Income Tax and Corporate Law News

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Prior period expenses

The Delhi court held that the question as to the year in which a deduction is allowable may be material when the rate of tax chargeable is different in different years. The court opined that where tax is levied at a uniform rate, it is immaterial whether the deduction is allowed in one assessment year or another. The tax department is not at loss in any event. The high court also observed that the tax department should restrain itself from raising points which do not affect the taxability of the assessee or the tax that the Department is likely to collect from the assessee in one year or other.

Suspense account

The discovery that many large companies are using a contradiction between two sets of rules (one on accounting standards, and another provided under company law) to improve the profits that they report, should come as a wake-up call to all those who believe that India now has good governance standards in companies. The clear intention of the companies which have parked foreign exchange losses on capital assets in the balance sheet, without booking them in the profit and loss account, is to boost the bottom line — in some cases, by substantial margins (as reported in this newspaper yesterday). All the companies involved have quoted legal opinion in their favour, and therefore have provided themselves with some cover for their actions. The question, though, is what is the correct thing to do, not what might pass muster in a legal dispute. And it seems clear enough that these losses should be booked in the profit and loss account. That is what India's accounting standards ask you to do. That is what the US accounting standards ask you to do. And that is what the international accounting standards ask you to do.

The fact that there is a loophole provided in company law is not a good explanation for ignoring the relevant accounting norm. Indeed, the accounting standard in question was issued by the same department of corporate affairs that is responsible for giving effect to company law, and it issued these standards as recently as in late 2006. Indeed, the department specifically said when notifying the accounting standard, in a footnote: "It may be noted that the accounting treatment of exchange differences contained in this Standard is required to be followed irrespective of the relevant provisions of Schedule VI to the Companies Act, 1956." When the authority that oversees company law is itself saying that the accounting standard over-rides the relevant provision in company law, there should be no ambiguity on what is the right thing to do.

IFRS coming . . . . .

In less than three years from now, in April 2011, India will have to comply with the International Financial Reporting Standards (IFRS), which have been issued by the International Accounting Standards Board (IASB); no fewer than 125 countries have already agreed to adopt these standards. There are 41 IFR standards so far, only two of which are the same as those followed in India. Adopting another 10 will need changes in company law, among other laws, and 29 will need changes in the standards currently prescribed by the Institute of Chartered Accountants of India. For instance, the Companies Act prescribes a fixed rate of depreciation for different categories of machinery and equipment — IFRS, however, says that depreciation should be based on an evaluation of the useful life of the machinery. The Companies Act, similarly, lists preference capital as equity while the IFRS says it is debt. Since this will affect the debt-equity and other financial ratios, it is clear that banking sector norms will also undergo a change. Similarly, the rules for how future liabilities are to be treated are different. The list goes on — a company needs to have five years of financial data for an IPO, but if all data are to be prepared under different rules, how will the stock market regulator deal with applications for public share issues? On the face of it, changing the Companies Act or other legislation that runs counter to IFRS is easy, but in practice, such legislative activity could take years. Given how companies are using the different provisions in existence today, all the relevant provisions of law and rules need to be aligned without delay.

I-T not likely to be made mandatory for remittances

Companies and individuals who wish to send funds overseas may now have to get the income tax department's green signal. If the thinking in the finance ministry is anything to go by, then those sending funds abroad will now require a certificate from the department.

Sources said a certificate from assessing officer (AO) prescribing the rate at which withholding tax is to deduct would be required. This regulation existed some years ago but was done away with to make the process less cumbersome. However, with increase in remittances, both corporate and individual, there is a growing feeling in the department that tax could be escaping the department's eye.

Sources feel the requirement of approval ahead of transfer of funds would ensure that the department gets taxes in time. They said the issue was discussed at I-T department's conferences in Bangalore and Mumbai in July.

The certificate issued by AO is to make the applicant's tax liability clear. If there is no tax liability, then the AO issues a certificate prescribing a nil rate of withholding tax. In case the assessee has a tax liability, the AO will prescribe the rate at which tax is to be deducted.

At present, funds can be remitted after furnishing a certificate from a chartered accountant that clarifies that appropriate tax has been deducted. These certificates have to be filed with the RBI, which then forwards them to the department post facto. The government had, in the Finance Act 2008, introduced sub-section 6 in section 195 of the Income-Tax Act, which had made it mandatory for companies to file a declaration as to how much money had been remitted out of the country. However, this declaration is also post facto, to be filed after the transfer of funds has taken place.

Tax experts feel this condition would create an unnecessary roadblock. They feel the department should specify a threshold or exempt requirement of NOC in cases where no tax is payable.

"This can create administrative bottlenecks considering that the department may not have adequate resources to handle all applications on a timely basis. A better option would be to provide a threshold below which CA certificates may still be allowed,” Ernst & Young partner Amitabh Singh said.

CORPORATE LAW CASE LAWS

FORTUNES STONES LTD VS REGISTRAR OF COMPANIES

Companies Act, 1956 – Section 224 (7) – Removal of statutory auditor – Failure to obtain prior permission of the Central Government – whether a continuing offence – Held, No

Brief Facts: The petitioner-company had appointed 'T' as its first statutory auditor. Subsequently, 'T' expressed its inability to audit the accounts and, therefore, the petitioner appointed a new auditor in the EGM held on 3-7-2000. On 15-06-2002, 'T' filed a complaint before the Regional Director, Department of Company Affairs against the petitioner as well as the new auditor alleging violation of section 224(7). The Regional Director conveyed his sanction on 9-9-2003 for launching prosecution against the petitioner. Thereafter, a show-cause notice was issued on 3-10-2003 followed by the complaint filed on 22-12-2004 and Trial Court took cognizance of offence by an order dated 6-1-2005. The petitioner filed the instant petition seeking quashing of the complaint and the proceedings before the trial court.

Decision: Petition allowed.

Reasons: A perusal of the complaint would show that the offence was for the contravention of section 224(7) which required a company to obtain the previous approval of the Central Government for removal of the auditor at a general meeting. Admittedly, the prior approval of the Central Government was not obtained when 'T' was removed as a auditor at the EGM held on 3-7-2000. The subsequent obtaining of the permission of the Central Government cannot rectify the contravention of section 224(7) which mandates a prior approval. By the very nature of the statutory requirement, the contravention can constitute only a one time offence and not a continuing one. The contention that the contravention in the instant case was a continuing one was to, accordingly, rejected.

The punishment for contravention of section 224(7) is only a fine as is evident from a reading of section 629A. In terms of section 468(2) (a) of the Code of Criminal Procedure the Trial Court was required to take cognizance within a period of six months. Not only was the complaint filed more than four years after the commission of the offence but the cognizance was also taken on 6-1-2005.

For the aforesaid reasons, the Trial court ought not to have taken cognizance of the offence under section 224(7) as it was beyond the period of limitation stipulated under section 468(2)(a) of the Code of Criminal filed in the Court of the Chief Metropolitan Magistrate and all proceedings consequent thereto are quashed.

RASBIHARI BANSAL VS COMMISSIONER OF INCOME TAX

Income Tax Act, 1961 – Section 254 (2) – Rectification of mistake apparent on record – Tribunal did not allow certain deduction – Assessee moved rectification application which was dismissed by the Tribunal – Whether Tribunal was right in rejecting the rectification application – Held, Yes.

Brief Facts: The Commissioner (Appeals) partly allowed the appeal of the assessee. Against this order, the revenue filed an appeal before the Tribunal where the assessee filed cross-objection. The Tribunal dismissed the appeal filed by the revenue and partly allowed the cross-objection filed by the assessee. Therefore, an application under section 254(2) was filed by the assessee on ground that an error had crept in the order of the tribunal where by his cross-objection relating to addition made on account of gross profit ratio had been disposed of and the Tribunal had not given attention to the evidence submitted by him. The tribunal dismissed that application holding that the application ws misconceived inasmuch as it sought the Tribunal to re-appreciate the material and evidence already on record, which was clearly contrary to section 254(2). The assessee appealed to the High Court.

Decision: Appeal dismissed.

Reasons: Section 254(2) enables the concerned authorities rectify any ‘mistake apparent from the record’. It is well-settled that an oversight of a fact cannot constitute an apparent mistake rectifiable under this section. Similarly, failure of the Tribunal to consider an argument advanced by either party for arriving at a conclusion is not an error apparent from the record, although it may be an error of judgment. The mere fact that the Tribunal had not allowed a deduction, even if the conclusion was wrong, it would be no ground fro moving application under section 254(2). Further, in the garb of application for rectification, the assessee cannot be permitted to reopen and to re-argue the whole matter, which is beyond the scope of section 254(2).

In the instant case, the assessee, in the garb of application for rectification, had sought to reopen and re-argue the whole matter, which is beyond the scope of section 254(2) and this was also the finding of the Tribunal. There is no reason to disagree with the findings given by the Tribunal of that aspect. The instant appeal being wholly misconceived and without any basis in dismissed.

Source: Net and Professional Books