 above.
6. Please inform me the reasons for delay in making the payment of refund under Section 4(1)(d) of the RTI Act for the following, since I am an "affected" person.
7. Please provide me certified copies of any instructions received from any higher authority of the Income Tax department or any other "Competent" Authority which has instructed the assessing officer or any other officer to delay the refund of excess income tax paid by me, in my Income Tax return under reference.
8. The Name, Office Address and Office telephone number of the Higher Officer to whom a First appeal will lie under Section 19(1) of the RTI act 2005

Further, the information requested in this application is pertaining to me only (the applicant) and is therefore not covered under Section 8(1)(j) or Section 11. Hence question of third party information, does not arise.

The CPIO/Assessing Officer is also requested to note that there is no sub clause in Section 8 or Section 9 of the RTI Act, under which, a CPIO has the option, of denying information, unless it serves a larger "public interest". Hence you are requested to provide the requested information, as per RTI Act 2005.

I am willing to pay any additional charges as determined by the CPIO/Assessing Officer under Section 7(3), and communicated to me with a reasoned order which includes detailed calculations which have been used for demanding the extra amount to be charged.

In case the CPIO/Assessing Officer has any doubts on the information requested above or needs any further clarification, he is free to call me on my contact numbers mentioned above.

The cheque of refund should be sent on my address ---- -- --------------------------------

Please find enclosed Draft /Bankers Cheque /IPO No. ---------------------, for ₹ 10.00, dated -----------------------payable to "Accounts Officer" towards payment of Application Fees for this RTI Application. The payees name on the IPO is as per DoPT Circulars F. No. 1/2/2007-IR dated 23 March 2007 and F. No. 10/9/2008-IR dated 05 December 2008.

Thanking You,

(----------------)

Encl:

1. Copy of Income Tax Return for the F.Y --------- (A.Y: -------) along with Computation
2. DD/PO/IPO No -------- for ₹ 10.00 dated -------
3. Copy of Form 16/16A

It is important to note that before making RTI application, person should ensure that Income Tax Refund has not been credited to his bank account directly. If amount of refund is less than ₹ 25000/-, the refund might have automatically been remitted to your bank account given at the time of filing your Return. If the amount of refund, is more than ₹ 25000, then a cheque might have been sent to your address mentioned in PAN or registered address of the company.

"You can make an application to the "Central Public Information Officer" (Your Assessing Officer) of Income Tax department personally or through registered post or Registered A.D. or Speed Post. RTI application should be addressed to the Central Public Information Officer (CPIO) /Assessing Officer, Income Tax department and their complete address."

Result of Using RTI

According to 'Tax Guru', so far, the success of RTI applications in the Income Tax department is concerned, the result is unbelievably approximately 100 per cent. In each and every case, the RTI application gets attended to immediately and you get pending refunds within 30 days (in some cases it takes more time to get refunds due to non-availability of your return; you are then requested to furnish duplicate copies with Indemnity bond on stamp paper of ₹10). It is a remarkable and most effective tool to get your income-tax refunds, in case it is pending for more than a year. As rightly pointed out on the 'Tax Guru' website, you have to be careful in framing the questions you asked for seeking information. Please note, that you are seeking information and not the opinion of the Central Public Information Officer (CPIO)/ Assessing Officer of the Income Tax Department. You cannot ask "why"; e.g., "why have you not issued my tax-refunds though overdue?" But, you can ask: "please inform when my overdue refunds will be issued." Believe me, on asking such a question, you will receive all the refunds due. The RTI Act is so powerful that the results in most of the cases are amazingly remarkable. The Act provides for a time-bound and defined process for citizens to access information. Severe penal provisions exist in the Act. Normally all laws provide penalty for the citizens for non-action or wrong action. Here is an Act which penalises bureaucrats for the same i.e. ₹250 per day for any default, subject to maximum penalty of ₹25,000/-, the 'Tax Guru' adds.

"So far, the success of RTI applications in the Income Tax department is concerned, the result is unbelievably approximately 100 per cent. In each and every case, the RTI application gets attended to immediately and you get pending refunds within 30 days (in some cases it takes more time to get refunds due to non-availability of your return; you are then requested to furnish duplicate copies with Indemnity bond on stamp paper of ₹10)."

How to Make the First Appeal

If you are not satisfied with reply from CPIO/Assessing Officer or have not received any reply from CPIO/ Assessing Officer within 30 days time limit prescribed by RTI Act 2005, you can make an appeal to the commissioner of Income Tax/Chief Commissioner of Income Tax of the concerned Income tax Office:

Contents of the appeal:

1. Name and address of the appellant
2. Name and address of the CPIO (Assessing Officer) against the decision of whom the appeal is preferred.
3. Particulars of the order including number, if any, against which the appeal is preferred.
4. Brief facts leading to the appeal.
5. Copy of the application to CPIO/Assessing Officer should be filed, and that you have fulfilled all the rules as per the act and rules there under and you have not received reply after the lapse of 30 days from the date of filing application or were the information received incomplete, misleading and wrong. Any other communication between you and the CPIO/Assessing Officer should be mentioned.
6. You should file the appeal after the lapse of 30 days from 1st application or 60 days from the original application or you may file petition to condone the delay (if any).
7. Find out name, designation and address of first appellate authority from the decision letter of CPIO/ Assessing Officer. If no reply is received, the concerned commissioner of Income Tax/Chief Commissioner of

Income Tax will be the first appellant authority.

8. If you want to be present during the first appeal hearing, mention it at the end of your appeal.
9. No fee is prescribed for filing the first appeal.
10. All photocopies of enclosures mentioned in the appeal should be self-attested by the applicant, under the word 'Attested' and full signature.
11. Retain one set of appeal and postal receipt and Regd. AD receipt for your record.
    a. You can deliver personally also, but mailing by registered AD/speed post is preferable. Couriers should be avoided.
    b. First Appellate Authority has to decide on the appeal within 30 days from the date of receipt of the first appeal. He can take a further 15 days (total 45 days), provided he gives the reasons for the delay in writing.
    c. The First Appellate Authority can give either a "spoken" order or a written order.

How to Make the Second Appeal

In case you are not satisfied with the decision/action taken by first appellant authority also, RTI Act provides the right to make a second appeal and the format is as under:

The Right to Information Act, 2005
APPEAL/COMPLAINT before CENTRAL INFORMATION COMMISSION
Under Section19 (Appeals) /18 (Complaint)

Appeal/Complaint No………… Dated…………
(for office use only)

If you are not satisfied with reply from CPIO/Assessing Officer or have not received any reply from CPIO/ Assessing Officer within 30 days time limit prescribed by RTI Act 2005, you can make an appeal to the commissioner of Income Tax/Chief Commissioner of Income Tax of the concerned Income tax Office:

As I am aggrieved by the decision of Central Public Information Officer and First Appellate Authority, I hereby file this appeal/complaint for your kind decision.

1.	Details of Appellant/complainant	
1.1	Full Name	
1.2	Full Address	
1.3	Phone/Cell No	
1.4	E mail ID	
2	Details of CPIO	
2.1	Name/Designation	
2.2	Full Address	
2.3	Name of Public Authority	
3	Details of First Appellate Authority	
3.1	Name/Designation of the FAA	
3.2	Full Address of First Appellant Authority(FAA)	
4	Date of RTI Application/First Appeal	
4.1	To CPIO and mailed on	
4.2	To First Appellant Authority and Mailed on	
5	Particulars of Decision	
5.1	Ref No. and Date of CPIOs decision	
5.2	Ref No. and Date of First Appellant Authority's decision	
5.3	Date of Personal hearing	
6	Details of Receipt of Replies by Appellant/ complainant from	
6.1	CPIO	
6.2	First Appellant Authority	
7	Details of Information sought:	
8	Brief Facts of the case:	
9	Reasons/Grounds for this Appeal/Complaint.	
10	Any other information in support of Appeal:	

Prayer/Relief sought for:

a) The information sought be ordered to be supplied immediately by registered post at my address - the onus to prove that denial of request was justified, is on the CPIO, as per Section 19(5) of the RTI Act 2005.
b) The information be now supplied to me free of cost.
c) I should be fully compensated for not supplying the information in the prescribed time limit and the breach of my right.
d) Public Authority be ordered to reimburse traveling and lodging-boarding expenses incurred by me for attending the hearing.
e) That the CPIO should be penalised under Section 20(1) of the RTI Act since he did not provide the information called for on false excuses. To instruct the CPIO, in writing, to follow the basic tenets of the RTI Act, as well as, carefully study and use various sections of the RTI Act.
f) Penalty as per RTI act be imposed on FAA for the delay, because the FAA did not have any reasonable cause for this delay - *Please do refer to judgment dated 28-04-2009 of Hon'ble High Court of Delhi in W.P. (C) 3845/2007 : Mujibur Rehman v/s CIC*
g) The matter is complainable under Section 18(1) (c) and (e) and punishable under Section 20(2) of RTI Act. It is also punishable under Section 20(1).
h) Disciplinary action be ordered to be initiated for not complying with the law against CPIO and FAA as per Section 20 (2) of RTI Act - has not furnished information within the time specified under sub-section (1) of Section 7 or malafidely denied the request for information or knowingly given incorrect, incomplete or misleading information.
i) FAA should be advised that his orders should always be "reasoned" and should consider all the points in the First Appeal and to always adhere to the time limits specified in the RTI Act.
j) To pass any other order, that the Hon'ble Commission may deem fit.
k) Personal Presence at hearing: Yes.

Declaration: I hereby state that the information and particulars given above are true to the best of my knowledge and belief. I also declare that this matter is not previously filed with this commission, nor is pending with any Court or tribunal or authority.

Place:
Date:

Signature of Appellant/Complainant

1. Fill in the above appeal/complaint form, index and in chronological order of progress. If you are filing appeal remove 'complaint/complainant' words. If complaint is being filed, cut words "second appeal/appellant".
2. Get it typed in double space.
3. Get one photocopy of:
   - Original application under RTI with its enclosures
   - First appeal with its enclosures
   - Bank demand draft/pay slip/postal order/cash receipt used for paying filing fee of ₹10/-and other charges
   - Copy of demand letter of CPIO for charges if any
   - Postal proof of mailing original application and first appeal
   - Postal AD slips/official acknowledgement received from CPIO and FAA
   - Decisions of CPIO and FAA if received
4. Arrange all papers as per index and then serially number all papers on right hand side top corner. This is one original set of second appeal/complaint.
   a. Prepare additional four sets as above by photocopying.
   b. Sign each page of appeal, index and chronology chart [all five sets].
   c. Self attest all the photocopies by signing under the word "Attested"
   d. Send one set by speed/regd./UPC post to each of CPIO and FAA and attach photocopy of proof of mailing to the original, extra copy of second appeal/complaint and your copy after filling details in index/chronology chart.
   e. Mail original set and one extra copy of set by registered AD to the commission at the following address:
      The Registrar,
      CENTRAL INFORMATION COMMISSION
      II floor, August Kranti Bhavan,
      Bhikaji Kama Place,
      NEW DELHI 110066
   f. Avoid courier services.
   g. Retain one set for your record and reference, with proof of mailing and AD received from CIC/CPIO/FAA for having received second appeal/complaint.
   h. If postal AD card is not received or acknowledgement letter is not received from CIC within 15 days of mailing, it is better to send by speed post copy of only second appeal/complaint [without enclosures] with a request to trace the same at CIC. Photocopy of regd. post receipt may also be mailed to CIC.
   i. You can consult local NGO/RTI activist for filing RTI application, first or second appeal to have better result. Services are generally free. ■

US Taxation — Basics that Indian Chartered Accountants Need to be Aware of

Globalisation and the opening of Indian markets to multinationals has seen vast movement of capital as well as human resources across international borders. International employment and international investments have become the order of the day. In the light of the fact that many Indian families now have a member in the US either as an employee on assignment or as a permanent resident, it becomes imperative to understand the implications of tax laws in USA combined with double taxation agreements and resultant interpretations. International financial transactions are by nature complex not just due to differences in currency but also differences in legal interpretations and practices. It is imperative that an Indian CA be able to answer when his client asks basic questions on US tax related matters either for him or for his family members who go to USA or live there part of the year. The objective of this article is to elucidate the fundamental rules of US tax laws that Indian Chartered Accountants need to be aware of.

CA. G. Karthikeyan
(The author is a member of the Institute. He can be reached at eboard@icai.org)

Income Tax in USA dates back to the time when USA was a colony ruled by the British, French and Spanish Empire. Income taxes were imposed intermittently until 1895 when un-apportioned tax on interest, dividend and rents was declared to be unconstitutional. The 16th amendment to the US constitution in 1913 modified the rules and income tax has been a means of funding for the federal government ever since.

Unlike India, income tax is levied at various levels in USA – federally, at state level and even at city and municipal level. Each tax authority collects its portion of tax directly from the taxpayer quite unlike India where income tax is a

central list item collected by the central government and then apportioned to states.

US tax laws and compliance rules are quite different from Indian tax practices and require an in-depth understanding of the rules based on which tax is computed. For example, in India every individual must file his or her own return but in the US a married couple can file a joint return and declare their joint income on one single return. While Indian tax laws no longer allow standard deduction, the same is an integral part of the US tax return for an individual.

Various credits and adjustments are also available to US taxpayers such as a child tax credit, education credits, etc. which benefit the individual significantly by directly reducing tax liability. This is akin to the tax rebate available in India. Foreign earned income may be excluded from total income up to USD 91,500 and credit may be claimed for foreign taxes paid on earned as well as unearned income. It is also possible to optimise between a credit and deduction to avail maximum benefits.

It is interesting note that the taxation system is built in such a way as to minimise evasion. Every document issued to a taxpayer (for wages, interest, dividend, capital gains, etc.) has a copy that is sent to the IRS by the issuer. Any failure to report such income immediately draws the attention of the IRS and prompts a levy notice.

Who Must File A Return?

A citizen or resident of the United States or a resident of Puerto Rico must file a federal income tax return if he meets the filing requirements for the category that applies to him.

- Individuals in general
- Dependents
- Children under age 14
- Self employed persons
- Aliens

Filing requirements apply even if no tax is owed. Requirement to file a return depends on the following three factors:

- Gross Income
- Filing Status
- Age

How to File a Return

Taxpayers must use one of three forms – Form 1040 EZ, Form 1040A or Form 1040 to file their taxes with the IRS. The Internal Revenue Service (IRS) is authorised to administer all income tax related matters.

The tax return may be filed on paper form 1040 or E-Filed using an authorised E-File provider. E-Filing uses a personal identification number to file the return electronically.

"Taxpayers must use one of three forms – Form 1040 EZ, Form 1040A or Form 1040 to file their taxes with the IRS. The Internal Revenue Service (IRS) is authorised to administer all income tax related matters. The tax return may be filed on paper form 1040 or E-Filed using an authorised E-File provider. E-Filing uses a personal identification number to file the return electronically."

Due Dates

1. The due date for filing the return is by 15th April, 2011 for the year ending 31st December, 2010. Taxpayers in the US generally follow the Calendar year for tax filing.
2. If taxpayer uses a fiscal year (a year ending on last day of any month except December), the return is due by the 15th day of the fourth month after the close of taxpayer's fiscal year.
3. If the due date falls on a weekend or a legal holiday as it does in 2011 (15th April is a local holiday in District of Columbia), due date is delayed until the next business day – in this case Monday 18th April, 2011.
4. If the taxpayer cannot file by the due date, an automatic extension of time can be availed by filing Form 4868.
5. In case of extension if taxpayer does not pay tax due by 15th April, he will owe interest and penalties.

Reporting of Income and Expenses

Taxable income must be figured on the basis of the tax year. A tax year is an annual accounting period used for keeping records and reporting income and expenses. Taxpayer may choose his accounting period (tax year) when he files his first return.

The taxpayer must also select an accounting method which accounts income and expenses for the year and clearly

shows total taxable income for the year. A Cash Method of accounting reports all income in the year in which taxpayer actually or constructively receives them. An Accrual Method of accounting generally reports income when it is earned rather than when it is received. Expenses are deducted when incurred rather than when paid.

US taxpayers normally follow a calendar year and cash method of accounting.

Social Security Number

Every US citizen and resident is allotted a unique identification number by the Social Security Administration (SSN) akin to the Permanent Account Number in India. This number is used by the IRS for identification purposes and is also the identifying criteria used by all authorities and agencies in the US to identify the individual.

The SSN must be entered on the tax return in the space provided. On a joint return the SSNs must be written in the same order as the names.

Non-resident or resident aliens are also normally allotted an ITIN (Individual Taxpayer Identification Number).

Third Party Designee

The IRS allows taxpayers to authorise a third party (like a CPA, friend, family member, paid preparer) to discuss the return with the IRS if required.

Filing Status

Income tax returns must be prepared and filed based on the filing status of the taxpayer. Five statuses can be used:

- Single
- Married filing joint
- Married filing separate
- Head of Household
- Qualifying Widow (er) with dependent child

Filing status is determined by whether a taxpayer is considered married or unmarried at the end of the tax year. A taxpayer is considered unmarried for tax purposes if on the last day of the tax year, he was unmarried or legally separated from spouse under a decree of divorce or separate maintenance.

Community Property: A peculiar provision found in the tax laws of some of the states in the federation relates to a marital property regime called community property. In a community property jurisdiction, most property acquired during marriage is owned jointly by both spouses and is divided upon divorce, annulment or death. Joint ownership is automatically assumed and this means that a married taxpayer owns half of any income designated as community income. This peculiar law has significant implications when married taxpayers decide to file returns separately. Many tax payers living in these States are very careful while choosing for divorce in the court of law.

Personal Exemptions

Exemptions have the effect of reducing taxable income. There are two types of exemptions – Personal Exemptions & Exemptions for Dependents. The amount of the exemption is same for each but rules applicable differ. Every taxpayer can claim an exemption for himself on the return. This exemption amounts to USD 3,650 for 2010. On a joint return this exemption can be claimed for both taxpayer and spouse. The taxpayer is also allowed one exemption each for the number of qualifying dependents claimed on the return. Qualifying dependents could be children, parents, relatives, etc. who meet certain conditions of dependency as prescribed by the law.

Heads of Income

The heads of income taxed in the US are similar to our own - salaries and wages, interest, dividend, capital gains, rental income, business income, pension distributions, etc. A major point of difference perhaps lies in the treatment of income from partnerships and S-Corporations (S-Corps are the rough equivalents of a private limited company) In India, partnerships and other such entities are taxed independently but in the US these entities are known as

"If the taxpayer is an employee, his employer will withhold income tax from his pay. This is similar to a system of tax deduction at source in India (TDS). Tax may also be withheld from other income like pensions, bonus, commissions, etc. In each case, the amount withheld is paid to the IRS on behalf of the taxpayer. If a taxpayer does not pay enough tax through withholding, he will have to pay estimated taxes. People who are in business for themselves normally pay their taxes this way."

pass-through entities indicating that the income earned by these entities is actually taxed in the hands of the respective partners or shareholders of the entity in question. Gross income can be further reduced by various adjustments such as unreimbursed moving expenses, education expenses for self, spouse or dependent, investments in retirement funds/pension plans, etc.

Credits

Credits are akin to the Indian concept of tax rebates. While deductions and adjustments reduce gross income, credits directly reduce the amount of tax payable. Credits may be refundable or non-refundable.

Refundable credits indicate that the credit is considered to be a payment of tax. Therefore, these credits are usually added to the federal tax withheld and the estimated tax payments made by the taxpayer and in case this total is more than the total tax payable, the excess is refunded to the tax payer.

Non-refundable credits may reduce tax to zero but if these credits are more than the tax, the excess is not refunded to the taxpayer.

Credits allowed include dependent care credit (child care expenses if both taxpayer and spouse are working), child tax credit, credit for the elderly, foreign tax credit, etc.

Tax Withholding & Estimated Tax Payments

Federal income tax in the US is a Pay-as-you-go tax. This can be done through (a) Withholding or (b) Estimated tax.

Withholding: If the taxpayer is an employee, his employer will withhold income tax from his pay. This is similar to a system of tax deduction at source in India (TDS). Tax may also be withheld from other income like pensions, bonus, commissions, etc. In each case, the amount withheld is paid to the IRS on behalf of the taxpayer.

Estimated Tax: If a taxpayer does not pay enough tax through withholding, he will have to pay estimated taxes. People who are in business for themselves normally pay their taxes this way. This is akin to advance tax in India. Estimated taxes are used to pay income tax and self-employment tax as well. Self employment tax refers to FICA i.e. social security and medicare tax which is similar to PF and ESI in India and works along the same principles. For employed taxpayers the employer bears half the FICA taxes and the balance is deducted from the employee's pay check.

While filing the return the taxpayer can take a credit for all the income taxes withheld or estimated taxes paid during that year. If the taxpayer did not pay enough taxes during the year, he may have to pay a penalty.

"India and the US are parties to a double taxation avoidance agreement and this also has various implications for Indian taxpayers working in the US. Taxpayers coming under the purview of the DTAA need to determine residential status according to each country's law and based on DTAA provisions resident and non resident status must then be decided for either country. Sometimes it may happen that a taxpayer per rules may turn out to be resident in both countries. In such situations the DTAA provides tie breaker rules to determine residency."

Residential Status & DTAA

India and the US are parties to a double taxation avoidance agreement and this also has various implications for Indian taxpayers working in the US. Taxpayers coming under the purview of the DTAA need to determine residential status according to each country's law and based on DTAA provisions resident and non resident status must then be decided for either country. Sometimes it may happen that a taxpayer per rules may turn out to be resident in both countries. In such situations the DTAA provides tie breaker rules to determine residency.

As an example, let us consider the case of an Indian citizen "A" who is seconded on an assignment to the US. He stays in the US from January 2010 to August 2010 and comes back to India by 20th August, 2010. In this case he would qualify as resident both in USA and India. The DTAA tie breaker rule provides that he should be considered a resident in India since he is a citizen here and has closer connections and a permanent home in India.

The DTAA and residential status determination, heads of income covered by the DTAA, preferential tax rates on those heads of income - all these play a major role in computation of tax for people falling under the purview of said laws.

Conclusion

The discussion above covers some salient points of tax computation under US tax laws as the internal revenue code per se is too comprehensive and exhaustive to summarise. It is imperative for practitioners to know and understand the basics especially if they must successfully advise client on matters of double taxation avoidance. The key to successful practice under these conditions is vested in the following:

- Good understanding of US tax laws
- Clarity of concepts covered by the DTAA
- Application issues
- Interpretation issues

In conclusion, a minor reference can be made to a case study involving interpretational issues under the DTAA. ■

Taxation of EPC Contracts – A Treatise

In recent years, the phenomenon of Engineering, Procurement, Construction contracts ('EPC contracts') has gained momentum with the import of technology, requirement in infrastructure and in sectors that require a high degree of expertise and technical skill. Appropriate structuring of EPC contracts is essential to minimise tax costs. Numerous conflicting decisions and time to time amendments in the statute created various complexities in respect of taxation income streams of an EPC contract. In this article we have discussed certain intricacies of taxability of EPC contracts in the light of the existing law and judicial precedents.

(Contributed by the Committee of International Taxation of the ICAI. Comments can be sent to citax@icai.org)

Introduction

India, considered among the world's fastest growing economy, needs to establish a foothold as a fully developed economy. To achieve this objective, the Indian government is giving more impetus to investments in infrastructure, power, manufacturing, real estate and allied sectors. These sectors need a huge capital investment which involves import of technology, critical machinery and projects from outside India. This thrust of technology and highly sophisticated machineries resulted into contracts with Global companies who will assist the Indian companies in designing, supply, setting up, installing and commissioning projects. Such contracts are commonly termed as Engineering, Procurement and Construction contracts ('EPC').

Such contracts are a comprehensive arrangement which typically encompasses all activities of the project - ranging from initial conceptualisation and design, providing or procuring the required goods and services from various sources, to construction, installation and commissioning of the project. These contracts are also often referred to as 'turnkey contracts' as they envisage the project owner merely having to 'turn a key' to commence operations upon completion of the contract.

EPC contracts thus have multiple facets requiring the contractor to perform a wide array of diverse yet integrated activities. This can be compared with a builder who also undertakes interior designing, furnishing, etc. and hands over a completely fully furnished house to an owner who simply moves into it.

Many a time, it is difficult for a single overseas contractor to execute and control such a huge contract while offering high degree of expertise and technical skill at the same time. Due to this reason, often EPC contracts are handled jointly by a consortium of contractors (located in and outside India) or a giant contractor operating across the globe wherein a part of the project is handled in India and a part outside India.

Meaning of Engineering, Procurement & Construction

Engineering	Procurement	Construction
Involves basic designing, planning and engineering for the project which can include preparing designs, plans, and technical specifications of equipments, analysis of various data, preparation of performance standards maintenance and training manuals, schedules of equipments, instructions for erection, etc.	Identifying, negotiating and arranging supplies of equipment, clearing of goods at ports, delivery to the site and provision of spare parts. In case of non-standard equipment, this could also involve design, fabrication and supply of equipment within the agreed time frame.	Activities includes Civil works, receiving and handling equipments on-site, on-site erection, project management, project monitoring, supervision, commissioning and testing of the project.

Taxability of EPC Contracts in India

Having discussed the above, it is imperative to understand the tax implications arising out of such contracts. For the purpose of taxation, the activities from EPC contract can broadly be divided into following two components depending upon where the activities are performed:

- **Offshore activities** – relates to the part of the work of the contact executed outside the country. These activities mainly comprises of rendering offshore services and offshore supply of equipments.
- **Onshore activities** - relates to the part of the work of the contact to be executed in India. These activities mainly comprises of onshore supply of equipments and material and rendering onshore services.

In order to remove any doubt about the legislative intent of the source rule, Finance Act, 2010 (w.e.f. from 1st June, 1976) substituted the Explanation with a new Explanation to specifically state that the income of a non-resident shall be deemed to accrue or arise in India and shall be included in his total income, whether or not, the non-resident has a residence or place of business or business connection in India; or, the non-resident has rendered services in India. After the said amendment, subject to provisions of DTAA, offshore services rendered under the EPC contracts may be taxable in India under the source rule though rendered outside India.

Activities under an EPC contract can be classified as under:

Nature of activity	Description of nature of work involved
Offshore Services	Includes rendering of services such as design and engineering, technical specifications of the work, data analysis, planning, etc. from overseas country
Offshore Supply	Includes the supply of equipment, materials and tools from overseas country
Onshore Supply	Includes procurement of misc materials, tools, consumables, etc locally in India for the executing of project
Onshore Services	Includes services to be rendered within India such as installation, construction and erection, commissioning and installation, etc

How Income from the Above Activities is Taxable?

<u>**Legal provisions:**</u>

Taxability under the Income-tax Act, 1961 ('Act')

Under the basic taxation scheme any income is brought within ambit of taxation by the charging provisions. The charging section, Section 5(2) of the Income-tax Act, 1961 ('Act') seeks to tax the income of a non-resident which is either:

- received or deemed to be received in India; or
- accrues or arises or is deemed to accrue or arise in India

In respect of a non-resident, Section 9 of the Act provides that all income, accruing from or arising through or from any business connection in India, is subject to tax in India. Further, it also provides that only so much of the income as can be attributed to the operations carried out in India would be taxable in India. After the recent amendment in the Act,

Section 9(1)(vii) now taxes the technical services which are being utilised by the Indian company.

Taxability under the Double Taxation Avoidance Agreements ('DTAA')

As per Section 90 of the Act, transactions with entities located in countries with whom India has entered into a DTAA would be governed as per the provisions of the Act or DTAA whichever are more beneficial to the assessee.

Generally, EPC contracts could be governed by the following articles of the DTAA:

Article 5 –Permanent Establishment ('PE')

PE is an artificial entity created for the purpose of taxing the income of a non-resident from business operations carried out by it in India. In a typical EPC contract, if the activities related to construction, assembly or installation project or supervisory activities in relation to a project exceeds a specified number of days prescribed in the relevant DTAA (varies between three months to twelve months under various treaties), it could lead to creation of Installation or Construction PE/Supervisory PE. Creation of the PE in India bestows Indian Revenue authorities the right to tax income of the non-resident attributable to PE activities in India.

Article 7 – Business Profits

Once the PE is established in India, the income of non-resident derived from the business activities connected with/attributable to that PE shall be taxed in India. On the contrary, if the PE is not created, the business income of the non-resident shall not be taxed in India.

It is clear that even after the withdrawal of Circular 23 and Instruction 1829, the taxpayers are still relying on the guiding principles laid down by the Circular 23 and Instruction 1829, in respect of taxability of offshore supplies and the same is upheld by judicial authorities as well. However, post the amendment in Section 9, the income from offshore services shall be taxable in India irrespective of the place of rendition. However, the taxpayers may still take shelter under the DTAA to reduce the tax burden.

Article 12/13 – Fees for Technical Services ('FTS')

Taxability of technical services rendered by a non-resident contractor shall be governed by Article 12/13 of any typical DTAA dealing with FTS. As per the said Article, any consideration paid for rendering technical, consultancy or managerial services by a non-resident shall be considered as FTS. FTS shall be taxed in the source country as per the rates in force. However, in case PE is established in India, the income from services in connection with PE shall be taxed under Article-7 as Business Profits and not as FTS.

Circulars/Instructions issued by the CBDT

It is pertinent to note that the Central Board of Direct Taxes ("CBDT") had issued circulars/instructions in the past to provide clarity in relation to taxability if certain international transactions. The same are briefly discussed as follows:

- **Circular No. 23 dated 23rd July, 1969 (F.No.7A/38/69-IT (A-II))** provided following clarifications:

Sale of goods/equipments	Taxability
From overseas company to an Indian *importer*	Where the transactions of sale between the two parties are on a principal to principal basis and sale is concluded outside India, no income accrues in India.
From overseas company to an Indian *subsidiary*	Transaction will not be deemed to accrue or arise in India under Section 9, provided that (a) the contracts to sell are made outside India, (b) the sales are made on a principal-to-principal basis and at arm's length, and (c) the subsidiary does not act as an agent of the parent company

- **Instruction no 1829, dated 21st September, 1989**, issued in the context of taxability of non-residents engaged in the execution of hydro electric power projects on turnkey basis was providing clear guidance to the tax officer in respect of taxability of turnkey projects. Instruction interalia provides -
  - Consortium of companies executing the individual scope of work will not constitute an Association of Persons ("AOP")
  - Profits from sale of equipments, on FOB basis, will not be deemed to accrue or arise in India as the title of the goods will pass outside India.
  - Services in respect of planning, design and engineering services rendered in India or abroad would be taxable as fees for technical services as per the provisions of Act or the applicable tax treaty.
  - Definite and separate scope of work should not be clubbed unless these are undertaken by the same foreign company.
  - Profits in respect of civil work contracts would be under the purview of provisions of Section 44BB of the Act.

The aforesaid circular and instructions, which had been in vogue for more than 20 years, has been largely relied upon by the taxpayers and has been followed by tax courts while adjudicating upon taxability of EPC contracts. However, the CBDT was of the opinion that the said Circular and Instruction were misused by many assesses and hence the same were withdrawn on 20th July, 2009. The implications of withdrawal of these circulars have been discussed at length in the subsequent paragraphs.

Generally, following arguments has been advanced/ vies has been adopted while examining the taxability of EPC contracts:

Nature of activity	Arguments advanced / views adopted by taxpayers
Offshore supply	Not taxable in India. The income falls outside the ambit of charging Section 5 read with Section 9 of the Act if the title is passed outside India and the payments are received outside India. Huge reliance placed on Circular 23, Instruction 1829 and Apex Court ruling in case of IHI (discussed below) to strengthen their position.
Onshore Supply	The income is taxable in India since the income accruing or arising in India is taxable under Section 5 of the Act.
Offshore Services	Post amendment in Section 9, the income may be taxable in India if services are utilised in India irrespective of the situs of rendering services.
Onshore Services	The income is taxable in India since the services are performed in India and the income accruing or arising in India is taxable under Section 5 subject to provisions of installation PE/Construction PE, as applicable.

However, the Indian Revenue authorities have been contending that in case of EPC contracts which are basically composite in nature, income from all the activities mentioned above should be taken together and will be taxable in India.

Position in Judiciary:

We are now summarising the key findings of judiciary in respect of taxability of EPC contracts:

1. **Ishikawajima-Harima Heavy Industries Ltd vs. DIT - 288 ITR 408 (SC)('IHI')**

   - Offshore Supply –
     - Transaction cannot be taxed in India if the property in the goods has been transferred outside India and payment for the same has been received outside India.
     - The fact that contract was signed in India is of no material consequences.
   - Offshore Services –
     - Sufficient territorial nexus between the renditions of services is necessary
     - Place of execution of contract is a key consideration
     - For income to be regarded as accruing or arising in India, it is necessary that the services not only be utilised within India, but also be rendered in India. Now Explanation to Section 9 has been substituted to overcome this observation
   - Since the payment for the offshore and onshore supply of goods and services has been clearly demarcated it cannot be considered to be a composite contract.
   - Force of Attraction Principle: The Hon'ble court relied upon the provisions of the OECD model convention which provides that even in case of a PE, income from business would be taxable in the State of residence. Thus, the Model Convention has decided against adopting the 'force of attraction of the PE'.[1]

2. **CIT vs. Hyundai Heavy Industries Co. Ltd. 291 ITR 482 (SC)**

   Supreme Court made very interesting observations in respect of attribution of profits and constitution of PE in case of offshore supplies, which are summarised as under:

   - For turnkey projects, offshore supplies where sale is concluded outside India will remain outside the Indian tax net unless the foreign supplier has a PE in India and offshore supplies are attributed to such PE.
   - It is the act of setting up a PE which triggers the taxability of transactions in the source state. In case, PE comes into existence after the transaction stood materialised, profits cannot be attributed to the PE.
   - Even if it is assumed that the supplies were necessary and are integral part of the installation, no portion of profits on such supplies could be attributed to the independent PE, unless the supplies were not at arm's length price.

3. **M/s. Xelo Pty Ltd. vs. DDIT (2009- TIOL-610- ITAT-MUM) (Mumbai Tribunal)**

   The Tribunal held that although the contract was a single one, separate identifiable considerations had been mentioned towards supply and rendition of services. There is no dispute that the receipt was for 'offshore supply'. It is the substance of the matter, rather than its form, which is crucial for determining the tax liability. The only objection that the contract is a single one, involving offshore as well as onshore components is of no relevance. If the intention of the parties to a contract flows clearly from the terms of the contract, then it is impermissible to negate it and make other inferences.

   Relying on decision of the Apex Court the case of IHI (supra) Tribunal held that offshore supply cannot be brought to tax in India where the equipment is handed

[1] New Explanation to Section 9 has been substituted to overcome this observation.

over to the ship on FOB basis and the property in goods passes to the Indian party, i.e. the sale of equipment is completed outside India though contract is a composite one.

4. **Authority of Advance Rulings ('AAR') in case of Hyosung Corporation (HC) vs. DIT 224 CTR 329**

- Based on the facts, AAR ruled that parties to a contract cannot be held to constitute an Association of Person ("AOP") when individual identities of the parties are maintained and critical prerequisites of AOP like unity of action, sharing of revenue or profit, etc. are not satisfied.
- Though the contract is on CIF basis, sale of equipment and materials took place outside India and hence income from offshore supply cannot be taxed in India.
- HC cannot be said to have supervisory PE within the meaning of Article 5(3) of the tax treaty, as the time limit for nine months of supervisory activity for constituting the PE has not been satisfied. In respect of the supervision of transportation and storage of equipment, AAR held that the said activity is carrying out only the contractual obligations incidental to the offshore supplies of goods and cannot be considered to be a supervisory activity, within the meaning of Article 5(3).

5. **Conflicting Ruling of Madras High Court - Ansaldo Energia Spa vs. ADIT 310 ITR 237**

Ansaldo Energia Spa ('AES') was an Italy based company engaged in business of selling and setting up of power plants. It had set up a subsidiary in India called Ansaldo Services Private Ltd. (ASPL). AES was awarded a turnkey contract by Neyveli Lignite Corporation (NLC) for setting up two thermal plants in India. The contract was awarded to AES on a single bidder basis.

At the instance of AES, the project was divided into four contracts as under

Contract 1 - offshore supply of equipment executed by taxpayer

Contract 2 - offshore services of supervision of erection and commissioning executed by taxpayer

Contract 3 - onshore supply of equipments executed by ASPL

Contract 4 - onshore services in relation to civil construction, erection, testing and the commissioning executed by ASPL

AES was responsible for the entire turnkey contract in its capacity as a single bidder and was also solely responsible and liable for all technical, management and all other services in connection with the contract.

The Revenue authorities contended that all the four contracts were controlled by the taxpayer and the turnkey contract was spilt up only for the tax purposes. The consideration for all the four contracts was unilaterally fixed by the taxpayer and neither NLC nor ASPL had any say in the matter. The Revenue alleged that the consideration of contracts 3 and 4 (loss making contracts) was loaded onto contract 1 for avoiding taxes. Taxpayer had a PE in India, and also a business connection with ASPL. ASPL was a facade created by the taxpayer and its corporate veil should be lifted for consolidating the four contracts and accordingly, a portion of income from offshore supplies was taxable in India.

On the other hand, AES contented that the contract is divisible and segregated the different portions of the turnkey contract from each other. Relying on SC decision in case of IHI (supra) it argued that since the contract for offshore supply was a separate contract and the sale pursuant to the contract was affected outside India and the consideration for the same was also received outside India, the income from offshore supply cannot be taxed in India. The Indian subsidiary had entered into contracts with other parties prior to the arrangement with NLC and accordingly, it was incorrect to consider it a facade created to avoid taxes.

In the facts of the case, given the degree of control exercised and rewards and responsibility of the contract assumed by AES the High Court, affirmed the findings of the Revenue and ruled against the taxpayer. Relevant observations of High Court are summarised as under:

Observation of High Court	Distinction drawn by High Court with IHI Ruling
• The contracts, in substance, were a single composite contract despite the apparent division into separate contracts. In substance a composite contract was split at a later stage with the Indian subsidiary for tax purposes. • In respect of the Indian subsidiary, HC observed that it was not competent to undertake the scope of work under Contracts 3 and 4 independently. The taxpayer continued to control and manages the activities of the Indian subsidiary and had overall responsibility for the execution of the activities under all the contracts. Accordingly, interlacing of the scope of work existed in respect of the separate contracts. • On account of interlacing of onshore and offshore scope of work, the taxpayer formed a PE in India in respect of execution of the entire contract and mere passing of title outside India in respect of offshore portion of the composite contract would not exempt the offshore supply from tax in India.	• Though a single contract was entered into in the case of IHI, the scope of activities to be performed was clearly demarcated. Whereas in the present case, a single contract was entered into initially which was split at a later stage. The activities proposed to be performed under the contracts, post division, were interlaced. • In IHI, the price payable for offshore and onshore activities was clearly demarcated. In the present case, price imbalance existed; price being skewed in favour of offshore supplies. • In IHI, the consortium members were competent to undertake the scope of work specified under the contracts entered into by them. In the present case, separate contracts were entered into by NLC with ASPL only at the insistence of the taxpayer.

> **With the introduction of Direct tax Code ('DTC'), EPC contractors should be prepared to shell out extra money towards payment of taxes. This is because the taxability of income by way of FTS has got a new dimension with a wider definition to include payment for development and transfer of a design, drawing, plan or software, or any similar other service and increased rate of tax on FTS i.e. 20 per cent from 10 per cent. Further, DTC proposes to introduce an additional tax on the branch profits @ 15 per cent.**

Having discussed the said decisions, it would be worthwhile to note the steps taken by the Revenue authorities to bring the EPC transactions into the tax net by undertaking the following measures:

Amendment in Section 9

Section 9 creates legal fiction for taxing income of non-resident derived from rendering technical services. As per the Apex Court's interpretation in IHI above, for an income to be taxable as FTS under Section 9, there must be sufficient territorial nexus between income and territory of India. In other words, the income from FTS shall be taxable only if the services are rendered as well as utilised in India.

Government clarified that the interpretation of Supreme Court in case of IHI is not the intention of legislature; an Explanation was substituted in Section 9 with retrospective effect from 1st June, 1976 by Finance Act 2007. The Explanation clarified that where income is deemed to accrue or arise in India as interest, royalty or FTS under Section 9, such income shall be included in the total income of the non-resident, regardless of whether the non-resident has a residence or place of business or business connection in India.

Subsequently, the Karnataka High Court, in its judgment in the case of Jindal Thermal Power Company Ltd. vs. DCIT (TDS), held that the amended Explanation does not do away with the requirement of rendering of services in India for any income to be deemed to accrue or arise to a non-resident under Section 9. It was held that on a plain reading of the Explanation, the criteria of rendering services in India and the utilisation of the service in India laid down by the Supreme Court in the case of IHI (supra) remains untouched and unaffected.

In order to remove any doubt about the legislative intent of the source rule, Finance Act, 2010 (w.e.f. from 1st June, 1976) substituted the Explanation with a new Explanation to specifically state that the income of a non-resident shall be deemed to accrue or arise in India and shall be included in his total income, whether or not,

(a) the non-resident has a residence or place of business or business connection in India;

or

(b) the non-resident has rendered services in India.

After the said amendment, subject to provisions of DTAA, offshore services rendered under the EPC contracts may be taxable in India under the source rule though rendered outside India. Thus, the ratio laid by IHI (supra) is no more good law. However, the ratio of Supreme Court decision still applies to offshore supplies.

Circular 23 & Instruction 1829 withdrawal - Causes and consequences

The year 2009 witnessed series of changes in the law governing taxability of EPC contracts. The first one being the withdrawal of Instruction 1829 by Instruction No. 5 dated 20th July, 2009 with subsequent withdrawal of Circular 23 by Circular No. 7 dated 22 October 2009, both with the "immediate effect".

The reason for withdrawal of the above Instruction 1829 and Circular 23 was stated as misuse by certain taxpayers on account of interpretation seeking relief which was not indented by the Instruction/Circular. The withdrawal of the Instruction 1829 and Circular 23 has not only created vacuum while dealing with the taxability of EPC contracts but has also raised question mark on the present and future of taxability of EPC contracts.

Circulars/Instructions issued by the CBDT are generally either explanatory or clarificatory in nature. These are enacted for the purpose of proper administration of a tax statute, are generally regarded as furnishing an aid in the construction of a provision. With their withdrawal the taxpayers will now be unable to directly place reliance on them in determining tax consequences of such transactions.

However, the withdrawal of the Circular/Instruction does not necessarily mean that an EPC contractor would now be liable to tax in India, in the situations described in Circular/ Instruction. The taxability of an EPC contractor, under the Act, would need to be evaluated, independent of the position stated in the Circular/Instruction having regard to the provisions of the Act and relevant case laws.

Judicial precedents after above changes in law

DIT vs. LG Cable Limited (2011- TII- 02-HC-DEL-INTL) (Delhi HC)	AAR in case of Joint Stock Company Foreign Economic Association Technopromexport [2010-TII-10-ARA-INTL]	AAR in case of Toshiba Plant Systems and Services Corporation (AAR No 864 of 2009)
• High Court concluded that the contract cannot be considered as a composite one and consideration received for offshore supply of goods cannot be taxed in India since o Scope of work of offshore and onshore activities are clearly defined o Consideration was separate and distinct o Title of the equipment passes outside India o PE has no role to play in execution of offshore contract • The HC further, distinguished the facts of LG's case from those of Madras HC ruling in the case of Ansaldo (supra) by stating that the Indian subsidiary of Ansaldo, was a legal facade which was created for taxation purposes and was not actually engaged in executing onshore contracts which is not the case in LG since the Indian project office is actually executing onshore contract. Further, a single contract was awarded to Ansaldo Energia SPA which was later on at the instance of Ansaldo, split into four separate contracts whereas in case of LG two separate contracts were awarded initially.	AAR observed that in the given facts offshore supply of goods/equipment would not be subject to tax in India. While arriving at the conclusion AAR relied on the following – • NTPC has invited bids for three separate works viz. offshore supply, onshore supply and onshore services. Three separate contracts have been drawn up at the inception only and hence facts of the case is distinguishable from the case of Ansaldo. • Property in the goods passed on outside India and payment has been made in the overseas country. • PE is for the purpose of carrying out the contract for onshore supplies and services including fabrication, installation and commissioning of the plant. PE has no role in offshore supplies.	On the questions raised by the applicant on the taxability in India in respect of the above arrangement, it was held by the AAR that: • Consideration received by the parent company is not taxable in India as it pertains to offshore supply and reliance placed by the applicant on the decision of the Hon'ble Supreme Court in case of IHI is to that extent valid. • Section 44BBB was applicable to the applicant as it was in the business of erection plant and machinery in approved turnkey power project.

From the above, it is clear that even after the withdrawal of Circular 23 and Instruction 1829, the taxpayers are still relying on the guiding principles laid down by the Circular 23 and Instruction 1829, in respect of taxability of offshore supplies and the same is upheld by judicial authorities as well. However, post the amendment in Section 9, the income from offshore services shall be taxable in India irrespective of the place of rendition. However, the taxpayers may still take shelter under the DTAA to reduce the tax burden.

Learning from above judgements

In view of foregoing, it is abundantly clear that the litigation under the EPC contracts largely revolves around the content and context of the contracts. Further, now in absence of beneficial circulars and instructions, the blanket reliance cannot be placed on anything for determining taxability of EPC contracts. In such circumstances it is pertinent to have robust documentation consisting of –

(i) Separate agreements in respect of offshore supplies, onshore supplies, offshore services and onshore services, wherever possible

(ii) When contract is a composite one, scope of work in respect of each services should be clearly and distinctly defined

(iii) Clear allocation of consideration for each activity

(iv) Substantiating evidences to show that property in goods/ equipment passes outside India

(v) Documentary evidence in the cases when the offshore services are linked to supply of equipment i.e. designing of product, etc and hence incidental to sale of equipment and not connected with PE in India

(vi) In case of installation PE, maintenance of appropriate documentation in respect of income attributable to such PE

DTC Impact

With the introduction of Direct tax Code ('DTC'), EPC contractors should be prepared to shell out extra money towards payment of taxes. This is because the taxability of income by way of FTS has got a new dimension with a wider definition to include payment for development and transfer of a design, drawing, plan or software, or any similar other service and increased rate of tax on FTS i.e. 20 per cent from 10 per cent. Further, DTC proposes to introduce an additional tax on the branch profits @ 15 per cent.

To conclude…

Though above rulings has given some relief to the EPC contractors in respect of offshore supplies of goods/ equipments, above referred amendments would have immense repercussions on the foreign tax payers –

(a) where the contract is awarded to a singular foreign company, the tax authorities will question the segregation of project into different agreements for offshore and onshore aspects of work as well as consideration attributed to such separate scope of work

(b) where the contract is awarded to a consortium, in spite of separate agreements between the members, existence of overall co-ordination agreement may have exposure of consortium becoming an AOP under the Act.

Further, on top of it, in view of the DTC proposals, the profitability of undertaking EPC contacts is likely to be impacted. ■

Performance Appraisal for Planned Growth of CA Firm

Performance appraisal is a process of obtaining, analysing and recording information about the relative worth of an employee. Its aim is to measure what an employee does and to devise ways to improve the performance. This technique can be effectively used for appraisal of partner level persons in a CA firm. It also assists in determination of compensation payable for their performance. Once adopted as a process, it brings transparency in the firm and helps in achievement of planned growth. This article explores the concept of Performance Appraisal for planned growth of CA firms.

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One of the dictionary meanings of the word *'process'* is *'continuous development with many changes'* It is to be noted that performance appraisal is not an event but a process that is to be followed periodically.

Partner level person in a CA firm for the purposes of this discussion is a person who influences performance of the firm by his decisions and work.

For Which CA Firms is it Relevant?

This exercise is relevant for those CA firms who have adopted a path of planned growth.

In order to remain focused in the chosen area of practice it is necessary for a CA firm to carefully set short term and long term goals. The goals of the firm are allocated to partner level persons in the form of KRA (Key Result Areas). Periodically the performance of the partner level person is appraised against the KRAs.

For Which CA Firms it is Not Relevant?

Many established CA firms are so sure of their traditionally set practice areas and the mode of practice adopted by them that they are averse to the process of reviewing their performance. In such cases this concept will not have much relevance.

When a fresh chartered accountant enters in to a CA practice he usually falls in one of the following scenarios-

i. He is inducted in a family owned firm.
ii. He joins a running firm as a partner.

iii. He starts a brand new firm from point zero either alone or with his friends who are in the same scenario

In scenario number one and two the fresher has a very limited choice and has to fall in the groove at least initially. In short, despite being inducted as a partner he is not able to influence the set thinking pattern of the CA firm and in reality is not a partner level person.

A fresh CA has a clear cut choice of selection of practice areas and setting of goals only in the third scenario.

In real life situations, however, very few fresh practitioners exercise this choice as the decision regarding setting of goals is influenced by easy and quick opportunities. Instead of driving the firm to the chosen areas, the practitioner prefers to get driven by the circumstances. Since it is easier to pluck the low hanging fruits, he finds sufficient justification for this approach.

The accepted practice areas in such cases usually involve labour oriented and less remunerative assignments. Many a time the practice areas initially look attractive but have no long term growth prospects. The work usually does not make use of full intellectual potential of the practitioner and over a period stops giving work satisfaction.

Goals of a CA Firm

Performance of a partner level person has to be benchmarked with the KRAs set for him. The KRAs of partner level person have to be synchronised with the goals of the firm.

Let us understand the common goals of a CA firm.

1. To establish a brand in client community in the chosen range of services and thereby attract clientele:

Building a brand means becoming well known in the chosen areas of practice. This is a strategic exercise having far reaching implications since it is not possible to change the brand image in the short term.

The ultimate objective is to improve performance of the firm as a whole. Therefore, setting of goals for development of an appropriate brand for the firm is the first goal of a CA firm.

2. To attract manpower to work and be associated with the firm in order to render the services:

In order to render efficient services to the clients, CA firms are dependent on its human capital. Once the firm establishes a brand image in the client community for rendering a quality service, the continuity of the same entirely depends on its ability to hire talented manpower.

In short development of a strong 'employer brand' is an important goal.

3. To develop and maintain a contemporary knowledge base and skill set for rendering the chosen range of services:

A CA firm in the course of its profession trades in knowledge. In the fast changing world the rate of obsolescence in knowledge base and skill set is very high. While choosing the core areas of practice it has to constantly strive to create and maintain the knowledge base and skill set.

> **Performance appraisal is not an event, but a process that is to be followed periodically. This exercise is relevant for those CA firms who have adopted a path of planned growth. In order to remain focused in the chosen area of practice it is necessary for a CA firm to carefully set short term and long term goals. The goals of the firm are allocated to partner level persons in the form of KRA (Key Result Areas). Periodically the performance of the partner level person is appraised against the KRAs.**

4. To render services to the clientele up to their satisfaction:

There is no substitute to client service. In order to achieve the goal of client satisfaction it is necessary to develop a system to understand the client expectations and then to design an execution methodology for exceeding the expectations.

5. To change and grow with the time:

CA firms have to strive hard in order to change in accordance with time and to grow. Due to lack of conscious effort the growth of old CA firms lag behind young generation CA firms. This goal suggests that success is not a chance but is a result of a carefully drawn strategic plan and continuous effort for achievement of the goals.

Setting of KRAs for Partner Level Persons

Once it is established that CA firms have to set goals for their well being and long term success, performance appraisal of partner level persons is inevitable.

As stated earlier, the step after the goals are set is to allocate responsibilities to the partner level persons in the form of KRAs. An attempt has been made to prepare an illustrative list of KRA based on each of the common goals stated above.

Brand building goal

- To study and continuously monitor environment for the scope of various core practice areas, related areas and upcoming areas.
- To analyse the market feasibility and identify the pockets where the probable clients are located.
- To visualise the links for reaching the clientele by following push and pull methods by remaining

within the Ethics Regulations of the Institute.

- To execute various strategies for becoming known amongst the client community in the chosen areas of practice.
- To develop clientele in the chosen areas of practice.

Development of a brand of 'preferred employer'

- To define the requirement of qualification and experience for rendering services in the chosen field.
- To locate the pockets where the human resources can be tapped
- To develop a bridge between the firm and the human resource and to reach there.
- To recruit an appropriate talent, to train them and to maintain an environment conducive for growth in their knowledge base and skill set.
- To walk the talk relating to firm policies.

Development and maintenance of contemporary knowledge base and skill set

- To initially define the requirement of knowledge and skill and various ways to continuously update the same.
- To locate the sources of knowledge and skill set.
- To connect the firm with the sources of knowledge and skill set.
- To ensure that the updating of knowledge and skills in the firm actually happens
- To ensure that there is a back up to each knowledge and skill resource.

Client servicing

- To maintain control over order intake by establishing the client acceptance policy
- To define parameters of client servicing
- To develop quality control and internal checks in client servicing.
- To supervise the service delivery methodology
- To collect client feedback and take corrective steps

Goal of planned growth

- To set short term and long term goals for growth
- To set up firm policies for achievement of the goals related to growth.
- To monitor various processes to ensure that the set path is followed
- To amend the goals and related policies to take care of various changes in the environment.
- To measure progress and give feedback to related persons

Measurement of Performance

KRAs are set for a particular time frame which may be a financial year and performance is measured for that period only. The success of measurement of performance against the KRAs lies in the process of setting of KRAs itself. In case the KRAs are not appropriately worded the performance measurement poses difficulties. It is advisable to decide the measurement criteria at the time of definition of KRA.

Let us take an example of one KRA from the aforesaid list of illustrative KRAs and make an attempt to measure performance.

- *To study and continuously monitor environment for the scope of various core practice areas, related areas and upcoming areas.*

The partner level person has to prepare and circulate the methodology proposed to be adopted by him to achieve this KRA. He will then periodically circulate the results and analysis of his exercise of monitoring of environment related to practice areas.

“There is no substitute to client service. In order to achieve the goal of client satisfaction it is necessary to develop a system to understand the client expectations and then to design an execution methodology for exceeding the expectations. CA firms have to strive hard in order to change in accordance with time and to grow. Due to lack of conscious effort the growth of some old CA firms lag behind young generation CA firms. This goal suggests that success is not a chance, but is a result of a carefully drawn strategic plan and continuous effort for achievement of the goals.”

At the end of the year his performance will be judged on the basis of the benefits derived by the reports circulated by the partner.

- *To define the requirement of qualification and experience for rendering services in the chosen field.*

This is an exercise of manpower planning. The partner level person has to take into consideration the services rendered by the firm, the services to be rendered in say next two years and then define the requirement of the depth of knowledge, experience and skill set required. On the face of it this will appear to be theoretical as CA firms employ articled trainees and semi qualified and qualified assistants and then allocate work to them and rarely do it in a reverse manner.

However this exercise will not only assist in recruitment, but will also help in allocation of work and in deciding the requirement of training of employees. The exercise will also help in preparation of job description of employees.

Performance can be measured against the success of the firm in execution of client work due to

allocation of work based on definition of qualification and experience.

- *To initially define the knowledge and skill requirement and to continuously update the requirement.*

This KRA is related to knowledge management. It can also be used as a basis for manpower planning.

Here the benchmarking is done with reference to the work handled by the firm. To take an example, the firm handling service tax work has to take into consideration the level of depth of knowledge of the service tax and generally that of the indirect tax laws. The size of the clientele also has to be taken into consideration as the complexities are proportionate to the size.

In order to measure performance against this KRA one needs to keep in view the work handled by the firm and the knowledge management practices.

- *To maintain control over order intake by establishing the client acceptance policy*

Key Result Areas (KRA) are set for a particular time frame which may be a financial year and performance is measured for that period only. The success of measurement of performance against the KRAs lies in the process of setting of KRAs itself. In case the KRAs are not appropriately worded the performance measurement poses difficulties. It is advisable to decide the measurement criteria at the time of defining the KRA.

Once the objective of planned growth is adopted this will be the most crucial policy. One may find fault in this KRA by saying that whether CA firms are in a position to reject any professional work. However, client screening is absolutely essential in order to achieve planned growth and an objective criteria has to be set for the same.

Performance measurement of this KRA will be easier as the partner level person will have to check the boxes in the policy and reviewer has to take that into consideration.

- *To set short term and long term goals for growth*

Here it may not be possible to directly measure the performance. In that case it will be advisable to check whether indirect measurement criteria can be used.

The performance can be measured by taking in to consideration the level of success achieved by the firm in the areas set as goals.

Conclusion

The success of the exercise lies in transparent measurement and reporting of feedback in order to ensure simultaneous growth of the firm and the partner level person. ■

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■

Arbitrage— An Opportunity to Gain

In economics and finance, arbitrage is the practice of taking advantage of a price differential between two or more markets: striking a combination of matching deals that capitalise upon the imbalance, the profit being the difference between the market prices. When used by academics, an arbitrage is a transaction that involves no negative cash flow at any probabilistic or temporal state and a positive cash flow in at least one state; in simple terms, a risk-free profit. A person who engages in arbitrage is called an arbitrageur — such as a bank or broker. Read on to know more.

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If the market prices do not allow for profitable arbitrage, the prices are said to constitute an arbitrage equilibrium or arbitrage-free market. An arbitrage equilibrium is a precondition for a general economic equilibrium. The assumption that there is no arbitrage is used in quantitative finance to calculate a unique risk neutral price for derivatives.

Conditions for Arbitrage

Arbitrage is possible when one of three conditions is met:

1. The same asset does not trade at the same price on all markets ("the law of one price").
2. Two assets with identical cash flows do not trade at the same price.
3. An asset with a known price in the future does not today trade at its future price discounted at the risk-free interest rate (or, the asset does not have negligible costs of storage; as such, for example, this condition holds for grain but not for securities).

Arbitrage is not simply the act of buying a product in one market and selling it in another for a higher price at some later time. The transactions must occur *simultaneously* to avoid exposure to market risk, or the risk that prices

"Also called risk arbitrage, merger arbitrage generally consists of buying the stock of a company that is the target of a takeover while shorting the stock of the acquiring company. Usually the market price of the target company is less than the price offered by the acquiring company. The spread between these two prices depends mainly on the probability and the timing of the takeover being completed as well as the prevailing level of interest rates."

may change on one market before both transactions are complete. In practical terms, this is generally only possible with securities and financial products which can be traded electronically. In the most simple example, any good sold in one market should sell for the same price in another. Traders may, for example, find that the price of wheat is lower in agricultural regions than in cities, purchase the good, and transport it to another region to sell at a higher price. This type of price arbitrage is the most common, but this simple example ignores the cost of transport, storage, risk, and other factors. "True" arbitrage requires that there be no market risk involved. Where securities are traded on more than one exchange, arbitrage occurs by simultaneously buying in one and selling on the other. See rational pricing, particularly arbitrage mechanics, for further discussion. Mathematically it is defined as follows: $P(V_T \geq 0) = 1$ and $P(V_T \neq 0) = 1$ where V_t means a portfolio at time t.

Examples

- Suppose that the exchange rates (after taking out the fees for making the exchange) in London are £5 = $10 = ¥1000 and the exchange rates in Tokyo are ¥1000 = $12 = £6. Converting ¥1000 to $12 in Tokyo and converting that $12 into ¥1200 in London, for a profit of ¥200, would be arbitrage. In reality, this "triangle arbitrage" is so simple that it almost never occurs. But more complicated foreign exchange arbitrages, such as the spot-forward arbitrage (see interest rate parity) are more common.
- One example of arbitrage involves the New York Stock Exchange and the Chicago Mercantile Exchange. When the price of a stock on the NYSE and its corresponding futures contract on the CME are out of sync, one can buy the less expensive one and sell it to the more expensive market. Because the differences between the prices are likely to be small (and not to last very long), this can only be done profitably with computers examining a large number of prices and automatically exercising a trade when the prices are far enough out of balance. The activity of other arbitrageurs can make this risky. Those with the fastest computers and the smartest mathematicians take advantage of series of small differentials that would not be profitable if taken individually.

Some types of hedge funds make use of a modified form of arbitrage to profit. Rather than exploiting price differences between identical assets, they will purchase and sell securities, assets and derivatives with similar characteristics, and hedge any significant differences between the two assets. Any difference between the hedged positions represents any remaining risk (such as basis risk) plus profit; the belief is that there remains some difference which, even after hedging most risk, represents pure profit. For example, a fund may see that there is a substantial difference between U.S. dollar debt and local currency debt of a foreign country, and enter into a series of matching trades (including currency swaps) to arbitrage the difference, while simultaneously entering into credit default swaps to protect against country risk and other types of specific risk.

Types of Arbitrage

- **Merger arbitrage:** Also called risk arbitrage, merger arbitrage generally consists of buying the stock of a company that is the target of a takeover while shorting the stock of the acquiring company. Usually the market price of the target company is less than the price offered by the acquiring company. The spread between these two prices depends mainly on the probability and the timing of the takeover being completed as well as the prevailing level of interest rates. The bet in a merger arbitrage is that such a spread will eventually be zero, if and when the takeover is completed. The risk is that the deal "breaks" and the spread massively widens.
- **Municipal bond arbitrage:** Also called *municipal bond relative value arbitrage*, municipal arbitrage, this hedge fund strategy involves one of two approaches. Generally, managers seek relative value opportunities by being both long and short municipal bonds with a duration-neutral book. The relative value trades may be between different issuers, different bonds issued by the same entity, or capital structure trades referencing the same asset (in the case of revenue bonds). Managers aim to capture the inefficiencies arising from the heavy participation of non-economic investors (i.e., high income "buy and hold" investors seeking tax-exempt income) as well as the "crossover buying" arising from corporations' or individuals' changing income tax

situations (i.e., insurers switching their munis for corporates after a large loss as they can capture a higher after-tax yield by offsetting the taxable corporate income with underwriting losses). There are additional inefficiencies arising from the highly fragmented nature of the municipal bond market which has two million outstanding issues and 50,000 issuers in contrast to the Treasury market which has 400 issues and a single issuer.

- **Convertible bond arbitrage:** A convertible bond is a bond that an investor can return to the issuing company in exchange for a predetermined number of shares in the company. A convertible bond can be thought of as a corporate bond with a stock call option attached to it. The price of a convertible bond is sensitive to three major factors:
  - *interest rate.* When rates move higher, the bond part of a convertible bond tends to move lower, but the call option part of a convertible bond moves higher (and the aggregate tends to move lower).
  - *stock price.* When the price of the stock the bond is convertible into moves higher, the price of the bond tends to rise.
  - *credit spread.* If the creditworthiness of the issuer deteriorates (e.g. rating downgrade) and its credit spread widens, the bond price tends to move lower, but in many cases, the call option part of the convertible bond moves higher (since credit spread correlates with volatility)
- **Depository receipts:** A depository receipt is a security that is offered as a "tracking stock" on another foreign market. For instance a Chinese company wishing to raise more money may issue a depository receipt on the New York Stock Exchange, as the amount of capital on the local exchanges is limited. These securities, known as ADRs (American Depositary Receipt) or GDRs (Global Depositary Receipt) depending on where they are issued, are typically considered "foreign" and therefore trade at a lower value when first released. However, they are exchangeable into the original security (known as fungibility) and actually have the same value.
- **Regulatory arbitrage:** Regulatory arbitrage is where a regulated institution takes advantage of the difference between its real (or economic) risk and the regulatory position. For example, if a bank, operating under the Basel I accord, has to hold 8 per cent capital against default risk, but the real risk of default is lower, it is profitable to securitise the loan, removing the low risk loan from its portfolio. On the other hand, if the real risk is higher than the regulatory risk then it is profitable to make that loan and hold on to it, provided it is priced appropriately.
- **Telecom arbitrage:** Telecom arbitrage companies allow phone users to make international calls for free through certain access numbers. Such services are offered in the United Kingdom; the telecommunication arbitrage companies get paid an interconnect charge by the UK mobile networks and then buy international routes at a lower cost. The calls are seen as free by the UK contract mobile phone customers since they are using up their allocated monthly minutes rather than paying for additional calls.

Price Convergence

Arbitrage has the effect of causing prices in different markets to converge. As a result of arbitrage, the currency exchange rates, the price of commodities, and the price of securities in different markets tend to converge to the same prices, in all markets, in each category. The speed at which prices converge is a measure of market efficiency. Arbitrage tends to reduce price discrimination by encouraging people to buy an item where the price is low and resell it where the price is high, as long as the buyers are not prohibited from reselling and the transaction costs of buying, holding and reselling are small relative to the difference in prices in the different markets.

Arbitrage moves different currencies toward purchasing power parity. As an example, assume that a car purchased in the United States is cheaper than the same car in Canada. Canadians would buy their cars across the border to exploit the arbitrage condition. At the same time, Americans would buy US cars, transport them across the border, and sell them in Canada. Canadians would have to buy American Dollars to buy the cars, and Americans would have to sell the Canadian dollars they received in exchange for the exported cars. Both actions would increase demand for US Dollars, and supply of Canadian Dollars, and as a result, there would be an appreciation of the US Dollar. Eventually, if unchecked, this would make US cars more expensive for all

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buyers, and Canadian cars cheaper, until there is no longer an incentive to buy cars in the US and sell them in Canada. More generally, international arbitrage opportunities in commodities, goods, securities and currencies, on a grand scale, tend to change exchange rates until the purchasing power is equal.

Risks

Arbitrage transactions in modern securities markets involve fairly low risks. Generally it is impossible to close two or three transactions at the same instant; therefore, there is the possibility that when one part of the deal is closed, a quick shift in prices makes it impossible to close the other at a profitable price. There is also counter-party risk, that the other party to one of the deals fails to deliver as agreed; though unlikely, this hazard is serious because of the large quantities one must trade in order to make a profit

Arbitrage transactions in modern securities markets involve fairly low risks. Generally it is impossible to close two or three transactions at the same instant; therefore, there is the possibility that when one part of the deal is closed, a quick shift in prices makes it impossible to close the other at a profitable price. There is also counter-party risk that the other party to one of the deals fails to deliver as agreed; though unlikely, this hazard is serious because of the large quantities one must trade in order to make a profit on small price differences.

on small price differences. These risks become magnified when leverage or borrowed money is used.

Another risk occurs if the items being bought and sold are not identical and the arbitrage is conducted under

the assumption that the prices of the items are correlated or predictable. In the extreme case this is risk arbitrage, described below. In comparison to the classical quick arbitrage transaction, such an operation can produce disastrous losses.

Competition in the marketplace can also create risks during arbitrage transactions. As an example, if one was trying to profit from a price discrepancy between IBM on the NYSE and IBM on the London Stock Exchange, they may purchase a large number of shares on the NYSE and find that they cannot simultaneously sell on the LSE. This leaves the arbitrageur in an unhedged risk position. ■

Book Building Mechanism in Issue of Shares – Some Issues

The years 2007 to 2009, saw many Initial Public offers (IPOs) and Follow-on public offers (FPOs) by Indian Corporates for raising funds from the investors in the capital market. Majority of them have used the book-building process to raise money from the stock markets. This article looks into some issues related to the book-building process.

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Meaning of Book-Building

Book-building is a price discovery process used in public issue of shares. The issuer sets a base price, and a price-band within which the investor is allowed to bid for shares.

The investor has to bid for a number of shares he wishes to subscribe to within this price-band. The issuer maintains an order book, in which the investor can state the number of shares they are willing to buy, at a price within the price-band; thereby an order book is built by the issuer of shares. Thus, the name derived i.e. "book-building".

Book-Building Process[1]

- A lead merchant banker has to be appointed as a book-runner by the issuer of securities.

- Number of securities and price band of issue is decided by issuer in consultation with merchant bankers.
- Syndicate members are appointed who accept orders from investors, inputting orders into an 'electronic book'. This activity is termed as 'bidding'
- Bids below floor price are rejected but bid price can be revised by bidder before issue closes.
- Some modes used to evaluate the bids include:-
  a) Price Aggression
  b) Investor quality
  c) Earliness of bids
- The final price is decided by book-runner and issuer at which securities get allotted
- While bidding for equity shares of a company, in a book-built portion, the bidder has to, along with bid-cum-application form submit a cheque/demand draft/stock invest for the amount of the bid in favour of the 'escrow account' of the escrow collection bank.

Price-Discovery in Case of Book- Building

Upon completion of the issue period, the merchant banker who manages the issue also known as the book running lead manager arrives at the issue price in consultation with the issuer, a price which is known as the "cut-off price".

This cut-off price is a price discovered by the market. The company issues the shares to the investors at this cut-off price. As a natural consequence, investors bidding at a price below the cut-off price are ignored for the purpose of issue of shares.

Method of Price-Discovery

This cut-off price is arrived at by means of method called "Dutch auction". Dutch auction refers to lowering of the price of an item until it gets its first bid at which price, the item is sold.

> **IPOs have during recent times lost the very meaning of 'public holding' in a publicly listed company. By merely offering 6.25 per cent of post-issue equity, shares of a company can get listed on BSE or NSE. Out of 18.75 per cent of post issue equity reserved for wholesale bidders, the said shares are allotted by company and book-runner lead manager, to persons of their choice. Such allottees can get shares without paying any amount at the time of bidding. If post listing, there is low floating stock; vested interests can easily manipulate the share price.**

Illustration

Say, ABC Ltd., wants to issue 1000,000 shares, having face value say, ₹10. Floor price has been kept at ₹60 and the price-band is between ₹72.

Say, at ₹72 the bids received from investors to buy 200,000 shares. Thus, cut-off price cannot be set at ₹72 since this would result in sale of only 200,000 shares.

The price now is lowered to ₹71, at which bids for 300,000 shares have been received. Thus, if cut-off price is set at ₹71, 500,000 shares will be sold. Thus, still leaving 300,000 shares for issue. The price is now lowered to ₹70 at which investors are ready to buy 500,000 shares. So, if the cut-off price is set at ₹70, all 1000,000 shares will be sold.

In this case, investors who have applied for shares at ₹72 and ₹71 will also be allotted shares. Excess money paid by them will be returned to them.

Some Issues in the Issue Price Mechanism

- As per SEBI guidelines, in case of IPOs and FPOs having issue price greater than ₹500 per share, the issuers are allowed to issue shares at face value of ₹1 per share, those having issue price below ₹500, at present mandatorily, face value per share has to be ₹10.
- The upper limit of price-band i.e. the cut-off price can not exceed 20 per cent to the base price.
  In the above illustration, both these points have been taken into account.
- The issuer may opt for either :-
  i) 75 per cent book-building process
  ii) 100 per cent book-building process

In case of 75 per cent book-building process at least, 25 per cent of issues shall be offered to the public, which shall be separately identified as 'net offer to public'. To the extent of this net offer to public, underwriting of shares shall be mandatory. In this case, balance 25 per cent will be issued at the price determined by book-building process.

Fixed Price Issue and Book-Built Issue[2]

- In case of fixed price issue, price at which securities are offered is known in advance to the investor. In case of a book-built issue, only an indicative price range is known.
- In fixed price issue, demand for securities offered is known only after closure of issue. Whereas, in a book-built issue demand for securities offered can be known everyday as the book is built.
- In fixed price issue, payment is made at the time of subscription and refund is made after allocation. In book-built issue payment is made after allocation.

Book-Building and Auctions – A Comparison[3]

What is an auction method for issue of shares?

In case of open auction, investors are asked to quote price and number of shares they wish to buy. In descending order of prices shares are allocated till issue gets exhausted. Lowest bid price is accepted as the deemed price and the investors pay this price. In case of oversubscription, shareholders are allotted shares on pro-rata basis.

An interesting point to note is that SEBI is considering auction-based method in pricing of IPOs on the premise that the method leads to greater transparency and efficiency in share sale process. The issuer gets the right price for shares offered and retail investors can buy the shares at price offered by QIBs for the shares.[4]

In the US, underwriting has been based more so on book-building mechanism. In France, a choice of mechanisms is given to issuers and an underwriter, which has to be made before preliminary documents announcing the IPO are published.

In the French IPO market a choice has to be made among the following:-

a) A fixed- price offer
b) An auction procedure
c) Book-building procedure

The first two are investor-driven mechanisms which give significant decision-making power to the investors. In book-building, the underwriter plays the central role, which has the best understanding of the market and ability and desire to place shares in 'good' hands.

Under-pricing of issue:

In case of under pricing of an issue the main cost is borne by original owners of the firm. The question on under pricing of issue by Book-Building and Auctions during IPO has been dealt as under:

As per Jenkinson and Ljungqvist (2001, P.40), in the case of issue pricing where there may be an under pricing of issue the seller of the issue (S) involves a middle man (M) and does not directly auction the issue at a reserve price (v) because :

i) All bad firms would flood in and knowing this, the shareholders would not be willing to pay much.
ii) Such adverse selection could destroy the auction market.

Auctions work well when buyer (B) knows the price (called 'u', which is the under priced price of the issue) exactly.

When B doesn't know u and u and v are correlated, an influx of low-v sellers in the auction market would lower expectation of u, conditional on S having opted for an auction.

In book-building process, M sees u and his bid allows B to infer u exactly, eliminating uncertainty. The bid made reveals M's signal about u. Thus, book-building process is superior and survives as it solves adverse selection problem, otherwise present if M is not involved and S and B are left with their own devices.

Some Issues Requiring Reconsideration During IPOs

As per capital market regulations, if promoters dilute more than 25 per cent during an IPO, retail investors can be allotted 35 per cent of the issue, while institutional investors and High net-worth individuals (HNI) category get 50 per cent and 15 per cent respectively.

The recent trend has seen promoters diluting less than 25 per cent stake, allowing them to cap the retail portion at maximum 30 per cent, with institutional portion going up at 10 per cent and this 5 per cent difference is quite substantial for small investors if issue size is large.

Thus, IPOs have during recent times lost the very meaning of 'public holding' in a publicly listed company. By merely offering 6.25 per cent of post-issue equity, shares of a company can get listed on BSE or NSE. Out of 18.75 per cent of post issue equity reserved for wholesale bidders, the said shares are allotted by company and book-runner lead manager, to persons of

Book-building is now one of the most preferred modes of issue mechanism both in Indian and global markets due to inherent strengths as it discloses more information. It has an edge over auctions which avoid adverse selection of stocks. Book-building is a good concept for tapping both wholesale and retail investors and represents a rapidly maturing capital market. Pros and cons of both auction and book-building method need to be adequately considered before any change of method is considered.

their choice. Such allottees can get shares without paying any amount at the time of bidding. If post listing, there is low floating stock; vested interests can easily manipulate the share price.

Thus, certain regulations like Rule 19(2) (b) of Securities Contracts Regulation Rules, introduced by SEBI in 1999, which allows promoters to allot 60 per cent of issue to QIBs, 10 per cent to HNIs and only 30 per cent to retail investors, on dilution of 10 per cent of equity stake, where issue size is more than ₹100 crores, require some reconsideration. Also greater provisions to improve the integrity of the process as well as maintaining arms-length relationship between those involved in book-building and their associates is necessary.

A Note on Amendment of Securities Contracts (Regulation) Rules – Minimum 25 per cent Public Shareholding in All Listed Companies:

The government has made it mandatory for all listed companies to have a minimum 25 per cent public float. Listed companies having public shareholding below 25 per cent mark will get the option to reach this limit by way of annual addition of at least 5 per cent. Thus, promoters of companies (including government) having lower than 25 per cent public float will have to shed more shares in favour of public holding.

Some prominent companies requiring promoter stake dilution/fresh issue*:

Company	Promoter Holding (per cent)
NTPC	84.5
SAIL	85.8
Power Grid Corporation	86.4
Wipro	79.5
MMTC	99.3
NMDC	90.0
NHPC	86.4
Hindustan Copper	99.6

**Source: The Hindu – Business Line dated 5th June, 2010*

According to the change in the listing guidelines, if post issue capital of the company calculated at offer price is more than ₹4000 crores, the company may be allowed to go public with 10 per cent public shareholding and comply with 25 per cent public shareholding requirement by increasing its public shareholding by atleast 5 per cent a year. The company can increase its public shareholding by less than 5 per cent in a year if such increase brings its public shareholding to 25 per cent level in that year.

This move is in sync with norms in developed countries viz. Singapore where a company must have public shareholding between 12 per cent and 25 per cent for an IPO, depending on its market capitalisation. 25 per cent public shareholding is mandatory in UK for both IPO and continuous listing.

The above move shall increase the free float and market capitalisation in the share market and deepen the equities segment. Moreover, new investors will get the opportunity to participate in equities through IPO route.

Conclusion

Book-building is now one of the most preferred modes of issue mechanism both in Indian and global markets due to inherent strengths as it discloses more information. It has an edge over auctions which avoid adverse selection of stocks. Book-building is a good concept for tapping both wholesale and retail investors and represents a rapidly maturing capital market. Pros and cons of both auction and book-building method need to be adequately considered before any change of method is considered.

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Report on Campus Placement Programme: February-March 2011

The Committee for Members in Industry organises Campus Placement Programmes for all levels of Chartered Accountants at frequent intervals throughout the year. The Committee for Members in Industry is committed to provide world class placement services to the Members and best accounting and finance talents to the industry.

In its endeavor to provide quality Accounting, Finance, Tax, Audit and Management Consultancy personnel to recruiting entities, the Committee has successfully organised one more round of Campus Placement Programme for newly qualified Chartered Accountants at 16 centres viz. Ahmedabad, Bangalore, Baroda, Bhubaneswar, Chennai, Coimbatore, Ernakulam, Hyderabad, Indore, Jaipur, Kanpur, Kolkata, Mumbai, Nagpur, New Delhi and Pune in February-March, 2011.

Brief summary of the placement programme of both the phases is as follows:

Number of Candidates Registered	5375
Number of Interview Teams	223
Number of Organisations	111
Number of Jobs Offered	1876
Percentage of jobs offered vis-a-vis registered candidates	34.90 per cent

Executive Summary

1. Highest salary offered for International posting in the Campus Placement Programme is 120,000 -150,000 USD PA (₹5486412.00 to ₹6858015.00000, 1USD=45.72010 INR).
2. Highest salary offered ever for Domestic posting in the Campus Placement Programme is ₹13.92 lakh per annum.
3. The minimum salary paid is ₹3.27 lakh per annum.
4. The average salary offered was ₹6.747 lakh per annum.
5. Total 1902 candidates have participated in phase I interviews and 4963 candidates have participated in phase II interviews after merger of candidates from smaller centres. In all 5375 candidates registered for availing the services of Campus Placement Programme.
6. Around 1876[1] jobs were offered to the candidates who participated in the Campus Placement Programme.
7. In all 34.90 per cent of registered candidates were offered jobs.
8. 1663 candidates accepted the job offers.
9. 111 entities including the corporate organisations and the Chartered Accountancy firms have participated in the Campus Placement Programme.
10. 223 Interview Panels participated in this Campus Placement Programme.

Salient features

1. Candidates were given two choices to meet the recruiting organisations. First at smaller cities and second (if the candidates has not been selected at smaller cities) at bigger cities.
2. The committee organised Orientation Programme for candidates to sharpen their soft skills and give updates on the Technical side.
3. In this Campus Placement Programme all the candidates have been permitted to attend the Orientation Programme at any of the centres to avoid the requirement to travel to centres chosen for interviews for attending the Orientation Programme.

The following table shows the statistical information of campus interview at a glance:

Phase I

Centre	Number of Interview Teams	Total Registered Candidates	Number of Offers made	Number of offers accepted
Ahmedabad	10	659	168	168
Bhubaneswar	8	78	47	39
Baroda	6	42	15	8
Coimbatore	8	43	25	8
Ernakulam	4	43	9	4
Indore	3	68	18	10
Jaipur	12	341	83	68
Kanpur	5	107	15	12
Nagpur	6	54	30	12
Pune	11	380	125	85
Total	**73**	**1902**	**535**	**414**

Phase II

Centre	Number of Interview Teams	Total Registered Candidates*	Offered	Accepted
Bangalore	21	324	117	108
Chennai	26	347	161	161
Hyderabad	12	200	55	45

* Comments/suggestions for improvement in placement programme, particularly to improve the penetration are welcome at placements@icai.org placements@icai.org

[1] This write up reflects the status as on 18-4-2011 10:00 AM. Results are awaited from some of the companies. For further details kindly visit http://www.cmii.icai.org

Centre	Number of Interview Teams	Total Registered Candidates*	Offered	Accepted
Kolkata	16	533	131	116
Mumbai	33	1776	429	394
New Delhi	35	1784	439	416
Special Recruitment Window	1	-	9	9
Rank Holder List	6	-	Awaited	Awaited
Total	**150**	**4963**	**1341**	**1249**

* The figures also include candidates merged from smaller centre to the bigger centres as per their choice.

Salary Range

Salary Range (per annum)	Number of Candidates February - March, 2010	Number of Candidates August - September,2010	Number of Candidates February - March, 2011
₹9,00,000 and above	43	79	108
₹7,50,000 to ₹8,99,000	227	169	413
₹5,00,000 to ₹7,49,000	656	756	989
₹3,50,000 to ₹4,99,000	272	137	142
₹2,50,000 to ₹3,49,000	17	3	11
Total	**1215**	**1144**	**1663**

As apparent from the statistics there has been a significant rise in the range of CTC offered by the organisation in the all three range of more than ₹5,00,000 lakh per annum to the candidates and the offers accepted by them.

The Chart above depicts the comparison between the number of the candidates selected within the various salary ranges offered during Campus Placement Programme February-March 2010, August-September 2010 and February-March 2011. It can be observed that in the recent programme higher salaries were offered to more number of candidates. Lesser number of candidates were offered lower salaries. This reflects a general rise in the pay packages that is being paid to the newly qualified Chartered Accountants.

Top Ten Remunerations offered during February-March 2011 Campus Interviews

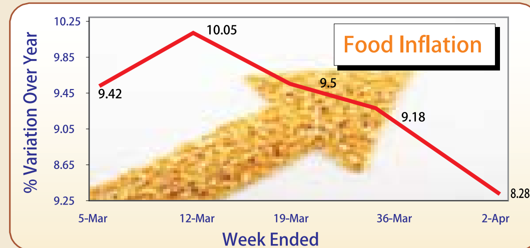
S No.	Company Name	Remuneration Offered (₹ In lakh P. A.)	Candidates Selected	Centre
1	Olam International Ltd	USD 1,20,000-1-,50,000 per annum (For International Posting)	2+2=4	Chennai & New Delhi
2	Aditya Birla Group	USD 50,000 per annum (For International Posting)	3	Hyderabad
3	ITC	1393200	2+6+1+2=11	Bangalore, New Delhi, Mumbai and Kolkata
4	Landmark Group	1319493	8+5=13	New Delhi and Mumbai
5	BPCL	1160000	6+2+4=12	Mumbai, Chennai and Kolkata
6	RAK Ceramics PSC, UAE.	1100000	15+11=26	New Delhi and Kolkata
7	ETA Star Group of Companies	1080000	6	Chennai
8	REC	1040000	8	New Delhi
9	ONGC	1000000	2	Chennai
10	J.M. Financial Limited	1000000	3	Mumbai

Top Recruiters during the February-March 2011 Campus Interviews

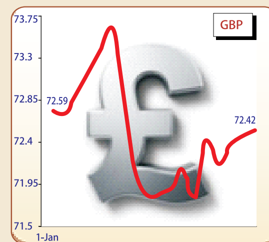
S No	Name Of Company	Accepted
1	ICICI Bank	309
2	TCS	101
3	Infosys	80
4	Canara Bank	55
5.a	Axis Bank	50
5.b	BHEL	50
5.c	RIL	50
6	Genpact	49
7	Bank of Baroda	39
8	Corporation Bank	39
9	Bank of India	36

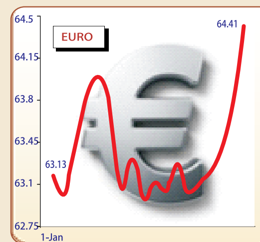
■

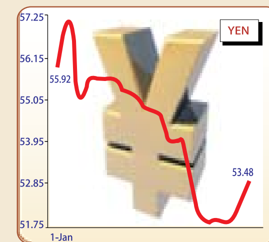
Economic Indicators



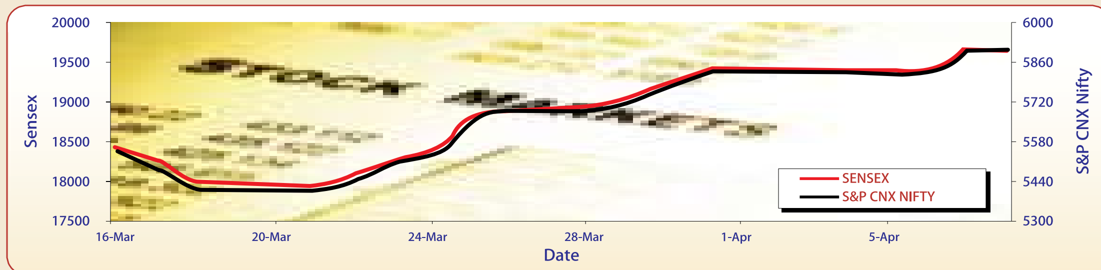
Indian Rupee vs. Major Foreign Currencies (March 16, 2011 to April 15, 2011)







Stock Markets



Selected Indicators

(per cent per annum)

Item	2010	2011					
	Feb- 26	Jan- 21	Jan- 28	Feb- 04	Feb -11	Feb- 18	Feb- 25
Cash Reserve Ratio(1)	5.75	6.00	6.00	6.00	6.00	6.00	6.00
Bank Rate	6.00	6.00	6.00	6.00	6.00	6.00	6.00
Base Rate(2)	11.00-12.00	8.25/9.50	8.25/9.50	8.25/9.50	8.25/9.50	8.25/9.50	8.25/9.50
Deposit Rate(3)	6.00-7.50	8.25/9.50	7.75/9.50	7.75/9.50	7.75/9.50	7.75/9.50	7.75/9.50
Call Money Rate (Weighted Average)(4)	4.22	6.77	6.91	6.83	7.11	7.58	7.61

Notes: (1) Cash Reserve Ratio relates to Scheduled Commercial Banks (excluding Regional Rural Banks).
(2) Base Rate relates to five major banks since 1st July, 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.
(4) Data cover 90-95 per cent of total transactions reported by participants. Call Money Rate (Weighted Average) is volume–weighted average of daily call money rate for the week (Saturday to Friday).

Readers are Invited to contribute write-ups or any relevant and interesting piece of information for this feature at eboard@icai.org.

ACCOUNTANT'S BROWSER

'PROFESSIONAL NEWS & VIEWS PUBLISHED ELSEWHERE'

Index of some useful articles taken from Periodicals/Newspapers received during March-April 2011 for the reference of Faculty/Students & Members of the Institute.

1. ACCOUNTING

An Evaluation of Social Accounting Disclosure in Corporate Annual Reports in India by Rechanna & B. Mahadevappa. *Indian Journal of Accounting,* December 2010, pp. 72-77.

Financial Management Call for Need-Based Structured Environment Accounting Standards by M.R. Kumara Swamy. *Journal of Financial Management & Analysis,* Vol.23/2, 2010, pp. 111-115.

Have IAS (International Accounting Standards)/IFRS Improved the Information Content of Intangibles in France? by Jean-Michael Sahut & Sandrise Boulerne. *Journal of Financial Management & Analysis,* Vol.23/2, 2010, pp. 52-62.

IFRS: The Balance Sheet Approach to Deferred Tax by Anand Banka. *BCAJ,* March 2011, pp. 15-20.

Introduction of IFRS – Issues & Challenges by K.C. Chakrabarty. *RBI Bulletin,* March 2011, pp. 309-313.

Linked in Tips for CPAs by Robin M. Hensley. *Journal of Accountancy,* March 2011, pp.44-47.

Voluntary Non-Financial Disclosure & the Cost of Equity Capital: The Initiation of Corporate Social Responsibility Reporting by Dan S. Dhaliwal etc. *The Accounting Review,* Vol.86/1, 2011, pp.59-100.

2. AUDITING

Building an Internal Audit Function by Susan Burch. *Internal Auditor,* February 2011, pp.46-51.

Fraud Reporting: Royal Treatment by David Malamed. *CA Magazine,* April 2011, pp. 45-47.

Raising the Stature of Internal Auditing by Stephen W. Minder. etc. *Internal Auditor,* February 2011, pp. 53-55.

The Role of the Internal Audit Function in the Disclosure of Material Weaknesses by Shu Lin etc. *The Accounting Review,* Vol.86/1, 2011, pp.287-323.

3. ECONOMICS

Applications of PPP Model in Key Infrastructure Sectors to Stimulate Economic Growth in India by Parimal Kr. Sen & Palash Garani. *The Management Accountant,* March 2011, pp.190-195.

Development & Public-Private Partnership by Sudarshan Maity. *The Management Accountant,* March 2011, pp.196-200.

Economic Survey 2010-2011: Prospects & Concerns. *Company Law Journal,* Vol.1, 2011, pp.134-164.

The Digital Divide in Rural South Asia: Survey Evidence from Bangladesh, Nepal & Sri Lanka by Yan Zhou, etc. *IIMB Management Review,* vol.23, 2011, pp.15-29.

India's Foreign Trade: 2010-11 (April-December). *RBI Bulletin, March 2011,* pp.329-341.

North-East Monsoon 2010: An Overview (1st October to 31st December, 2010). RBI Bulletin, March 2011, pp. 323-328.

Public-Private Partnership & its Application in India by Sukamal Datta. etc. *The Management Accountant,* March 2011, pp.201-205.

Public-Private Partnership Projects: A Tool for Economic Enrichment by Arindam Ghosh & Asit Gope. *The Management Accountant,* March 2011, pp. 184-189.

Quarterly Industrial Outlook Survey: October-December 2010 (52nd Round). *RBI Bulletin,* March 2011, pp. 343-364.

The Reserve Bank of India Making a Difference in Your Daily Life by Duvvuri Subbarao. *RBI Bulletin,* March 2011, pp.291-308.

4. EDUCATION

ICT-enabled Services & Activities of the Inflibnet by Jagdish Arora & P. Prakash, *University News,* 21st to 27th March, 2011, pp. 19-23.

Should We Welcome Foreign Universities in India?: Time for Introspection! by V. Shivkumar. *University News,* 14th to 20th February, 2011, pp.1-5.

5. INVESTMENT

Analysis of Takeover Defenses & Hostile Takeover by A.S. Dalal. *Company Law Journal,* Vol.1, 2011, pp.113-125.

Core Investment Companies: A Tight Leash? by Anup P. Shah. *BCAJ,* March 2011, pp.21-25.

Impact of Privacy & Confidentiality on Valuation: An International Perspective by Tom Cooper, etc. Journal of *Financial Management & Analysis,* Vol.23/2, 2010, pp.1-11.

Public-Private Partnership in Financial Market Regu-lation: A Case of Credit Rating Agencies by Mausumi Bhattacharyya. *The Management Accountant,* March 2011, pp.206-208.

6. MANAGEMENT

Corporate Governance Survey: A Holistic View for Altruistic Practice by Vijaya B. Marisetty. *IIMB Management Review,* Vol.23, 2011, pp.30-38.

Financial Management Focus on Working Capital Utilisation in the Indian Cotton Textile Industry: Methodological Analysis by Chinta Venkateswara Rao. *Journal of Financial Management & Analysis,* Vol.23/2, 2010, pp.63- 84.

A Step-by Step Guide to Smart Business by Eric T. Anderson. *Harvard Business Review,* March 2011, pp.98-105.

7. TAXATION & FINANCE

Finance Bill, 2011: Personal Taxation for Current Year 2011-2012 by R. Balakrishnan. *Taxman,* 19th to 25th March, 2011, pp.112-117.

Finance Bill, 2011: Union Budget 2011 & LLP Taxation By Sanjiv Agarwal. *Taxman,* 19th to 25th March, 2011, pp. 148-150.

The Spread of Aggressive Corporate Tax Reporting: A Detailed Examination of the Corporate-owned Life Insurance Shelter by Jennifer L. Brown. *The Accounting Review,* Vol.86/1, 2011, pp.23-57.

Taxability of Fees from Offshore Services – Post Finance Act, 2010 by Ankit Virendra & Sudha Shah. BCAJ, March 2011, pp.9-13.

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

Auditors Role Likely to be Widened to Check Misuse of Public Issue Funds

The ministry of corporate affairs is planning to ask auditors to comment on disclosures made by companies on the use of proceeds from rights issue and qualified institutional placements (QIPs) in addition to initial public offerings (IPOs). To broaden the scope of vigil on public issues and safeguard investor interests, the ministry is also keen that auditors comment and verify on the actual deviation of the use of proceeds from the objects as stated in the offer document. Sources in the ministry said that, at present, the auditor is required to only comment and verify the managements disclosure of the use of proceeds. They said the ministry may also consider creating a special cell for keeping record of companies launching IPOs. This will serve as an additional market mechanism to verify management disclosures.

*(**Source:** http://www.indianexpress.com/)*

IT Department to Review All Realty Deals to Unearth Black Money

The income tax department plans to review realty deals following allegations of rampant use of black money in many transactions. "We will take appropriate action wherever we find involvement of black money in such transactions," said Sudhir Chandra, chairman, Central Board of Direct Taxes. Chandra said the department would begin scrutiny of property deals in the national capital region and follow it up in other metros. The value of most real estate transactions in the national capital are suppressed to save on stamp duty, capital gains tax and wealth tax and are believed to have black money component as high as 65 per cent, said another income tax official. The black money component continues to remain high despite most states now fixing circle rates, or minimum rate at which a property can be registered, for various localities. The income tax department receives data on all property registrations worth more than 30 lakh as a part of its special data capturing mechanism from property registrars.

*(**Source:** http://economictimes.indiatimes.com/)*

Finance Ministry to Float Discussion Paper on Taxing More Services

Finance Ministry will soon come out with a discussion paper on service tax to increase its contribution to the overall tax kitty and align it with the proposed Goods and Services Tax (GST). "The Finance Ministry is working on a discussion paper on taxation of services to get opinion and feedback before moving to GST," a source told Press Trust of India. The source further said, based on the feedback, the ministry would decide on the need to prepare negative list of services, adding, "The services sector contribute more than 50 per cent of the GDP but its representation in revenue is relatively low." Finance Minister Pranab Mukherjee in his Budget 2011-2012 speech had said that many experts have argued that it will be desirable to tax services based on a small negative list, so that many untapped sectors are brought into the tax net. "Such an approach will be very conducive for a nationwide GST. I propose to initiate an informed public debate on the subject to help us finalise the approach to GST," Mukherjee had said.

*(**Source:** Press Trust of India)*

Get Income-tax Refunds in a Month, File e-Returns

There is an incentive for taxpayers who file their income-tax returns electronically - they will get their refunds within a month. To speed up refunds and encourage electronic filing of tax returns, the Central Board of Direct Taxes has promised expeditious refunds. The wait for refunds in the case of physical tax returns ranges between five to ten months. "We want tax-payers to file electronically as that helps in faster processing of refunds," Sudhir Chandra, chairman, Central Board of Direct Taxes, told reporters. As on 31st December, 2010, there were about 40 lakh refund cases pending with the tax department. Last year, a Comptroller and Auditor General report had highlighted that it takes as much as ten months for a taxpayer to get his refund. Reports of widespread corruption and frauds in issue of refunds have also spurred a revamp of the refund system. "The whole idea is that small taxpayers should not face any hardship in his interface with the department," Chandra added. "A refund banker scheme is already in place in the whole of country to ensure that taxpayers get refunds well in time," said an income-tax department official. Income-tax authorities send data to State Bank of India which in turn issues refund directly to tax-payers under the refund banker scheme. Chandra said the CBDT will, by June, notify guidelines for small salaried tax-payers having annual income of ₹5 lakh who will not be required to file tax returns if they do not have refund claims. E-filing, which was formally launched on 13th October, 2006, is mandatory for companies but remains optional for individuals

*(**Source:** http://beta.profit.ndtv.com/news)*

Now, You Can Claim Income-tax Deductions for Fines Paid to RTO

Now you can claim income-tax deduction for fines paid to the RTO that are compensatory in nature. In a recent order, Income-tax Appellate Tribunal (ITAT) has held that fines paid to RTO are allowable expenditure under the Income-tax Act. According to the provisions of the Income-tax Act, 1961 if a person is penalised for violating a law, the penalty paid for the offence is not allowable as expenditure for the purpose of computing his income under the Income-tax Act. The rationale behind this principle is that the income-tax law should not be seen supporting or encouraging people to violate the laws of the land. However, in the past, the courts have drawn a distinction between fines that are compensatory in nature and those that are penal in nature. They have also held that the former can be allowed as deduction but not the latter. The ITAT, in a recent order, underlined this difference further in a case involving Bharat C Gandhi, proprietor of Darshan Roadlines. The taxpayer was transporting consignment in excess of the permitted dimension as well as the weight limits. Since the firm carried out 230 such trips, it had to pay over 73 lakh to the RTO check posts as compounding fees. The income tax officer disallowed the expenditure on the ground that the payment is same as penalty for violation of the Motor Vehicles Act. The aggrieved taxpayer moved the ITAT with the counsel Jignesh R Shah, arguing that the compounding fees paid by a transporter for violation of dimension and weight limits under the Motor Vehicles Act cannot be construed as a penalty. He said that expenses are incurred out of commercial expediency. The cargo was indivisible and there was no other alternative except

by exceeding the limits under the Motor Vehicles Act. The RTO always knew that the taxpayer was carrying cargo exceeding the limits and therefore levied a fee. According to Shah, the fee paid is not in violation of law but an option given to the taxpayer to transport the goods by paying overloading charges. Therefore, Shah argued, such fees should be allowed as expenditure. Accepting this argument, e ITAT held that the compounding fees paid were not in the nature of penalty, but were allowable as expenditure incurred out of commercial expediency.
*(**Source:** http://economictimes.indiatimes.com/)*

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HC Rejects Income Tax Department Appeal on Tax Refund Issue

Over an issue of tax refund, a division bench of the Gujarat high court has rejected the income tax department's appeal against Nirma Chemicals Works Limited (NCWL). The department challenged the order of Income Tax Appellate Tribunal (ITAT) before a bench comprising Justices Akil Kureshi and Sonia Gokani. The ITAT had held that NCWL was entitled to get the refund. Nirma Chemicals Works Limited had filed returns of income on 20-11-2000 for assessment year 2000-2001. During the year under consideration, it had purchased 54,368 special premium notes (SPNs) of Nirma Ltd at the rate of ₹355 per note having face value of ₹200. Such SPNs were redeemed during the same year at the rate of ₹361. NCWL thus earned net income of ₹268908 and offered it as its business income. Since Nirma Ltd had deducted tax at source on entire difference between face value of ₹200 and redemption price of ₹361 and thus collected ₹1925715, NCWL claimed refund of such TDS. However, the Assessing Officer declined the claim. This issue was raised before the CIT (Appeals) who also declined the claim. However, the ITAT in appeal accepted the case of the company. Referring to Section 199 of the Income Tax Act and putting stress on words for the assessment year for which such income is assessable, the tribunal had found that there was no dispute that NCWL was owner of the security which after purchase from market was redeemed. It observed that the tax was deducted from amount payable to the NCWL and it alone was entitled to claim credit for such security. The Tribunal opined that in transaction for earning this income NCWL had already offered such income to tax and income corresponding to the tax deducted at source was not included as income of the NCWL. The division bench noted in an order made available today, When M/s. Nirma ltd had deducted tax at source on such transaction and when it was found that such tax was in excess of tax liability of the assessee, tribunal in our opinion rightly directed the Assessing Officer to refund the same.
*(**Source:** http://www.thehindubusinessline.com/)*

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Preparation of Negative List for Service Tax Likely to Start Soon

The Finance Ministry expects to begin the compilation of the negative list for service tax soon. Negative list is a list of items on which tax will not be charged as compared to a positive list which the government already has. The government believes that service tax contribution to the overall tax kitty can be increased significantly if a negative list is prepared. "Deliberations are expected to start soon on the negative list," Department of Revenue joint secretary V K Garg said on the sidelines of a workshop on service tax organised by the Bengal Chamber of Commerce and Industry. The Finance Ministry may choose to get inputs and public opinion first and then prepare a discussion paper based on that.
*(**Source:** http://www.hindustantimes.com)*

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Service Tax Liability Too Fixed at Invoice Stage

The Central Board of Excise and Customs has tweaked service tax rules, making service providers liable to pay tax as soon as they issue an invoice to their clients. Under the earlier rules, service tax became due only when a provider received payment for the service. This was at variance with the taxation of goods. States levy sales tax (value-added tax) on goods when the invoice is issued. Excise duty is also paid at the factory gate when the goods leave the factory on issuance of an invoice. The new rules provide a consistent regime for taxation of goods and services and aim to set the stage for the Goods and Services Tax (GST), which the government intends to roll out from April 2012. The Central Board of Excise and Customs had put out a draft of these rules for discussion in August last year. "The rules have been changed following public feedback," a finance ministry official said. In cases where an invoice is issued periodically or not issued within 14 days of completion of service, a service provider will have to pay tax on completion of the service.
*(**Source:** http://www.business-standard.com/india/)*

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India for Review of Tax Treaty with Mauritius

India is set to step up pressure on Mauritius to review its tax treaty with the country. The finance ministry has asked the ministry of external affairs to initiate talks with Mauritius on the issue. "The finance ministry has written to MEA for renegotiation of the tax treaty to ensure exchange of information of banking transactions and assistance in tax matters," Central Board of Direct Taxes chairman Sudhir Chandra told reporters. Indian tax authorities are keen to introduce provisions in the treaty that will restrict its benefits to genuine investors through a limitation of benefit clause. Such a clause exists in other tax treaties such as India-Singapore one wherein investors have to meet certain conditions such as minimum expenditure and a track record of two years in Singapore to avail the benefit of the DTAA.
*(**Source:** http://timesofindia.indiatimes.com/)*

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Indian firms Make a Profit of ₹6 Lakh Per Employee

Indian companies pay a salary of ₹4.8 lakh to each of their employee on an average, but earn a profit of ₹6 lakh per employee in return, says a new survey. According to a study titled 'Measuring Human Capital - Driving Business Results', organisations in India pay an average remuneration of ₹4.8 lakh and earn ₹6 lakh of profit per employee, which makes the human capital return ratio on investment to 1.79 for organisations in the country. Besides, companies make an investment of ₹7,000 on learning and development (L&D) per employee. It further said that Indian companies make a pure profit of ₹15 from every ₹100-worth revenue generated by their each employee. "With India being the fastest growing economy, organisations that would maximise their human capital contribution to business performance, would be the ones to best leverage the positive economic environment," the study says.
*(**Source:** http://timesofindia.indiatimes.com/)*

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IFRS Foundation to Enhance IFRS Taxonomy to Reflect Common Reporting Practice

The IFRS Foundation announced recently that it will publish supplementary tags for the IFRS (International Financial Reporting Standards) Taxonomy that reflects disclosures that are commonly reported by entities in their IFRS financial statements. By publishing these supplementary tags, the IFRS Foundation is taking a first step in providing additional elements as part of its XBRL (eXtensible Business Reporting Language) taxonomy that reflect common reporting practice across the world and across industries. The publication of these common-practice tags will enable entities to create IFRS financial statements in XBRL with fewer entity-specific taxonomy tags, thereby enhancing the comparability of information. The common-practice tags are being developed through the analysis of over 200 financial statements – i.e.; line items from Statements of Financial Position, Comprehensive Income, Cash Flows and Changes in Equity, and block-tagged notes and accounting policies - that have been prepared in accordance with IFRSs by entities from a broad range of geographical areas and industries, including financial institutions and insurance companies. These tags will be published over the coming weeks as a draft supplement (i.e. as an interim release) to the IFRS Taxonomy 2011. These tags will be subject to the same due process that is applied to the development of the core IFRS Taxonomy and they will consequently be published for public review and consultation. These initial common-practice tags will be the first part of a process that the IFRS Foundation plans to undertake in order to enhance the usability of the IFRS Taxonomy by reflecting common reporting practice. The next part of the process will involve examining financial statement note disclosures in detail and identifying common reporting practice in these note disclosures. As part of this effort, the Foundation has published a call for listed IFRS filers to participate in a voluntary task force on XBRL detailed tagging. The results of this initiative are expected later in the year and will be used to improve the common-practice tags published by the IFRS Foundation.

*(**Source:**http://www.ifrs.org/News/)*

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SEC Charges India-Based Affiliates of PWC for Role in Satyam Accounting Fraud

The Securities and Exchange Commission recently sanctioned five India-based affiliates of PricewaterhouseCoopers (PwC) that formerly served as independent auditors of Satyam Computer Services Limited for repeatedly conducting deficient audits of the company's financial statements and enabling a massive accounting fraud to go undetected for several years. The SEC found that the audit failures by the PW India affiliates – Lovelock & Lewes, Price Waterhouse Bangalore, Price Waterhouse & Co. Bangalore, Price Waterhouse Calcutta, and Price Waterhouse & Co. Calcutta – were not limited to Satyam, but rather indicative of a much larger quality control failure throughout PW India. Both SEC and PCAOB *(Public Company Accounting Oversight Board)* the two American regulators have imposed their largest ever penalties on PW India. USD 6 million by the SEC and USD 1.5 million by the PCAOB.

*(**Source:**http://www.sec.gov/news/)*

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IAESB Proposes Revised Standard on Professional Values, Ethics, and Attitudes

The International Accounting Education Standards Board (IAESB) recently released for public exposure a proposed revision of International Education Standard (IES) *4, Professional Values, Ethics, and Attitudes.* The revised standard, part of the IAESB's project to improve the clarity of its standards, proposes that the development of professional values, ethics, and attitudes be addressed by learning and development activities that occur throughout the career of the professional accountant. IES 4 will be helpful to educational organisations, employers, regulators, government authorities, and other stakeholders who support the learning and development of professional accountants. IES 4, drafted in 2004, prescribes the values, ethics, and attitudes that professional accountants should acquire during the education program leading to qualification. In addition to a formal program assessment and a learning outcome approach, the IAESB also proposes a requirement on reflective activity—where professional accountants and students undertake the practice of documenting experiences relating to lessons learned from ethical dilemmas and situations." The assessment of the elements of professional accountancy programs—including professional values, ethics, and attitudes as outlined in IES 4—is essential to both the development and the maintenance of competence," stated Mark Allison, chairman of the IAESB. "It lays the foundation for aspiring professional accountants to exercise professional judgment in the public interest." As part of its project to improve the clarity of its standards, the IAESB has undertaken a project to redraft all eight of its IESs in accordance with its new clarity drafting conventions. This project began in December 2010 with the proposed revision of IES 7, *Continuing Professional Development: A Program of Lifelong Learning and Continuing Development of Professional Competence.* The current timetable envisages that all IESs will have been revised and redrafted, or redrafted only, by the first quarter of 2013.

*(**Source:**http://press.ifac.org/news/)*

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Three New Draft Q&As on the IFRS for SMEs Posted

The SME Implementation Group, responsible for assisting the IASB on matters related to the implementation of the IFRS for SMEs, published recently, for public comment, three more questions and answer documents (Q&As) on the IFRS for SMEs. The new Q&As cover the topics which are Captive insurance subsidiaries, interpretation of 'traded in a public market' and investment funds with only a few participants.

*(**Source:** http://www.ifrs.org/News/)*

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Canadian Securities Regulators Provide Guidance on IFRS Transition Disclosures

The Canadian Securities Administrators (CSA) has recently published CSA Staff Notice 52-*328, Disclosures About Accounting Policies in the Year of Changeover to International Financial Reporting Standards.* This notice responds to specific questions that have been received by the CSA staff on disclosure about accounting policies in an issuer's interim and annual Management's Discussion and Analysis (MD&A) in the year of changeover to International Financial Reporting Standards (IFRS).

*(**Source:**http://www.iasplus.com/)*

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G20 Finance Ministers Will Watch Convergence Efforts

The G20 Finance Ministers and Central Bank Governors in

a meet on 14th to 15th April, 2011 in Washington DC agreed, among other things, to closely watch the progress of the IASB and FASB's convergence efforts. The final official report states: "We will review at our next meeting progress made by the IASB and FASB towards completing their convergence project by the end of 2011 and look forward to the outcome of the ongoing IASB governance review process. "The full communiqué is available on the French Department of Trade and Industry's website. Following the joint IASB-FASB meeting, Sir David Tweedie and Leslie Seidman had conceded that they need to extend the timetable for several of their projects. They maintained, however, that they intend to finish the convergence programme by end of 2011.
*(**Source:**http://www.iasplus.com/)*

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Chairmen of the IASB and FASB Extend Convergence Timeline

In a recent podcast, Sir David Tweedie, Chairman of the IASB, and Leslie Seidman, Chairman of the FASB, discussed the achievements of the convergence project and provided a revised timeline for completing the remaining projects. The IASB and FASB will be extending, by a few months, the timeline for completing their convergence projects on revenue recognition, leases, financial instruments and insurance contracts. Chairman, FASB explained that the delay is due to the significant amount of constructive feedback received and that it will take additional time to work through all the issues. Both the Boards are expected to issue an updated convergence progress report shortly, which will be posted on the IASB and the FASB websites.
*(**Source:**http://www.iasplus.com/)*

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IFRS Foundation Publishes XBRL Examples, SEC Issues 'No Action' Letter for US IFRS Filers

The IFRS Foundation has recently published a set of 12 illustrative examples in XBRL for the IFRS Taxonomy 2011. These examples illustrate how the IFRS Taxonomy 2011 should be used to tag IFRS financial statements (including notes) in XBRL, and in accordance with the XBRL architecture outlined in The IFRS Taxonomy 2011 Guide and The Global Filing Manual. The examples are intended to help preparers understand how to apply the taxonomy to create instance documents and entity-specific extensions using both block tagging and detailed tagging, and also XBRL and Inline XBRL. In response to United Statements Securities Exchange Commission (SEC) concerns about the suitability of the existing IFRS Taxonomy 2011 for US filing purposes and the outcomes of a pilot XBRL study, the IFRS Foundation has recently announced the taxonomy is to be extended to include more terms that are commonly used in practice. In the meantime, the SEC has issued a 'no action' letter, in which it states: " We are of the view that foreign private issuers that prepare their financial statements in accordance with IFRS as issued by the IASB are not required to submit to the Commission and post on their corporate websites, if any, Interactive Data Files until the Commission specifies on its website a taxonomy for use by such foreign private issuers in preparing their Interactive Data Files."
*(**Source:**http://www.iasplus.com/)*

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Taxman Targets 1,200 SMEs Over Record Keeping

The Taxman in UK has sent letters to more than 1,000 SMEs to arrange visits to check their record keeping. As recently revealed, by a leading accountancy journal, HM Revenue & Customs sent out letters before replying to the formal consultation period on the spot checking of small businesses' records. The Revenue will be seeking confirmation that businesses are maintaining "accurate and adequate" business records. A HMRC spokesman confirmed that around 1,200 businesses will be checked in the first round.
*(**Source:**http://www.accountancyage.com/aa/news/)*

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Tax Blamed for 'Unattractive' Investment Climate

Tax is among the primary factors deterring companies from investing in the UK, according to a new report. The CBI has called for an end to the 50p personal tax rate and lower business levies, saying the commitment to cut corporation tax to 23 per cent is "welcome", but the government should aim for 18 per cent in the long term. It claimed investment will play a critical role in the economic recovery, plugging the yawning void of muted public and consumer spending, but warns "the UK's reputation as a good place to invest is under threat". The study, entitled 'Making the UK the best place to invest', canvassed 400 companies. It calls for government to allow private provision of public services, accelerate moves towards a low-carbon economy and ramp up provision of high-speed broadband. Director-general John Cridland said: "With competition for international capital so fierce, the government must play up our strengths and remove the stumbling blocks to investment. Time isn't on our side and we have less than five years to turn things around."
*(**Source:** http://www.accountancyage.com/aa/news/)*

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June Deadline Too Tight for International Standard Setters

The deadline for International Financial Reporting Standards convergence has been stretched by as much as six months, as the International Accounting Standards Board admitted its June target has slipped out of reach. Instead, the body has said it will need "a few more months" to finalise the standards, before quantifying its position with "we intend to try to finish this convergence programme by end of 2011". Chairman of the US Financial Accounting Standards Board, laid out the issues still to be resolved; among them, the controversial rule on accounting for financial instruments. IASB chairman Sir David Tweedie will step down in June, and the body had been eager to complete convergence before his departure. However, the resolution of three key issues - revenue recognition, leases and financial instruments and insurance as a joint project - remains stubbornly out of reach.
*(**Source:** http://www.accountancyage.com/aa/news/)*

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66 per cent Favour Two-Tier International Standards Over UK GAAP

Two-thirds of UK businesses are in favour of a two-tier accounting system based on International Financial Reporting Standards, as per a new report. According to a survey conducted by one of the Big Four Audit Firms on 290 companies it was found the majority back the move, while 27 per cent called for three-year delay on transitioning, and 6 per cent opposed the plan altogether. The consultation on IFRS for SMEs launched by the Accounting Standards Board is drawing to a close; in it, the body proposed a simplified version of the international guidelines, known as FRSME. Just over one-third of respondents said they are switching to full IFRS, while 24 per cent envision adopting FRSME and the remaining 41 per cent had yet to decide.

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Data Destruction[1]

Data Thefts now are often so smooth and slick that people don't even realise they were robbed. The biggest thing crooks need to infiltrate your life or business and cause major problems is the data that you have on file in the harddisk.

Data Destruction

Information in the modern age is as valuable as cash. Criminals can use personal data to steal identities, allowing them to get credit in someone else's name and then go on a spending spree. The data with CA's reveals financial profile of a client. Data that is no longer required for the accounts can not simply be thrown out. It must also be securely destroyed to prevent theft.

According to the Section 43-A of the amended Information Technology Act, 2000, the following liability may arise for the data loss: ***"Compensation for failure to protect data:*** *Where a body corporate, possessing, dealing or handling any* ***sensitive personal data*** *or information in a computer resource which it owns, controls or operates, is* ***negligent*** *in implementing and maintaining* ***reasonable security practices*** *and procedures and thereby causes wrongful loss or wrongful gain to any person, such body corporate shall be liable to pay damages by way of compensation, to the person so affected."*

In the following paragraphs, some methods have been given for data destruction in a secure way for prevention of theft:

Shredding your hard drive

Just as you get paper shredders you also get hard drive shredders. Put your hard drive into the shredder and it makes mincemeat of it. After that it is practically impossible to assemble back the hard drive and retrieve data from it.

Disrupting the magnetic field of your hard drive *(degaussing)*

Although degaussing may not seem as drastic as shredding this is also a secure way of completely destroying your data. Information on your hard drive is stored and kept at one place by a magnetic force like a glue. The information is stored in bits and bytes with this magnetic glue as base. If you destroy this place all the bits and bytes get scattered and the sequence is permanently disrupted. It's like arranging 100 marbles on a table in a particular sequence. Then you wildly shake the table and the entire sequence is destroyed. After that if somebody comes to that table there is no way to find in what sequence the marbles had been placed. The same happens with degaussing.

A degaussing machine is not as expensive as a hard drive shredder and you can keep it in your office if you have to occasionally destroy your data completely and securely.

Overwriting sectors that were previously occupied by your data

After the file is deleted in a normal way the space allocated to it is simply made available for overwriting in case that space is needed. So it is a matter of chance. The space made available by deleting a particular file may be overwritten immediately or it may take a couple of months for that to happen. There are some programs that immediately override the space left open after deleting the file. This way you can delete single files securely and completely without disturbing your hard drive's magnetic field or shredding your hard drive altogether. There are many programs available online that can help you securely and completely delete individual bits of information.

Burn your hard drive

Burning a hard drive is not as easy as throwing it in the fire. Different metals have different melting points so you may have to study what sort of heat would be required to completely melt or incinerate your hard drive.

Use Licensed Software

Licensed Software's like ERASER, SECURE ERASE, DBAN, DEGAUSSERS also can also be used for data destruction.■

[1] Contributed by Mr. Prashant Mali, Mumbai

Invitation for Expression of Interest for Authoring Publications Relevant to the Members in Practice of ICAI

The Committee for Capacity Building of CA Firms and Small & Medium Practitioners is meant to encourage and enhance close links between the Institute and the Chartered Accountants in Practice, so as to provide for them, a base of reference in terms of knowledge, expertise, skills and assistance in their professional growth, simultaneously pursuing the goal of providing newer opportunities to the practitioners & Firms.

One of the major responsibilities of CCBCAF & SMP is to bring out publications for various topics relevant for the Members in Practice of the Institute of Chartered Accountants of India (ICAI).

The CCBCAF & SMP invites Expression of Interest from members of the Institute and other experts who are interested in developing/preparing basic drafts of the publications on topics relevant to the Members in Practice of ICAI. The intending authors of the CCBCAF & SMP publications are expected to have appropriate level practical experience in the relevant area along with the knowledge of various aspects of practice.

The CCBCAF & SMP publication has to be prepared as self-learning booklets in the form of handbooks with proper mix of theory and practical case studies.

Apart from getting recognition, among their professional brethren, for their contribution in preparing the background materials, the authors of the accepted publication materials will get:

1. Their names printed in the Publications
2. Honorarium and reimbursement of incidental expenses as per the prevailing policy of the Institute. (Which will depend upon the size, time and efforts to be required to prepare such publication materials).

The intending authors are required to send a formal request letter with the following details, to The Secretary, CCBCAF & SMP, The Institute of Chartered Accountants of India, Post Box No.7100, Indraprastha Marg, New Delhi – 110 002. Sending proposals by email at spal@icai.in with a copy to sambit.mishra@icai.org is preferred:

1. Brief profile of the author
2. Specific experience and expertise in the relevant topic for which they offer themselves to write the background materials which will enable the CMII secretariat for allotting the preparation of material for them
3. Proposed coverage of the Publication (in about 2,000 – 3,000 words)
4. Sources of primary and secondary data based on which the Publication material will be written
5. Time frame within which they can submit the publication material.

It may be noted that mere submission of the Expression of Interest may not lead to the allotment of the particular publication materials to a particular applicant. The Institute reserves the right to request any other expert (though they might not have offered their expression of interest in this regard) to prepare publication materials. No communications will be entertained in this regard. Only selected authors will be individually communicated.

Indicative topics on which CCBCAF & SMP would like to bring out publications are given below:

1. Auditing, Assurance, and Ethics Pronouncements for Practitioner & CA Firms
2. Quality Control for an Audit of Financial Statements: A case of Small & Medium Practitioner
3. Mentoring Guidelines for Small & Medium Practitioners
4. Evaluating and Improving Performance: A Guide for Small & Medium Practitioners
5. Handbook for the Practitioners
6. Managing Risk to Enhance the Practitioner Value
7. E-Business and the Small & Medium Practitioners
8. Handbook for Information Security Governance:
9. Issues & Perspectives of Financial Reporting by Small & Medium Practitioners
10. A study of Mergers & Acquisitions: An International Perspective
11. Implementing the Accounting Standards: Technical Issues in various CA Firms
12. Issues in Auditing Standards, Expectations, and compliance requirements in Various CA Firms
13. Cost & Financial Management: Practitioner/CA Firms perspective
14. LLP: Practitioner/CA Firms perspective
15. MDP: Practitioner/CA Firms perspective

16. A Roadmap to GST
17. A Roadmap to Direct Tax Code
18. Value Added Business Controls - The Right Way to Manage Risk in case of Small & Medium Practitioners
19. Auditors' Report under the Companies Act – Issues on CARO, Documentation
20. Export Documentation: A Guideline for Small & Medium Practitioners
21. Professional Opportunities: A Snapshot for Small & Medium Practitioners
22. Other topics relevant to Practitioners/CA Firms

Chairman
Committee for Capacity Building of CA Firms and Small & Medium Practitioners

Campus Placement Programme for Newly Qualified Chartered Accountants

Exclusively Structured for
Small & Medium sized Enterprises (SMEs) &
the Small and Medium sized CA Firms

In its endeavor to provide ***quality Accounting, Finance, Tax, Audit and Management Consultancy personnel to small and medium sized Industries*** and to provide a platform to the newly qualified Chartered Accountants, CMII would be conducting a Campus Placement Programme:

Campus Placement Programme at a Glance:

Centres	Dates
Bangalore, Chennai, Kolkata, Mumbai and New Delhi	18th & 19th May, 2011
Ahmedabad, Indore, Kanpur ,Ludhiana , Pune, Chandigarh, Coimbatore, Hyderabad , Jaipur & Nagpur.	19th May, 2011

Minimum Salary Offer Requirements(Per Annum):

i) SMEs* at all centres	₹3,00,000/-
(ii) SMPs	₹2,40,000/-

* the Small and Medium Enterprises would include all commercial, industrial and business reporting enterprises, whose turnover for the immediately preceding accounting period on the basis of audited financial statements does not exceed ₹50 Crores.

Participation Fees*

Particulars for SME's	**Fee per centre per day (₹)** Day1**	**Day2**
Bangalore, Chennai, Kolkata, Mumbai and New Delhi	₹10,000	₹7,500
Ahmedabad, Indore, Kanpur ,Ludhiana , Pune, Chandigarh, Coimbatore, Hyderabad , Jaipur & Nagpur.	₹7,500	
Common to all Centres: Conducting interviews on the immediate following day of the day of initial interviews	₹5,000	

Particulars for SMP's	**Fee per centre per day (₹)** Day1**	**Day2**
Bangalore, Chennai, Kolkata, Mumbai, New Delhi, Ahmedabad, Indore, Kanpur ,Ludhiana, Pune, Chandigarh, Coimbatore, Hyderabad , Jaipur and Nagpur.	₹7,500	₹5,000
Common to all Centres: Conducting interviews on the immediate following day of the day of initial interviews	₹2,500	

* Plus Service Tax as applicable.

** Day/Slot will be allotted based on First Come First Serve Basis and Number of Jobs offered.

Last date for Company Registration	2nd May 2011 (Upto 05:00 PM)
Last date for Shortlisting by Companies	12th May 2011 (Upto 05:00 PM)
Consent sending by Candidates	15th May - 16th May 2011 Upto 11:00 AM(Morning)

For Further Details:

Secretary, CMII of ICAI Placement Coordinator, ICAI	Website	www.cmii.icai.org
	Email	placements@icai.org , spal@icai.in
	Telephone	011-30110450, 30110548
	Fax	011-30110583

Note:Candidates registered for Campus Placement Programme conducted during February-March, 2011 and who have not accepted the job offers are eligible for this Campus Placement Programme i.e. they need not register themselves again but they have to validate (resubmit)their resume in the www.cmii.icai.org.

Organised By: Committee for Members in Industry

The Institute of Chartered Accountants of India,
'ICAI BHAWAN',Post Box Number 7100,
Indraprastha Marg,
NEW DELHI - 110 002

Contribution to the Question Bank of CPT

The Common Proficiency Test (CPT) is an entry level test meant for 10+2 students to the Chartered Accountancy Profession having multiple choice objective questions. The level of knowledge expected is basic knowledge with the objective to develop conceptual understanding of the subject concerned.

With a view to augment the Question Bank in the Subjects of Accounting/Mercantile Laws/General Economics/Quantitative Aptitude of Common Proficiency Test, it has been decided to invite questions from Chartered Accountants/Subject experts working in various Colleges/Universities/Public/Students pursuing Chartered Accountancy Course etc.

The contributor can contribute as many questions as he/she can, but in a lot of minimum of 20 questions in the subjects of Accounting/Mercantile Laws/ General Economics/Quantitative Aptitude in the following manner:-

- The questions should be of objective with four probable answers for each question. The correct answer for each question is also required to be given.
- Fill in the blanks having four alternative answers.
- Small paragraph containing two to three lines followed by a question having four alternative answers.
- Numerical having four alternative answers (in Fundamentals of Accounting, Mathematics and Statistics).
- Simply worded Case studies involving multiple concepts be also prepared. The case study could be something like a practical situation described in 3 to 4 lines in simple language with application of single/multiple concepts and requiring students to choose one answer from amongst four answers whereby the analytical/logical ability and intelligence of the students is tested.

Since the CPT is an entry level Test meant for 10+2 students, the level of knowledge expected is basic knowledge and the questions should be aimed at testing the conceptual understanding and fundamentals of the subject than merely testing the memory of candidates. The difficulty level of the questions should be of 10+2 level and capable of being answered/solved in less than one minute.

While framing the questions, the questions be framed in such a manner that each one of the four answers given for a particular question, per se, appear to be the right answer thereby requiring the candidate to use his analytical ability to find the correct answer.

- The language of the questions to be sent should be English only and is clear, correct, unambiguous and free from any doubt. The language conveys the same meaning as was intended by you.
- The copyrights of the questions so submitted shall vest with the Council of the Institute. The contributor of the questions shall ensure that the questions so submitted to the Institute are not parted with by him/her to any other Body/Person and shall be meant only for the exclusive use by the Council of the Institute.

- **It may please be noted that the questions framed by you should be original and not already published in some books or journals or study material of the Institute or reference/ text books available in the market or also from question papers of any other examinations or material distributed by any coaching institution. The requirement is the questions that are original and framed with the meticulous care and genuinely.**
- For each question framed and forwarded and accepted by the Council of the Institute for augmentation of the Question Bank of CPT, ₹250/- per question selected/accepted will be paid as honorarium. In addition to honorarium payable towards questions selected, ₹100/- (fixed) will be paid for other services also. The questions may be sent in a sealed envelope superscribed "Question Bank – CPT" to Shri G. Somasekhar, Additional Secretary (Exams),The Institute of Chartered Accountants of India, Indraprastha Marg, New Delhi – 110002 by name or by e-mail to srdd_exam@icai.in While sending the questions by post/mail, please mention your name and complete postal address alongwith contact details including mobile number. All correspondence on the subject should be treated as secret.

Interested persons may kindly contribute to the Question Bank of CPT.

(G. Somasekhar)
Additional Secretary(Exams)

ANNOUNCEMENT

The Institute of Chartered Accountants of India (ICAI) intends to utilise the services of Members of ICAI and others in the field of ICAI Ethics as **Faculty**. The interested persons may please send their willingness along with the Bio-Data by E-mail esb@icai.org or by post to the following:

The Secretary
Ethical Standards Board (ESB)
The Institute of Chartered Accountants of India
Indraprastha Marg
New Delhi – 110002

Invitation to Join Panel of Examiners

The Institute is in the process of strengthening its panel of examiners with professionals/academicians/ resource persons for all the papers in CA IPCE and Final (New Course) Examinations in general and for the following subjects in particular:

1. Strategic Financial Management
2. Advanced Auditing and Professional Ethics
3. Advanced Management Accounting
4. Information Systems Control and Audit
5. Direct Tax Laws
6. Indirect Tax Laws
7. Taxation
8. Business Law, Communication and Ethics
9. Information Technology

Persons who have the requisite proficiency in the above subjects, inclination for evaluation of answer books and who can spare time may send in the Empanelment Form duly filled in to the Sr. Deputy Director (Exams), The Institute of Chartered Accountants of India, ICAI Bhawan, Indraprastha Marg, New Delhi – 110002. The form may be obtained by sending a request letter or in the alternative, downloaded by clicking on to link http://220.227.161.86/15857ExaminersEmpanelmentForm.pdf

Readership Survey: Collecting Feedback on the Journal

As part of our continuous effort to improve upon the content and quality of *The Chartered Accountant* journal, we will be glad to know our readers' experiences and expectations from us through an online readership survey, which has been hosted on the website of our Institute www.icai.org. Readers are requested to take this survey by 15th May, 2011, and make this whole process effective, so that your feedback can be considered by the Editorial Board for further improving our Journal.

- Editor

Invitation for Empanelment as Resource Persons for the Programmes to be Organised by the Committee for Capacity Building of CA Firms and Small & Medium Practitioners

The Committee for Capacity Building of CA Firms and Small & Medium Practitioners of the Institute of Chartered Accountants of India proposes to organise the following programmes during the year 2011-2012 which are broadly relevant to the Members of ICAI in Practice.

1. Workshop on Capacity Building Measures of CA Firms & New Professional Avenues

Indicative topics for these workshops

- i. IFRS
- ii. Taxation
- iii. Corporate Governance
- iv. Accounting Standards
- v. Investment
- vi. Information Technology
- vii. Auditing
- viii. Valuations
- ix. Mergers and Acquisitions
- x. Capital Market
- xi. Portfolio Management
- xii. A Roadmap to GST
- xiii. A Roadmap to DTC
- xiv. Practice Management
- xv. Other Topics Relevant to the Practitioners/ CA Firms

2. CFC Meet
3. Seminar/Conference on Capacity Building Measures of CA Firms
4. Interactive/Brainstorming session with CA Firms
5. Networking Summit
6. Management Development Programmes/ Executive Development Programmes

Experts who have more than three years of experience in the relevant area and who have delivered lectures at various forums of Chartered Accountants are eligible for the enlistment in the Panel of Experts.

Experts who are interested to be associated with The Institute of Chartered Accountants of India as Resource Persons are requested to send/e-mail their resume to Dr. Surinder Pal, Secretary at the following address :

Committee for Capacity Building of CA Firms
and Small & Medium Practitioners
The Institute of Chartered Accountants of India
ICAI BHAWAN
I.P. Marg,
New Delhi –110 002
E-Mail: spal@icai.in, sambit.mishra@icai.org
Tel No. 011-30110430

It would be appreciated if the resume including all details regarding qualification, Membership no. of ICAI (if any), Experience, areas of specialisation, contact address, etc. is sent at the earliest, preferably within 15 days.

Chairman
Committee for Capacity Building of CA Firms
and Small & Medium Practitioners, ICAI

Invitation to Collaborate in the Activities of Committee for Members in Entrepreneurship & Public Services

The ICAI is proud to acknowledge various professional achievements which its members in Entrepreneurship or Public Service have achieved during the course of their professional career or otherwise. In order to encourage and enhance their participation in the institute's activities and to enhance the efficacy of ICAI work program by factoring their perspective and vision with the institute, the ICAI has constituted a new Committee for Members in Entrepreneurship & Public Services. The objective of the Committee is to associate members in entrepreneurship or public service, to have a constant interface with ICAI and to solicit their suggestions for restructuring the institute initiatives towards this niche segment of members.

While ICAI also sends across along with the fee circular a data sheet to capture the profile of individual member, it is somehow seen that many a times such communications miss the attention of esteemed members.

The announcement hereof is for the attention of not only such members in Entrepreneurship or in

Public Services but membership in general as well so that while members in Entrepreneurship & Public Services update their profile as per the 'Performa' mentioned below, the other members can provide the details of such members whom they have come across through their dealing with such class of professionals.

Performa

Name
Membership No.
Address for Communication
Contact No.
Email
Nature of Professional Engagement

A) Members in Public Services

- **i. Working/Worked as a Public Servant i.e. MP/MLA**
- **ii. Associated with a constitutional Authority i.e. Judiciary/Appellate Tribunal**
- **iii. Working with regulatory bodies i.e. SEBI, RBI, IRDA etc**
- **iv. Civil Servant (Serving in Group A or Group B of Allied Services in Government of India)**
- **v. Serving with any State Government**
- **vi. Priest in a Church/Temple**
- **vii. Any other, please specify**

B) Entrepreneur Members (excluding Chartered Accountancy firms)

- **i. Nature of Business**
- **ii. Form of Business**
- **iii. Date of Establishment**

C) Members running NGOs

Please send duly filled in form to Secretariat of the Committee for Members in Entrepreneurship & Public Services, The Institute of Chartered Accountants of India, ICAI Bhawan, PB No. 7100, Indraprastha Marg, New Delhi – 110 002, India. Ph +91 11 30110487, 39893989 (Extn. 487), fax +91 11 30110591, e-mail: cmeps@icai.in

Invitation for Authoring Publication on Ethical Issues

The Ethical Standard Board (ESB) of Institute of Chartered Accountants of India (ICAI) invites application from members for authoring a publication 'Do's And Dont's for Members on Ethical Issues'. The interested members may please send their willingness along with Bio-Data by E-mail to esb@icai.org or by post to:

The Secretary
Ethical Standards Board (ESB)
The Institute of Chartered Accountants of India
Indraprastha Marg
New Delhi – 110002

Classifieds

4843 Midsized firm having Self owned office (3,000 sq. ft.) in Western suburbs of Mumbai seeks proposals for merger from reputed, financially sound firms. Email: hari4246@gmail.com

4844 Wanted qualified/semi qualified C.A./article Suri Malhotra & Associates, 15a/44 Pratap Chambers-II, Flat no.202, WEA Karol Bagh, New Delhi-110005. Contact V.K. Malhotra: 9818555642/011-25496826. Email:malhotravirender@yahoo.co.in

4845 Kochi based CA firm require young/experienced Chartered Accountants. Excellent exposure to Tax/Company/ IS audit & consultancy and be groomed to eventually become partners of the firm. Firms interested in merger also can mail proposal to: sebdom1@gmail.com

4846 Chartered Accountant qualified during the year 1989 worked in various industries in India as well as in the Middle East seeks partnership in an existing firm in Trichur or Cochin. Please contact: abchap@omantel.net.om

Insurance against Professional Indemnity

An Insurance Protection for Members in practice & CA Firms of ICAI...
An Initiative of the Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI...

The **Committee for Capacity Building of CA Firms and Small & Medium Practitioners (CCBCAF & SMP)** of ICAI has arranged insurance protection for members in practice/firms in the form of specially designed professional indemnity insurance at a reasonable premium. The scheme is already in effect for the Members in practice/ Firms of the ICAI.

Highlights

This policy is meant for professionals to cover liability falling on them as a result of errors and omissions committed by them whilst rendering professional service. Legal cost and expenses incurred in defence of the case, with the prior consent of the insurance company, are also payable, subject to the overall limit of indemnity selected.

Only civil liability claims are covered. Any liability arising out of any criminal act or act committed in violation of any law or ordinance is not covered.

Eligibility:

Chartered Accountants, individual/jointly or Proprietorship Concern or a Partnership Firm/ Partnership.

The applicants/firms should not have been subjected to disciplinary action by the Institute.

Premium Rates:

For Individual Members in Practice:

For SI of 10 lakh, the premium proposed is ₹1000/-(1:1),₹803/-(1:2),₹705/-(1:3) and ₹600/-(1:4).

Ratios indicate relationship between AOA and AOY

Additional: Per Capita for named professional employee-₹100

Excess:1/2 per cent of Any One Year Limit subject to minimum ₹5,000/-and maximum of ₹1 lakh. (as per Market Agreement) For higher limits.

For Chartered Account Firm:

The premium of 0.10 per cent shall be as per rates for Individual Chartered Accountants and shall be applied on the AOY limit chosen. All named professionals shall be charged ₹100/-extra over and above the basic premium.

For Example: If the CA firm chooses a Sum Insured of ₹2 crore the Premium rate of 0.10 per cent is to be applied on the AOY limit and each professional (including partners) have to be charged ₹100/- each. For example a CA firm with 20 professionals including 9 partners will pay ₹20, 000/- plus 20X ₹100 totalling to ₹22, 000/- .This would be on 1:1 ratio. If the ratio is 1:2,the Premium rate would be .08 per cent if the ratio is 1:3,the Premium rate would be .07 per cent and if the ratio is 1:4,the ROL would be .06 per cent on the indemnity limit chosen.

* Jurisdiction: India only

*Above Premium rates are subject to Service Tax @10.3 per cent.

Members and CA firms desirous to avail the benefits under this scheme may please contact directly to New India Assurance Co. Ltd. or Committee Secretariat at the following address:

Assistant Manager (Development)
New India Assurance Co.Ltd.
Divisional Office No.141600,Jeevan Seva Bldg.,
2 floor,S.V. Road,Santacruz(W),Mumbai-400054
Email-ashok.lal@newindia.co.in
Phone No.-022-26633289

Secretary
Committee for Capacity Building of CA Firms and Small & Medium Practitioners
ICAI Bhawan, Indraprastha Marg
New Delhi-110002
E-mail: ccbcaf@icai.org
Phone: 011-30110430

Provision of 15-Minutes Reading and Planning Time Allowance to the Candidates of Chartered Accountants Examinations (Effective from May-2011 CA Examinations)

The Council of the Institute, based on the recommendation of the Examination Committee has decided to allow 15-minute reading and planning time allowance to the candidates in the Chartered Accountants Examinations before the scheduled commencement of the examinations i.e, if the examination commences from 2.00 PM, then the candidates will be given Question Papers at 1.45 PM. This reading time will not be available for CPT and all post qualification Courses Examinations.

The objective of providing question paper 15 minutes before the scheduled time is to:

(i) Enable the candidates to read the question paper thoroughly (without encroaching on the examination duration) and

(ii) Chalk out the strategy to answer the questions. Candidates are required to note the following in this regard:

(1) The candidates will not be allowed to leave the Examination Hall under any circumstances from 1.45 PM to 3.00 PM.

(2) The candidates shall be allowed to enter the hall from 1.30 PM upto 2.30 PM only.

Any breach of the above requirements would be treated as adopting Unfair Means by the students concerned and applicable disciplinary action would be taken on such erring students.

(G. Somasekhar)
Additional Secretary(Exams)

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Announcement Containing Certain Extracts Taken from a Communication Addressed by the Ministry of Corporate Affairs to the Three Professional Institutes Namely, ICAI, ICWAI and ICSI on the Steps to be Taken in Respect of "Information" Received against Members/Firms Registered with the Respective Institutes

(i) As soon as it comes to the notice of the Institute, either on the basis of press reports or otherwise, that a member of the Institute has been, or appears to have been, arrested by the police or any other law enforcement agency, it shall immediately take steps to obtain details in respect of the matter from the concerned agency and such other sources as may be appropriate. On receipt of details, if it is ascertained that the member was indeed arrested, the Institute shall treat this as "information" under Section 21(2) of the respective Acts, and shall initiate disciplinary action and take such further steps as may be necessary.

(ii) If details as per (i) above are not received within three weeks of the matter coming to the notice of the Institute, the Institute shall nevertheless initiate disciplinary action on the basis of available information treating it as "information" under Section 21(2) of the respective Acts and take such other steps as may be necessary to pursue the matter. If details are subsequently received from the law enforcement agency or other appropriate source, they shall be appropriately taken into account.

(iii) The Institute shall take steps to pursue such matters vigorously and bring them to a conclusion as early as possible, while following the procedures correctly.

(iv) The Institute shall continuously monitor press reports and take note of matters involving its members which fall within the scope of these directions or otherwise bring disrepute to the profession.

(v) The Institute shall put out the factual details of such cases on its website in all such cases in the following format:-

INFORMATION# REGARDING MEMBERS ARRESTED BY LAW ENFORCEMENT AGENCIES

Name of Member	Membership No.	Gist of information received by/available with Institute	Action initiated by the Institute

 # Certain issues in connection with the above, including timing and nature of disclosure, have been taken up with the Ministry for clarification

This information shall remain on the website till the disciplinary proceedings are concluded. The details in the above format shall also be published in the Institute's journal in the month following initiation of action.

For the Attention of Top Corporates — CMII Outreach Programme

The Outreach programme has been conceived with the idea of bringing the members in Industry closer to ICAI and the broad agenda for each outreach programme is as under:

1. Highlighting the activities of ICAI and the CMII.
2. To interact with ICAI representatives on matters of professional interest.
3. To encourage senior members to renew their membership of ICAI.
4. To encourage new members to apply for membership.
5. To solicit views from members in industry about what they expect from ICAI.
6. Participation of Members in Industry in research projects of ICAI.
7. To encourage formation of CMII Study Circles in different areas.

An Outreach programme kit designed by CMII would be given to all the participants in the programme.

Corporates having **more than 25 Chartered Accountants** and interested in conducting Outreach Programme are requested to contact the Secretary, Committee for Members in Industry, The Institute of Chartered Accountants of India, Indraprastha Marg, New Delhi - 110002, Tel. No. (011) 30110491, E-mail: cmii@icai.in, service_mii@icai.in

CPE 12 Hours

THREE DAYS RESIDENTIAL REFRESHER COURSE
At Vandanmedu, Kerala
(Land of Hills and Spices Plantations)

Organised by: Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI
Hosted Jointly by: SIRC of the ICAI & Alleppey Branch of SIRC of the ICAI

Date & Time	**Venue**
May 27th to 29th 2011 (Friday – Sunday)	'Carmelia Haven Resort' (A Plantation Theme Resort) Vandanmedu (Thekkady) (Thekkady - Munnar Route) Iduki Dt. , Kerala

Theme

With advent of globaliation and challenges posed by the liberaliation 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 populariing 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 RRC will highlight on emergent issues of profession.

27th May, 2011 12 P.M. to 2 P.M.	**Registration of Participants**
27th May, 2011 12 P.M. to 3 P.M.	**Inauguration and Special Address by** CA. G.Ramaswamy, President, ICAI CA. Jaydeep N. Shah, Vice-President, ICAI
Topics to be Discussed	**Speakers**
Emerging Opportunities for Practicing Chartered Accountant Professionals	CA. Atul C. Bheda, Central Council Member, ICAI & Vice-Chairman, CCBCAF & SMP, ICAI
Service tax – Recent Amendments with Emphasis on Certain Services	CA. Rajendra Kumar P. Central Council Member, ICAI
Provisions of Section 40a(ia) of the Income-tax Act, 1961.	CA. R. Krishnan
Charitable or Religious Trusts – Direct Taxes and FCRA	CA. M.C. Joseph
An Analysis of New Schedule VI Requirements and Impact of IFRS on Balance Sheet Format.	CA. Gopalakrishnan A.
Salient Features of Direct Tax Code	CA. R. Krishnan
29th May, 2011 1.15 P.M. to 1.30 P.M.	Valedictory Session

Delegate Fee:
Residential (Including accommodation, breakfast, lunch, dinner, all other entertainments, compliments and course material)
- **For Members:**
- Per Participant – (on twin sharing basis) ₹6000/-
- For Alleppey ARS Members (twin sharing basis) ₹5500/-
- Per Participant – (single occupancy) ₹10000/-
- Accompanying person:
- For Spouse (including child below age 5 years): ₹5500/-
- Per Child (with out extra bed) ₹1600/- (age up to 15)
- Per Child (with extra bed) ₹2600/-
- **For Non Members**
- ₹7500 (on twin sharing basis)

Non Residential
- Members ₹3500/-
- Members (ARS Alleppey) ₹3000/-
- Non Members ₹4500/-

Fees payable by DD/Cheque in favor of **'Alleppey Branch of SIRC of ICAI' payable at Alleppey. Send it to**: Alleppey Branch of SIRC of ICAI, "ICAI Bhavan", Behind District Co-operative Bank Building Lane, M.O. Ward, Opp. Town Hall, Alleppey, Kerala – 688001

Programme Chairman C.A. Vijay Kumar Garg Central Council Member, ICAI & Chairman, Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI ☎: 09414041872, ✉ : chairman.ccbcaf@icai.org	Programme Director CA. Shanmukha Sundaram K. Chairman, SIRC of ICAI ☎: 09443349727 ✉ : chairmansirc@gmail.com
For Registration and Further Details Chairman, Alleppey Branch of SIRC of ICAI, ☎: 09847057700, ✉: antonymalayil@gmail.com Secretary, Alleppey Branch of SIRC of ICAI, ☎: 09895214442, ✉: alleppey@icai.org	

CPE 12 Hours

National Conference for IT Industry at Bangalore

Organised by: Committee for Members in Industry
Hosted Jointly by: Bangalore Branch of SIRC of ICAI

Date & Time 24th and 25th June (Friday & Saturday), 2011	**Venue** Hotel Le-Meridian, Sankey Road, Bangalore
Inaugural Session – 9.00 am – 10.30 am	
CA G.Ramaswamy, President, ICAI	**CA. Jaydeep N Shah, Vice-President, ICAI**
Timings	**Topics to be discussed**
Day 1 **Technical Session 1 –** 10:45 a.m. – 01:00 p.m.	**Direct Tax Issues impacting the IT Industry** **Taxation of Employees** Expatriates & On-Site Employees, Residential Status, Allowances, Foreign Tax Credit , With holding Tax , ESOP's etc.
Technical Session -2 01:45 p.m –03:45 p.m.	**Indirect Tax issues impacting the IT Industry** Classification and Valuation of Services, Exemptions, Abatements & Special Rates, CENVAT Credits
Technical Session- 3 04:00 p.m. – 05:30 p.m.	**VAT – Issues currently affecting the IT industry** Customisation of Software, Manpower Deployment, Maintenance Contracts, Double Taxation (VAT & Service Tax), Upgrade of Software & Hardware, Sale in the course of Import, Recent Judgements
Day 2 **Technical Session- 1** 10:00 a.m. – 11:00 a.m.	**Service Tax - Issues specific to the IT/ITES Industry** Export and Import of Services, Expediting Refunds, Goods v/s Services
Technical Session 2 11:15 a.m. – 12:15 p.m	**Accounting Standards for the IT Industry - Issues**
Technical Session 3 02:00 p.m. – 03:15 p.m.	**International Taxation – Framework for the IT Industry** Royalties and Technical Fees – Judicial Trends, Withholding Tax - Issues
Technical Session 4 03:30 p.m. –05:00 p.m.	**International Taxation– Other issues** Transfer Pricing – Recent trends, Transfer Pricing – Issues arising during Assessments

Fees Members- ₹3000/- ; Non- Member – ₹4000 /- Payment should be made by Cheque / DD in favour of **"Bangalore Branch of SIRC of ICAI""** payable at Bangalore and should be sent to - **Bangalore Branch of ICAI,** The Institute of Chartered Accountants of India, ICAI Bhawan, 16/O, Millers Tank Bed Area, Vasant Nagar, Bangalore - 560 052	
Programme Chairman CA K.Raghu Chairman – Committee for Members in Industry	**Programme Coordinator** CA Venkatesh Babu Chairman, Bangalore Branch of SIRC of ICAI
For Registration and Further Details please contact Bangalore branch of the ICAI at **✉:dcobangalore@icai.org or ☎:080- 30563541**	

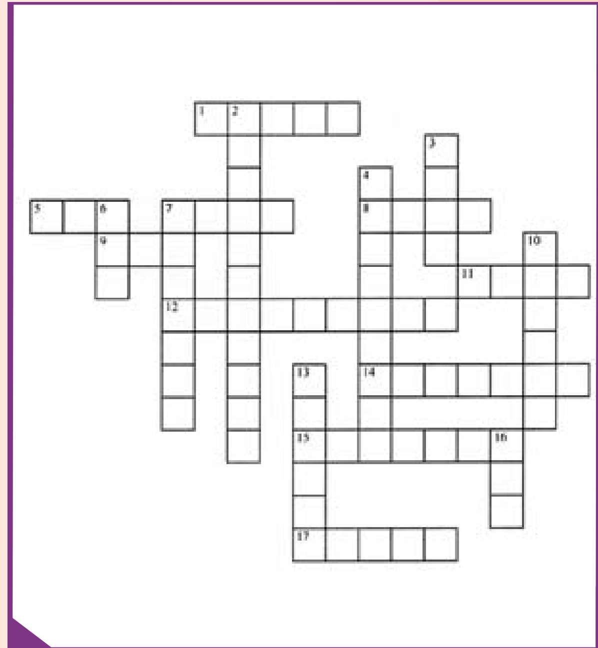
CPE 6 Hours

National Seminar on XBRL – Extensible Business Reporting Language

Organised by: XBRL India
Jointly with: Continuing Professional Education Committee (CPE) and Committee for Members in Industry (CMII) of the ICAI
Hosted by: Bangalore Branch of SIRC of ICAI

Date & Time 27th May, Friday,2011 9.00 am – 5.00 pm	**Venue** Hotel Lalit Ashok, Bangalore
Topics to be discussed	
Date & Time 24th and 25th June (Friday and Saturday), 2011 9.00 am – 5.30 pm	**Venue** Hotel Le-Meridian, Sankey Road, Bangalore
Technical Session – 1 - An Introduction to XBRL • What is XBRL, • XML/XBRL Basic Concepts , • Advantages of XBRL, • Global XBRL Initiatives	
Technical Session – 2 - XBRL Taxonomies • Key concepts of taxonomies, • Indian GAAP Taxonomy, • Mapping, Tagging and assigning context, • Creating Instance docments	
Technical Session – 3 - Financial reporting and XBRL • XBRL based Financial Reporting- Case Studies, • XBRL based Regulatory Reporting - Case Studies	
Technical Session – 4 - XBRL Implementation Tool • Implementing XBRL solutions, • Overview of XBRL Generation Process, • XBRL Tools and Solutions – Case studies, • Taxonomy Editing and Extensions	
Technical Session- 5 • Opportunities for Chartered Accountants in XBRL, • XBRL India- Roadmap	
Fees Member – 1750/-; Non Member- 2000/- Payment should be made by Cheque / DD in favour of **"Bangalore Branch of SIRC of ICAI""** payable at Bangalore and should be sent to - **Bangalore Branch of ICAI,** The Institute of Chartered Accountants of India, ICAI Bhawan, 16/O, Millers Tank Bed Area, Vasant Nagar **Bangalore - 560 052**	
CA K.Raghu **Programme Chairman and Director, XBRL India**	**CA. Atul Bheda** **Programme Coordinator and Director, XBRL India**
For Registration and Further Details please contact Bangalore branch of the ICAI at **✉:dcobangalore@icai.org or ☎:080- 30563541**	

CROSS WORD 059



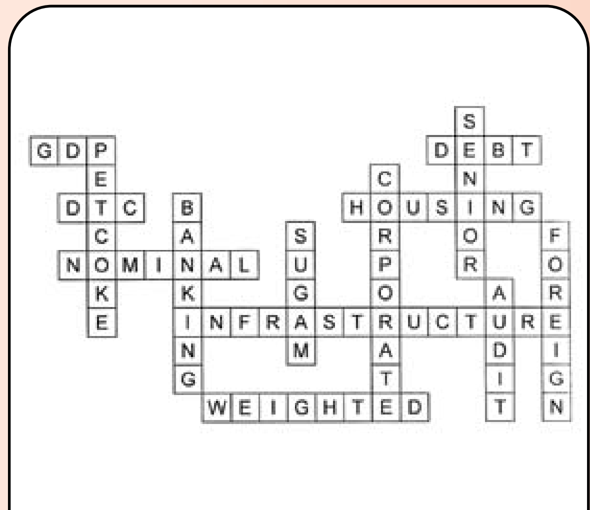
ACROSS

1. A new web based service named _______ has been launched by the ICAI for the benefit of the members.
5. 'Partnership' in the Chartered Accountants Act, 1949 has been clarified to include _______ also.
7. MoU renewed with this organisation for the registration of CFCs.
8. Recently, the RBI has recognised this qualification for the purpose of System Audit of banks.
9. The Council has approved the MRA with this organisation.
11. Filing of financial statements in the ________ format has been made compulsory for the certain class of companies.
12. Highest CAs were recruited by this bank during the recently concluded Campus Placement Programme of the ICAI.
14. CENVAT credit on input services can be availed on receipt of ________. (7)
15. _________ and financial services provided to a Scheduled Bank, by any other Scheduled bank, in relation to inter-bank transactions are exempted from Service Tax.
17. New return forms issued by the CBDT are ________ and 'SUGAM'. (5)

DOWN

2. A new Directorate in the CBDT will be established relating to _________ Budget. (11)
3. Service Tax in respect of services provided by the Chartered Accountants shall be on _______ basis. (4)
4. CBEC has clarified that where 'whole of service tax' is exempted by virtue of a notification then ________ cess would also be Nil. (9)
6. Submission of ______ has been made mandatory for the allotment of the Director Identification Number (DIN).
7. Every deposit taking NBFCs shall maintain a minimum _________ ratio of atleast 15 per cent. (7)
10. A person resident outside India desiring to establish a ________ in India shall apply to RBI through an Authorised Dealer. (6)
13. For Excise purposes it has been clarified through recent notification that "packing material" also includes ______. (6)
16. First outreach programme of the ICAI was held at this company.

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 058

1 Venkatesan: I am going to get married and I will be soon visiting a girl's family for that purpose. Give me some advice.
CA. Thyagarajan: Well! I do have one suggestion for you—Look for a girl who appeals to you as strongly as IT Refund.

2 Examinations are funny too:
- 80% of the final exam will be based on the one lecture you missed and the one book you didn't read.
- If you are given an open-book exam, you will forget your book.
- If you are given a take-home exam, you will forget where you live.