



THE CHARTERED ACCOUNTANT JOURNAL

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
SET UP BY AN ACT OF PARLIAMENT



“Freedom is like birth. Till we are fully free, we are slaves....No charter of freedom will be worth looking at which does not ensure the same measure of freedom for the minorities as for the majority....True non-violence should mean a complete freedom from ill-will and anger and hate and an overflowing love for all....Complete independence does not mean arrogant isolation or a superior disdain for all help....If it is man's (sic) privilege to be independent, it is equally his duty to be inter-dependent... Freedom of the individual is at the root of all progress.”

Mahatma Gandhi

Advertisement

Corporate Social Responsibility and Chartered Accountants

The gigantic corporate growth has done India good. But there is even better side of this development. In the backdrop of tough competition and 'Liberalisation – Privatisation – Globalisation' (LPG) wave sweeping through countries and continents, more and more corporations are realising that a growth without a social face cannot be sustained for long. They are gradually heeding the concepts like 'inclusive growth', 'responsible business enterprise', 'convergence of accounting standards' and to cap it all — good corporate governance practices. They are successfully intertwining their corporate social responsibility (CSR) with their business strategies to the benefit of all.

The CSR is no longer a cliché but a popular benevolent thinking in action. As such, corporate activities today extend to almost every sphere of life, from manufacturing to service, education, hospitality, environment and even spirituality. But much more is still required to be done to make a real difference at the ground level at large, particularly in rural India. There is growing perception that the concept of voluntary CSR has not picked up in India as it should have. As such, the Government is somewhat rightly actively considering to make it mandatory for corporate to earmark part of their profit for CSR initiatives in the new Companies Bill. The new Corporate Affairs Minister Mr. Veerappa Moily has rightly said that Indian corporate *need to develop a culture of voluntary CSR...CSR cannot be considered only as a charity it is more of a social business*. The two per cent mandatory provision for CSR spend in the Companies Bill 2009 should indeed stay. According to a recent study, the mandatory spend on CSR may lead to Indian companies collectively Spending close to \$2 billion (about ₹8,700 crore) a year on CSR programmes. But if we go by the sense of good economics, this spending on CSR will ultimately benefit the corporate in the long run, facilitating their sustainable growth besides benefiting the society in general.

As rightly observed by former Corporate Affairs Minister Mr. Salman Khurshid: *there is a strong need for establishing socially responsible business models as Corporate Social Responsibility (CSR) is not merely a question of morality but an example of good economics*. There is a need for an effective Government-NGO-Corporate partnership to do away the scepticism about CSR as just another tool of the

ultimate business objective of maximising profits. It is time that Governments encourage corporations in their civic activities through supportive legislations. It is time that there is greater corporate accountability, and convergence of accounting standards to ensure transparency, efficacy and user-friendliness of corporate financial statements. SEBI has done its bit so far as statutory aspect of Corporate Governance and CSR is concerned. Revised Clause 49, Independent Directors, Whistle Blower Policy, etc. have all been steps in the right direction.

The need of the hour is the business models where making profits and doing social environmental good go hand in hand. This background not only offers a plethora of professional opportunities for the chartered accountants but also puts important social responsibility on them. They can play a crucial role with respect to both statutory and voluntary aspects of CSR. They are already proving to be an effective facilitator and implementer of the modern approaches like transparency in corporate financial disclosure, restructuring and tax compliance. Further, they can help corporations devise such strategies, policies and projects that serve both their business as well as social goals. They can ensure that the corporate values and social values never come in conflict.

When associated with the corporate-aided community projects, the CAs can ensure that the projects benefit the intended lot and their social objective is not lost in corporate exercise of profit maximisation or building brand equity. CAs have the potential to be the most effective tool of good corporate governance involving CSR. It is high time that professionals help create responsible enterprises.

With more and more companies embracing entire world as their workplace and market place, corporate governance backed by the concept of corporate social responsibility has become the key to business success. CSR-based policies are fast emerging as the corner stone of corporate governance. This presents a great challenge and opportunity for the professionals who can be of great help in creating an enabling environment for better CSR and corporate governance.

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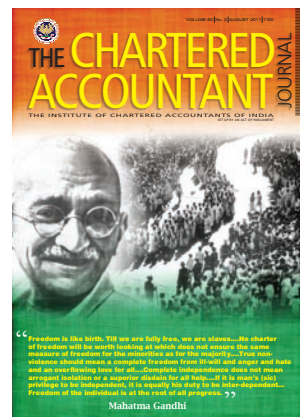
Read on a brief report of the function organised at Vigyan Bhawan, New Delhi on 1st July, 2011 to mark the 'CA Day' i.e. Foundation Day of the Institute. Governor of Madhya Pradesh and Past President of the ICAI CA. Rameshwar Thakur was the Chief Guest of the very well attended function. Deputy Chairman of Rajya Sabha CA. K. Rahman Khan and Minister of State, Ministry of Corporate Affairs, Shri R. P. N. Singh were the Guests of Honour. Secretary, Ministry of Corporate Affairs, Shri D. K. Mittal delivered a special address.

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Smile Please





CA. G Ramaswamy, President, ICAI

Dear Friends,

Father of our nation, Mahatma Gandhi has said: *The spirit of political and international liberty is universal and, it may even be said, instinctive...I want freedom for the full expression of my personality. I must be free to build a staircase to Sirius if I want to...* He wanted independence for the country in its real and fullest

sense. India has built itself over the years and, today, we are very proud to admit before the world that we are one of the most politically-vocal nations of our world. We believe in what Mahatma Gandhi had observed once: *The condition of India is unique. Its strength is immeasurable. We need not, therefore, refer to the history of other countries. I have drawn attention to the fact, that when other civilisations have succumbed, the Indian has survived many a shock.* Our Independence Day, 15th August, is not more than a couple of weeks ahead of us and all we need to do at present is to simply extend our enthusiasm and spirit of the 63rd CA Day celebrations, which we celebrated quite whole-heartedly in the Institute and in its Regional Councils and their Branches with the help, cooperation and support of all our stakeholders. I would like to extend my heartfelt gratitude to them in retrospect.

The 63rd CA Day was celebrated by many corporate and forums across the nation. Various programmes and cultural activities were organised that witnessed both formal and informal gatherings along with the active participation of the chartered accountants, i.e. members of the Institute. The main function was organised on 1st July at Vigyan Bhawan in New Delhi. ICAI Web TV was made functional by the Hon'ble CA. Rameshwar Thakur, H. E. Governor of Madhya Pradesh. ICAI Connect was formally launched by Shri D. K. Mittal, Secretary, Ministry of Corporate Affairs. Exclusive website for Practitioners and CA Firms was launched by the Hon'ble Shri R. P. N. Singh, Minister of State, Ministry of Corporate Affairs, and ICAI-ROC software was launched by the Hon'ble CA. K. Rahman Khan, Deputy Chairman, Rajya Sabha, Parliament of India. The Day was also celebrated by all the CPE Study Circles for members-in-industry across the nation. Every year on this day, we are reminded of our glorious tradition and the hard and arduous efforts of our forefathers because of which the profession enjoys a standing today. This day is also about our reconciliation with our past and with our understanding that we acknowledge the heritage and greatness of our profession and its role in the intellectual development of our society and state. It is time for all of us to express our love to the grandeur of our profession.

At this point of time, I would like to convey my good wishes from the core of my heart: *May all stakeholders*

grow bigger and taller along with our Institution and the profession!

Now, let us have a look at some of the significant developments in the accountancy profession in the past one month:

ICAI Welcomes Dr. M. Veerappa Moily, New Corporate Affairs Minister

I am happy to acknowledge that Dr.(Shri) M. Veerappa Moily has taken charge of the Ministry of Corporate Affairs (MCA) as the new Corporate Affairs Minister. I am sure that under this new dynamic leadership, the Ministry will bring in new dimensions in the development and growth of our corporate world. Here I also wish to record my gratitude and appreciations to the former Corporate Affairs Minister Shri Murli Deora for his support and encouragement in our initiatives for the profession. I am sure that Dr. Moily would play a very positive and proactive role in the Ministry and, consequently, this will give a positive boost to the ongoing uplift of our profession too, as he himself says: *I am a reformist and wherever I go, I have the reform agenda.* We wish him our best wishes for a successful tenure in the Ministry.

Initiatives with Government Offices/Officials: Partner in Nation-Building

ICAI on MCA Working Group under Agreement with Netherlands Ministry: The MCA has inked an agreement with the Ministry of Economic Affairs, Agriculture and Innovation of Netherlands on corporate governance and corporate social responsibility (CSR). The letter of intent to this effect was signed recently in New Delhi by the MCA Secretary Shri D.K.Mittal and H.E. Netherlands Ambassador to India Mr. Bob Hiensch, on behalf of the Government of Netherlands. As per the *Letter*, working groups in the areas of corporate governance, CSR and other aspects of corporate affairs are to be established by both the sides. Accordingly, the MCA has decided to constitute a working group with the MCA Additional Secretary Shri Sudhir Mittal as the Chairman and representatives of Tata Services Ltd., NTPC Ltd. and other Institutes as members. I have been nominated from the ICAI by the MCA.

HRD Working Group to Implement ASs in Educational Institutions: A group has been constituted by the Ministry of HRD for the implementation of accounting standards in all educational institutions of Department of Higher

Education of the Ministry. The Group comprises, apart from me, the ICAI Vice-President CA. Jaydeep N. Shah, the ICAI immediate past-President CA. Amarjit Chopra, and my Central Council colleague CA. Manoj Fadnis from ICAI, and Mrs. Neelam Sudhir Kumar, Controller of Accounts, Ministry of HRD, Shri Siddique, Former Finance Officer, Jamia Millia University, Shri A. K. Dogra, JS (FA), UGC, and Shri M. Arumugan, Dy. Commissioner (Finance), Kendriya Vidyalaya Sangathan, New Delhi, who have been nominated by Ministry of HRD. First meeting of this group was held recently.

Very recently, I along with my Central Council colleague CA. M. Devaraja Reddy had the opportunity to meet the Union HRD Minister Shri Kapil Sibal. During the meeting we have again discussed the issues involved in implementation of accounting standards in the educational institutes. We also invited him to the Global Educational Summit to be organised by the Institute soon.

National Voluntary Guidelines on Social, Environmental & Economic Responsibilities of Business: Recently the Ministry of Corporate Affairs has brought out the National Voluntary Guidelines on Social, Environmental & Economic Responsibilities of Business for the Corporate Sector. I along with the ICAI Vice-President was present on this occasion. The Guidelines emphasised the importance of responsible business towards inclusive and sustainable development, and it is designed to be used by all businesses in the country including the MSMEs. They encourage adopting the 'triple bottom line' approach wherein the financial performance is achieved by also being socially and environmentally responsible. They outline the nine principles and the core elements for each of the principles which are integral to business strategy and operations. Also, they provide a framework for implementation, monitoring and reporting.

ICAI to Partner in RBI's Financial Literacy Project: I am happy to inform all stakeholders of the profession as well as the well-wishers of the Institute that the Reserve Bank of India (RBI) has shortlisted the ICAI to be a part of its project relating to financial literacy. As you all know that the RBI had launched its Project on Financial Literacy way back in 2007 to create awareness, especially among the masses, on matters

relating to banking and finance. It has asked us to submit a detailed proposal on the activities to be undertaken by the ICAI during this association, which we would submit to the RBI shortly.

ICAI Attends MCA Meeting on Independent Directors: A Core Group had been constituted sometime back by the Ministry of Corporate Affairs to make recommendations on issues pertaining to Independent Directors. The first meeting of the Group was held recently under the Chairmanship of the Additional Secretary of MCA, which was also attended by the ICAI Secretary Shri T. Karthikeyan. It was decided to prepare a draft code of conduct for Independent Directors and circulate it among all members of the Group for consideration.

Quality Review of Audit Services: Quality Review Board established by the Government of India under the CA Act, 1949, at a meeting held recently has decided to initiate the process of quality review/inspection of audit services of the audit firms.

International Initiatives: Building and Strengthening Ties Conclave for Trade Officials of Missions in India: I am happy to inform you that we have recently successfully organised a conclave of trade officials of Missions in India, where there were participants from about 37 countries apart from the officials of the Ministry of External Affairs of India. Our External Affairs Minister, Shri S. M. Krishna, gave the keynote address in the forum, where deliberations were held by representatives of embassies focusing on taxation, transfer pricing, doing business in India and our role and support in institutionalisation of accountancy profession. African countries like Uganda and Gambia expressed their interest in seeking our support in developing the accountancy profession and establishing institution in their countries.

IFAC Leadership to Visit India: I am also happy to inform that a delegation comprising IFAC President Mr. Goran Tidstorm, and the IFAC Chief Executive Mr. Ian Ball are visiting India in the last week of July 2011 to discuss the thrust areas of IFAC including high-quality technical standards in IFRS while promoting the value of professional accountants, the development of

the accounting profession in developing nations, etc. During their visit, they will also have meetings with the Ministry of Corporate Affairs, the Ministry of Commerce and Industry, the Controller General of Accounts and Comptroller and Auditor General of India. Another important agenda to be discussed during their visit will be an increase in fees structure of IFAC for ICAI.

Global Reporting Initiatives: The Global Reporting Initiative (GRI) is a network-based organisation that pioneered the world's most widely used sustainability reporting framework. GRI's reporting framework is developed through a consensus-seeking, multi-stakeholder process. Recently, their representatives Dr. Aditi Halder, Director, GRI Focal Point India, and Ms. Marjolien Baghuis, Director, Communications and Network Relations, had a meeting with the undersigned to discuss the ways to promote sustainability reporting in India. To begin with, it has been decided to hold joint workshops in India to create awareness about the sustainability reporting and its benefits to the stakeholders.

ICAP Golden Jubilee Celebrations: I would also like to extend my good wishes to the people of Pakistan, especially the accountancy professionals, as the Institute of Chartered Accountants of Pakistan (ICAP) will also be celebrating the Golden Jubilee soon. I would be visiting the ICAP to be part of the celebrations of the profession and will participate in the two-day ICAP Golden Jubilee Conference to be held shortly this month with the theme *Accountants and Social Responsibility*.

India-Japan IFRS Dialogue in India: A delegation from Japan is visiting Bangalore and Delhi in early August 2011 for the second *India-Japan IFRS Dialogue*. Key stakeholders from SEBI, RBI, MCA, Ministry of Finance, NSE and CAG have been invited to participate in the IFRS Dialogue to be held in Bangalore.

International Arbitration Conference in Malaysia: My Central Council colleague CA. Sanjeev Maheshwari attended the Asia Pacific Regional Arbitration Group Conference 2011 in Malaysia along with the ICAI Addl. Secretary Shri Rakesh Sehgal, which while focusing on international arbitration in challenging times, enabled the delegates to interact with the Chambers of

Commerce and also other key functionaries. My Central Council colleagues CA. Rajkumar S. Adukia and CA. P. Rajendra Kumar also attended an international conference organised recently by the Institute of Internal Auditors in Malaysia.

Initiatives for Stakeholders

Training Programme on Concepts Applicable to Autonomous Bodies: Recently, the Institute organised a training programme, *An Insight on the Concepts Applicable to Autonomous Bodies*, for accounting personnels of autonomous bodies of Maharashtra, Madhya Pradesh, Goa and Chattisgarh, and for members of the profession in Mumbai. I, along with Shri K. P. Sasidharan, Director-General (Autonomous Bodies) of the C&AG of India, my Central Council colleagues CA. Anuj Goyal and CA. Sanjeev Maheshwari, and the WIRC Chairman CA. Shriniwas Y. Joshi inaugurated the programme, which was participated by more than 150 officials of autonomous bodies of the state and members of the profession.

FEE's Conference on Audit Policy: To help bring clarity in the issues of audit quality, sustainable growth of the profession and bridging the expectation gap, the Federation of European Accountants (FEE) recently organised a high-level conference on Audit Policy. The objective was to bring together all stakeholders and to discuss the role and value of audit and the building of a European market, providing a platform to the leaders of the accountancy profession from various countries comprising the European Union. My Central Council colleagues CA. Abhijit Bandyopadhyay and CA. Rajkumar S. Adukia attended the Conference along with the Secretary of the AASB of the Institute, where eminent personalities including the European Commission's Commissioner for Internal Market & Services; Chairman, PCAOB, USA, and Chairman, Financial Reporting Council, UK, addressed the audience.

Significant Decisions: Some significant decisions have been taken in the Institute in the interest of the profession on agenda relating to the conduct of the profession:

- Broad principle as proposed by the Accounting Standards Board on which the *Concept Paper* would be developed for the revision of the existing notified accounting standards has been approved.
- *Draft Statement/Guidance Note to the Revised Schedule VI* to the Companies Act, 1956, as prepared by the Accounting Standards Board of the Institute, has been approved.
- As you are aware, a special group was constituted by us of study the Guidelines of MPLAD scheme with an objective to recommend areas for improvement with reference to the accounts and audit part of the Scheme. The Group had finalised its draft report on the basis of views expressed at a meeting of Rajya Sabha Standing Committee in April 2011. I would also like to recall that in terms of the discussion held in the Committee, the views of the Office of C&AG were also sought on the draft report. Recommendations of this special group on accounting and auditing aspects of the *Members of Parliament and Local Area Development* (MPLAD) Scheme have been approved.
- Recommendations on the Study Group on formulation of *Policy and Procedure for Conversion of Existing CA Firms into LLP* have also been approved. I wish to recall here that the MCA had issued a general circular in 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. We had decided to allow all existing CA firms to convert themselves into LLPs, and bring out a format for making an application for conversion to an LLP.
- Guidelines for professional accountants on *Know Your Client* (KYC), as finalised by the study group under the convenorship of my Central Council colleague CA. Charanjot S. Nanda as constituted by the Ethical Standards Board of the Institute, under

which the practicing members are required to gather information about their clients for whom they are doing attest function have been approved. These guidelines will be recommendatory in nature.

Lane Adjacent to ICAI Headquarters Named after Prof. T. S. Grewal: As a tribute to Prof. T. S. Grewal's immense contribution to the commerce education in India, the lane adjacent to the ICAI Headquarters building has been named as Prof. T. S. Grewal Lane. A ceremony was held recently under the chairpersonship of the Mayor of Delhi, Prof. Rajni Abbi, which was attended by a large number of members from Delhi, several Council members, officers and staff of the Institute. Family members of late Prof. Grewal were also present.

Fast/Firm Action in Disciplinary Cases: Upholding the *Code of Ethics* and the law of the profession, two meetings of the Board of Discipline (u/s 21) and seven meetings of the Disciplinary Committee (u/s 21B) of the Institute have been held whereat hearing in 3 and 35 cases were concluded respectively and were finalised but for the last meeting held recently in Hyderabad. Besides, 46 cases were disposed off by the Board of Discipline/Disciplinary Committee till *prima facie* stage. In the forthcoming meeting(s) of the Board of Discipline/Disciplinary Committee, the *prima facie* opinion of the Director (Disciplinary) of the Institute in 60 cases would be placed.

Convocations for Newly-Enrolled Members: I am happy to inform that Convocation for newly-enrolled members that were admitted during the September 2010 to March 2011 was held successfully in Delhi recently with a total attendance of 820 enthusiastic members, many of whom came with their family. The programme started with the Institute's Motto song followed by addresses by the dignitaries on the dias including myself, the ICAI Vice President CA. Jaydeep N. Shah, my Central Council colleagues CA. V. Murali and CA. Naveen N.D. Gupta, and the NIRC Chairman CA. Rajesh Sharma. A special address as part of our newly incorporated Mentor Programme was also delivered. The programme was well attended by Central and Regional Council Members from the Northern Region. Convocations will also be held in Mumbai and Chennai very soon and then a

little later in Kolkata, Chandigarh, Kanpur and Jaipur as well.

Convocation for Successful Candidates of Master in Business Finance Certificate Course:

Convocation for the 47 successful candidates of the first batch of the Certificate Course on Master in Business Finance, who qualified for the *Certificate Course*, was organised successfully in Delhi recently.

CA Final and CPT Results Declared: A Female-Power Show
May 2011 CA Final Examination:

The results of the CA Final Examination have been declared recently. Pass percentage of male and female candidates for both Group I and II are 19.81 and 21.91 per cent, respectively. Pass percentage of male and female candidates for Group I and Group II are 35.97 and 37.09, and 25.51 and 29.22 per cent, respectively. Female candidates have done better than their male counterparts in all the Groups individually too. EIRC (eastern region) has given most pass percentage for both Group I and II this year, i.e. 26.78, whereas NIRC and CIRC stand close second and third with 21.76 and 20.56 per cent, respectively, as pass percentage for both Group I and II. Individually too, EIRC has the best pass percentage for Group I, i.e. 41.64 per cent, as well as for Group II, i.e. 31.66 per cent. It is noteworthy that the top three all-India rank holders for the CA Final Examination are all female candidates: Maitreyee N. Rajaput, Arti Jain and Charmy S. Seth. I congratulate all of them and would like to make an appeal to all other female student candidates: *Hard work pays. Always keep your spirits high.*

June 2011 CPT (Paper-Pencil mode) Examination:

The results of the Common Proficiency Test (Paper-Pencil Mode) held recently were also declared. This time, 33.31 per cent candidates have been declared pass. Here too female candidates have taken a lead with a 36.26 pass per cent against male candidates with 31.67 pass per cent. Region-wise, overseas candidates have fared better than those from other regions in India with 57.24 pass per cent, whereas NIRC and EIRC were distant second and third with 38.44 and 36.73 pass per cents respectively. Region-wise too, female candidates have done better than their male counterparts.

June 2011 ISA Assessment Test: Results of the Information Systems Audit (ISA) Assessment Test held on 18th June, 2011, have been declared. Pinal Bhupendrabhai Jariwala and Puneet Gupta have achieved top ranks in old pattern and new pattern respectively.

We are all set to celebrate the true spirit of independence with all our heart. But at the same time, let us not forget that all independence comes with a responsibility that when we coexist, fundamental laws of cooperation, tolerance and mutual progress must govern our existence. Let us express our belief in each other's individuality. Let us have respect for all citizens of our beloved nation. Let us not forget that when it comes to choosing between humanity and human boundaries — our choice and guiding angel must always be humanity. Nothing should supersede our need for love and tolerance. One of the celebrated philosopher during the French revolution, Jean Jacques Rousseau, expressed in his most important treatise, *The Social Contract*: Man was born free, and he is everywhere in chains. One man thinks himself the master of others, but remains more of a slave than they.

It is sad that we continuously fight in our life to achieve salvation and independence in their fundamental sense, and, in the course of that, we do achieve success, glory and even financial independence, but the goals and vision with which we start our struggle are generally forgotten and abandoned. So is the case of our freedom struggle, about 64 years have passed since we got independence, i.e. in 1947, we are still enslaved by our desire. Despite having achieved a social standing in life, we are still bound by the boundaries set by race, religion, region, gender and language. While I understand these boundaries are natural for common people, I am sure at the same time that these would never exist for an emancipated and grown-up society. We should have come out of this slavery after such a long journey we have undertaken in a politically free country.

Independence is when we do the right thing freely. However, I understand that a literal independence will never exist as we all are bound together by our needs, sorrows and joys. It is fine that we

are not independent that way. But the fact that some people on the basis of race, religion, region, gender and language are being forced to succumb to their independence and are forced to lead an isolated life within our own social space, we still have to go a long way to achieve independence in its most fundamental sense.

Right to *independence* comes out of a more fundamental duty called *responsibility*. Unless we will be ready to be responsible, independence will have no real and productive existence in our life. That is why a modern political philosopher Emma Goldman says: *The most unpardonable sin in society is independence of thought*. Voltaire, the French historian and philosopher, too has similar opinion when he expresses ironically: *The true character of liberty is independence, maintained by force. Injustice in the end produces independence*. Here, he too is referring to independence without responsibility. We are independent and, going by the natural succession, we must be both responsible and independent. Emotions of mutual tolerance and progress must govern our existence. Let us have a faith in each other's individuality. Let us have respect for all citizens of the nation. Our actions must always be guided by humanity and not by man-made or political boundaries. Nothing should supersede our need for love, tolerance and progress.

Happy Independence Day to all!



CA. G Ramaswamy

President, ICAI

July 24, 2011

New Delhi

July 2011 Issue Worth Preserving for Long Times to Come

➤ It gives me pleasure to write that the July 2011 issue of the journal was highly informative and knowledge-enhancing with all the features well planned and effectively designed. While the Editorial and the President's message provided valuable insights into the progress of the profession, the contents and articles under the features 'From the Leaders Accountancy', 'Nostalgia', 'Did You Know', 'Celebrations' 'In-Quotes', 'International Taxation' and 'Ind AS' were noteworthy and went a long way in enhancing our knowledge base. The issue was indeed a special issue worth preserving for long times. Congratulations to the Editorial Board for planning the issue.

-CA. S. Jain

June 2011 Issue Provided Valuable Insight into XBRL

➤ It is immense pleasure to say that the June, 2011 issue of "Chartered Accountant" Journal was so informative and has given great insight regarding the XBRL. The 'Minimum Recommended Scale of Fees of CA in Metro and Non metro' is a very helpful step taken by the Council. I

really appreciate the editorial board for the incomparable work done for the June 2011 issue especially the design and presentation of each article.

-CA. Jomon C.V, Mumbai

Article on IFRS was Highly Informative

➤ The article on "IFRS - Convergence in India" published in May 2011 issue of "The Chartered Accountant" is highly informative & rich with content. Congratulation to the author, and thanks to ICAI for publishing such a nice article.

-CA. Subash Mishra, Bhubaneswar

➤ The article titled "IFRS - Convergence in India" published in May 2011 issue is an excellent one. It has not only updated the readers about the latest status of IFRS Converged standards but also the author has very lucidly explain the benefit to be accrued out of Convergence. Congratulation to the author. I also thank ICAI for bringing such a nice article.

-CA. Sanjeev Das, Kolkata

Journal is Unique, Inspires Professionals

➤ The March 2011 and the next

issues of *The Chartered Accountant* of the Journal are unique as we recall the idealistic and thoughtful golden words of Pandit Jawaharlal Nehru made on the eve of independence day 14th August, 1947. Incidentally it was told before the formation of ICAI in 1949. I hope that this and coming generations will be encouraged to implement the good ideas of great leaders. The destiny of the nation lies in the hands of people who are law abiding, true to the ethics and uphold the morals. Here is the place for CAs to discharge their duties without fear or favour in spite of several hurdles and drawbacks in the system. This is a step "on the verge of bold advance" and high standard espoused by the Pandit Jawaharlal Nehru followed by Dr. Rajendra Prasad and Dr. Ambedkar, etc.

➤ The legendary SWAN was stated to have been able to separate milk and water (probably if adulterated). Similarly the AUDITOR has to distinguish the differences between right and wrong. I congratulate the new office bearers for their service to the profession by glorifying the values of the golden words of venerable leaders.

-CA Sethuraman.T.J, Cuddapah

Editor

For the Attention of Readers

Readers' attention is specifically invited to the fact that the views and opinions expressed or implied in The Chartered Accountant journal are those of the respective authors only, and not of the ICAI. The ICAI bears no responsibility of any sort whatsoever in case of any action taken by any reader based on any article published in the Journal.

Write to Editor

'Information is Power' and our ever-evolving profession needs more and more of that today than ever before. Do you have any relevant points to make, experiences to share, and views to spread among the CA fraternity? If yes, e-mail us at ebboard@icai.org/nadeem@icai.org or write to:

The Editor, The Journal Section, ICAI, A-29, Sector 62, Noida (UP) - 201309

Clarifications in July 2011 Issue

1. Readers' attention is invited on p.167, where the seventh point of the column, *Did You Know?* should be read as **After the first Council of the Institute started functioning, there were 1689 members (569 Fellows and 1,120 Associates) as on April 1, 1950.**
2. Readers' attention is also invited on p.116, where the designation of Mr. C. R. Sundaramurti should be read as 'Controller General of Accounts' instead of 'Comptroller General of Accounts of India' as published.

- The Editor

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Strengthening Ties



Meeting with President of India

H. E President of India Smt. Pratibha Devisingh Patil was recently apprised about the activities of the accountancy profession by President, ICAI CA. G. Ramaswamy and Vice-president ICAI CA. Jaydeep N. Shah.



ICAI Leadership Greets New Minister MCA

President ICAI CA. G. Ramaswamy and Vice-president ICAI CA. Jaydeep N. Shah greets and welcomed new Minister of Corporate Affairs Shri M. Veerappa Moily. (14th July, 2011)



Meeting with Governor, Madhya Pradesh

President ICAI CA. G. Ramaswamy in a meeting with Hon'ble Shri Rameshwar Thakur, Governor of Madhya Pradesh at New Delhi. [29th June, 2011]



Conclave of Trade Officials

President ICAI CA. G. Ramaswamy, and Vice President, CA. Jaydeep N. Shah, along with Hon'ble Shri S.M. Krishna, Minister of External Affairs during the Conclave of Trade Officials from Missions in India at New Delhi. [11th July, 2011]



Meeting with Minister HRD

President ICAI CA. G. Ramaswamy along with Central Council member CA. M. Devaraja Reddy in a meeting with Union Minister of HRD Shri Kapil Sibal.



Naming of Road as Prof T.S. Grewal Marg

Mayor Municipal Corporation of Delhi Prof. Rajni Abbi naming the lane adjoining the ICAI Headquarters as 'Prof. T. S. Grewal Marg' in the memory of his contribution to commerce education. President ICAI CA. G. Ramaswamy and Central Council member CA. Charanjot Singh Nanda gracing the occasion among other dignitaries. [6th July, 2011]

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Bhutan Delegation

President ICAI CA. G. Ramaswamy along with Central Council member CA. Charanjot Singh Nanda in a meeting with the Delegation of Audit and Assurance Standards Board of Bhutan. [14th July, 2011]



Orientation Programme at SIRC

President ICAI CA. G. Ramaswamy being presented a memento by Chairman SIRC of ICAI CA. K. Shanmukha Sundaram during Orientation Programme organized by SIRC for the Chairmen and Secretaries of Branches of SIRC at Chennai. [27th-28th June, 2011]



Visit to Madurai Branch

Inauguration of proceedings by President ICAI CA. G. Ramaswamy during his visit to the Madurai branch of ICAI. [2nd July, 2011]



Golden Jubilee Celebrations, Pune

President ICAI CA. G. Ramaswamy in the presence of Vice President, ICAI CA. Jaydeep N. Shah, Chairman, WIRC CA. Shrinivas Y. Joshi, Central Council member CA. S.B. Zaware and other dignitaries inaugurating the Golden Jubilee Celebrations of Pune Branch of WIRC of ICAI. [28th June, 2011]



Training Programme for Officials of Autonomous Bodies (C&AG)

Photograph taken during Training Programme for the Officials of Autonomous Bodies (C&AG) and Members of the Profession at Mumbai. Seen in the picture (L to R) CA. Shrinivas Y. Joshi, Chairman, WIRC of ICAI, CA. Anuj Goyal, Central Council member, CA. G. Ramaswamy, President ICAI, Shri K.P. Sasidharan, Director General (Autonomous Bodies), office of C&AG of India & CA. Sanjeev Maheshwari, Central Council member. [23rd & 24th June 2011]



Bhoomi Pujan, Gwalior

President ICAI CA. G. Ramaswamy and Vice President, ICAI CA. Jaydeep N. Shah see with Central Council member CA. Ravindra Holani and other dignitaries during Bhoomi Pujan ceremony for building of Gwalior Branch of ICAI. [21st June, 2011]



CA Day Celebrations, Trivandrum

President ICAI CA. G. Ramaswamy at the CA Day Celebrations organized by Trivandrum Branch of SIRC of ICAI during 1st to 3rd July 2011 at Trivandrum.



Seminar on Service Tax

President ICAI CA. G. Ramaswamy along with Chairman SIRC of ICAI CA. K. Shanmukha Sundaram and Central Council member CA. Rajendra Kumar P. inaugurating the Seminar on Service Tax at Chennai. [12th June, 2011]

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Know Your Ethics*

Ethical Issues in Question-Answer Form

Q. Can a Chartered Accountant in practice/firm give advertisement in press?

A. Yes, the members in practice may advertise through a write-up setting out the services provided by him or his firm and particulars of his firm **subject to Advertisement Guidelines issued by the Council (published in July, 2011 issue of the journal).**

Direction given by the Council under Clause (7) of Part I of the First Schedule to the CA Act provides that a chartered accountant in practice/firm cannot give advertisement in press. However, a special exemption has been made as regards publication of the name and address of a member or that of his firm, with the description chartered accountant(s), in an advertisement appearing in the press in the circumstances as listed below, provided that the advertisement is not displayed more prominently than is usual for such advertisements or the name of the member or that of his firm with the designation chartered accountant(s) appears in type not bolder than the substance of the advertisement:

- Advertisement for recruiting staff in the members own office.
- Advertisement inserted on behalf of clients requiring staff or wishing to acquire or dispose of business or property.
- Advertisement for the sale of a business or property by a member acting in a professional capacity as trustee, liquidator or receiver.

When advertising for staff, it is desirable that members should avoid the expression such as "a well-known firm", since this would savour of advertisement. Similar considerations apply to advertisements for articled assistants. The advertisements should not contain any promotional element nor should there be any suggestion that the services offered by the chartered accountants or his firm are superior to those offered by other accountants.

Q. Whether a member can appear on television/radio or give lectures at forums?

A. Yes, direction given by the Council under Clause (7) of Part I of the First Schedule to the CA Act prescribes that a member may appear on television/radio or give lectures at forums and may give his name and describe himself as chartered accountant. Special qualifications or specialised knowledge directly relevant to the subject matter of the programme may also be given. But no reference should be made, in the case of practicing member, to the name and address or services of his firm. What he may say or write must not be promotional of him or his firm but must be an objective professional view of the topic under consideration.

Q. Whether companies in which chartered accountants have been appointed as directors on their Board can

publish description about the chartered accountant's expertise, specialisation and knowledge in any particular field or add appellations or adjectives to their names in the prospectus or public announcements issued by these companies?

A. The Council's attention has been drawn to the fact that more and more companies are appointing chartered accountants as directors on their Boards. The prospectus or public announcements issued by these companies often publish descriptions about the chartered accountants' expertise, specialisation and knowledge in any particular field or add appellations or adjectives to their names. Attention of the members in this context is invited to the provisions of Clause (6) and (7) of Part I of the First Schedule to the CA Act.

In order that the inclusion of the name of a member of the Institute in the prospectus or public announcements or other public communications issued by the companies in which the member is a director does not contravene the above noted provisions, it is necessary that the members should take necessary steps to ensure that such prospectus or public announcements or public communications do not advertise his professional attainments and also that such prospectus or public announcements or public communications do not directly or indirectly amount to solicitation of clients for professional work by the member. While it may be difficult to lay down a rigid rule in this respect, the members must use their good judgement, depending upon the facts and circumstances of each case to ensure that the above noted provisions are complied with both in letter and spirit.

It is advisable for a member that as soon as he is appointed as a director on the Board of a company, he should specifically invite the attention of the management of the company to the aforesaid provisions and should request that before any such prospectus or public announcements or public communication mentioning the name of the member concerned, is issued, the material pertaining to the member concerned should, as far as practicable be got approved by him.

Q. Whether a Chartered Accountant/Firm is permitted to use logo on letter-heads, stationery, etc.?

A. No, the use of logo/monogram of any kind/form/style/design/colour etc., whatsoever, on any display material or media e.g. paper stationery, documents, visiting cards, magnetic devices, internet, signboard by the Chartered Accountant firm of Chartered Accountants is prohibited. Use/printing of member/firm name in any other manner tantamounting to logo/monogram is also prohibited. However, a common CA logo has been allowed to the members, provided it is used in correct manner within terms of the Council Guidelines. ■

* Contributed by the Ethical Standards Board of the ICAI

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ICAI Celebrates Tradition of Professional Excellence, Launches New Initiatives on its 63rd Foundation Day



Starting with a handful of 1,700 members, today, the strength of the Chartered Accountant fraternity has grown to 1,73,517 members. On the education front, we began with mere 259 students and today has almost 8.47 lakh students as part of the ICAI. Recalling the inception of a tradition of professional excellence that started in 1949, The Institute of Chartered Accountants of India (ICAI) celebrated its 63rd Foundation Day on 1st July, 2011. The main function was organised at Vigyan Bhawan, New Delhi, where the regulator of the Accountancy Profession in India took stock of its progress, growth and service to the nation, and launched various new initiatives and value added services for accounting fraternity in the country. Governor of Madhya Pradesh and Past President of the ICAI CA. Rameshwar Thakur was the Chief Guest of the very well attended function. Deputy Chairman of Rajya Sabha CA. K. Rahman Khan and Minister of State, Ministry of Corporate Affairs, Shri R. P. N. Singh were Guests of Honour. Secretary, Ministry of Corporate Affairs, Shri D. K. Mittal delivered a special address. The following is a brief report of the function organised to mark the 'CA Day'.



▲ Shri T. Karthikeyan

At the outset **Shri T. Karthikeyan, Secretary, ICAI** welcomed the large gathering that included dignitaries, members and students of accountancy profession and other guests. In his address, Shri Karthikeyan said "1st July has a great significance for the Accountancy Profession in India, as on this day, in the year 1949 the Chartered Accountants Act was passed by Parliament. Every year the Institute celebrates this day as CA Day."



▲ CA. G. Ramaswamy

In his Presidential address, **CA. G. Ramaswamy, President, ICAI**, said: "1st July, is a day for introspection for the CA profession. The profession has made its presence felt dominantly in trade, industry, public administration and every other part of social and economic life. The phenomenal growth in the membership base is a reflection of the confidence and trust which the industry and public at large has in this glorious profession."

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He assured that the Institute would continue its endeavours to come up to the expectations of the government and regulators by framing appropriate guidelines/directions for its members to ensure appropriate disclosures in financial information of the industry. Its representation on the various committees of regulators is the manifestation of the trust that the system as a whole reposes in this profession.

The President added: "On this occasion of Foundation day, the institute would rededicate itself to reinforce the values of *excellence, independence and integrity* – the virtues which we imbibe in our professional work. The Occasion definitely gives us a moment to ponder over what we achieved so far as a profession and what we achieved as a member." He shared with the gathering various initiatives launched by the ICAI in the recent past, some major ones of which are as following:

- **Report on Uniform Accounting and Auditing Framework for Political Parties:** The Institute has prepared a format for the disclosure of the entire income and expenditure of political parties. The report on the Uniform Accounting and Auditing Framework for Political Parties has been submitted to the Election Commission. The implementation of the recommendations, by appropriately amending the relevant laws would go a long way in bringing more accountability among the political parties.
- **Group Formed to Address the Issue of Black Money:** In the wake of the ongoing demand from various groups and political parties to bring back the black money stashed in the overseas market, the ICAI has constituted a Group to provide necessary inputs/suggestions on effectively addressing the menace of black money and related issues in view of public interest involved. The inputs/suggestions given by the Group will be submitted to the Government.
- **Chain of Workshops on XBRL:** The Ministry of Corporate Affairs had mandated certain class of companies to file their financial statements in XBRL format for the year ended 31st March, 2011. In order to educate members on XBRL and providing hands-on training on the process, XBRL India has planned a chain of workshops to be organised at various locations across the country. During the first phase, workshops will be organised to provide training on XBRL filings in selective big cities using the resources of the Information Technology

Training Centres of the Institute. Three leading companies having expertise in XBRL filings will be the knowledge partners for this initiative. This training will help members to understand XBRL, which is emerging as the most popular reporting language across the world.

The President said that for the profession to play a greater role in building the nation, the members need to be trained with the latest IT skills. As the profession is increasingly growing global it is important to equip practising members and CA firms with more IT tools that will in turn increase their efficiency in the global competitive environment.

After his address a number of value-added services namely ICAI Web TV, ICAI Connect, Website for Practitioners and CA Firms, Online Registration Form, ICAI-RoC Software, ICAI-Tax Suite Software, etc. were launched, the details of which have been given in the latter part of this report. On this occasion the following publications were also released:

1. Technical Guide on Audit in Automobile Industry
2. Technical Guide on Expatriates Taxation
3. Economic Impact of Quarterly Reporting



▲ Shri D. K. Mittal

While delivering the special address, **Shri D. K. Mittal, Secretary, Ministry of Corporate Affairs** complimented the CA fraternity for having achieved a unique distinction in professional spheres of the country. He said: "The profession in India has reached a distinction of becoming the 2nd largest accounting body and more importantly has earned the trust and confidence of the society at large because of the basic core competence that they possess." He also opined that the ICAI is helping India to win the battle against corruption through ethical governance.



▲ Shri R. P. N. Singh

Minister of State, Ministry of Corporate Affairs, Shri R. P. N. Singh in his address said: "Accountancy profession is at its threshold. The role of chartered accountants has undergone sea-change and they have become total Business Solution Providers. ICAI, during its sagacious journey of over 62 years, has intensified its focus on emerging social and economic trends in order to raise the profession of accountancy to new heights of excellence."

He further added that "chartered accountants will rise to the occasion and bring further glory to this profession which in context of India's emergence as an economic power has all the more role to play."

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CA. K. Rahman Khan

The Guest of Honor, **Deputy Chairman of Rajya Sabha CA. K. Rahman Khan**, in his address said: "Before the Constitution of India was born the need for accountancy profession was felt. The contribution of the Institute to the overall development of the country makes me feel proud of my being its Alumni. Our Institute has been a great strategist and innovator and has kept its quality standards very high because of the process of continuous reforms in education and training and thus, bringing in the chartered accountants is a fine element of professional competence." He reiterated the need for transparency especially where the government money was being routed to reach the grass root level. He emphasised on the social responsibility aspect besides the ethical concept.

He further said that the institute must aggressively take up accounting and auditing related issues like *presumptive loss*, and also suggest measures to the government to improve the efficiency of public expenditure. "Now that the CAG has said that calculating presumptive loss and reporting it was very much within its domain (legal), there is need for defining it or having standards around this concept. This is a must to avoid confusion in the society," He added.

"The civil society is losing faith in governmental systems. The chartered accountants are not responsible for this. But accounting and auditing professionals do have a role to play in streamlining the system," he said, adding that there was no dearth of laws in India. He highlighted the fact that the government had not been able to adopt accrual-based accounting although the effort in this direction had started nearly two decades ago.



CA. Rameshwar Thakur

Speaking on the occasion as the Chief Guest, **Governor of Madhya Pradesh and Past President of the ICAI CA. Rameshwar Thakur** remarked: "It is a moment of truth for the profession to be a fundamental edifice to be overall process of national development. The profession has developed itself as an enabling instrumentality for businesses, governments, regulators and the stakeholders." The Governor added that "the accountancy profession in India is one profession which has a potential lead role to play; be it any sector of economy. I have full faith that the members of the profession have the requisite knowledge and

skills to exploit the challenges and convert them into opportunities."

Hailing the accountancy profession and its members, CA. Rameshwar Thakur said: "The profession has developed itself as an enabling instrumentality for helping and understanding the financial affairs of businesses, governments, regulators and the stakeholders. The role that the profession has to play is providing high quality financial information, facilitating market discipline, and fostering confidence in various stakeholders about the financial markets. Quality and integrity of information are the hallmark of the chartered accountant's professional practice and the basis for brand differentiation. This is true of the developing countries, which compete with each other, for mobilisation of financial resources."

He added that "Chartered accountants play an essential role in society, providing reliable and transparent information about public and private bodies. They are the trustees of the society, at large, and have to shoulder onerous responsibility of protecting and preserving the trust. They not only have to be adept at work but also have to adopt with the changing environment."

The Governor said that the move to transit to accrual accounting would certainly invigorate the financial resources of the Government and thus lead to hallmark steps in the process of national governance. "The Institute has a great task on hand to help the Government in this direction."

He advised that if the accounting profession has to serve public interest in a developmental context, it should look much beyond and position itself to play a direct and more pro-active role in formulation of economic policies and guiding implementation thereof. He further added that "as the profession grows, rules and regulations alone would not safeguard the conduct of the members. They are more meant to convey what is permissible and what would be frowned upon. Being a chartered accountant myself and having been in active practice for few decades, I would like to advice every member to uphold the dignity of the profession to conduct them honestly, without fear or favour in carrying out their professional duties."

"The accounting profession has a long and distinguished history of guarding the integrity of financial statements. As a statutory body, the Institute owes a responsibility to evolve accounting and financial framework that facilitates economic growth with certain sense of discipline and stability. I would like to emphasise that our profession owes a moral responsibility to society to sustain the highest degree of professionalism and excellence," he added.

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▲ CA. Rameshwar Thakur

The Vote of Thanks was given by **Vice President of the ICAI CA. Jaydeep N. Shah**. He thanked the dignitaries and guests for sharing their words of wisdom and encouragement with the CA fraternity and assured them to proactively take up the issues highlighted by them. The Vice President said: "The Institute of Chartered Accountants of India, since its inception in 1949, has been the hallmark of transparency, fair play and efficiency in the field of accounting and auditing. Today the CA profession has attained enviable height as it possesses strong intellectual heritage and a tradition of trust." Vice President also added that "It is the multi-faceted education and training of the ICAI that empowers chartered accountants to confidently face all challenges. The initiatives taken by the Institute have helped the accounting professionals in creating an efficient space where they can deliver and contribute to the growth of our nation. Chartered accountants are truly *partners in nation building*. It shall be our sincere endeavour to contribute towards the growth of Indian economy."

CA. Kamlesh S. Vikamsey, Past President, ICAI later addressed a technical session on "LLP form of CA Practice" which was followed by another session on "Revised Schedule VI" addressed by **CA. Dolphy D'souza**.

.. □ ..

New Services for Members and Students Launched

The 63rd Foundation Day of the ICAI saw a range of value added services launched for the benefit of our members, students and other stakeholders. As developing the IT infrastructure is high on the agenda of the Institute for 2011-2012, many of the facilities introduced will surely provide better and round the clock services ranging from 24x7 access to lectures of eminent speakers, online registration, networking and web portals, etc. The following is a brief account of the services introduced:



▲ ICAI Web TV

ICAI Web TV Portal

The ICAI Web TV was made functional by the Chief

Guest, the Governor of Madhya Pradesh and Past President of the ICAI, CA. Rameshwar Thakur. Under this initiative Educative videos are hosted on a the ICAI Web TV which will enable members to stream lectures of eminent speakers and watch them on their desktops, laptops and mobile phones at their convenience. All important live events of ICAI are being beamed live on Web and Mobile platforms using cutting-edge technology. Members across the country can participate in the webinars that will be announced by the Committee for Members in Industry from time to time.



▲ ICAI Connect

ICAI Connect

The ICAI Connect was formally launched by Secretary, Ministry of Corporate Affairs Shri D.K. Mittal. ICAI Connect is part of the drive to bring together all the Chartered Accountants who have not opted or renewed their membership of ICAI. ICAI Connect initiative will make the foundation of ICAI even stronger by active participation of our members in Industry and practice. In this dynamic environment, it is important for all Chartered Accountants to remain an active member of the Institute. The aim of ICAI connect is to converse the privilege and other benefits of being a members of the Institute so that Chartered Accountants who are not members of the Institute will get membership of the Institute and will renew their membership timely.

Project Parivartan "0" BETA

The project took a comprehensive 360 degree view of the existing processes and benchmarked them with the global best practices. 'Beta' version of the new ICAI website was released by Minister of State for Corporate Affairs Shri R. P. N Singh. The main objective of this Beta release was to share the new perspective on how the Institute perceives to capture thoughts and transform the ICAI Web Portal into a truly members and students friendly.

Online Form for Registration for CPT Course

This facility will enable the students to register

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themselves 24*7 to CPT course using the online form. This would also have the facility to pay course fee online using credit/debit cards/net banking of various banks. This will bring the students closer to the doorsteps of the ICAI, and other such forms will also be available online in due course.

Website for Practitioners and CA Firms

Exclusive website for Practitioners and CA Firms www.icaai.org.in was launched by Minister of State, Ministry of Corporate Affairs, Shri R. P. N. Singh. The website will enable the practitioners and firms to create their websites and upload the details of their firms as per the norms laid down by the Council of the Institute of Chartered Accountants of India. The website provides a platform for the CA firms to upload their firms' details and gives them an opportunity to reach out to the members and CA firms practising worldwide.



▲ ICAI-ROC Software

ICAI-ROC Software

The ICAI-ROC software was launched by Deputy Chairman of Rajya Sabha CA. K. Rahman Khan. The

software has been uploaded in the website www.icaai.org.in. 'ICAI-ROC' Software on MCA21 Compliance provides the facility to prepare Auto filing of e-Forms, Shares Records/Certificates, Meetings and Minutes, Resolutions/Drafting, Annual Return forms and maintenance of Registers and Reports, etc. The members who are desirous of this software may send their special request on committee's website www.icaai.org.in. The details of use and benefits are given on the website www.icaai.org.in and published elsewhere in the journal.



▲ ICAI-Tax Suite Software

ICAI- Tax Suite

The ICAI- Tax Suite was launched by Deputy Chairman of Rajya Sabha CA. K. Rahman Khan. ICAI- Tax Suite contains the Income Tax, TDS, Audit Reports, Project Report/CMA, Form Manager, AIR (Annual Information Return), Service Tax and Document Management and will help the Practitioners and CA Firms. 'ICAI-Tax Suite' software has also been uploaded on the website www.icaai.org.in, so that members can download it free of cost. ■



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Legal Decisions¹

DIRECT TAXES



Section 9 of the Income-tax Act, 1961, read with Article 7 of DTAA between India and USA - Income - Deemed to accrue or arise in India

US-applicant carrying on bill discounting activities for Indian group company is not liable to tax in India in view of the Double Taxation Avoidance Agreement between India and USA as discount given does

not represent interest paid upfront

ABC International Inc. USA, In re, May 3, 2011 (AAR)

The applicant US-company provides various financial services. It wants to carry out bill discounting activities for its Indian group company ABC India for purchase of promissory note, 'PN', at a discount on 'without recourse' basis and make remittance of purchase price (i.e., face value minus discounting charges). It wants to carry out these activities without having any physical presence in India.

ABC India proposes to transact with the applicant for purchase of bills of exchange drawn by them on the buyer in pursuance of goods sold under normal/merchandise trade as well as purchase of promissory notes (PN) issued by such buyer. The discount for purchasing the PN will be calculated on the basis of various factors such as prevalent LIBOR plus certain margin depending upon the market condition. ABC-India will send the requisite set of documents alongwith endorsed PN through their bank. The applicant will make the payment of PN purchased (after deducting its discounting charges as per the agreement) to the bank, which in turn will make the payment to ABC-India. In no case the applicant makes ABC India liable to make payment to the applicant in case of delay or default in payment by the entity who issued the PN.

The Authority for Advance Rulings held that discounting of a bill amounts to purchase of the negotiable instrument and it does not involve any relationship of debtor and creditor between the endorser and the endorsee. As a general rule, an endorsement of a promissory note does not also result in an assignment of the original debt.

As per the definition, for any interest to accrue, there must be a borrowing, debt, deposit or obligation to repay.

In the absence of any of those elements present, it is difficult to postulate accumulation of interest or its payment. When a promissory note is discounted, no doubt keeping in mind the prevailing rate of interest, no obligation is incurred for repayment of the money by the person who discounts the instrument or the person who gets it discounted, except that in the case of a discounting with recourse, the person who gets it discounted continues to be liable to the endorsee. In a case of endorsement without recourse, even that possibility does not arise. Of course, the person who gets the instrument discounted pays for getting present payment on an instrument that becomes due for payment at a later date. But that consideration cannot be treated as payment of interest upfront in the context of the Law Merchant and the Negotiable Instruments Act and the commercial and legal implications of a discounting of an instrument.

But in a simple transaction of discounting of a bill of exchange and prompt payment, there is no contract implied or express to deem the amount involved as a deposit or loan. In instant the case it cannot be said that the parties intended the amount involved as a loan or as money owed. It was purely a discounting of a promissory note payable at a future date and making of immediate payment on taking a discount. It cannot be held that any payment of interest is involved in the proposed transaction. The promissory note to be discounted is also not to bear any interest on the purchase price covered by the note for the delayed payment.

The underlying element that can give rise to interest is the existence of a debt claim. In other words, a debt has to exist for interest to be generated. However, discounting of a promissory note does not involve the creation of a debt or the coming into existence of a debtor-creditor relationship, and the discount given does not represent interest paid upfront by the resident company when it gets the note discounted. Thus, the discount given could not be held to be interest within the meaning of Article 11 of the DTAA.

The purchase price payable for the goods is represented by the promissory note executed by the purchaser and it is payable in future without interest. So, all that the discounting achieves is that it enables the seller to realise the price of the goods then and there or prematurely but at a cost. That cost cannot be termed as interest paid by the seller.

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

The promissory note taken by the seller, an Indian tax resident in lieu of the price to be paid, is a promissory note payable on demand. This is clear from the facsimile of the promissory note produced by the applicant. No place of payment is specified, nor is it put forward that the purchaser, the debtor, would apply to the seller to specify the place of payment. Hence applying the normal rule that the debtor must seek the creditor, the payment is to be made in India to the Indian entity. It is this promissory note payable in India that is discounted by the applicant. The discounted amount is sent to India as can be seen from the Discounting Agreement produced. On discounting, the income accrues or is deemed to accrue. An amount can accrue or arise if a legal right to receive it is acquired. On discounting the promissory note, the legal right to receive the proceeds accrues to the applicant. If so, the income to the applicant accrues in India. It is not disputed that it is the business income of the applicant. That business income accrues in India, though realised later. Such business income is taxable in India under the Income-tax Act subject to the rights conferred by or the protection afforded by the DTAA.

Under Article 7 of the DTAA, the profits of an enterprise of a contracting State shall be taxable only in that State unless the enterprise carries on business in the other contracting State through a permanent establishment situated therein. It is the case of the applicant that it has no permanent establishment in India. Assuming for the purpose of this ruling that the applicant has no permanent establishment in India, the income is not interest income, Article 11 of DTAA is not attracted. Thus, it has to be ruled that the income of the applicant from discounting would not be taxed in India, on the case set out by the applicant in the light of Article 7 of DTAA.

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Section 9 read with Section 195 of the Income-tax Act, 1961, read with Article 12 of DTAA between India and USA - Income - Deemed to accrue or arise in India

Where as per requirement of foreign service receiver, applicant recruited managerial personal from foreign affiliate company and reimbursed salary and expenses paid by foreign affiliate; to expatriate employees, amounts reimbursed by applicant are taxable as "Fees for Included Services (FIS)" under DTAA and also under Act

Verizon Data Services India (P) Ltd., In re, May 27, 2011 (AAR)

The applicant is a wholly owned Indian subsidiary of U.S. company Verizon. The applicant is engaged in providing services relating to development and maintenance of telecom software solutions and information technology services. The applicant exports services from India to Verizon US. Verizon-US feels that applicant needs individuals from US. Therefore, three of employees of US

affiliate GTE-OC are to be recruited. The applicant entered into a Secondment Agreement with GTE-OC.

The applicant submits that payments made are in nature of reimbursement of salary and expenses paid by GTE-OC to expatriate employees. The salary and benefits paid to expatriate employees have suffered withholding tax under section 192. The same amount cannot be subjected to withholding tax under section 195.

The Authority for Advance Rulings held that the preamble of the Personnel Secondment Agreement states that to perform certain managerial services, the applicant has procured the services of US based personnel who are under the employment of GTE-OC. A team of three employees has been sent by GTE-OC. One of them has assumed the position of the Managing Director of the applicant company. While these employees are providing services to the applicant, they will remain the employees of GTE-OC. Their employment can only be terminated by GTE-OC. It goes to show that it's GTE-OC who has rendered managerial services to the applicant company. For the items paid or provided to the employees, the applicant is to reimburse GTE-OC on the basis of bills presented by GTE-OC. At the time of remittance, the obligation to withhold taxes is upon the applicant and if any amount is held as taxes the applicant is required to pay GTE-OC an additional amount. In other words, the applicant is required to pay the amount net of taxes. This again is an important aspect of the agreement. Firstly, it is GTE-OC's employees who are to perform managerial services in India and secondly, the applicant is liable to bear the taxes on the remittances. There is no argument that the remittances are in consideration for the services rendered. The reason for the applicant to bear the taxes on the impugned payments to GTE-OC lies in the fact that the services rendered by GTE-OC are liable to tax in India.

Without GTE-OC the seconded employees have no locus standi vis-à-vis the applicant. It is a trite law that the capacity in which the person receives the amount determines its taxability in his hands. In that view of the matter the sums that are remitted by the applicant accrue and arise to GTE-OC for providing services to the applicant. What accrues and arises to the employees is by virtue of their employment with GTE-OC. The application of the income by GTE-OC while making payment of salaries to its employees has nothing to do with its accrual. The nature of the two receipts, one in the hands of GTE-OC for rendering services and the other in the hands of employees by way of salaries spring from different sources and are of different character and represent different species of income. By correlating the two payments/receipts in the Personnel Secondment Agreement, neither the nature nor substance of the transaction would change to give it the character of reimbursement. The name given to the transaction does not decide the nature of the transaction. A receipt is what it is and not what it is called. The salaries

are paid out of the income of GTE-OC. The total income of GTE-OC may be the sum total of receipts under different heads of income, for example: business, royalties, fees for included services, house property, interest, dividends etc. but the expenditure incurred by way of salaries to the employees cannot *ipso facto* determine the nature of the income which is to be brought to tax either under the Act or under the DTAA in the hands of GTE-OC. Therefore, the amounts paid by the applicant to GTE-OC represent income in the hands of GTE-OC.

One of the seconded employees is to perform the function as Managing Director of the applicant and other two are to supervise and provide directions in the manner through which the activities of the applicant are to be carried out and to liaise with the parent company in USA.

It is fairly clear that the functions performed by these seconded employees are purely managerial in nature.

From the memorandum of understanding of the DTAA it is clear that the services which are not in the nature of technical services, the make available clause would not apply. As the services provided by GTE-OC are in the nature of managerial services, the payments made by the applicant are covered under "fees for included services" under Article 12 (4) of the DTAA. As the services are managerial in nature, the payments are also covered under "fees for technical services" as defined under *Explanation 2* to section 9(1)(vii) of the Act.

The amounts reimbursed by the applicant represent income accruing to GTE-OC and accordingly charged to tax within the provision of section 195. The amounts reimbursed by the applicant are taxable as "Fees for Included Services (FIS)" under the DTAA and also under the Act.

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Section 41(1) read with Section 256 of the Income-tax Act, 1961- Remission or Cessation of trading Liability

If loan is taken for acquiring any capital asset, waiver thereof would not amount to any income exigible to tax; on other hand, if this loan is taken for trading purpose and is treated as such from very beginning in books of account, waiver thereof may result in income moreso when it is transferred to Profit and Loss account

Logitronics Pvt. Ltd v. CIT, February 18, 2011 (DEL)

The assessee-company was engaged in the business of manufacturing of electronic products. It was enjoying loan facility from State Bank of India (SBI). As on 31.03.1998, the principal amount of loan due to the bank was ₹4,76,92,213 and outstanding interest was ₹1,90,42,295. During the pendency of recovery proceedings, the assessee had settled the matter with the SBI for payment of ₹1,85,00,000 against loan of ₹4,76,92,213 (principal amount), the remaining sum of ₹1,90,42,295 was waived. In the tax return filed by the assessee, it showed interest waived as income but not the amount of loan waived by

SBI. The amount of interest written off i.e., ₹1,90,42,295 was credited to profit & loss account and was offered for taxation. However, the principal amount written off i.e. ₹2,91,42,213 that was directly taken to balance sheet under the head capital reserve, was not offered for taxation. The Assessing Officer held that even waiver of principal amount of loan was also taxable.

The Delhi High Court held that in the context of question of waiver of loan amount, the answer would depend upon the purpose for which the said loan was taken. If the loan was taken for acquiring the capital asset, waiver thereof would not amount to any income exigible to tax. On the other hand, if this loan was for trading purpose and was treated as such from the very beginning in the books of account, the waiver thereof may result in the income, moreso when it was transferred to Profit and Loss account.

In the instant case, the assessee had obtained the loan or credit facility by way of hypothecation of finished goods, semi-finished goods, raw material, book debts, receivable claims, securities and rights by way of first charge, which indicated that the assessee had obtained the loan facility for its business activity or trading operations. However, the Tribunal noted that this aspect of the matter whether the whole amount of the loan had been utilised either for the purpose of acquiring capital asset or for the purpose of business activity or trading activity had not been looked into or examined by the Authorities below. For this reason, the Tribunal has restored the case to the file of the AO for fresh adjudication. There was no reason or occasion for the assessee to feel aggrieved by the order and prefer this appeal. Thus, no substantial question of law arose.

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Section 41(1) read with Section 28(iv) of the Income-tax Act, 1961- Remission or Cessation of trading Liability

Where assessee engaged in the business of sale/purchase of shares and business of taking loans and further providing it to parties, wrote back unclaimed loan taken from a party, which was obtained as a part of source of funds employed by assessee in its business, amount was to be treated as receipt of capital nature and could not be added in assessee's taxable income

Logitronics Pvt. Ltd v. CIT, February 18, 2011 (DEL)

The assessee is an investment company engaged in the business of sale/purchase of shares and business of taking loans and further providing it to the parties. The AO found that the assessee had credited a sum of ₹25,00,000 in Profit and Loss Account on account of remission of liability with respect of certain unsecured loans appearing in its financial results. This amount represented loan taken from one SHPL more than ten years ago. Since there was no communication from the party and no claim was made for so many years the loan was written back. It was treated

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as capital receipt and was not taken as taxable income in the computation of assessable income for the assessment year in question. The AO held that the amount as written off liability was the income of the assessee and added in the taxable income. The Commissioner (Appeals) confirmed the order of the Assessing Officer. However, the Tribunal deleted the addition made.

The Delhi High Court held that what was to be seen is as to whether the aforesaid loan was taken for trading purpose or it was to generate some capital assets. The assessee was an investment company engaged mainly into the business of purchase and sale of shares. It was also engaged into taking business loans and further profits done to the parties. The Commissioner (Appeals) held that the amount of loan was utilised for its financing business. The Tribunal accepted the plea of the assessee that loan was not used in the financing business, but was used in long term investment made in shares. Thus, it was explained that the assessee was a company engaged, *inter alia*, in the business of finance and making investments in shares. The loan obtained by the assessee from SHPL was part of the source of funds employed by the assessee in its business. In pursuance of the business of financing, the assessee advanced loans at interest. Such loans were advanced out of interest-free own funds available with the assessee in the form of share capital and reserves or out of borrowed funds in the form of loans, etc. The loans borrowed were to augment the funds available with the assessee, to be advanced on interest. Such loans borrowed were a source of funds. It could not be said that the assessee was in the business of borrowing and advancing loans – it could never be the business of an assessee to borrow money by way of loans. Thus, the money borrowed, was only a source of funds.



Furthermore, the Tribunal reached a finding of fact that the amount of loan was not used in financing business. Having regard to these findings of facts constituting the nature of loan, the question was to be answered in affirmative and, accordingly, the appeal by the Revenue was also to be dismissed.

Section 44BB read with Section 9 of the Income-tax Act, 1961- Non-resident, business of exploration mineral Oils, etc.

Once it is held that the income is from its oil exploration and production activities as envisaged under section 44BB if a part of the income falls under 'Royalties' or 'Fees for Technical Services', there is no scope to assess such receipts under these heads; revenues earned or to be earned by applicant under seismic data acquisition and processing contracts in India are taxable under section 44BB

Bergen Oilfield Services AS, Norway, In re, May 16, 2011 (AAR)

The applicant, a Norway company provides geophysical services to oil and gas exploration industry. Cairn-India has awarded contract to the applicant to carry out 3D Marine Seismic Data Acquisition services in the offshore coastal areas. The applicant states that the services rendered by it will be utilised by the Cairn in its oil exploration and production activities under the ambit of section 44BB. The applicant further stated that for the purposes of conducting seismic surveys, the vessel is mobilised from outside India to the site area in India where the work is to be carried out. Similarly, when the vessel is demobilised, after completion of the work, it involves moving out of equipment and personnel from the site area. The applicant is paid for mobilisation as well as demobilisation of its vessel from the site area. The question arose as to whether entire mobilisation/demobilisation revenues received by the applicant with respect to seismic data acquisition and/or processing contracts would be taxable in India or revenues attributable to distance travelled by the vessel in India would be taxable in India.

The revenue contended that the services contemplated in section 44BB are services other than those coming within the purview of *Explanation 2* to section 9(1)(vii). The services of exploration industry extended by the applicant fall under *Explanation 2*. It was submitted that the income by way of fees for technical services chargeable under section 9(1)(vii) has to be computed under section 44DA in a case like this where the service provider has a Permanent Establishment in India. It is contended that the exclusion clause in *Explanation 2* does not apply in the case of the applicant because it is not undertaking a mining or like project. Such project is undertaken by someone else and certain technical

services are rendered by the applicant to the business enterprise that takes up the project. In short, the revenue contended that section 44BB would come into play only if the applicant goes out of the purview of section 9(1)(vii), read with *Explanation 2* thereof.

The Authority for Advance Rulings held that the issue had arisen in the case of *Geofizyka Torun Sp. Zo.o.*, In re [2010] 186 Taxman 213 (AAR - New Delhi), wherein this Authority held that: "If the business is of the specific nature envisaged under section 44BB, the computation provision therein would prevail over the computation provision in section 44DA. In other words the income received by a non-resident businessman for the technical services provided in relation to prospecting and extraction of mineral oil, will be governed by section 44BB for the purposes of computation. If all the services that are in the nature of technical services within the meaning of *Explanation 2* to section 9(1)(vii) are to be computed in accordance with section 44 DA, very little purpose will be served by incorporating special provision in section 44BB for computing the profits in relation to the services connected with the exploration and extraction of mineral oils. The provision will then operate in a very limited field."

It cannot be said that section 44BB will become otiose or altogether redundant, but its scope and content will be unduly curtailed by adopting the interpretation sought to be placed by the revenue." Therefore, revenues earned

or to be earned by the applicant under seismic data acquisition and processing contracts in India are taxable under section 44BB of the Income-tax Act at of effective tax rate of 4.223 per cent.

Once an assessee opts to come under section 44BB(1) of the Act, the provision itself deems its profits and gains as 10 per cent of the aggregate of the amounts specified in sub-section (2). Sub-section 2(a) specifies that that aggregate amount is the amount paid or payable whether in or out of India to the assessee on account of provision of services in India. In the scenario, there is no scope for splitting up the amount payable to the assessee. If the assessee wants to seek such a splitting up it has to go under section 44BB(3) of the Act.

The scheme of computation of income under section 44BB does not provide any leeway to apply simultaneously both the sub-sections (1) and (3) of section 44BB to the income arising from the business activities falling under the ambit of section 44BB(1). It even goes to the extent that if a part of the income falls under 'Royalties' or 'Fees for Technical Services', there is no scope to assess such receipts under these heads, once it is held that the income is from its oil exploration and production activities as envisaged under section 44BB. If the applicant desires to know the answers to the two issues, then it has to first exercise the option to get its income computed under section 44BB(3). In view thereof, the entire mobilisation/demobilisation revenues received by the applicant with



respect to seismic data acquisition and/or processing contracts would be taxable in India at effective rate of 4.223 per cent.

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Section 147 read with section 154 of the Income-tax Act, 1961- Income Escaping Assessment

Income Tax Officer can give up a rectification proceedings initiated under section 154 and then proceed to make an income escaping assessment under section 147 for same assessment year

CIT v. India Sea Foods, January 17, 2011 (KER)

Both the first appellate authority as well as the Tribunal declared the reassessment as invalid only by virtue of the fact that prior to initiation of proceedings for reassessment, the Assessing Officer issued notice for rectification of assessment under section 154 and it is after giving up the same that too, without issuing any express order, the assessment was reopened.

The Kerala High Court held that if an assessment happens to be an under-assessment or a mistaken order, the course open to the Assessing Officer is either to rectify the assessment if it is a mistake falling under section 154 or to make income escaping assessment under section 147. Both these provisions are self-contained provisions wherein conditions for invoking the powers and the procedure to be followed and the time limit within which orders are to be passed are mentioned.

In the instant case the Assessing Officer first felt that the excessive relief granted in the computation of relief under section 80HHC is a mistake that could be rectified under section 154 and following the mandatory requirement contained under section 153(3), notice was issued to the assessee. The assessee brought to the notice of the Assessing Officer that there was no apparent mistake in the proceedings issued and so much so, assessment could not be rectified. The Assessing Officer apparently accepted the objection raised by the assessee and gave up the proceedings initiated under section 154. But the assessee was not informed that the proceeding initiated under section 154 was

dropped. However, after expiry of the period provided for rectification of assessment under section 154, the Assessing Officer initiated proceedings under section 147 for making income escaping assessment by issuing notice under section 148. Admittedly notice under section 148 was issued within time and reassessment also was completed under section 147 within the statutory period. The question to be considered was whether the initiation of proceedings under section 154 and the dropping of the same without issuing an express order in that regard will affect the validity of re-assessment under section 147.

The fact that the Assessing Officer initiated rectification proceedings under section 154 does not mean that he should stick to the same only and proceed to issue orders as proposed. The very purpose of issuing a notice to the assessee is to give him opportunity to raise objection against the proceeding which includes the assessee's right to question the maintainability of the rectification proceedings. If the assessee convinces the officer that rectification is not permissible, the Assessing Officer is absolutely free to give up the same and see whether there is any other recourse open to him to achieve the purpose i.e. to bring to tax escaped income. In this case even though the Assessing Officer did not issue any specific order dropping the proceeding initiated under section 154 based on the objection filed by the assessee, the only inference possible after expiry of the time provided for completion of proceedings under section 154 is that the Assessing Officer has given up the proposal. Further, when a notice is issued under section 148 for making income escaping assessment, the Assessing Officer obviously made it clear that the proceedings under section 154 is dropped and he proposes to proceed with reassessment under section 147. In fact, even if the Assessing Officer had proceeded with the rectification proceedings under section 154 which was not sustainable, it was open to the Commissioner of Income Tax to exercise his powers under section 263, set aside the order issued under section 154 and direct the Assessing Officer to consider income escaping assessment under section 147 which the Assessing Officer is free to initiate. In this case the Assessing Officer himself realised the mistake of initiating

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rectification proceedings and when he noticed that the correct recourse open to him under the Act was to make an income escaping assessment, he was entirely free to do it and there was nothing wrong in the Assessing Officer giving up rectification proceedings, though initiated by him based on reply filed by the assessee and then initiating an income escaping assessment by issuing notice under section 148 within the statutory period.

Section 201 of the Income-tax Act, 1961- Deduction of tax at source- Failure to deduct or pay, Consequences of

Even where in proceedings under section 201, in show cause notice Assessing Officer had observed that in acquisition of shares, capital gains were deemed to accrued or arise in India and, therefore, TDS was to be deducted by appellant on making payment, matter might be remitted to Assessing Officer to ascertain jurisdictional issue; and it is open to assessee to approach High Court under Article 226 of the Constitution

Richter Holdings Ltd. v. Asstt. Director of Income-tax (International Taxation), June 13, 2011 (KAR)

It was averred that the first respondent issued a show cause notice to the petitioner/appellant Cyprus company regarding proceedings under section 201(1) and 201(1A) in respect of indirect acquisition of 51 per cent shares of Sesa Goa Limited without deduction of TDS. It was further averred from the show cause notice that after expressing a tentative opinion in respect of reasoning given, the Assessing Officer had observed that objections/reply/details might be furnished before the next date of hearing, but at the end of the show cause notice, the Assessing Officer has observed that in view legal provision, the company Westglobe Ltd. along with Richter Holdings Ltd. Cyprus had jointly acquired indirectly 2,00,74,834 shares of Sesa Goa for total consideration of Rs.4087 crores on which capital gains deemed to accrue or arise in India. Therefore, in accordance with provision of section 195 TDS was to be made deducted on these payments made to the company Earlyguard. The petitioner contended that the said show cause notice was not a show cause notice at all and the Assessing Officer has already prejudged the matter and wherefore, no useful purpose would be served in giving a reply to the show cause notice.

The Single Judge declined to interfere with the show cause notice on the ground that the petitioner, having received the show cause notice, should approach the first respondent-assessing officer and give its reply and all the contentions that were urged in the writ petition could be urged before the Assessing Officer.

The Karnataka High Court held that having regard to the contents of the show cause notice, it was clear that it was open to the appellant to urge all the facts including jurisdictional fact before the Assessing Authority by placing



the version of the appellant with corroborative evidence, documentary or otherwise. On a reading of the show cause notice, no person of ordinary prudence would come to the conclusion that no useful purpose would be served by remitting the matter to the first respondent. Further, in view of the decision of the Supreme Court in *Vodafone International Holdings B.V. v. Union of India* [2009] 221 CTR (SC) 617, the interest of the appellant could further be safeguarded by directing that the appellant would appear before the first respondent by raising jurisdictional fact and the jurisdictional fact would be tried as a preliminary issue and if the appellant would be aggrieved by the finding on the preliminary issue relating to jurisdictional fact, it was open to the appellant to approach the High Court under Article 226 of the Constitution. Therefore, the show cause notice issued by the first respondent did not call for interference in exercise of writ jurisdiction of the High Court.

Section 245R of the Income-tax Act, 1961- Advance Rulings – Procedure on receipt of application

Authority for Advance Rulings has jurisdiction to see whether the transaction is designed prima facie for avoidance of Income-tax

ABC International Inc. USA, In re, May 3, 2011 (AAR)

The authority for advance rulings has jurisdiction to see whether the transaction is designed *prima facie* for avoidance of Income-tax. Section 245R(2) of the Act must receive a purposive interpretation. The proviso to section 245R though placed in the context of the initial allowing of the application (really, admitting for consideration) for consideration and for giving a ruling, its object is clear. It seeks to prevent the obtaining of a ruling when the question is already in the seisin of the regular authorities under the Act, when it involves a determination of fair market value of any property or when it relates to a transaction or issue that is designed *prima facie* for the avoidance

of income-tax. It is true that at the stage of allowing the application under section 245R(2) of the Act, the Authority can and should consider all these questions. But that fact does not prevent the Authority from considering the question when the application is taken up for rendering a ruling under sub-section (4) of section 245R of the Act. After all, the object of the proviso to section 245R(2) is very clear. It is to tell the Authority to decline a ruling if any one of those aspects is involved. If after the order under section 245R(2) is made and while the application is being considered under section 245R(4), it becomes apparent that one of the provisos is attracted, it behoves this Authority to decline a ruling. After all, section 245R is an integrated section not only dealing with the admission of an application but also its final disposal and the mere fact that the disabilities are placed at the earlier stage, cannot lead to the position that the disabilities should be ignored even when they become discernible when the application is taken up for final disposal.

Proviso (iii) to section 245R(2) of the Act gives the Authority for Advance Rulings the jurisdiction to test the transaction projected before the Authority to see whether it is designed *prima facie* for the avoidance of income-tax. Proviso (iii) to section 245R(2) enables this Authority to test the transaction or issue for finding out whether as put forward, it was designed for the avoidance of income-tax.

What is the effect of the use of the expression *prima facie* in the provision? According to the P. Ramanatha Aiyar's Law Lexicon, *prima facie* means, 'at first sight, on the first appearance, on the face of it; so far as can be judged from the first disclosure, presumably; a fact presumed to be true unless disproved by some evidence to the contrary, arising at first sight, based on the first impression'. The expression used is not *ex-facie*, meaning, in the light of what is apparent. The use of the expression *prima facie* thus, gives a little leeway to this Authority to consider the question of avoidance of tax, but still, it gives to this Authority only the jurisdiction to consider the question *prima facie*. This seems to suggest that this consideration can only be at the initial stage of the application. To confine it to that stage would really defeat the purpose of the introduction of the proviso. But since the intention appears to be not to confer on this Authority the jurisdiction to thoroughly examine the facts and circumstances to come to a definite conclusion as to whether a scheme for avoidance of tax is involved, the inquiry in this regard can only be of a limited nature. Thus, considered on the facts of this case, it is difficult to say *prima facie* that there is a scheme for avoidance of income-tax. Counsel for the applicant pointed out that in terms of the Treaty, the income would be the 'business income' of the applicant and would be taxable under the Statute in the USA. All ABC entities involved have separate corporate identities and legal existence. It is one thing to say that one can pierce the corporate veil in an appropriate case but the existence of a series of legal entities validly

incorporated under the relevant laws, cannot be ignored. There is also nothing illegal in one subsidiary dealing with another subsidiary. There is no case here that the transactions leading to the discounting of the promissory note are sham or illegal. When it is so, the transaction is to be tested in the light of Law Merchant wherever apt and the provisions of statute law wherever they apply.

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Section 254 of Income-tax Act, 1961- Appellate Tribunal – Orders of

Where Tribunal had relied upon a decision of another Tribunal which had not been cited at time of hearing, order of Tribunal could not be recalled

Geofin Investment (P) Ltd. v. CIT, May 27, 2011 (DEL)

The petitioner submitted that the tribunal had erred in dismissing the application under Section 254(2) as the tribunal in its order, had referred to and relied upon decision of another ITAT Bench which had not been cited at the time of hearing.

The Delhi High Court held that there was no merit in the said contention. Under Section 254(2), a mistake apparent from the record can be rectified. The power is circumscribed and limited. There should be mistake which is apparent before the power can be exercised. This is a mandatory pre-condition.

The Tribunal in its order, referred to the controversy in question relating to disallowance made on account of short term capital loss and long term capital loss. The entire issue was examined on merits including the judgments relied upon the petitioner assessee. After examining the matter in detail, the tribunal allowed the appeal filed by the revenue. While allowing the appeal, the tribunal also referred to another decision of ITAT, Mumbai Bench. Reliance and reference to reasons stated in the said case could not be regarded as a mistake apparent from the record. It is not unusual or abnormal for Judges or adjudicators to refer and rely upon judgments/decisions after making their own research. In view of the aforesaid, there was merit in the present writ petition and accordingly the same was dismissed.

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Section 256 of the Income-tax Act, 1961- High Court – Reference to

Non-traceability of record, shortage of staff cannot be held to be sufficient cause for condoning department's delay in filing appeal

Commissioner of Income-tax v. Indian Hotels Co. Ltd, May 9, 2011 (SC)

Condonation of delay of 656 days in filing the appeal before the High Court was rejected. Explanation for the said delay were that; (i) due to circumstances beyond control, the appeal could not be filed in time; (ii) the case records were old and not traceable; (iii) procedural

formalities were involved in the Department and the papers were to be processed through different officers in rank for their comments, approval, etc., and then the preparation of the draft of appeal memo, paper book and (iv) there were administrative difficulties such as shortage of staff. It was further submitted that the appellant had good chance of succeeding in the appeal and if the relief as prayed for was not granted, grave and irreparable loss would be caused to the revenue.

The Supreme Court held that the explanations did not make out a sufficient cause for condonation of delay in filing the appeal before the High Court. Therefore, the Special Leave Petition was to be dismissed.

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

Where Commissioner while passing order under section 263 has given a specific direction that Assessing Officer should pass consequential orders within a period of three months but no consequent order was passed even after three years, time limit would be held to have expired

Commissioner of Income-tax, Delhi-IV v. Goyal M.G. Gases (P) Ltd, February 23, 2011 (DEL)

Under section 263(1), the Commissioner is empowered to call for and examine the record of any proceeding under the Act and if he considers that any order passed by an Assessing Officer is erroneous insofar as it is prejudicial to the interest of the revenue. He may, after giving the assessee an opportunity of being heard and after making or causing to make such enquiry as he deems fit, 'pass such order thereon as the circumstances of the case justify', including an order enhancing or modifying the assessment, or cancelling the assessment and directing a fresh assessment. In view of this provision it is clear that the Commissioner may pass any order as the circumstances of the case justify.

Where the Commissioner, while passing the order under section 263, has given a specific direction that the Assessing Officer should pass the consequential orders within a period of three months approximately, this direction would certainly fall within the expression 'such order thereon as the circumstances of the case justify' appearing in section 263(1). The consequential order had not been passed for over a period of approximately three years and eight months. Where no period of limitation is prescribed then, in any event, a reasonable period of limitation ought to be adopted. The non-specification of a period of limitation does not mean that the Assessing Officer can wait interminably or for an infinite period before passing the consequential order. And, in the context of the direction given by the Commissioner for passing the consequential orders within three months approximately, a period of three years and eight months is certainly much beyond the reasonable period that could be allowed to

the Assessing Officer to pass the consequential order. Therefore, it was to be concluded that the time-limit for framing the consequential order had expired.

Rule 10B of the Income-tax Rules, 1962 read with Section 92C of the Income-tax Act, 1961 – Determination of arms length price under Section 92

Where (i) assessee manufactured all season wipers and snow wipers, which were exported to associated enterprise to be sold in the market of USA (ii) associated enterprise provided to assessee certain parts free of cost and manufacturing process of wipers does not require any advance technology (iii) associated enterprise also purchased such wipers from Chinese manufacturers, CUP method, would be the most appropriate method for determining Arm's Length Price [Assessment Year 2006-2007]

Clear Plus India (P) Ltd. v. Dy. CIT, January 11, 2011 (ITAT-DEL)

The assessee manufactured all season wipers and snow wipers, which were exported to the associated enterprise which had given interest free unsecured loan of about Rs. 1.81 crores to the assessee on 31.03.2006, i.e., on the last date of concerned financial year. The associated enterprise also purchased such wipers from Chinese manufacturers. The assessee maintained invoices of Chinese goods purchased by the associated enterprise. The associated enterprise had provided to the assessee certain parts, being blister, flexer and boot free of cost. The manufacturing process of the wipers did not require any advance technology. The assessee had used CUP method to justify its sale price. An analysis was made in respect of all kinds of wipers with respect to the sale price of the assessee and the sale price of Chinese manufacturers to the associated enterprise. In this analysis the assessee added the price of blisters, flexer and boots to the price at which wipers were sold to the associated enterprise for the reason that Chinese manufacturers used their own parts in the process of manufacture. From the analysis, it was seen that the price charged by the assessee from the associated enterprise in respect of the wipers of the sizes of "11 to 24" was more than the price charged by the Chinese manufacturers. However, the position was reverse in respect of "26 and 28" all season wipers. In the case of snow wipers, the invoices raised by the assessee were of higher amounts than those of the Chinese manufacturers.

The main question was whether, CUP was the most appropriate method in the case of the assessee for determining arm's length price.

The Delhi Bench of Tribunal held that rule 10B prescribes the method for determine arm's length price by different methods. In case of CUP method, it is provided that the price charged or paid for property transferred

or services provided in a comparable uncontrolled transaction, or a number of such transactions, is identified. Such price is adjusted to account for difference, if any, between the international transaction and the comparable uncontrolled transactions or between enterprises entering into such transactions, which could materially affect the price in the open market. The adjusted price so obtained is to be taken as arm's length price.

In the instant case, goods were sold by the Chinese manufacturers in the USA market. The assessee had also sold the goods in U.S.A. market. Therefore, market conditions in the territory of sale were the same. In view thereof, the buyer in the USA market would be more concerned with quality and price rather than economic conditions prevailing in China and India.

CUP method is the most direct method for determining arm's length price. CUP method is a preferred method and it leads to more reliable results vis-a-vis the results obtained by applying transaction profit method. The focus is on the market in which products are acquired. The CUP method could validly be employed provided product comparability is established. Therefore, it would have been appropriate for the assessee to make the data of the associated enterprise available to the Assessing Officer, at least in respect of sale of Chinese and Indian wipers so as to establish the comparability. Nonetheless that by itself would not displace the CUP method, which is objective in terms of the purchase price of the associated enterprise. Accordingly, in the instant case, CUP method was the most appropriate method for determining arm's length price.

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INDIRECT TAXES



Excise/Customs

Heading 8803 of the First Schedule to the Customs Tariff Act, 1975- Aircraft

No rulings is required on classification of imported parts of aircraft and ground handling equipment when same is agreed upon by supplier-importer and concerned Commissioner; exemption be available under Notification No.

39/36-Cus, dated 23-7-1996 on production of certificate procured from Ministry of Defence

AmSafe Services India Pvt. Ltd., In re, May 13, 2011 (AAR)

The applicant is a subsidiary company of AmSafe-UK. The applicant proposes to import and supply parts of aircraft and ground handling equipment to Hindustan Aeronautics Limited (HAL), a Public Sector Undertaking. The supplies to HAL from the Customs Port or from the private bonded warehouse shall be made against a custom duty exemption certificate (CDEC) provided to the applicant by HAL.

The applicant has claimed that the goods proposed

to be imported by it for supplies to HAL are classifiable under heading 8803 of the First Schedule to the Customs Tariff Act, 1975 as parts of aircraft, even though based on the individual description of the goods, these may independently be otherwise classifiable under different headings of the said First Schedule. The applicant has also claimed that it is eligible for the exemption from basic Customs duty and additional Customs duty on such imported parts in terms of the entry at Serial No. 10 of Notification No. 39/96-Cus dated 23.7.1996 on the basis of Customs Duty Exemption Certificate (CDEC) made available to it by HAL.

The Authority for Advance rulings held that the Commissioner has since indicated vide its letter dated 12th April, 2011 that pursuant to the directions of the Authority the applicant had a meeting with the officers of the Department. Apparently the applicant has explained the basis adopted by the Department for the classification under HSN of the various parts proposed to be imported by the applicant. The Commissioner has informed through the Departmental Representative appearing in the proceedings that vide its letter dated 1st April, 2011, the applicant has revised the HSN classification of the goods which they intend to import and sell in India and, therefore, there were no disputed classifications. In view of the aforesaid developments and in view of the lack of detailed information before it, the Authority would not go into the merits of the classification of various items adopted by the Commissioner of Customs and accepted by the applicant.

Notification No. 39/96 exempts various goods of the description specified in the Table annexed to the Notification from the whole of the duty of customs leviable thereon under the First Schedule and the additional duty leviable thereon under Section 3 of the Customs Tariff Act, 1975 subject to the conditions specified in the corresponding entry of the said Table. Serial No. 10 *inter alia* exempts aircrafts, aircraft parts, aircraft engines and aircraft engine parts. The entry at S. No. 10 indicating the goods (covering aircrafts related goods) and conditions subject to which the exemption is available.

From the text of the operative part of notification 39/96-Cus dated 23.7.1996, it is observed that the scope of the exemption in the notification is not confined only to goods falling under a particular chapter or a heading of the First Schedule. All goods specified in the Table and falling anywhere in the First Schedule to CTA, 1975 would be eligible for the exemption subject to fulfillment of the conditions specified therein. Accordingly the applicant is eligible for the exemption in respect of aircrafts, aircraft parts, aircraft engines etc. specified against Serial No.10 subject to fulfillment of the corresponding conditions irrespective of the fact whether such goods are classified under heading 8803 or any other heading of the First Schedule to CTA, 1975.

The exemption in Notification No. 39/96-Cus. dated

23.7.96 are (i) is intended for imports by certain specified entities; (ii) only some of the entities are required to produce a certificate; (iii) the certificate has to be signed by different authorities for imports by different class of entities.

The exemption shall apply only if the conditions specified in column (3) against Serial No. 10 of the notification are complied with i.e. the applicant shall produce a duty exemption certificate showing the details of the purchase order placed by the Ministry of Defence and the quantity of items required to be imported to execute the order in accordance with the conditions. The duty exemption certificate shall also indicate the details of the purchase order placed on the foreign suppliers indicating the description and the quantity of the items as specified in the conditions of exemption. The exemption shall not be available if the duty exemption certificate is signed by the General Manager, Procurement Division, HAL and countersigned by its Managing Director. The exemption shall apply only if the certificate contains the prescribed information and is signed by an officer not below the rank of a Joint Secretary to the Government of India in the Ministry of Defence.

Service Tax

Section 65(12) of the Income-tax Act, 1961- Banking and other Financial Services

Leasing of locomotives, coaches and wagons for a short duration to a lessee on rent, bearing no correlation to either life of equipment or cost of equipment, would not be exigible to service-tax

BITES Ltd. In re, April 8, 2011 (AAR)

The applicant provides consultancy services in various facets of transportation like Railways, Highways, Airports, Urban transport, Ropeways etc. in India and abroad. The company intends to enter into business of providing locomotives, coaches, wagons, etc. under Operating Leasing Agreement in the domestic market. The criteria for that may be company to take locomotives either on operating lease or through outright purchase from Indian railways which in turn may be leased or sub-leased to the prospective clients in India.

The applicant has stated that it proposes to operate on dry lease of its locomotives, coaches and wagons etc. and dry lease is a leasing arrangement of equipment for definite periods with obligation on the lessee to return the leased article on the expiry of the term and pay rent as agreed to during the term of the agreement. This should not be considered a transaction that attracts liability for service-tax.

The Authority for Advances Rulings held that the definition speaks of "financial leasing service" including equipment lease or hire purchase. Financial leasing is indicated as meaning a lease transaction where

four elements have to cumulatively exist including the payment of the lease amount being calculated as to cover the full cost of the asset together with the interest charges and the lessee being entitled to own the leased asset at the end of the period after making the lease payment.

A transaction of hire purchase contemplates the payment of the value of the equipment by the hirer and transfer of title to the hirer at the end of the transaction. In fact, it is said that generally in a transaction of equipment lease or hire purchase, it is the hirer who identifies the equipment to be leased/purchased and determines the value to be paid and all that the lessor has to do is to pay the money for the equipment and negotiate with the hirer to pay rental or instalments to be fixed for use of the equipment taking note of the price paid by the lessor and the interest on the investment made by him. The term of the lease (or the period) is also generally chosen by the lessee. Therefore, when clause (12) of Section 65 dealing with "banking and other financial services" takes in financial leasing services including "equipment leasing" and "hire purchase"; the natural way of understanding the transactions of equipment leasing and "hire purchase" is as transactions analogous to "financial leasing services", in the definition of which they are included. Actually, hire purchase even otherwise falls under that category.

It appears to be logical to understand the expression "equipment leasing" as having an element of financing like a "hire purchase" or a "financial leasing service" and it cannot be understood as taking in a mere leasing of an equipment for a short duration unrelated to the life and cost of the equipment and without the intention of giving the lessee the option to purchase the equipment on the expiry of the term or on fulfilling its obligation to pay the



hire charges (which takes in the value of the equipment itself) in instalments in terms of the transaction.

Section 65(12) of the Act defines banking and other financial services. The intention manifested is to deal with financial services. Whether it is financial services rendered by a banking institution or by a non-banking institution, those will fall under the definition. Originally, in addition to a banking company or a financial institution including a non-banking financial company, any other body corporate rendering such a service was also included. With a view to rope in other commercial concerns undertaking the business of rendering financial services, the definition was amended to include them. The services remained banking and other financial services. Financial services included financial leasing services and that included equipment leasing and hire purchase.

The thrust of the definition was always on financing as a service, whatever form it took and whoever undertook it. It is, therefore, easier to understand the expression "equipment leasing" as a leasing involving financing with a view to enable the lessee to acquire title to the equipment at the end, and that, that alone is covered by the definition and not a lease of an equipment simpliciter. Unless financing is involved, the leasing of equipment would not come within the purview of Section 65(12) of the Act.

In the instant case the equipment is purchased or taken on lease by the applicant. It is proposed to be granted on a lease for a short term (in fact, on behalf of the petitioner it is submitted that it was proposed to grant a lease for two years only). The lease amount or rent is to bear only a small proportion to the cost of the equipment. The term of the lease has no correlation with the life of the equipment which on the expiry of the short term, would revert to the control of the applicant. The subject matter of the lease was to be in the possession and effective control of the lessee during the term of the lease. There was no intention to convey the title to the equipment to the lessee on the expiry of the term or to confer on the lessee an option to purchase the equipment. It appears to be a simple case of hiring of locomotives, coaches/wagons for a short duration on a rent to be paid by the lessee who was entitled to have the equipment under its control and risk during the term of the lease. Such a transaction cannot come within the purview of "financial leasing services" contained in Section 65(12) of the Act.

Since exclusive possession and effective control of the equipment is to be transferred to the lessee during the term of the lease, section 65(105)(zzzzj) cannot also be attracted. The proposed leasing of the locomotives coaches/wagons by the applicant for a short duration to a lessee on a rent, and the term of rent bearing no correlation to either the life of the equipment or the cost of the equipment, same would not be exigible to service-tax under the Finance Act, 1994 on the basis of the definition in Section 65(12) of the Act.

Section 66A of the Finance Act, 1994, read with Sections 51 and 53 of the SEZ Act, 2005- Services received from outside India

Services of maintenance, repair and overhauling services provided to domestic and international airlines in SEZ are taxable; no exemption is provided under SEZ Act

MAS-GMR Aerospace Engineering Company Ltd, In re, May 13, 2011 (AAR)

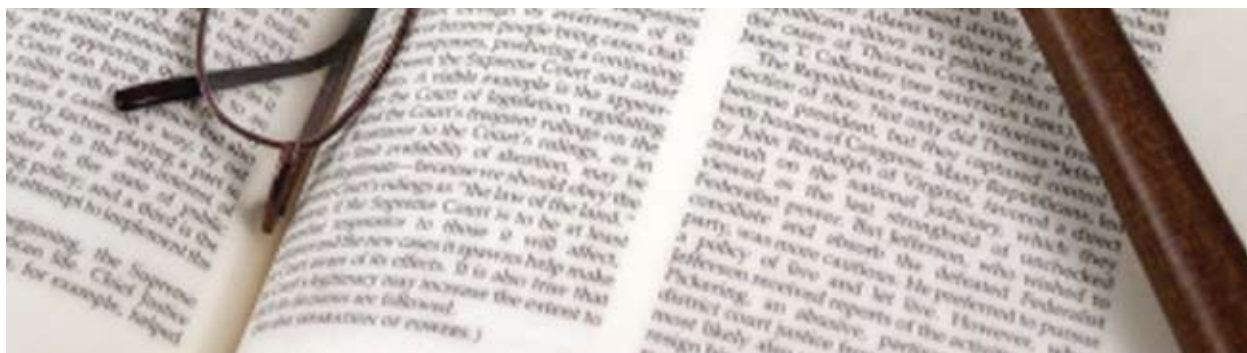
The applicant is a joint venture company of GMR, Hyderabad International Airport Limited, Hyderabad and Malaysian Aerospace Engineering, SDN-BHD, Malaysia. The applicant has obtained a registration as a co-developer of an aviation specific SEZ adjacent to the Hyderabad Airport. The applicant either through itself or its 100 per cent subsidiary or by a Special Purpose Vehicle (SPV) has proposed to set up a unit within the SEZ. The applicant has proposed to provide maintenance, repair and overhauling (MRO) facilities to domestic as well as foreign aviation entities. The applicant proposes to enter into a contract with an overseas entity located in Singapore who will procure contracts for MRO services from domestic and foreign airlines. The overseas entity will sub-contract to the applicant the contract for MRO services which will be carried out in the SEZ. The applicant will be paid in convertible foreign exchange by the overseas entity. The applicant also proposes to enter into direct contracts with domestic and foreign airlines who will pay the applicant in convertible foreign exchange.

The applicant proposes to carry out the entirety of the MRO services within the SEZ. According to the applicant the activity of repair gets concluded when the repair is carried out on the aircraft. Therefore, the service is received by the recipients as soon as the repair activity is carried out inside the SEZ. The consumption of the service is also therefore simultaneous.

The authority for advance rulings on the issue whether SEZ's are outside customs territory of India held that where the exempted goods/services entered into a SEZ are not utilised for authorised operations or are not duly accounted for, penal action can be taken against the entrepreneur or developer *inter alia* under the Customs Act, 1962 and other Customs Laws. In other words, Customs laws have been made applicable to SEZs in the SEZ scheme itself under specific situations. This provision complements the provisions of sub-section (1) of Section 53 of the SEZ Act and is a confirmation that SEZs have been declared as being outside the Customs territory of India for a specified purpose only that is, undertaking authorised operations.

A reference is also invited to Section 26 of the SEZ Act which lists out the exemptions from Customs and Excise duties for goods moving in and out of SEZ. If an SEZ were really deemed to be a territory outside India as the applicant would like to believe there was apparently

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no need for such an expansive list of exemptions & concessions. Infact there was no need to exempt goods from customs and excise duties under Indian laws when such goods are intended to be supplied to foreign lands. Likewise there was no need for granting exemptions under Section 7 of the SEZ Act from payment of taxes, duties or cesses under 21 different fiscal statutes listed in the First Schedule to the Act if SEZs were to be deemed to be territories outside India. Consequently all enactments (whether relating to fiscal levies, labour laws, banking laws or any other law) which apply to the territory of India apply in equal measure to the notified areas of special economic zones as well. If a particular law is applied to SEZs with modifications (the Income Tax Act, 1961 applied to SEZ under Section 27 of the SEZ Act), it cannot lead to an inference that other laws which may not have been specifically mentioned in the SEZ Act have no application to SEZs. All central laws apply to SEZs with modifications or exceptions, if any, as provided in the SEZ Act itself or in rules made thereunder.

Provision of Section 51 of the SEZ Act relating to the said Act having an overriding effect would need to be invoked only if any inconsistency is noticed between the provisions of the SEZ Act and any other law for the time being in force.

Section 64 of the Finance Act provides that Chapter V of the Act extends to the whole of India except the State of Jammu and Kashmir. Services provided to and from an entity in a SEZ are provided from India. Section 53(1) of the SEZ Act does not make the Finance Act, 1994 inapplicable to a SEZ. In the absence of any inconsistency there is no need to invoke section 51 of the SEZ Act.

Section 66A of the Finance Act, 1994 provides for levy of service tax under certain specified situations on services received from outside India. The applicant has claimed that since the MRO services are provided in a SEZ which according to him is outside India no such tax is leviable under the said provision. However, as discussed in the preceding paragraphs SEZs are deemed to be outside the customs territory of India only for undertaking authorised operations; all other enactments are applicable to the operations carried out in the SEZs. The MRO services would therefore be performed within the

territory of India and Section 66A will have no application in the context of these activities. The services provided by the applicant would be taxable under Section 66 of the said Finance Act, 1994.

The aforesaid MRO services provided by the applicant cannot also be considered as export of taxable services under the Export of Services Rules, 2005 since in terms of clause (ii) of Rule 3 (1) of the Export of Services Rules, services specified in sub-clause (zzg) of clause (105) of Section 65 of the Finance Act shall be considered as export only if such services are performed outside India. SEZs being part of India, performance of such services in the SEZs does not entitle them to be categorized as exports of taxable services.

It was to be concluded that:

- (i) Service tax is applicable on the services rendered by the applicant to the overseas entity for contract with:- (a) Domestic airlines who operate domestic flights to India; (b) Domestic airlines who operate international flights; and (c) Foreign entities who operate international flights.
- (ii) Service tax is applicable on the services rendered by the applicant directly to: (a) Domestic airlines who operate domestic flights to India; (b) Domestic airlines who operate international flights; and (c) Foreign entities who operate international flights.
- (iii) Service tax will be chargeable on the services rendered within the SEZ unless specifically exempted under the SEZ Act or under the Finance Act, 1994 or any Rules or Notifications there under. There is no such exemption presently available in respect of MRO services proposed to be provided by the applicant.
- (iv) MRO services proposed to be carried on by the applicant will be chargeable to service tax on an interpretation of Section 66A of the Finance Act, 1994 read with Rule 3(ii) of the Import of Service Rules
- (v) MRO services rendered to the overseas entity for: a) Domestic airlines who operate domestic flights to India; (b) Domestic airlines who operate international flights; and (c) Foreign entities who operate international flights. will not qualify as export of services under the Export of Service Rules, 2005. ■

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 are requested to use the citation/website or weblink to access the full text of desired circular/notification. Readers are requested to submit their feedback and suggestions on the coverage and utility of the column at eboard@icai.org.

DIRECT TAXES



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

I. Notifications

1. Notification No. 35/2011 dated June 23, 2011

The Central Government has, in exercise of the powers conferred by clause (v) of Explanation to section 48, specified the Cost Inflation Index for the financial year 2011-12 as 785.

2. Notification No.36/2011 dated June 23, 2011

Under section 139(1C), the Central Government may, by notification in the Official Gazette, exempt any class or classes of persons from the requirement of furnishing a return of income having regard to such conditions as may be specified in that notification.

Accordingly, the Central Government has, vide this notification, exempted an individual whose total income does not exceed ₹5 lakh from the requirement of furnishing a return of income under section 139(1) for A.Y.2011-12, if his total income consists of only income chargeable to income-tax under the head "Salaries" and interest, not exceeding ₹10,000, from savings bank account in a bank chargeable under the head "Income from other sources".

The other conditions to be satisfied by such individual to avail the benefit of this exemption are that he should have –

- (1) reported his PAN to his employer;
- (2) reported his interest income from savings bank account to his employer and his employer should have deducted tax thereon;
- (3) received Form 16 from his employer, wherein his PAN and details of income and tax deducted at source and deposited to the credit of the Central Government should be mentioned;
- (4) discharged his total tax liability for the assessment year through TDS and its deposit by the employer to the Central Government;
- (5) no claim for refund of taxes due to him for the income of the assessment year; and

- (6) received salary from only one employer for the assessment year.

Further, the exemption from the requirement of furnishing a return of income-tax shall not be available where a notice under section 142(1) or section 148 or section 153A or section 153C has been issued for filing a return of income for the relevant assessment year.

3. Notification No.37/2011 dated July 1, 2011

The Central Board of Direct Taxes has, through this notification, notified the Income-tax (Sixth Amendment) Rules, 2011. As per this notification, clauses (a) and (aa) of the proviso to Rule 12(3) have been substituted by new clauses (a) to provide that Firms/ individuals and HUF subject to tax audit are now mandatorily required to file return of income for A.Y.2011-12 and thereafter electronically under digital signature.

The complete text of the above notifications can be downloaded from: <http://law.incometaxindia.gov.in/DIT/Notifications.aspx>

II. Press Release

1. Press release No.402/92/2006-MC (15 of 2011) dated June 24, 2011

The Government of India has signed a protocol on June 24, 2011 amending Double Taxation Avoidance Agreement (DTAA) with Government of Singapore for effective exchange of information in the tax matters.

The complete text of the above-mentioned press release can be downloaded from: http://www.incometaxindia.gov.in/archive/PressRelease_DTAASingapore_06272011.pdf

INDIRECT TAXES



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

A. SERVICE TAX

I. Notification:

1. Notification No. 41/2011 ST dated June 27, 2011: Rule 7 of Point of Taxation Rules, 2011 has been amended to provide that point of taxation in case of taxable

consulting engineer's service would be the date on which payment is received or made. However, if the payment is not made within a period of six months of the date of invoice, the provisions of this rule would not apply.

B. CENTRAL EXCISE

I. Notification:

1. **Notification No. 15/2011-CE (NT) dated June 30, 2011:** Budget 2011-12 had withdrawn the exemption from central excise duty available on 130 items. A nominal duty of 1 % ad valorem has been imposed on these items with the condition that no credit of the duty paid on input and input services is taken. A new quarterly return "Form E.R.- 8" has been notified vide this notification which would be submitted by the assessee clearing goods by paying excise duty @ 1%.

II. Circular:-

1. **Circular No. 947/8/2011-CX dated June 21, 2011:** The Board has clarified that uniforms or made-up articles like quilt, blankets, towels, linen etc. bearing the name or logo of a school, security agency, company, hotel or airline etc. cannot be treated as "branded" products merely because the name of the school, institution or company or their logo is either printed, embroidered or etched on them as in all these cases, there is no nexus between such a name or logo & the product at the time of its sale which is essential ingredient in the definition of the term "brand name". It has been clarified that unless such garments/ made-ups also bear a brand name in addition to the name or logo of the school, security agency, hotels, airlines and company, such goods would not attract the excise duty. It may be noted that affixing of name of the tailor or manufacturer on such garments would also not constitute a brand name. Further, excise duty would also not be leviable on blankets which are supplied to the defence establishment, armed forces, police forces etc. against tenders that stipulate that the name of the manufacturer should be clearly indicated or marked on the product as affixing the name of the manufacturer on such goods would not, by itself, bring them within the ambit of branded goods. Presently, a certificate from a Chartered Accountant about the aggregate value of clearances for home consumption in the preceding financial year is accepted for the purpose of claiming the benefit of small scale exemption contained in *Notification No. 8/2003-CE dated 1.3.2003*. It has now been decided that self certification by a manufacturer may also be accepted for this purpose. Since, the Central Excise law does not prescribe any specific record which is to be maintained by such assessee, records

of production, clearance & purchases that are maintained for the purpose of VAT purposes can be accepted for purposes of central excise.

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

CORPORATE LAWS



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

1. Guidelines for Declaring Financial Institution as Public Financial Institutions under Companies Act, 1956

www.mca.gov.in

The MCA has issued General Circular 34/2011 dated June 2, 2011 stating that in terms of section 4A(2) of the Companies Act, 1956 the Central Government is empowered to notify in the Official Gazette such institutions as it may think fit to be a public financial institution (PFI). In the past, the MCA was declaring an institution as a PFI if it meets any one of clauses (i) and (ii) of section 4A(2) of the Act. Now, the MCA has framed the following criteria for declaring any financial institution as a PFI:

- a) A company or corporation should be established under a special Act or the Companies Act being Central Act;
- b) Main business of the company should be industrial/ infrastructural financing;
- c) The company must be in existence for at least three years and their financial statement should show that their income from industrial/ infrastructural financing exceeds 50% of their income;
- d) The net-worth of the company should be ₹1,000 crore;
- e) The company is registered as infrastructure finance company (IFC) with the RBI or as a housing finance company (HFC) with the National Housing Bank;
- f) In the case of CPSUs/SPSUs, no restriction shall apply with respect to financing specific sector(s) and net-worth.

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

2. The Companies (Cost Audit Report) Rules, 2011

www.mca.gov.in

The MCA has issued Notification No. G.S.R. 430(E) dated June 3, 2011 notifying the Companies (Cost Audit Report) Rules, 2011. These rules shall apply to every company in respect of which an audit of the cost records has been ordered by the Central Government under section 233B(1) of the Companies Act, 1956. The rules specify the manner and mode of appointment of a cost auditor, form of cost audit report, timeline for submission

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of the cost audit report, rights of cost auditor in relation to the production of the accounting records, penalty for contravention of the rules, etc. One may refer to the above citation and website for further details.

3. Clarification on Rates of Depreciation for Purpose of Declaration of Dividend by the Generation/Supply of Electricity Companies

www.mca.gov.in

The MCA has issued General Circular No. 31/2011 dated June 6, 2011 in relation to providing depreciation for the purpose of declaration of dividend under section 205 in case of companies referred to in section 616(c) and it was noticed by the MCA that despite having clear provision in section 616(c) of the Companies Act, 1956, companies engaged in generation/supply of electricity are approaching the MCA for fixing rate of depreciation in individual cases. The MCA has clarified that section 616(c) of the Companies Act, 1956 provides that the same shall apply to companies engaged in the generation or supply of electricity except insofar as the said provision is inconsistent with the provisions of the Indian Electricity Act, 1910 or the Electricity Supply Act, 1948 as repealed by enactment of the Electricity Act, 2003. The Ministry of Power had, vide resolution dated January 6, 2006 notified the Tariff Policy in terms of section 3 of the Electricity Act, 2003 which provides that rates of depreciation as notified by the Central Electricity Regulatory Commission (CERC) would be applicable for the purpose of tariffs as well as for accounting. The CERC, while notifying the regulation vide Notification dated 19-1-2009, in exercise of powers conferred under section 178 of the Electricity Act, 2003, had also notified the rates of depreciation as well as the methodology for computing such depreciation and which is to be provided up to 90% of the cost of asset. Since the rates of depreciation and the methodology notified under Electricity Act, 2003 are inconsistent with the rates given in Schedule XIV of the Act and the former being special Act, it shall prevail over the rates notified under Schedule XIV of the Companies Act by virtue of section 616(c) of the Companies Act. Accordingly, it is clarified that companies referred to in section 616(c) of the Companies Act can distribute dividend out of profit arrived at after providing for depreciation following the rates as well as methodology notified by CERC and the same shall be sufficient compliance of section 205 of the Companies Act, 1956. One may refer to the above citation and website for further details.

4. Guidelines for Fast Track Exit Mode for Defunct Companies

www.mca.gov.in

The Ministry of Corporate Affairs ("MCA") has issued General Circular No. 36/2011 dated June 7, 2011 in relation to giving an opportunity for fast track exit to a

defunct company, for getting its name struck off from the register of companies. The MCA has stated that there are a number of companies which are registered under the Companies Act, 1956, but due to various reasons are inoperative since their incorporation or which have commenced business but became inoperative or defunct later on. Such companies may be desirous of getting their names strike off from the register of companies maintained by Registrar of Companies. In terms of section 560 of the Companies Act, 1956, the Registrar of Companies (ROC) may strike off the name of such companies on satisfying the conditions and as per present practice, a company desirous of getting its name struck off has to apply to the ROC in e-form 61 and that all pending statutory returns are required to be filed along with e-form 61. The MCA has decided to modify the existing route through e-form 61 and has prescribed new Guidelines for "Fast Track Exit mode" for defunct companies under section 560 of the Companies Act, 1956. The guidelines stipulate and provide the definition of a 'defunct company', types of companies eligible and procedure to be adopted by such companies and by the ROC and also provides the format of affidavit and indemnity bond for the purpose. One may refer to the above citation and website for further details.

5. Additions to Notified Financial Institutions u/s 4A of Companies Act, 1956

www.mca.gov.in

The MCA has issued Notification No. SO-1355(E) dated June 10, 2011 whereby it has notified the following financial institutions as notified financial institutions in terms of section 4A(2) of the Companies Act, 1956:

- Gujarat Industrial Investment Corporation Limited.
- Andhra Pradesh Industrial Development Corporation Limited.
- Karnataka Urban Infrastructure Development and Finance Corporation Limited.
- L&T Infrastructure Finance Company Limited.

6. Mandatory Filing for Defaulting Companies – Section 610

www.mca.gov.in

The MCA has issued Circular No. 38 dated June 20, 2011 whereby it has stated that in order to ensure corporate governance and proper compliances of provisions of Companies Act, 1956, no request, whether oral, in writing or through e-forms, for recording any event based information/changes shall be accepted by the ROC from such defaulting companies, unless they file their updated balance sheet and profit and loss accounts and the annual return with the ROC. In order to have better understanding of the circular, it is now further clarified that this requirement would also be applicable to those defaulting companies and their Directors which have not

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filed the balance sheet or the annual return for any of the financial years 2006-07, 2007-08, 2008-09 and 2009-10 with the ROC as required by section 220 and/or 159 of the Companies Act, 1956. This requirement shall be effective from July 3, 2011. One may refer to the above citation and website for further details.

7. Amendment to Filing of Financial Statements under XBRL Mode

www.mca.gov.in

The MCA has issued General Circular No. 43/2011 dated July 7, 2011 clarifying that the filing on the MCA 21 portal in the XBRL mode will be effective in respect of financial statements closing on or after 31 March, 2011 instead of the year 2011-12. It is also provided by this Circular that besides signing by signatories as specified by section 215 of the Companies Act, 1956, the statutory auditor has to certify the financial statements prepared in XBRL mode for filing on MCA-21 portal. Also, phase-1 class of companies as per earlier MCA Circular 9/2011 dated 31 March, 2011 and later exempted from XBRL filing (under Power sector, Insurance sector, NBFC and Banking sector) who are unable to file their financial statements would be exempted from additional fee due to delay in filing up to September 30, 2011. One may refer to the above citation and website for further details.

8. Integration of DIN and DPIN

www.mca.gov.in

The MCA has issued General Circular No. 44/2011 dated July 8, 2011 in relation to integration of the Director's Identification Number (DIN) issued under the Companies Act, 1956 with the Designated Partnership Identification Number (DPIN) issued under Limited Liability Partnership (LLP) Act, 2008. Currently, the MCA has been issuing two separate identification numbers as DIN to an individual for becoming a director of a company under Companies Act, 1956 and DPIN for a partner in an Limited Liability Partnership under the Limited Liability Partnership (LLP) Act, 2008. To avoid this duplicity and give ease to the stakeholders, the MCA has decided to issue only one identification number to an individual for both the purposes. Hence, with effect from July 9, 2011 no fresh DPIN will be issued and any person, who desires to become a designated partner in an LLP has to obtain DIN by filing e-form DIN-1. If DIN has already been allotted, it shall also be used as DPIN for all purposes under the LLP Act, 2008. Similarly, if a person has been allotted DPIN, it will also be used as DIN for all purposes under the Companies Act, 1956. And, if a person has been allotted both DIN and DPIN, the DPIN will stand cancelled and DIN will be used as DIN as well as DPIN for all purposes under the LLP Act, 2008 and the Companies Act, 1956.

It is also stated in this Circular that in terms of Circular no. 32/2011 dated May 31, 2011, the MCA has

made Income Tax Permanent Account Number (PAN) mandatory for obtaining DIN for Indian nationals. Further, all existing DIN holders, who have not furnished their PAN at the time of obtaining DIN, are required to furnish their PAN to the MCA by filing e-form DIN-4 by September 30, 2011. Similarly, all DPIN holders, who had not furnished their PAN at the time of obtaining DPIN, are required to furnish their PAN to the Ministry by filing e-form DIN-4 by 30 September, 2011, failing which their DPIN/DIN will be disabled and they will also be liable for penalty. One may refer to the above citation and website for further details.

9. Name Availability Guidelines, 2011

www.mca.gov.in

The MCA has issued General Circular No. 45/2011 dated July 8, 2011 superseding of all the previous circulars and instructions issued by MCA regarding name availability. All the applicants and the ROCs are advised to adhere to the revised guidelines while applying for, or approving, a name. Under the provisions of section 20 of the Companies Act, 1956, no company is to be registered with undesirable name or if it is identical with or too nearly resembling with:

- Name of a company in existence and names already approved by the ROC;
- Name of an LLP in existence or names already approved by the Registrar of LLP;
- A registered trade-mark or a trade-mark which is subject of an application for registration, of any other person under the Trade Marks Act, 1999.

It is also stated in the Circular that while applying for a name in the prescribed e-form-1A, using Digital Signature Certificate (DSC), the applicant shall be required to furnish a declaration to the effect that he has used the search facilities available on the portal of the MCA, i.e. www.mca.gov.in/MCA21, for checking the resemblance of the proposed name(s) with the companies and LLPs already registered or the names already approved. If this declaration is certified by a professional, the name will be made available by the system online to the applicant without backend processing by the ROC. This facility is not available for applications for change of name of existing companies. The name, if made available to the applicant, shall be reserved for sixty days. In case of a foreign company incorporating its subsidiary company, then the original name of the holding company as it is may be allowed with the addition of word India or name of any Indian state or city, if otherwise available. Change of name shall not be allowed to a company which is defaulting in filing its due annual returns or balance sheets or which has defaulted in repayment of matured deposits and debentures and/or interest thereon. These guidelines and revised e-form 1A would be implemented with effect from 24 July, 2011. One may refer to the above citation and website for further details and the revised forms.

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10. Issue of Certificate by Digital Signature - List of Certificates to be issued by RoC Notified

www.mca.org.in

The RBI has issued General Circular No. 39/2011 dated June 21, 2011 in relation to its earlier dispensations whereby it was informed that in order to cut timelines and another step towards 'green initiative', it has been decided that all certificates and standard letters issued by the ROC will now be issued electronically under the Digital Signature of the ROC. The MCA has already developed thirteen such digitally signed certificates and the same has been implemented under MCA-21 system as mentioned below:

S. No.	Certificate Description	Form ID	Implementation date
1	Certificate of Registration for Modification of Mortgage, etc. u/s 132 read with section 135 of the Companies Act, 1956. (STP)	Form 8	29-May-11
2	Memorandum of Satisfaction of Mortgage, etc., Section 140 of the Companies Act, 1956 (STP)	Form 17	29-May-11
3	Certificate of Registration of Mortgage, etc. Under Section 132 of the Companies Act, 1956 (STP)	Form 8	29-May-11
4	Certificate of Incorporation	Form 1	12-Jun-11
5	Certificate for Establishment of Place of Business In India	Form 44	12-Jun-11
6	Certificate of Registration for Modification of Mortgage, etc. u/s 132 read with section 135 of the Companies Act, 1956. (NON STP)	Form 8	12-Jun-11
7	Memorandum of Satisfaction of Mortgage, etc., Section 140 of the Companies Act, 1956 (NON STP)	Form 17	12-Jun-11
8	Certificate of Registration of Mortgage, etc. Under Section 132 of the Companies Act, 1956 (NON STP)	Form 8	12-Jun-11
9	Fresh Certificate of Incorporation Consequent upon Change of Name	Form 1B	12-Jun-11
10	Fresh Certificate of Incorporation Consequent upon Change of Name on Conversion to Public Limited Company	Form 62	12-Jun-11
11	Certificate of Registration of Company Law Board order for Change of State	Form 18	12-Jun-11

12	Certificate of Registration of the Special Resolution Confirming Alteration of Object Clause(s)	Form 23	12-Jun-11
13	Fresh Certificate of Incorporation Consequent upon Change of Name on Conversion to Private Limited Company	Form 1B	12-Jun-11

It is also clarified that the remaining certificates are planned to be implemented by July 3, 2011. The Registrar of Companies are advised that after the date of implementation of Digital Certificates, no certificates shall be issued manually. All such pending certificates which are required to be issued manually should be issued by June 30, 2011. One may refer to the above citation and website for further details.

11. Change in Constitution -- Grant of Prior Approval to Members of Stock Exchanges/Sub-brokers

www.sebi.gov.in

The SEBI has issued Circular No. CIR/MIRSD/2/2011 dated June 3, 2011 whereby it has stated that the requirement of members of the stock exchanges and sub-brokers to obtain prior approval from SEBI for change in status or constitution has been done away with and that the members of the stock exchanges would be required to take prior approval from SEBI for change in control. It is clarified that the stock exchanges will continue to grant prior approval to their members and sub-brokers for change in status or constitution, which would include:

- in case of a body corporate, amalgamation, demerger, consolidation or any other kind of corporate restructuring covered by section 391 of the Companies Act, 1956 (1 of 1956) or the corresponding provision of any other law for the time being in force and for change in its managing director, whole-time director or director appointed in compliance with rule 8(4A)(v) of the Securities Contracts (Regulation) Rules, 1957 and any change in control over the body corporate;
- any change between the legal forms like individual, partnership firm, Hindu undivided family, private company, public company, unlimited company or statutory corporation and other similar changes;
- in case of a partnership firm any change in partners not amounting to dissolution of the firm;
- any other purpose as may be considered appropriate by the stock exchanges

It is provided that the stock exchanges shall submit a periodical report with details of the changes in status or constitution of the members / sub-brokers, as per the format and in accordance with guidelines given at Annexure A to this Circular. One may refer to the above citation or website for further details.

12. Shareholding of Promoter/Promoter Group to be in Dematerialised Mode

www.sebi.gov.in

The SEBI has issued Circular No. Cir/ISD/3/2011 dated June 17, 2011 in relation to its earlier dispensation on "trading rules and shareholding in dematerialised mode" whereby in order to moderate sharp and destabilising price movements in shares of companies, to encourage better price discovery and to increase transparency in securities market, it was mandated that securities of companies are to be traded in normal segment, if and only if, the company has achieved at least 50% non-promoter shareholding in dematerialised form and maintained the same on a continuous basis. Now, in order to further promote dematerialisation of securities, encourage orderly development of the securities market and to improve transparency in the dealings of shares by promoters including pledge/usage as collateral, SEBI in consultation with Stock Exchanges, has decided that the securities of companies shall be traded in the normal segment of the exchange, if and only if, the company has achieved 100% of promoter's and promoter group's shareholding in dematerialised form latest by the quarter ended September 2011 as reported to the stock exchanges. Where the companies do not satisfy the above criteria, the trading in securities of such companies shall take place in trade-for-trade segment. For this purpose, the exchanges shall take the latest shareholding pattern as required to be submitted by the listed companies with exchanges in pursuance to the listing agreement as of the preceding quarter or of any subsequent date. One may refer to the above citation and website for further details.

13. Periodical Report -- Grant of Prior Approval to Bankers to an Issue, Debenture Trustees, Depository Participants, and Credit Rating Agencies

www.sebi.gov.in

The SEBI has issued Circular No. CIR/MIRSD/8 to 11/2011 dated June 20, 2011 in relation to the requirement of taking prior approval by the Bankers to an Issue from SEBI for change in status or constitution which has been now dispensed with. However, the Bankers to an Issue would be required to take prior approval from SEBI for change in control. It is now clarified that commencing from the quarter ended June 30, 2011, all Bankers to an Issue shall report the following change(s) to SEBI in their quarterly reports

- a) Amalgamation, demerger, consolidation or any other kind of corporate restructuring covered by section 391 of the Companies Act, 1956 (1 of 1956) or the corresponding provision of any other law for the time being in force
- b) Change in director, including managing director/whole-time director



- c) Change in shareholding not resulting in change in control.

If there is no change during the relevant quarter, it shall be indicated in the report. Similar circulars are also issued for SEBI (Debenture Trustees) Regulations, 1993, SEBI (Depositories and Participants) Regulations, 1996 and SEBI (Credit Rating Agencies) Regulations, 1999. One may refer to the above citation and website for further details.

14. Admission of LLP as Members of Stock Exchanges

www.sebi.org.in

The SEBI has issued Circular No. CIR/MIRSD/12/2011 dated July 11, 2011 in permitting members of stock exchanges to change their constitution as that of an LLP. This was based on requests from various stock exchanges to permit LLP to be admitted as members of stock exchanges so as to enable them to get registration as stock broker under SEBI (Stock brokers and Sub-brokers) Regulations, 1992. It is clarified in this Circular that the Securities Contract Regulation Rules, 1957 (SCRR) do not explicitly mention LLPs as the LLP Act, 2008 was a subsequent development and as per the LLP Act, LLP is a body corporate. Sub-rule 4A and 5 of Rule 8 of the SCRR provides that Limited Liability Companies (LLC) and partnership firms are eligible to be admitted as members of stock exchanges and in this context LLPs are akin to LLC and partnership firms. Hence, as the Parliament has put in place a legal framework for LLPs, stock exchanges may consider granting membership to LLPs subject to the LLP complying with the conditions laid down in Rule 8(4A) of the SCRR, as far as it applies to LLPs. One may refer to the above citation for further details.

FEMA

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

1. Opening of Branch / Subsidiary / Joint Venture / Representative Office or Undertaking Investment abroad by Non-Banking Financial Companies (NBFCs)

Circular No. DNBS(PD) CC. No. 222 /03.10.001/2010-11 dated June 14, 2011

Notification No. DNBS(PD) 229/CGM(US)/2011 dated June 14, 2011

In terms of Regulation 7 of Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004, an Indian party requires prior approval of the concerned regulatory authorities both in India and abroad, to make an investment in an entity outside India engaged in financial services activities.

RBI had vide its circular DNBS (PD).CC. No.173/03.10.01 /2009-10 dated May 3, 2010 advised that all NBFCs desirous of making any overseas investment must obtain "No Objection" (NoC) of the Department of Non-Banking Supervision of RBI before making such investment, from its Regional Office in whose jurisdiction the head office of the company is registered. A NoC in this regard will be issued by RBI to a NBFC, subject to the NBFC fulfilling the conditions enumerated in the NBFC (Opening of Branch/Subsidiary/Joint Venture/Representative Office or Undertaking Investment abroad by NBFCs) Directions, 2011 issued by RBI vide Notification No. DNBS(PD)229/CGM(US)/2011 dated June 14, 2011. These directions are in addition to those prescribed by Foreign Exchange Department of RBI for opening of branches abroad or for investments in Joint Venture/Wholly Owned Subsidiary.

The above circular and notification are available on RBI website at:

<http://www.rbi.org.in/scripts/NotificationUser.aspx?id=6460&Mode=0>

2. Discussion Paper on FDI Policy - Rationale and Relevance of Caps issued by Department of Industrial Policy & Promotion (DIPP)

DIPP has, on June 23, 2011 issued a discussion paper on "FDI Policy – Rational and Relevance of Caps" with an objective to examine whether some elements of FDI policy need to be reviewed and invited comments from all the stakeholders by July 15, 2011.

The above discussion paper is available on DIPP website at:

http://www.dipp.nic.in/DiscussionPapers/DiscussionPaper_relevance_23June2011.pdf

3. Liberalisation / Rationalisation of Overseas Direct Investment (ODI)

Circular No.: A.P. (DIR Series) Circular No.73 dated June 29, 2011

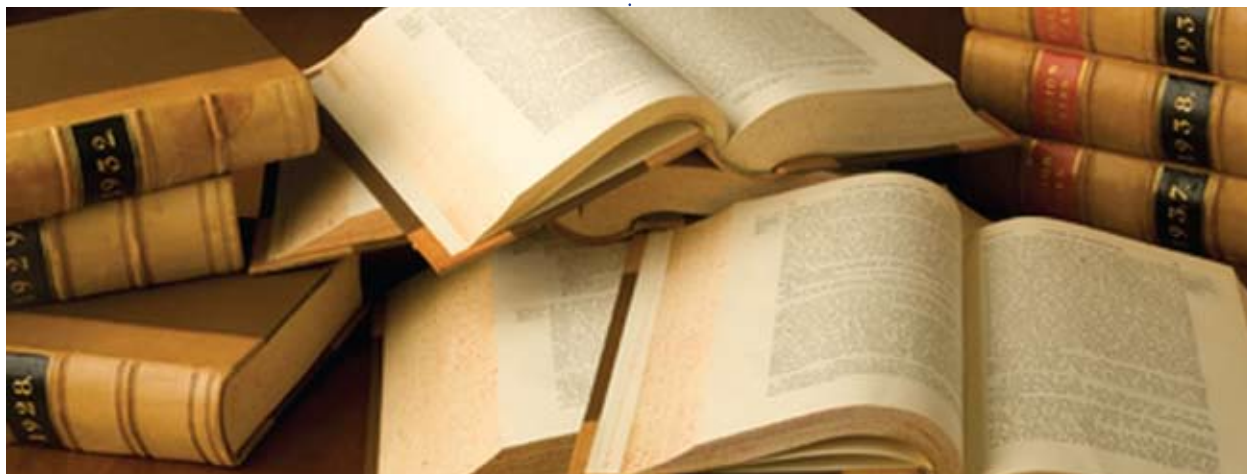
Ref.: Circular No.: A.P. (DIR Series) Circular No.69 dated May 27, 2011

With a view to restating the various provisions relating to transfer by way of sales of a joint venture (JV) or wholly owned subsidiary (WOS) outside India with and without write off, RBI has on June 29, 2011 issued circular consolidating the existing guidelines in this regard as under:

1. Transfer by way of sale of shares of a JV / WOS

An Indian Party, without prior approval of RBI, may transfer by way of sale to another Indian Party (which complies with the provisions of Regulation 6 of FEMA Notification 120/RB-2004 dated July 7, 2004) or to a person resident outside India, any share or security held by it in a JV or WOS outside India subject to the following conditions:

- (i) the sale does not result in any write off of the investment made.
- (ii) the sale is to be effected through a stock exchange where the shares of the overseas JV/ WOS are listed;
- (iii) if the shares are not listed on the stock exchange and



the shares are disinvested by a private arrangement, the share price is not less than the value certified by a Chartered Accountant / Certified Public Accountant as the fair value of the shares based on the latest audited financial statements of the JV / WOS;

- (iv) the Indian Party does not have any outstanding dues by way of dividend, technical know-how fees, royalty, consultancy, commission or other entitlements and / or export proceeds from the JV or WOS;
- (v) the overseas concern has been in operation for at least one full year and the Annual Performance Report together with the audited accounts for that year has been submitted to the Reserve Bank;
- (vi) the Indian party is not under investigation by CBI / DoE/ SEBI / IRDA or any other regulatory authority in India.

2. Transfer by way of sale of shares of a JV / WOS involving write off of the investment

Indian Parties may disinvest, without prior RBI approval in the following cases where the amount repatriated on disinvestment is less than the amount of the original investment, subject to the conditions listed above at items (ii) to (vi):

- (i) in cases where the JV / WOS is listed in the overseas stock exchange;
- (ii) in cases where the Indian Party is listed on a stock exchange in India and has a net worth of not less than Rs.100 crore;
- (iii) where the Indian Party is an unlisted company and the investment in the overseas venture does not exceed USD 10 million and
- (iv) where the Indian Party is a listed company with net worth of less than ₹100 crore but investment in an overseas JV/WOS does not exceed USD 10 million.

The Indian Party is required to submit details of such disinvestment through its designated AD category-I bank within 30 days from the date of disinvestment. An Indian Party, which does not satisfy the conditions stated above, shall have to apply to RBI for prior permission.

4. Foreign Direct Investment (FDI) in India - Issue of equity shares / preference shares against import of capital goods / machineries / equipments and Pre-operative/pre-incorporation expenses, under the Government route

Circular No.: A.P. (DIR Series) Circular No.74 dated June 30, 2011

Consequent to the amendment in Consolidated FDI Policy issued by the Department of Industrial Policy & Promotion vide Circular 1 of 2011 dated March 31, 2011, RBI has decided to permit issue of equity shares / preference shares for the following categories of transactions under the Government route of the FDI scheme subject to



compliance of the conditions prescribed in the aforesaid circular:

1. Import of capital goods/ machineries / equipments (including second-hand machineries)
2. Pre-operative/pre-incorporation expenses (including payments of rent, etc.)

All requests for conversion should be accompanied by a special resolution of the company. Government's approval would be subject to pricing guidelines of RBI and appropriate tax clearance.

The above circular and notification are available on RBI website at:

<http://www.rbi.org.in/scripts/NotificationUser.aspx?Id=6489&Mode=0>

5. Buyback / Prepayment of Foreign Currency Convertible Bonds (FCCBs)

Circular No.: A.P. (DIR Series) Circular No.75 dated June 30, 2011

RBI has, on June 30, 2011, extended the time limit for premature buyback of FCCBs from June 30, 2011 to March 31, 2012 subject to compliance of all the terms and conditions of buyback/ prepayment of FCCBs, as prescribed. Further RBI has liberalised the procedure for such buy-back as described in the circular in detail.

The above circular is available on RBI website at:

<http://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=6490&Mode=0>

6. Redemption of FCCBs

Circular No.: A.P. (DIR Series) Circular No.01 dated July 04, 2011

RBI has, on July 4, 2011, allowed the Indian companies to refinance the outstanding FCCBs subject to compliance with certain conditions prescribed in the circular.

Restructuring of FCCBs involving change in the existing conversion price is not permissible. However, proposals for restructuring of FCCBs not involving change in conversion price will be considered under the approval route depending on the merits of the proposal.

The above circular is available on RBI website at:

<http://www.rbi.org.in/scripts/NotificationUser.aspx?Id=6596&Mode=0>

[illegible]

(The author is Chairman, Insurance Regulatory and Development Authority [IRDA]. He can be reached at chairman@irda.gov.in)

during the earlier period with the four subsidiaries competing with each other in the non-life arena, and the lone player in the life sector consolidating by leaps and bounds; it was always felt that the

flavour of competition has been conspicuous by its absence. The privatisation introduced during the late last decade of the twentieth century has brought in a new sense of competitive spirit in the players; apart from the introduction of some world-class players into the Indian domain. All this has certainly added a new dimension to the very aspect of insurance business in India.

A cursory look at some of the statistics will certainly add credence to the type of growth achieved over the last ten years. There are currently nearly two dozen players each in the life and non-life domains; and the number has been growing steadily over the last few years. It goes to show the keenness of the players to tap the immense potential that is available in the country. The total first year premium of life insurers (during the financial year 2010-2011) which reflects the new business secured during the year stood at ₹1,25,826 crore, registering a growth of nearly 15 per cent over that of the previous year. The non-life insurers, apart from the stand-alone health insurers, underwrote a total premium of ₹42,569 crore as against the previous year's figures of ₹35,816 crore registering a healthy growth of nearly 16 per cent. Apart from the tremendous business growth, the investments of the insurance companies have attained significantly large volumes which play a major role in the overall economic development of the country. For example, the investment portfolio of life insurers as at the end of the financial year 2009-2010 showed a whopping figure of ₹12,05,155 crore and that of non-life insurers stood at ₹66,372 crore.

The three specialists in health insurance mustered a total business of ₹1,529 crore during the year which is more than 44 per cent higher than the previous

year's performance. Even among the regular non-life insurance companies, health insurance as a class has grown tremendously which is a very positive trend in a domain where the total coverage – including the government sponsored schemes – of the population under any arrangement for health-related coverage does not go beyond 10 per cent to 12 per cent. While there are a few problems associated with this class mainly owing to the low awareness levels, we have been addressing the issues progressively on an on-going basis; and it is expected that this class of insurance will demonstrate even greater purpose-oriented growth during the years to come. Portability of Health insurance, issues pertaining to the Third Party Administrators, standard treatment protocols, etc. are some of the top priorities for

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us and we are confident that there will be a lot of ground gained in the near future.

There have been several regulatory developments that have been very significant for the growth of the industry in the post-liberalisation period. To quote some of the important ones, detariffing of the non-life arena has been a very important milestone. It was being felt that despite the opening-up of the industry, an administered pricing stifled the freedom of the players. After a series of checks for assessing the maturity of the players to handle the freedom, it was eventually felt that the Indian insurance market is mature enough for the pricing freedom. It is gratifying to note that the confidence reposed in the players has not been belied and we have not had an occasion to intervene in the day-to-day affairs of any player. However, we have been exhorting the players of the importance of their achieving operational surpluses and not depending unduly on their investment incomes to offset their underwriting losses. In a scenario that typically demonstrates a high volatility in the interest rates, it is common knowledge that undue dependence on investment incomes would be highly risky.

The Indian insurance market has been exclusively agency-driven, historically. While several milestones have been achieved with the 'agent' being the centre of all activity, the professionalism associated with intermediation was felt to be greatly limited – especially in designing the vital risk management function of corporate entities. Accordingly, several distribution channels like brokers, corporate agents, bancassurance, etc. have been introduced in the liberalised regime; and have been operating successfully along with the ubiquitous agent. It was

often expressed by the clientele as also by the media that there is an element of mis-selling by the intermediaries. We have taken several measures to ensure that this trend is arrested; and subsequent results have indicated that there is vast improvement in this regard.

In a domain that is typically representative of low awareness levels, there is need for identifying all areas that need to be consolidated in empowering the client. One way of achieving this is by ensuring that the distribution channels are thoroughly professional; and that they fulfill their role of need-identification, followed by a need-based selling. We have taken several measures to achieve this and a constant review of the training needs of the distributor is a step in this direction. Further, there should be ways of ensuring that the awareness levels of the insuring public itself improve over a period of time. This would go a long way in setting at rest most problems associated with mis-selling, problems of adverse selection, doing away with litigation that leads to a no-win situation, controlling frauds, etc. We have been actively taking several measures to improve the understanding levels of the average policyholder through conduct of seminars, press releases, sponsorship of educational programs in the radio and visual media etc. Besides, the players themselves are encouraged to promote healthy campaigns that contribute towards a steady rise in the awareness levels of the policyholders and prospects.

Despite all the measures being taken by the regulator and the players, there is a huge role for every stakeholder to participate in a campaign of such an importance. The basics of the operation of the insurance contracts need to be understood even by the policy-

Apart from the average rise in the awareness levels of the general populace through various methods, specific professionals like the Chartered Accountants have a huge role to play – especially in the corporate sector. With their vast understanding of the financial services, CAs are typically positioned to be excellent ambassadors of the cause of spreading the importance of risk management that would eventually lead to protection of invaluable assets. Further, being an important component of some of the professional roles like surveyors and loss assessors, Chartered Accountants can be very effective mediators between the insurers and the insured in reducing avoidable controversies and insurance related litigation.”

holder belonging to the lowest stratum of the society in order that the growth of the insurance industry itself is based on sound business ethics. Only such a regime will ensure that several misconceptions associated with the industry are set at naught; and the industry makes steady progress with the average buyer volunteering to buy insurance rather than being driven to do it.

Apart from the average rise in the awareness levels of the general populace through various methods, specific professionals like the Chartered Accountants have a huge role to play – especially in the corporate sector. With their vast understanding of the financial services, CAs are typically positioned to be excellent ambassadors of the cause of spreading the

importance of risk management that would eventually lead to protection of invaluable assets. Further, being an important component of some of the professional roles like surveyors and loss assessors, Chartered Accountants can be very effective mediators between the insurers and the insured in reducing avoidable controversies and insurance related litigation. In the aftermath of large corporate failures globally, the emphasis on financial reporting on public domains in order to enable the user to draw his own conclusions has been gaining lot of importance. The CAs can play the role of enabling the players to successfully fulfilling this function, on one hand; and enabling the users to make a proper interpretation of the details, on the other effectively, thus contributing to the accomplishment of a strong domain. There has also been growing importance of compliance with statutory/regulatory requirements in order that the incidence of financial scams and/or corporate debacles is kept in check. It is a Chartered Accountant who is best placed to handle such assignments in view of his ability to understand the requirements and successful reporting – no wonder that most compliance officers in large corporate undertakings are CAs.

Above all, there is growing importance of attaining uniform standards of reporting in financial services, globally. While the task is stupendous, the Chartered Accountant can contribute a lot towards proper interpretation of the standards; and their adoption by the Indian corporate domain so that in the end we move towards attaining global standards in terms of business achievements as also a proper reporting.

IRDA & ICAI

Apart from the very generalised role play for CAs mentioned above,

there is a lot that CAs can do for the betterment of the Indian insurance industry; and in pursuit of this, IRDA, from the very beginning, had a close association with ICAI. IRDA was of the view that it should retain its inherent powers to decide the way the insurance business is to be regulated but involve ICAI and take its suggestions/recommendations in policy matters relating to accounting, audit and investments. It was thus in 1999 that IRDA constituted Accounting Committee and approached ICAI to nominate Chartered Accountants of repute and stature to lay down standards in framing IRDA's Accounting and Investment Regulations. IRDA felt that it would be appropriate that the accounting committee be made as a Standing Committee on Accounting Issues (SCAI) and have members primarily drawn from the CA profession with merit and stature to advise the IRDA on matters within their domain. Today the vice president in the office of the ICAI represents the profession in the SCAI. The SCAI is headed by a past President of ICAI, and has practicing members from ICAI,

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the insurance business is to be regulated but involve ICAI and take its suggestions/recommendations in policy matters relating to accounting, audit and investments. It was thus in 1999 that IRDA constituted Accounting Committee and approached ICAI to nominate Chartered Accountants of repute and stature to lay down standards in framing IRDA's Accounting and Investment Regulations.

Actuarial Society of India, CAs from the industry (representing Life and Non-Life Business both from PSUs and private sector), and CAs who specialise on security systems, to advise IRDA on policy matters relating to:

1. Specific needs of accounting, auditing and investments of the insurance industry covering both Life and Non-Life Business
2. IFRS-4 on insurance contracts, IFRS-7 on financial instruments and to suggest a roadmap to implement the recommendations of IFRS committee of IRDA
3. Adoption of accounting and auditing standards for both Life and Non Life business
4. Insurance industry specific standards, valuation procedure, disclosure norms under accounting regulations
5. Norms for revenue recognition, provisioning and assets classification
6. Regulations of investments of Life and Non-Life insurers
7. Best practices under investment risk management systems and process
8. Periodical reporting and formats for such reporting under accounting and investment regulations
9. Other policy issues relating to accounting, investment and audits as may be referred to the committee

International Standards on Investments

As the Indian economy is growing at a fast pace, it is important that it has strong and robust systems that meet the minimum international standards that are mandated by International Association of Insurance Supervisors (IAIS). It may be seen that insurance investments grew from around ₹1 lakh crore in the year 2000, when the sector

was opened for private players, to a staggering ₹14 lakh crore in 2010. As the investments represent the policyholders' money which requires to be protected, IRDA felt the need for tighter controls which at least meet the minimum standards of IAIS in respect of:

- a. Investment Asset Mix
- b. Diversification (Spread) of investment risk
- c. Classification of investments
- d. Investment management structure
- e. Risk management systems
- f. Systems to prompt the regulator of any systemic issues
- g. Other Regulations:
 1. Safe keeping of assets
 2. Preventing insider trading
 3. Asset-Liability Management
 4. Standard Operating Procedure (SOP)
 5. Contingency plans to mitigate effects of deteriorating condition

Need for a Different Approach

The humongous insurance investments with demanding international standards mandated by IAIS; and business needs along with technology development in the financial market required a robust system to be put in place. To address these fast paced developments, IRDA, in 2008 amended the investment regulations to address the growing complexity of insurance investments, both under traditional and unit linked platform. Such amendments should take into consideration the following, which are very specific to insurance:

- a. The insurance liabilities represent the present value of future liability. Hence the regulations, apart from addressing the liabilities, should also address 'Solvency' needs.
- b. As the Insurance Act does not permit liabilities to be funded through borrowings, a few more safe avenues should

be permitted to generate investment income.

- c. As payouts depends on 'contingent' event, and is a 'process', liquidity needs are factored in investment policy, and should be enabled through regulations
- d. As insurers are 'Risk Carriers', insurance investments are to be held in 'safe' assets. Hence, regulations limit the exhaustive category of investments. The audit mechanism put in place should ensure that investments are not made beyond the categories and limits permitted under the regulations.
- e. Standards mandated should be same for both state-owned and private players – providing a level-playing ground; and the best available technology for a 'dynamic' monitoring/reporting should be put in place.
- f. Investment operation, being dynamic, for an effective control should be based on 'Exception' reporting

Monitoring Systems – IRDA's Methodology

The total insurance industry investments, as at 31st March, 2011 are around ₹14 lakh crore. Regulators globally usually do not have the adequate numbers of and/or adequately trained staff to fully and effectively carry out the supervision mandate. As such, to rely on professional bodies is inevitable. As ICAI is a regulator of Chartered Accountants who play a key role in certifying and attesting the various activities in an insurance company, IRDA had engaged ICAI in laying down the standards in the area of accounting and investments; and systems relating to these functions. Hence, the model that is in place engages CAs to carry out the audits as per the procedures laid down by ICAI.

To put it differently, the chartered accountant is the regulator at the insurer's office. But the key is to lay down standards for such audits, so that the regulator's control requirements (both systems and transaction) are fully addressed.

Toward the above, IRDA introduced the systems audit to be certified through CAs; and the transactions process through such systems to be audited through concurrent audit by CAs so that IRDA secures a good hold on an extremely huge portfolio in a country which has the second highest population in the world. Thus by engaging CAs through ICAI, the monitoring mechanism of IRDA will have a clear institutional backup. While implementing the institutional model IRDA had:

1. Retained the business controls within IRDA's Board, where ICAI is also a member, represented by its President in office.
2. Decided on the various controls to be checked, and periodicity in which such checking should be done. As checking and reporting are essentially an audit function, the same had been kept under the control of ICAI.
3. In this connection, IRDA, through ICAI had issued the following 'Technical Guides':
 - a. Technical guide on Re-view and Certification of Investment Risk Management Systems and Processes of insurance companies.
 - b. Technical guide on inter-nal/concurrent audit of investment functions of insurance companies.
4. The audit is done on 100 per cent of transactions to report 'exceptions' to the Board of insurer, with the comments of audit committee of the board.
5. The insurer is required to file with IRDA, the audit report, with the feedback of the audit

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committee and along with Board's response to such exceptions on a quarterly periodicity.

6. The audit is aimed at providing IRDA the focus to look at systemic impact such exceptions would bring out.

RESPONSIBILITIES OF CAs

1. Internal/Concurrent Audit should:
 - a. Cover 100 per cent of transactions and report exceptions.
 - b. Examine Investment Policy (IP), Standard Operating Procedure (SOP), its implementation, and review.
 - c. Compliance to regulations, circulars and guidelines.
 - d. Fund accounting process leading to computation of NAV in the case of ULIP funds.
 - e. Report on systems and process supporting investment operations covering Front, Mid and Back Office.

2. Confirmation on:
 - a. Implementation of audit committee recommendations.
 - b. All investments made follow SOP issued by Investment Committee (IC).
 - c. Classification of investment risk by IC for ranking (risk based monitoring/reporting).
 - d. Implementation of dealing employee guidelines.
 - e. Implementation status of systems and process – Phase 1.
 - f. Segregation of shareholder/policyholder funds, its accounting and identification at custodian level.
 - g. Reporting of Chief Investment Officer (CIO) and Chief Financial Officer (CFO) – for segregation of investing and its accounting.
 - h. Compliance to exposure norms and certification of NAV and its declaration.
 - i. Reporting of fund performance and regulatory compliance to insurer's Board.

Opportunities for CAs

The insurance sector has thrown open challenging jobs for the Chartered Accountants in Finance, Risk Management, Planning and Operations functions in insurance companies. CAs are known for their keen analytical ability, excellent technical skills and meticulous working style; and with their effective communication and interpersonal skills, can emerge as insurance specialists.

In this scenario, CAs are thrust with responsibility to authenticate various types of information submitted to the regulator by an insurance company. Thus CAs have a dual role to play. While within the insurance company, they play a crucial role in providing the management the analysis of business and also project the way forward, the practicing CAs who do the audit have their

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commitment towards the public and other stakeholders including the regulator.

Thus, CAs can play the following roles:

1. As employees in insurance companies can take up the following:
 - a. Chief Investment Officer
 - b. Equity Research
 - c. Dealer in Debt/Equity Market
 - d. Compliance Officer
 - e. Fund Manager
 - f. Risk Manager
 - g. Fund Accounting & NAV Calculation
 - h. Framing Standard Operating Procedure
2. External support services in the following areas:
 - a. Statutory Audit
 - b. Internal Audit
 - c. Concurrent Audit
 - d. Information Systems Audit
 - e. Risk Assessment
 - f. Risk Advisory
 - g. Framing Standard Operating Procedure
 - h. Framing Investment Policy

3. Apart from the above, CAs can undertake the following:
 - a. Insurance management,
 - b. Insurance marketing,
 - c. Underwriting management,
 - d. Claims management,
 - e. Product development,

Way Forward

As the insurance sector is growing at a rapid pace, the need for CAs, who are equipped with the needs of the industry will be in acute demand. Towards this demand ICAI should be in a position to supply Chartered Accountants to bridge the gap that exists now. In this connection, ICAI may like to take a look at the following:

1. Review the historical patterns of specialisations that the CAs take to - and based on this study revamp the CA course curriculum to channelise the CAs into their preferred areas of specialisations.
2. On the same count, integrate the Diploma in Insurance Risk Management (DIRM) and Diploma in Information Systems Audit (DISA) courses with the CA course. The content of these courses needs to be revamped with a bias for more practical training in the respective fields.
3. Collaborate with sector regulators for carrying out the above.
4. Integrating Information Security and Systems study into the CA curriculum.
5. Making it mandatory for CAs to have a six months industrial training in their area of specialisation.
6. Revisit the terms of reference of the Committee on Information Technology and the Committee on Insurance and Pension; and enlarge the scope of these committees with larger representation from industry so that the industry needs are well addressed. ■

Capitalisation of interest during pre-operative period in Cable and Telecommunication Industry

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 closely held public limited company is engaged in the business of providing cable TV (both analog and digital services) and broad band internet service in the State of Orissa and its neighbouring states, like West Bengal, Andhra Pradesh and Chhattisgarh. The company is registered under the Companies Act, 1956. The company prepares its annual financial statements as per the provisions of the Companies Act, 1956. The company plans to expand its operations to different states of India in near future.
2. The company has a three-tier organisation structure consisting of stations, regional headquarters and corporate office. The stations are grouped under different regions and report to the corporate office through the regional headquarters. The regional headquarters provide various services to the projects under construction and the operating stations under their jurisdiction.
3. The company is undertaking the following process for a location in project stage:
 - (a) Make selection of potential sites where the company operations are to be taken up. Bring approval of right of way from the local authority to lay cable in that locality. Then the company sets up an office and installs the network operating centre from where the services are to be provided to its customers.
 - (b) Immediate arrangement is made to have full contents from different broadcasters on payment to provide the services to the customers. Arrangement of intercity connectivity from available sources is also made for providing the broadband services from the company's control room. Once the facilities are available, company starts laying the cables and creates new passing which enable the company to provide cable and data connection to its customers. It also deploys necessary manpower to run the operations and provide services to its customers. All the above arrangements have an initial cost for the new location.
4. According to the querist, passings are created in phases in different areas one after another depending upon the market demand and also the environmental situation. Normally, there is a time lag between the availability of the first pay channel and connecting the first customer. It is not practically possible to arrange for all the pay channels at a specific time. Irrespective of whether the customer is connected or not, the pay channel liability starts from the day the company gets the decoder box to receive the signals. A customer will also not be interested to avail a connection when all the channels are not available in the network.
5. The querist has stated that there are also initial operational hurdles in new locations and the business moves very slowly and considering its nature of activities, it takes time to consolidate the business. Getting a sizeable number of customers takes a pretty long time. This time period varies from six months to two years depending upon the market where the operations have been started by the company.
6. The company, as per its business plan, mixed the funding requirement of both equity and debt to meet the capital expenditure including the pre-operational expenses at new locations and expansion and up-gradation in its existing locations. The nature of the activities is such that the same materials are used both for capital expenditure and the repair and maintenance activities. It is also difficult to bifurcate the loan and equity amount that is spent to purchase fixed assets for different locations. The total assets requirement of all locations is pooled and then loan is arranged for the entire lot. The querist has stated that it is difficult to identify direct relationship between the loan and the capital item purchased as per paragraph 8 of Accounting Standard (AS) 16, 'Borrowing Costs'.

7. The querist has further stated that based on the provisions of paragraph 8 of AS 16, the interest cost on debt taken for new locations and up-gradation of the existing operations is being charged to the profit and loss account from the day one the interest liability arises in view of no proper calculation/allocation of interest being done asset/location wise.
8. *The company is now of the view that since borrowings are mainly for acquisition of new fixed assets for new locations and expansion of its activities in present locations, the interest cost for the period during which the test run is continuing and a sizeable number of customer base is not created at the relevant locations ought to be capitalised as per paragraph 9 read with paragraph 4(a) of AS 16 and not charged off fully to the profit and loss account* (emphasis supplied by the querist).
9. As per the querist, if the debt cost from the day one is charged to the profit and loss account, there would be serious bottom line problem and the company would never be able to make bottom line positive with such huge interest cost burden during its initial period of expansion.
12. The Committee notes from the Facts of the Case that the company is entering into new locations and is also expanding in its existing locations, and for this, it is incurring borrowing costs. The Committee is of the view that broadly, such borrowing costs can be classified into two categories, viz., (i) those borrowing costs that are directly attributable to construction/creation of an asset and (ii) those borrowing costs that are not directly attributable to such construction/creation.
13. For the sake of convenience, at first, the Committee deals with the second type of borrowing costs, i.e., those which are not directly attributable to construction of an asset. In this regard, the Committee notes paragraph 6 of AS 16, notified by the Central Government under the Companies (Accounting Standards) Rules, 2006, which provides as follows:

“6. Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalised as part of the cost of that asset. The amount of borrowing costs eligible for capitalisation should be determined in accordance with this Standard. Other borrowing costs should be recognised as an expense in the period in which they are incurred.”

From the above, the Committee is of the view that the borrowing costs that are not directly attributable to construction/creation of an asset (e.g., borrowing costs related to repair charges of an already existing centre or for expenses relating to deployment of manpower) should be expensed in the period in which these are incurred.

B. Query

10. The querist has sought the opinion of the Expert Advisory Committee that considering the nature of the business and assets of the company, whether (i) the company ought to capitalise borrowing cost for the period as stated in paragraph 5 above when commercial operation is not feasible for certain period initially, and (ii) charging off fully the interest to the profit and loss account will not be proper in view of applicability of AS 16.

C. Points considered by the Committee

11. The Committee while expressing its views has examined only the issues raised in paragraph 10 above and has not examined any other issue arising from the Facts of the Case, such as, treatment of other expenses during the pre-operative period, allocation of general borrowing costs, capitalisation in parts/phases and bifurcation of loan and equity components, etc. At the outset, the Committee also wishes to point out that from the Facts of the Case, the nature of the assets, which are being constructed or coming into existence as a result of construction activity is not clear. In other words, what is the ‘qualifying asset(s)’ in the extant case is not clear. Accordingly, in the following paragraphs, the Committee is laying down the broad principles to be kept in mind while capitalising the borrowing costs.

14. As regards the first type of borrowing costs, i.e., which are directly attributable to construction of an asset, the Committee notes the definition of the term ‘qualifying asset’ and paragraph 5 of AS 16 which are reproduced below:

“A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.”

“5. Examples of qualifying assets are manufacturing plants, power generation facilities, inventories that require a substantial period of time to bring them to a saleable condition, and investment properties. Other investments, and those inventories that are routinely manufactured or otherwise produced in large quantities on a repetitive basis over a short period of time, are not qualifying assets. Assets that are ready for their intended use or sale when acquired also are not qualifying assets.” (Emphasis supplied by the Committee.)

From the above, the Committee notes that only those assets that necessarily take a substantial period of time to get ready for their intended use or sale can be considered as qualifying assets in the context of capitalisation of borrowing costs as per AS 16. The assets which are ready to use when acquired cannot be considered as qualifying assets within the meaning of AS 16, although there may be some time lag between their acquisition and actual use. The Committee further notes the Explanation to the definition of the term 'qualifying asset' and paragraphs 14, 16 and 20 to 22 of AS 16, notified by the Central Government under the Companies (Accounting Standards) Rules, 2006, which provide as follows:

Explanation:

"What constitutes a substantial period of time primarily depends on the facts and circumstances of each case. However, ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of facts and circumstances of the case. In estimating the period, time which an asset takes, technologically and commercially, to get it ready for its intended use or sale is considered."

"14. The capitalisation of borrowing costs as part of the cost of a qualifying asset should commence when all the following conditions are satisfied:

- (a) expenditure for the acquisition, construction or production of a qualifying asset is being incurred;***
- (b) borrowing costs are being incurred; and***
- (c) activities that are necessary to prepare the asset for its intended use or sale are in progress."***

"16. The activities necessary to prepare the asset for its intended use or sale encompass more than the physical construction of the asset. They include technical and administrative work prior to the commencement of physical construction, such as the activities associated with obtaining permits prior to the commencement of the physical construction. However, such activities exclude the holding of an asset when no production or development that changes the asset's condition is taking place..."

"20. An asset is normally ready for its intended use or sale when its physical construction or production is complete even though routine administrative work might still continue. If minor modifications, such as the decoration of a property to the user's specification, are all that are outstanding, this indicates that substantially all the activities are complete."

21. When the construction of a qualifying asset is completed in parts and a completed part is capable of being used while construction continues for the other parts, capitalisation of borrowing costs in relation to a part should cease when substantially all the activities necessary to prepare that part for its intended use or sale are complete."

22. A business park comprising several buildings, each of which can be used individually, is an example of a qualifying asset for which each part is capable of being used while construction continues for the other parts. An example of a qualifying asset that needs to be complete before any part can be used is an industrial plant involving several processes which are carried out in sequence at different parts of the plant within the same site, such as a steel mill."

15. On the basis of the above, the Committee is of the view that the company should evaluate what constitutes a substantial period of time considering the peculiarities of the facts and circumstances of its case, such as, nature of the asset being constructed. In this regard, time which is taken by an asset, technologically and commercially to get ready for its intended use or sale should be considered. The Committee notes from the Facts of the Case that the time taken to prepare the assets in question for its intended use is not clear. However, the querist has stated that there is a time lag to arrange for the pay channels and that the customer would not be interested to avail the facility unless all the channels are available. The Committee is of the view that once the asset is technologically ready, evaluation of optimum number of channels for commercial feasibility (i.e., commercial exploitation) of the asset should be done based on facts and circumstances of the case. In the view of the Committee, when a facility is technologically and commercially ready for distribution to the end-customers, the subsequent activities do not add value to the asset and therefore, the borrowing costs incurred thereafter should not be capitalised. The Committee is also of the view that the querist's argument on business feasibility, viz., consolidation of business and getting sizeable number of customers is not a criterion for determining the commercial readiness to estimate the substantial period of time. The Committee is of the view that commercial readiness should be determined on the basis of the assets providing output which can be commercially exploited in the market, not necessarily at profit. In this context, the Committee also wishes to point out that when a group of assets is being constructed and if an asset of that group can be individually used, the borrowing costs incurred in respect of it should cease to be capitalised

as and when that asset is ready for its intended use, as discussed above.

the profit and loss account will not be proper in view of AS 16.

D. Opinion

16. On the basis of the above, the Committee is of the following opinion on the issues raised in paragraph 10 above:

- (i) No, the time taken in getting a sizeable number of customers, as being argued by the querist in paragraph 5 above, should not be a consideration for determining "substantial period of time". Accordingly, borrowing costs incurred during that period should not be capitalised. Capitalisation of borrowing cost would depend on whether the constructed asset meets the definition of 'qualifying asset' and other provisions of AS 16, as discussed above.
- (ii) In case the interest incurred is not directly attributable to construction/creation of an asset, it should be fully expensed in the period in which it is incurred. However, if the interest incurred is directly attributable to construction/creation of a 'qualifying asset' as per the provisions of AS 16, as discussed in paragraphs 14 and 15 above, charging it off to

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 .

Revised Schedule VI and its Comparison with Existing Schedule VI: An Overview



Ministry of Corporate Affairs, Government of India has recently replaced the existing Schedule VI by a Revised Schedule VI wherein several changes in the presentation and disclosures requirements vis-à-vis the existing Schedule VI have been made. The changes are mostly inspired from the International Financial Reporting Standards and it has been mandated that Revised Schedule VI shall come into force for the Balance Sheet and Profit and Loss Account to be prepared by all the companies for the financial year commencing on or after 1-4-2011 i.e. financial year 2011-2012 onwards. Accordingly the financial statements for the companies in respect of financial year 2010-2011 shall continue to be governed by old Schedule VI. This article provides an overview of the Revised Schedule VI and comparison of the same with the existing Schedule VI.

Introduction

The form and contents of Balance Sheet and Profit and Loss Account of companies are regulated as per Section 211 of the Companies Act, 1956.

Sub-section (1) of Section 211 of the Companies Act, 1956 requires that every balance-sheet of a company must comply with the following three requirements:

1) It must give a true and fair view of the state of affairs of the company as at the end of the financial year.

- 2) It must, subject to the provisions of this section, be in the form set out in Part-I of Schedule-VI or as near thereto as circumstances admit or in such other form as may be approved by the Central Government either generally or in any particular case; and
- 3) Due regard must be had, as far as may be, in preparing the balance sheet to the general instructions for preparation of Balance Sheet under the heading 'Notes' at the end of that part.



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he Revised Schedule VI is based on existing accounting

standards and not on Ind AS and is, therefore, applicable on all companies. Accordingly as and when date of implementation of Ind AS is notified, a separate set of Schedule VI would be issued in respect of companies preparing their financial statements as per Ind AS wherein additional formats like Statement of Changes in Equity, Other Comprehensive Income would be required to be prepared apart from several other changes. ☺☺

Sub-section (2) of above section requires that every Profit and Loss account of a company must:

- 1) give a true and fair view of the profit or loss of the company for the financial year, and
- 2) comply, subject to the provisions of the section, with the requirements of Part II of Schedule VI so far as they are applicable thereto.

The Part II of Schedule VI does not prescribe form of Profit and Loss account and mandates only the requirements to be complied with while preparing and presenting the same, whereas in Part I proforma of Balance Sheet has been set out along with general instructions for its preparation. However, the above requirements are not applicable to any insurance or banking company or other class of company where form of balance-sheet, Profit and Loss account has been specified in or under the Act governing such class of company.

The existing Schedule VI was substituted by the Companies (Amendment) Act, 1960 and since then has been amended several

times. The vertical format of the Balance Sheet was later inserted by Notification No. GSR 220(E), dated 12th March, 1979.

The latest amendment in the Schedule VI has been made by Ministry of Corporate Affairs (MCA), Government of India vide Notification No S.O. 447(E) dated 28th February, 2011 wherein in exercise of the powers conferred by sub-section (1) of Section 641 of the Companies Act, 1956, the Central Government has replaced the existing Schedule VI by a revised Schedule VI. In the said notification reference has been made to the Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006. Accordingly, the revised Schedule VI has nothing to do with the converged Indian Accounting Standards (Ind AS) as uploaded on website of Ministry of Corporate Affairs on 25th February, 2011 for which date of applicability has not yet been notified.

Although initially the Ministry of Corporate Affairs website stated that revised Schedule-VI is applicable from FY 2010-2011 which was later withdrawn and for some time MCA remained silent regarding applicability of the same due to which situation of dilemma was created which was later on resolved through statement on MCA website that the revised schedule shall be effective from 01-04-2011 i.e. FY 2011-2012 onwards. Accordingly, the financial statements for the companies in respect of financial year 2010-2011 shall continue to be governed by old Schedule VI.

Revised Schedule VI – Influences From IFRS

Although the applicability of the Ind AS converged with IFRS, which was earlier slated to be implemented in a phased manner starting from 1st April, 2011 has been deferred, however, the instant revision of

Schedule VI can be considered as a step towards convergence to IFRS to some extent with regard to presentation of financial statements as many features/disclosures have been taken from these international standards, some of which are stated below:-

- Accounting Standards have been given supremacy over Schedule VI. This is in line with IFRS which mandates that no statute can override the Standards.
- The schedule sets out minimum requirements for disclosure which is in spirit of IAS 1 “*Presentation of Financial Statements*” which also provides flexibility in format of financial statements to the companies.
- Bifurcation of assets and liabilities amongst current and non-current is required. The definition of current/non current and operating cycle has been taken from IAS 1.
- Proposed dividend is not recognised and only disclosed in consonance with the IFRS. Although this will be effective only after necessary change is made in existing AS 4.
- Cross referencing of each item of the financial statements to related information in the notes which is also as per IAS 1.

However, as already discussed, the Revised Schedule VI is based on existing accounting standards and not on Ind AS and is, therefore, applicable on all companies. Accordingly, as and when date of implementation of Ind AS is notified, a separate set of Schedule VI would be issued in respect of companies preparing their financial statements as per Ind AS wherein additional formats like Statement of Changes in Equity and Other Comprehensive Income would be required to be prepared apart from several other changes.

Basic Overview and Comparison with Old Schedule VI

The overview of Revised Schedule VI and its comparison with old Schedule VI are deliberated as under:-

1) Applicability: As discussed earlier it has been specifically stated on the website of Ministry of Corporate Affairs, Government of India that the revised schedule VI shall come into force from 01-04-2011. Accordingly the revised schedule VI shall be applicable for all the companies from financial year 2011-2012 onwards. Therefore, the financial statements for the companies in respect of financial year 2010-2011 shall continue to be governed by old Schedule VI.

2) Contents: The contents of the Revised Schedule VI are as under:-

- I) General Instructions for preparation of Balance Sheet and Statement of Profit and Loss of a company.
- II) Form of Balance Sheet (only vertical format) with General Instructions for preparation of Balance Sheet. (PART-I).

III) Form of Statement of Profit and Loss with General Instructions for preparation of Statement of Profit and Loss. (PART-II.)

For comparison the contents of Old Schedule VI are stated as under:-

- I) Form of Balance Sheet (including disclosure requirements) both in horizontal as well as vertical form with general instructions for its preparation (PART-I)
- II) Requirements as to Profit and Loss Account. (PART-II)
- III) Interpretation (PART III).
- IV) Balance Sheet Abstract and Company's General Business Profile. (Part IV).

From comparison of contents, the following changes are seen:-

- a) Balance Sheet Abstract and Company's General Business Profile as provided in Part-IV has been removed, which is a welcome move as this statement was of no real purpose and meant for statistical purposes.
- b) Horizontal format of Balance Sheet known as conventional or customary form of Balance Sheet has been deleted. Accordingly, now onwards only vertical format is to be used.
- c) Form of Statement of Profit and Loss has been provided in Part II, which was not prescribed in old Schedule VI.

d) Further Part III on Interpretation, which contained explanation of provision, reserve, etc. has been scrapped as these terms are already covered in the Accounting Standards. It has been stated in revised Schedule VI that for the purpose of this schedule, the terms used shall be as per the applicable Accounting Standards.

Overriding Effect of Accounting Standard and Flexibility

The general instructions of revised Schedule VI specifically provide that where compliance with the requirements of the Act including Accounting Standards require any change in treatment of disclosure including any change in head/subhead or any changes interse, the financial statements or statements forming part thereof, the same shall be made and the requirements of the Schedule VI shall stand modified accordingly. Even it has been stated that the format of the Balance Sheet and Statement of Profit and Loss as given in schedule sets out minimum requirements for disclosure and can be changed when such presentation is relevant to an understanding of the company's financial position or performance or to cater industry/sector-specific disclosure requirements or when required for compliance with the amendments to the Companies Act, 1956 or under the Accounting Standards.

The general instructions of revised Schedule VI specifically provide that

where compliance with the requirements of the Act including Accounting Standards require any change in treatment of disclosure including any change in head/subhead or any changes interse, the financial statements or statements forming part thereof, the same shall be made and the requirements of the Schedule VI shall stand modified accordingly. ☺



Due to above it can be stated that now onwards there is no possibility of conflict between Accounting Standards with Schedule VI as in any such event or in case of any change in Companies Act or Accounting Standard, the requirements of the Schedule-VI shall stand modified accordingly.

Disclosure Requirements

The disclosure requirements as specified in Part I and Part II of Revised Schedule VI are in addition to and not in substitution of the disclosure requirements specified in the Accounting Standards prescribed under the Companies Act, 1956. Due to this, the Schedule VI is not bulky as several disclosure requirements already covered in Accounting Standards have not been reiterated.

Further it has been stated that additional disclosures specified in the Accounting Standards shall be made in the notes to accounts or by way of additional statement unless required to be disclosed on the face of the Financial Statements. Similarly, all other disclosures and as required by Companies Act, 1956 shall be made in the notes to accounts.

Notes to accounts, which was earlier not specifically defined has been defined, as containing information in addition to that presented in the financial statements and shall provide where required (a) narrative descriptions or disaggregations of items recognised in those statements and b) information about items that do not qualify for recognition in those statements.

As per revised Schedule VI each item on the face of the Balance Sheet and Statement of Profit and Loss shall be cross referenced to any related information in the notes to accounts. Accordingly, there is a column for stating the Note number in proforma for Balance Sheet as

Under revised schedule VI the upper half is referred to as Equity and Liabilities and later half is shown as Assets whereas in old schedule VI the same were referred as Sources of Funds and Application of Funds. Accordingly the current liabilities (including short term provisions) are to be shown in upper half of balance-sheet under Equity and Liabilities whereas in old schedule VI (vertical form) it was shown as deduction from current assets, loans and advances and net current assets are disclosed on Assets side. Due to this the Balance Sheets totals would increase to the extent of the current liabilities. ☺



well as Statement of Profit and Loss. It is pertinent to mention here that in the old schedule VI there was a Column for indicating Schedule No. in the Balance Sheet, accordingly the concept of schedules has been eliminated. This approach is inspired from the para 113 of Ind AS 1 (IAS 1) "Presentation of Financial Statements" which enunciates that each item in the primary statements should be cross referenced to any related information in the notes.

It has further been prescribed that except in case of the first Financial Statements laid before the Company (after its incorporation) the corresponding amounts

(comparatives) for the immediately preceding reporting period for all the items shown in financial statements including the notes shall also be given.

It has also been stipulated that once a unit of measurement is selected, it should be used uniformly in the financial statements.

Form of Balance Sheet and General Instructions

As discussed, Part I of the Revised Schedule VI prescribes the Form of Balance Sheet and general instructions for preparing the same. The important highlights of the same are deliberated as under:-

a) Current/Non Current Classification: The most important change in entire Revised Schedule VI is classification of all the assets and liabilities between current and non current.

The general instructions for preparation of Balance Sheet define current/ non current asset/liability as under:

An asset shall be classified as current when it satisfies any of the following criteria:

- It is expected to be realised in, or is intended for sale or consumption in, the company's normal operating cycle;
- It is held primarily for the purpose of being traded;
- It is expected to be realised within 12 months after the reporting date; or
- It is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least 12 months after the reporting date.

All other assets shall be classified as non-current.

An operating cycle is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents. Where the normal operating cycle cannot be identified, it is assumed to have duration of 12 months.

A liability shall be classified as current when it satisfies any of the following criteria:

- (a) It is expected to be settled in the company's normal operating cycle;
 - (b) It is held primarily for the purpose of being traded;
 - (c) It is due to be settled within 12 months after the reporting date; or
 - (d) The company does not have an unconditional right to defer settlement of the liability for at least 12 months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.
- c) Currently all loans and advances (except capital advances) are shown under Current Assets and Loans and Advances but now onwards the same needs to be bifurcated between current and non-current, accordingly the sub heading of long term loans and advances has been introduced in Revised Schedule VI.
- d) The provisions also need to be bifurcated among long term and short term, the latter one being classified as current, and former being classified as non-current e.g. employee related provisions; accordingly subheading of long term provisions has been introduced.

All other liabilities shall be classified as non-current.

It is pertinent to mention here that the definitions of current/non-current asset, operating cycle and current/non-current liability are as given in para 66, para 68 and para 69 of IAS 1 'Presentation of financial statements'.

The above bifurcation of assets and liabilities between current and non-current would require major reclassifications in the Balance Sheets of all companies and would have impact on the current ratio. Some of such instances of reclassifications are as under:-

- a) Presently even the current maturities to long term debt are shown as part of long term debt and only disclosure of amount due to be repaid within one year is made. However, as per revised Schedule VI current maturities to long term debt would be depicted as 'Other Current liabilities' and
- b) As per old schedule VI interest accrued and due on long term loans were shown as part of the long term loans but in revised schedule VI the same is to be shown as current liabilities.



The form of Statement of Profit and Loss has been introduced in schedule VI for the first time. The format of Statement of Profit and Loss does not depict any appropriation item on its face, as the below the line adjustments i.e. dividend, bonus shares and transfer to/from reserves, etc are to be disclosed under "Reserve and Surplus" in the Balance Sheet. However the amount set aside or proposed to be set aside to reserve/withdrawn from reserve needs to be disclosed as additional information in the notes. ”

Under old Schedule VI all the provisions were being shown under Current Liabilities and Provisions.

- e) Under old schedule VI the trade receivables (Debtors)/ Trade payables (creditors) were always shown as Current, but in revised schedule VI, these can also be shown as Non Current. It appears that where the credit is offered on deferred credit basis or the payment is not/ expected to be received from debtors within normal operating cycle/12 months from reporting period, the same needs to be disclosed as Non Current.

For understanding the above definitions let us apply the same in following cases:-

- a) As of 31st March, 2011, a property developer has inventories of residential units which it expects to sell in three years. Historically similar residential units have been sold in three years. As of 31st March, 2011, should the inventories of residential units be classified as current or non current assets?
 - An asset shall be classified as current when it satisfies any of the four criteria. Since, the inventories of residential units in the given case, satisfy the first requirement i.e. it is expected to be realised in, or is intended for sale or consumption in, the entity's normal operating cycle, the residential units should be classified as current assets.
- b) A primary school requires a deposit to be paid upon enrolment into the school. Should the student leave the school, this deposit is refundable within three months. However, based on historical evidence the majority of students enrolling to primary school continue with school and receive the



deposit back at the end of six year period. How should the deposits be classified?

- The deposits should be classified as current liabilities. Despite the historical evidence that indicates that the majority of the deposits are only repaid at the end of six year period, the deposits are payable on three months notice. Revised Schedule VI states that a liability should be classified as current when 'the entity does not have an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date'. Therefore, the deposits should be classified as current liabilities.

c) As of 31st March, 2011, Company X has breached a covenant and as per the terms of the agreement the bank loan became immediately payable. On 5th April, 2011, the bank agreed to waive the covenant. As of 31st March, 2011, should the loan be classified as current or non-current liability?

- The liability is classified as current because, at the balance sheet date, the entity does not have an unconditional right to defer its settlement for at least 12 months after that date.

b) Disclosure of current liabilities:

Under revised schedule VI the upper half is referred to as Equity and Liabilities and later half is shown as Assets whereas in old schedule VI the same were referred as Sources of Funds and Application of Funds. Accordingly, the current liabilities (including short term provisions) are to be shown in upper half of balance-sheet under Equity and Liabilities whereas in old schedule VI (vertical form) it was shown as deduction from current assets, loans and advances and net current assets are disclosed on Assets side. Due to this the Balance Sheets totals would increase to the extent of the current liabilities.

As the Revised Schedule VI is applicable from Financial Year 2011-2012 onwards and as previous year figures would be required the companies are suggested to prepare parallel financial statements for the FY 2010-2011 on basis of revised Schedule VI, which would save lot of time next year as these figures can be used as comparables in the financial statements for FY 2011-2012 prepared as per Revised Schedule VI. ☺☺

c) Disclosure of Accumulated

Losses: Debit balance of Profit and Loss shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserve and Surplus' after adjusting negative balance of surplus, if any shall be shown under the head 'Reserve and Surplus' even if the figure is in the negative. As per old Schedule VI the accumulated losses were to be shown on Asset side as Profit and Loss account after Miscellaneous Expenditure.

d) Proposed Dividend: Part I of Old Schedule VI requires 'proposed dividends' to be shown under "Provisions" and paragraph 3 (xiv) of Part II of the same requires the "proposed dividends" to be disclosed in the Profit and Loss account. In consonance to this para 14 of the Accounting Standard 4 "Contingent and Events Occurring After the Balance Sheet Date" also requires that dividends in respect of period covered by financial statements, which are proposed or declared after balance sheet date but before date of approval, should be adjusted in accounts.

However, now para 6(U) of the General Instructions for preparation of Balance Sheet of Part I of Revised Schedule VI does not require the provision for proposed dividend to be made and only desires disclosure of same in notes to

accounts, which has been inspired from para 12 and 13 of IAS 10 "Events after the reporting period" wherein it is specifically stipulated that such dividends do not meet the criteria of a present obligation as per IAS 37 Provisions, Contingent Liabilities and Contingent Assets. Further, IAS 1 "Presentation of Financial statements" stipulates that such dividends are disclosed in the notes.

Although Revised Schedule VI does not require provision for proposed dividend, however, as discussed earlier the Accounting Standards have an overriding effect over Revised Schedule VI and accordingly companies will have to account for the same until revision to this effect is made in AS 4.

e) Additional classification/disclosures/Changes: The new schedule VI prescribes certain fresh/change in disclosures, some of which are as under:-

- i) Share capital:** Reconciliation of number of shares outstanding at beginning and at end of reporting period, shares in the company held by each shareholder holding more than 5 per cent shares specifying the number of shares held, etc.
- ii) Share Application Money** not exceeding the issued capital and to the extent not refundable shall be shown under head Equity and Share application money to the extent refundable i.e. the amount in excess of subscription or in case of requirements of minimum subscription are not met, shall be separately shown under "Other current liabilities".
- iii) Reserves and Surplus:** Nature and purpose of each reserve to be stated only for those aggregated under "Other Reserves".
- iv) Long Term Borrowing:** Bonds/ Debentures (along with rate

of interest and particulars of redemption or conversion) shall be stated in descending order of maturity or conversion, Terms of repayment of term loans and other loans are still required to be disclosed. Further period and amount of continuing default as on balance sheet date in repayment of loans and interest also needs to be disclosed, which was not required in old Schedule VI.

v) Short term Borrowing: Here also period and amount of continuing default as on balance sheet date in repayment of loans and interest needs to be disclosed.

vi) Fixed Assets: Details in respect of tangible and intangible assets need to be given separately and their amount also depicted on the face of balance sheet separately, which was not earlier the case as a single schedule was prepared wherein the intangible assets were also included.

vii) Tangible Assets: Assets under lease to be classified separately. Explanations in old Schedule VI removed. One of such Explanation was regarding adjustment of exchange rate variation in cost of fixed assets which was still not operative in view of the specific stipulation in the AS 11 "The Effects of Changes in Foreign Exchange Rates" notified by Companies (Accounting Standard) Rules, 2006"

viii) Intangible Assets: New head like mastheads and publishing rights, Mining Rights, Recipes, formulae, models, designs and prototypes introduced.

ix) Capital Advances are required to be presented separately under the head "Long term loans and advances". Presently they were being shown as part of fixed assets/capital work in

progress in absence of any heading available in existing Schedule VI for such advances.

x) Non-current investment: Against five heads available in old Schedule VI wherein there was no residual head the new one provides eight classifications, which includes the residual head of other non-current investments.

xi) Trade receivables: The term sundry debtors has been replaced with trade receivables and instead of showing entire amount as current assets under old Schedule VI, bifurcation of same into non current and current is now required. Further separate disclosure of trade receivables outstanding for a period exceeding six months from the date they become due for payment as against the billing/accounting date is required now.

xii) Cash and cash equivalents: Bank deposits with more than 12 months maturity to be disclosed separately, which was not required till now. The bifurcation of bank deposits among scheduled and non scheduled banks has been dispensed with.

xiii) Contingent liabilities and Commitments: These were required to be disclosed as footnote to Balance Sheet under old Schedule VI and are now required to be disclosed in notes to accounts, further disclosure of all financial commitments (not only capital commitment) are required under Revised Schedule VI.

Form of Statement of Profit and Loss and General Instructions

As discussed earlier, form of Statement of Profit and Loss has been introduced in schedule VI for the first time. The highlights of the form of Statement of Profit and

Loss and general instructions for preparing the same are as under:-

- a) The format of Statement of Profit and Loss does not depict any appropriation item on its face, as the below the line adjustments i.e. dividend, bonus shares and transfer to/from reserves, etc. are to be disclosed under "Reserve and Surplus" in the Balance Sheet. However, the amount set aside or proposed to be set aside to reserve/withdrawn from reserve needs to be disclosed as additional information in the notes.
- b) In respect of a company other than a finance company, revenue from operations shall disclose separately in notes revenue from (a) sale of products (b) sale of services (c) other operating revenues less:- (d) Excise Duty. In case of finance company, revenue from operations shall include revenue from (a) Interest and (b) Other financial services. It has further been stated that revenue from each of the above heads shall be disclosed separately by way of notes to accounts to the extent applicable. The above disclosure is more detailed than old Schedule VI.
- c) Additional information regarding aggregate income or expenditure exceeding 1 per cent of the revenue from operations or ₹1,00,000/-, whichever is higher, need to be disclosed by way of notes. Till now any item exceeding 1 per cent of total revenue or ₹5000/-, whichever is higher, was to be shown as a separate head in P&L Account and should not have been combined under head "miscellaneous expenditure".
- d) The quantitative disclosure in respect of raw material, opening and closing stocks for each class of goods in case of manufacturing company and

quantity details in respect of purchase made, opening and closing stock as required under the old Schedule VI has been liquidated. Even the detailed quantitative information in respect of each class of goods manufactured in regard to the licensed capacity, installed capacity and actual production is not required.

- e) Prior Period Items are to be separately disclosed. Although the same are still being disclosed separately in view of Accounting Standard 5 "Net Profit or Loss for the period, Prior Period and Extraordinary Items and Changes in Accounting Policies", but the old Schedule VI didn't specifically mandated the same.
- f) Payment to the auditor *inter alia* for reimbursement of expenses to be separately disclosed.
- g) Gain/Loss on foreign currency transactions and translations to be separated into Finance Costs and Other Expenses.
- h) Broad heads shall be decided taking into account the concept of materiality and presentation of true and fair view of financial statements,

Rounding Off of Figures

The limit of turnover and the extent of rounding off has been relaxed in the revised Schedule VI, which stipulates that financial statements of companies having turnover less than one hundred crore can be rounded off up to millions, whereas at present the rounding off could be made up to thousands only. Further for companies having turnover above hundred and less than five hundred crore, the rounding off can now be made up to crores, whereas in old Schedule VI the same was allowed up to millions.

Conclusion

The Revised Schedule VI is a step



in right direction as supremacy has been provided to the Accounting Standards and the Companies Act, 1956, which would avoid disputes as well as save time of legislature in making time to time amendments in Schedule VI. It can also be considered as a step towards convergence to IFRS to some extent with regard to presentation of financial statements as many features as discussed have been taken from these International Financial Reporting Standards.

As the Revised Schedule VI is applicable from Financial Year 2011-2012 onwards and as previous year figures would be required, the companies are suggested to prepare parallel financial statements for the FY 2010-2011 on the basis of revised Schedule VI, which would save a lot of time next year as these figures can be used as comparables in the financial statements for FY 2011-2012 prepared as per Revised Schedule VI. Further, the exercise for presentation of financial statements as per Revised Schedule VI would be helpful to entity migrating to Indian Accounting Standards converged with IFRS whenever the same are applicable as Para 21 of Ind AS 101 'First-time Adoption of Indian Accounting Standards' states that the first time adopter shall present latest corresponding previous periods' financial statements prepared as per the previous GAAP (reclassified in format as per Ind. AS) when presenting its first Ind AS financial statements. ■

Reforms in Government Accounting and Financial Reporting



The public finance reform in India is reflected in the regulatory framework prescribed for the government accounting and financial reporting reforms. The Financial Responsibility and Budget Management Act (FRBM) of 2003, combined with General Financial Rules (GFR) of 2005, Government Accounting Rules, 1990, Indian Government Accounting Standards (IGAS), and Outcome Budget, all demonstrate the unflinching commitment of the nation for financial reforms in the government. The rule based financial statements are being replaced by principles and standard based accounting; and cash based to accrual based system of accounting, to maintain India's predominant position as an economic power at the corridors of global economy. This article discusses reforms in Government Accounting from professional perspective.



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The Union Finance Minister inaugurated a conference on accrual based accounting and financial reporting on 21st June, 2011 at the office of the Comptroller and Auditor General of India (CAG) where finance ministers from the centre, states, and union territories as well as key stakeholders including ICAI participated.

Globally, the paradigm for public financial management has been changing quite rapidly. Australia and New Zealand initiated accounting reforms as part of an integrated financial management and accounting and budgeting reforms. Canada and United Kingdom started with accounting reforms followed by budgetary reform after a gap of three to five years. United States and Spain combined modified accrual accounting with cash budgeting

as of now. Though the international experience demonstrates a flexible approach, benefits of accrual accounting and financial reporting can be fully realised only when budgetary reforms are undertaken simultaneously.

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and standard based accounting; and cash based to accrual based system of accounting, to maintain India's predominant position as an economic power at the corridors of global economy.

Existing System of Government Accounting

As per Articles 266 and 267 of the Constitution of India, government accounts are maintained in three parts: Part-1: Consolidated Fund of India (CFI); Part-2: Public Account; and Part-3: Contingency Fund. CFI transactions are classified into functions and programmes largely in alignment with plan heads of development with a six tier hierarchical architecture. Articles 112 and 202 relate to the Annual Financial Statements of the Union and the State Governments respectively. These statements require that expenditure shows separately as charged upon the CFI, depicting 'charged' and 'voted' expenditure, and expenditure on 'revenue account' distinguished from 'other expenditure', thereby requiring categorisation of revenue and capital expenditure. As India has followed the policy of planned allocation of resources for economic development and that Plan and Non-Plan expenditure should also be distinctly shown.

Transactions on Public Accounts are recorded as receipts and disbursements and classified into the broad categories of Small Savings, Reserve Funds, Deposits and Advances, Suspense and Miscellaneous, Remittances, and Cash Balance. The financial reporting framework includes presentation of two audited annual accounts – the Finance Accounts and the Appropriation Accounts. These are prepared separately for the Union Government, each of the State Governments and Union Territories having Legislative Assembly. The Appropriation Accounts, being

Transition to accrual based accounting for all the three tiers of government - Union, States, Urban Local Bodies (ULB) and Panchayati Raj institutions(PRI) over the years is time and resource intensive. The Thirteenth Finance Commission wanted the government to move forward with caution. The Commission advocated a 'bubble up' approach to this transition. In this approach, local bodies like large municipal bodies and PRIs would adopt accrual accounting initially. For this purpose, , the National Municipal Accounting Manual incorporating the principles of accrual accounting has already been prepared with an intention to facilitate the 'bubble up' process to percolate to all the three tiers of government. Already, 48 ULBs in 17 states have switched over to accrual based accounting. ”

compliance reporting on legislative appropriations and grants, explanations are provided for significant variance, both excesses and saving, between the original demand and final appropriation and final appropriation and actual expenditure.

The Finance Accounts contain the financial statements of the government concerned with statements showing functional head-wise distribution of receipts and disbursements during the year and debt and other obligations at the end of the year. Information on financial assets and guarantees issued by the government is also provided in this document. Budget documents use Fiscal Deficit to

show Government's revenue-expenditure gap and measures its dependence on non government savings for funding its expenditure. The Revenue Deficit is also reflected. The emphasis in these documents is on flows into and out of Consolidated Fund, deficit and its financing from various sources. As per the provisions of the FRBM Act, additional disclosures are also being made of assets held by the Government including non-financial assets, arrears of tax and non-tax revenues and guarantees.

Reforms in Government Accounting

The government approved the Twelfth Finance Commission (TFC)'s recommendation in 2004 to introduce accrual based accounting, standardising accounting classification up to object level head for all states, adding eight more statements relating to subsidies, and separate expenditure statements on salaries, pensions, committed liabilities, maintenance expenditure, segregation of salaries and non salary portions and liabilities and repayment schedule on outstanding debts.

Transition to accrual based accounting for all the three tiers of government - Union, States, Urban Local Bodies (ULB) and Panchayati Raj institutions(PRI) over the years is time and resource intensive. The Thirteenth Finance Commission wanted the government to move forward with caution. The Commission advocated a 'bubble up' approach to this transition. In this approach, local bodies like large municipal bodies and PRIs would adopt accrual accounting initially. For this purpose, the National Municipal Accounting Manual incorporating the principles of accrual accounting has already been prepared with an intention to facilitate the 'bubble up' process to percolate to all the three tiers of government. Already, 48 ULBs in 17

states have switched over to accrual based accounting. Four states, namely Gujarat, Karnataka, Kerala and West Bengal adopted double entry accounting for PRLs. Besides, 18 states accepted the accrual based accounting in principle, 16 states accepted the Model Accounting System developed by Ministry of Panchayati Raj, which can be easily converted to accrual basis.

The Second Administrative Reforms Commission recommended appointment of a task force for conducting a cost benefits analysis and to suggest modification in the Appropriation Accounts and Finance Accounts. It observed that accrual based accounting might be tried initially in certain organisations like departmental commercial undertakings such as Railways where tangible benefits could be derived within a short period of two to three years and thereafter, on the basis of experience, the system could be extended to other departments. In order to effectively implement the transition, the accounting personnel should be trained in the concept of accrual based accounting in the government; a detailed road map to be drawn; the plan, budget, and accounts are to be aligned and a viable robust transparent financial information system is to be created.

Cash Based Accounting Versus Accrual Based Accounting

Currently government accounts are kept on cash basis, recording actual cash received and disbursements made without indicating amount due to or from government during the accounting period. The cash-based system of accounting is based on inputs and outputs with reference to the budget and is inadequate in providing complete financial position of government at a given point for resource management. It does not reflect

the changes in financial position; reporting government's accrued liabilities on interest payments due or dues on account of pensions and retirement benefits, enabling to track current as well as non-financial assets. The present system does not represent assets held by government, the cost of holding and operating these assets, and providing services by the government's departments or future commitments. Further, in a cash based system, tax revenues can be collected in excess during a period followed by high incidence of refunds, payments can easily be deferred to future periods and revenues due in the future could be compromised by providing for one-time receipts without recording or reporting in the financial statements.

While accrual based accounting

G ASAB has prepared a roadmap for accrual accounting, specifying activities and milestones to be completed for migration to accrual accounting; a detailed operational framework and an overall architecture of the accounting model suitable to constitutional reporting requirements. The transition may take nearly five to six years in three stages: in the first stage, value addition is made by adding separate statements on salaries, subsidies, interest, pension etc; in the second stage, value addition can be made in the extant system with greater disclosures such as arrears in revenue, committed liabilities, etc., before the final stage of conversion to accrual based accounting. ☞

records consumption of resources during a period, focuses on cost of resources consumed, and recognises income as it is earned; cash based system records only cash flows. In accrual accounting, in addition to cash flows, unpaid consumptions – payables and unrealised incomes – receivables – are also recorded. The revenue flows from an output are matched with the consumption of resources that produced the output helping in bringing out the operating performance of an entity, whereas cash accounting does not apply matching principle. Accrual accounting provides a complete measure of an entity's financial position at any given point of time by a comprehensive presentation of entity's assets and liabilities. The perceived benefits in switching over to accrual accounting in government may lead to better management of receivables and payables, assets, liabilities, contingent liabilities, assessment of full cost of service delivery, and assessment of fiscal sustainability of operations.

Government Accounting Standard Board (GASAB)

Accounting is not meant merely for systematic recording of receipts and expenditure, or exercising budgetary and expenditure control, but should help management as a powerful instrument in planning, quality decision making and effective financial management, reflecting true and fair value of government's financial position. As per article 150 of the Constitution of India, the President, on the advice of the CAG, prescribes the form in which the accounts of the union, states and the union territories are kept. The Government of India established the Government Accounting Standards Advisory Board (GASAB) in 2002 under the aegis of the Comptroller and Auditor General (CAG) with members of

all stakeholders including premier accounting services from the government and ICAI to suggest accounting reforms indicating a road map, Operational Framework, guidelines and Indian Government Accounting Standards (IGASs) for gradual migration to accrual based accounting.

Accordingly GASAB prepared a roadmap for accrual accounting, specifying activities and milestones to be completed for migration to accrual accounting; a detailed operational framework and an overall architecture of the accounting model suitable to constitutional reporting requirements. The transition may take nearly five to six years in three stages: in the first stage, value addition is made by adding separate statements on salaries, subsidies, interest, pension, etc; in the second stage, value addition can be made in the extant system with greater disclosures such as arrears in revenue, committed liabilities, etc., before the final stage of conversion to accrual based accounting.

As of now, different stakeholders, such as the Civil Ministries and Departments, Department of Posts, Ministry of Railways and Ministry of Defence at the Union level and the States and Union Territories having Legislature are at different stages in terms of their preparedness and may take different time-periods to achieve the suggested level of reforms to implement accrual accounting. Migration to accrual accounting must be within a uniform operational framework so that the final accounts of the governments, both the union and the respective states and the union territories with legislature fall within a uniform reporting framework. This also requires uniformity in the classification system. The "Operational Guidelines for Accrual Based Financial Reporting" provide the necessary guidance

for the transition to accrual based accounting and financial reporting.

Challenges in Implementation

A robust IT backbone, functionally similar to Enterprise Resource Planning (ERP) systems like SAP is required to be established across the country integrating the three tiers of government encompassing the Centre, States, Union Territories and ULBs and PRIs for maintenance of accurate, authentic and reliable data, generation of accounting records and comprehensive financial statements. A few states have constituted Task Forces for preparing for the transition and providing training and guidelines. Several new statements are also added in the existing Finance Accounts of the states.

Besides, many states have already computerised the treasury systems and the Central Government has also undertaken the computerisation of treasuries in 626 districts, relevant codes are amended by the State/UTs. Provisions of appropriate accrual heads of accounts would be necessary when treasury computerisation is taken up, even though these heads may not be utilised in the very near future. Any effort in this direction would only improve the efficiency of the administration and the confidence of the stakeholders on the administration providing various analysis and MIS reports. Decision makers will be accountable for those decisions, accelerating project implementation process bringing transparency and increased efficiency in government functioning.

Besides creating necessary IT infrastructure and data base, enormous efforts are required for nationwide capacity building, skill development and training for accelerating the transition process. This involves intensive training

Besides creating necessary IT infrastructure and data base, enormous efforts are required for nationwide capacity building, skill development and training for accelerating the transition process. This involves intensive training to the accounting personnel in various government organisations. Many of these functionaries do not have professional qualifications and those who have also need to upgrade their skills and competence to make the change over smooth. ICAI can consider imparting appropriate training programmes to the accounting personnel all over the country to transform them to accounting technicians in government accounting to discharge their responsibilities efficiently, proficiently and greater accuracy and confidence to facilitate the changeover to accrual based accounting system in government smooth. ☺☺

to the accounting personnel in various government organisations. Many of these functionaries do not have professional qualifications and those who have also need to upgrade their skills and competence to make the change over smooth. ICAI can consider imparting appropriate training programmes to the accounting personnel all over the country to transform them to accounting technicians in government accounting to discharge their responsibilities efficiently, proficiently and greater accuracy and confidence to facilitate the changeover to accrual based accounting system in government smooth. ■

Social Audit and Its Relevance in India



Social Audit is proposed as a supplement to conventional audit to help government department, public agencies and NGOs, etc. understand and improve their performance as perceived by the stakeholders. Social Audit is a process by which an organisation accounts for its social performance to its stakeholders and seeks to improve its future social performance. Social auditing is a way to document and hold a company accountable for its social and ethical Business practices. Social audit involves social accountability, which is a process by which accountability is exacted from accountability holders through direct or indirect citizen action and engagement. India, where large scale public welfare schemes are run by government, NGOs and also by some companies, needs social audit culture all the more. More so because even today a crisis of credibility, confidence and trust persists with respect to government projects, programmes and schemes. Leakage of funds in public programmes and misuse of shareholders' and stakeholders' resources is a commonly perceived scenario. Chartered Accountants are the one of the groups of professionals that is able to understand and to fulfill the objectives and requirement of Social Auditors. Read on to know more.



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Social Audit-Genesis and Evolution

The concept of Social Audit originated in the European and American countries in the middle of the 20th centuries as a process of monitoring, appraising and measuring the social performance of the Business organisations. In the 1970s, Abt Associates (the American consultancy firm) conducted a series of social audits which were incorporated into its annual reports. The term Social was proposed by Howard R. Bowen in 1953, in his article on "Social Responsibilities of a Businessman".

What is Social Audit?

Social Audit is a process by which an organisation accounts for its social performance to its stakeholders and seeks to improve its future social performance. Social auditing is a way to document and hold a company accountable for its social and ethical business practices. Social Audit is a process of evaluation and reporting which is similar, in some respects to a financial audit but focuses on social performance rather than financial performance. It is a tool for evaluating how satisfactorily an organisation has discharged its social responsibility. Thus, it provides the strongest and indisputable direct evidence for inputs, processes, financial and physical reporting, compliance verification, assurance against misuse, fraud and misappropriation, and utilisation of resources and assets. Social Audit is a reform tool aimed at strengthening accountability and transparency in the implementation of projects and policies. It is a method for organisation to plan the internal and external consequences of the organisation's social and commercial operations.

Relevance of Social Audit

- **Governance and Accountability:** At its simplest, Accountability refers to a process by which individuals or organisations are answerable for their actions and consequences that follow from them. What remains unclear, however, is the issue of who is entitled to hold these individuals or organisations to account and mechanism that should be used in order to do so.

The *Traditional approach to Accountability* refers to the conventional method of formal authority over individual/organisation and right to hold them to account. But this approach to accountability often

fails to empower those who are most affected by an organisation's decisions.

Meanwhile, the *Stakeholder Approach to Accountability* goes beyond the traditional approach and domain of formal authority. This approach is more participative in nature and democratic in spirit.

- **Social Accountability:** It means public accountability through civic management. It is a process by which accountability is exacted from accountability holders through direct or indirect citizen action and engagement. Social accountability ensures transparency, reduces leakage, forces proper spending of funds, generates trust and peace and creates demand-led improvement in services. It has both intrinsic value of strengthening democratic relationships of empowering people and in being instrumental in developing effectiveness through better services delivery and better governance. In a sense, it is a continuing audit and a constant check on malfeasance.

Social Audit vs. Financial Audit

Social Audit is often misinterpreted as another form of audit to determine the accuracy of financial or statistical statement or reports and the fairness of the facts they present.

A conventional financial audit focuses on financial records and their scrutiny by an external auditor following accounting principles whereas the Social Audit is much more holistic having a greater scope for measuring, understanding and improving the social performance of an activity of an organisation.

Financial audit is geared towards verification of reliability and integrity of financial information whereas Social Audit examines performance of a department/programme *vis-à-vis* its stated core values in the light of community values and the distribution of benefits among different social groups reached through good governance principles.

Financial Audits of an NGO of a development project primarily focus on:

- ▶ Financial Documentation
- ▶ Appropriateness of Expenses
- ▶ System of processes
- ▶ Budgetary framework

But does not adequately address or capture two crucial issues that are integral to the existence or purpose of every NGO. They are:

- Issue of Relevance, and
- Area of effectiveness

In case of Financial Audit, there is no standardisation or prescribed format available for preparation of financial statement by the NGOs. The financial

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By Social Audit, the organisation can better manage its risks, as it can enhance its social focus by covering any adverse social impacts highlighted by it in a social audit report. It enhances organisational reputation. By demonstrating its social performance and commitment to social objectives, the organisation enhances its reputation among and gains political capital with stakeholders. It affects positive organisational change. Information on social performance allows management to take constructive action to improve it. ”

statement prepared by the NGOs does not meet the reporting expectation of gamut of all the stakeholders.

The Income and Expenditure account is a point in the case. The Income and Expenditure account gives us information on excess of income over expenditure or *vice versa*. In either of the case, it does not communicate anything about the financial health of the organisation.

Objectives of Social Auditing

The broad objectives of any social engagement will be the following:

- Assessing the physical and financial gap between needs and resources available.
- Creating awareness among beneficiaries and providers of social and productive services.
- Increasing efficacy and effectiveness of development programmes.
- Scrutiny of various policy decisions, keeping in view stakeholders interest and priorities, particularly of marginal section of the society.
- Estimation of opportunity cost for stakeholders of not getting timely access to public services.

However, specific objectives of the social Audit engagements will depend on the context.

Benefits of the Social Audit

- ▶ **Increased social focus- Tool for Risk Management:** The organisation can better manage its risks, as it can enhance its social focus by covering any adverse social impacts highlighted by it in a social audit report.
- ▶ **Enhanced credibility:** It enhances organisational reputation. By demonstrating its social performance and commitment to social objectives, the organisation enhances its reputation among and gains political capital with stakeholders.
- ▶ **Helps in policy decision:** It affects positive organisational change. Information on social

performance allows management to take constructive action to improve it.

- ▶ **Increased confidence:** It provides increased confidence in social areas. Social auditing offers a roadmap on how to move forward productively on social issues and for addressing/managing stakeholder concerns.
- ▶ **Positive support from stakeholders:** It permits stakeholders to have a say in the organisation and its policies and behaviors.
- ▶ **Disclosure of achievements:** It allows the organisation to report on its achievements based on verified evidence rather than on anecdotes and unsubstantiated claims.

India and Social Audits

India is fast progressing both in terms of technological innovations as well as economic advancement. We no longer discuss the future of India. We say the future is India. There are four important factors that determine a country's future-

- ▶ **Growth** - Rate of growth, quality of growth and scope of growth
- ▶ **Globalisation** - Trade, investment, communication
- ▶ **Geo-Politics** - Relations with neighbours
- ▶ **Governance** – Another important factor that is of crucial importance is “Governance”. Good Governance refers to a system which ensures participation and efficiency, but most importantly Good Governance must ensure Accountability.

Why Social Audit is Required in India:

Former Prime Minister late Shri Rajiv Gandhi had once famously said that only 16 Paise out of one Rupee sanctioned by government reach poor. In an article in 19th December 2004 edition of Times of India, Aiyar Swaminathan had commented that “Likelihood of money reaching the poor would be higher if we simply drop the money by helicopter or gas balloon into rural areas than route it through employment programmes”. The situation with respect to our government/public schemes has not changed much since then. Even today a crisis of credibility, confidence and trust persists with respect to government projects, programmes and schemes. High economic growth is threatened by corruption at all levels. Leakage of funds in public programmes and misuse of shareholders and stakeholders resources is a common scenario. There has been a growing tendency of depriving the marginalised in the name of “Development”. Of late, it is being noticed that ‘Social Conscience’ is fast eroding and the Means don't matter— the End justifies any means. Inequitable resource allocation is a common concern in the country. This background calls for the

culture of social audits to take roots in the country, in both private and public sector.

Social Audits in India (Present Status):

- Social audit is one of the audit functions with focus on monitoring various programmes. In India, it is used in the context of the effectiveness of the schemes/programmes run by the Government of India
- Social Audit in India does not ordinarily have any relation with corporate or business institutions.
- Companies engaging in Corporate Social Responsibility (CSR) do not generally produce a social audit report regarding their organisations.
- Social Audit in India is usually targeted at the public works by the government and usually with a methodology of involving public through physical verification of works, records assessment, public hearing and mass mobilisation, etc.
- Social Audit is used for exposing corrupt practices of public administration or enforcement of rights.

Social Audit gained significance especially after the 73rd Amendment of the Constitution relating to Panchayat Raj Institutions. That empowered the *gram sabha* to conduct Social Audits in addition to its other functions, and it was by far the only legislative reference to the concept of social Audit. The Right to information Act, 2005 is also a key pillar of support for Social Audit system in India. This was enacted by Parliament of India to provide for setting out the practical regime of the right to information for citizens. Section 17 of National Rural Employment Guarantee Act, 2005 provides for regular “Social Audits” so as to ensure transparency and accountability in the scheme. ”

Legislative Support Available to Social Audit in India

(a) The 73rd amendment of the Indian Constitution: Social Audit gained significance especially after the 73rd Amendment of the Constitution relating to Panchayat Raj Institutions. That empowered the *gram sabhas* to conduct Social Audits in addition to its other functions, and it was by far the only legislative reference to the concept of Social Audit.

Right to information Act, 2005: This is also a key pillar of support for Social Audit system in India. This was enacted by Parliament of India to provide for setting out the practical regime of the right to information for citizens.

The Act applies to all states and union territories of India, except the state of Jammu and Kashmir. This Act also requires every public authority to computerise records for wide dissemination and to proactively publish certain categories of information so that the citizens need minimum resources to request for information formally. This is again a support for Social Audit system in India.

National Rural Employment Guarantee Act, 2005 (NREGA): Section 17 of this Act provides for regular “Social Audits” so as to ensure transparency and accountability in the scheme. It is the responsibility of the state government to conduct the Social Audit. The state government will conduct the Social Audit according to the pre-designed “Schedule of Social Audit”. The state government is to ensure that the agencies for conducting Social Audit are trained.

The Draft “**NREGA Transparency and Public Accountability Rules**” lay down detailed guidance for conduct of Social Audit.

The government has been instrumental in establishing an independent Social Audit Society for carrying out the Social Auditing of NREGA in the state. This society is called “**Society for Social Audit**”



At present Social Audit is conducted by various agencies appointed by Central and State Government. However, Chartered Accountants can play a vital role in the social reporting framework by ensuring the effectiveness of the social audit programme in non-corporate as well as corporate sector, which in turn would contribute positively to the society at large. Chartered Accountants with social sector orientation and working collaboratively with social sector professionals are eminently suitable to undertake capacity building and training of human resources who will be involved in undertaking the actual Social Audit. ☺☺

Other social sector programmes also laid down provisions and procedure for "Social Audit". For example:

The ministry of Housing and Urban Poverty alleviation has laid down Social Audit methodology and operational guidelines for various schemes. The **Andhra Pradesh Government** engaged MV foundation, a voluntary organisation working on the issue of child labour and children's right to education, to conduct "Social Audit" of Mid-Day Meals in Andhra Pradesh.

Social Audit and Chartered Accountant

It is very much clear that the scope of Social Audit is much beyond financial audit.

In a commercial organisation, many of the issues have the potential to be translated into financial terms. But in the case of non-profit organisations (NGOs), it becomes more difficult. The whole process of involvement for transformation would not be possible to be translated into financial terms easily.

The financial audit would lose some of its significance if the concept of impact cannot be integrated in it. Therefore, a process of Social Audit would look at the whole gamut of the impact the programme has on communities and eventually to judge its success.

We also need to recognise the fact that Social Audit is not completely in the domain of Chartered Accountants as they involve various tools and processes which may not be their domain of expertise. Therefore, we need to look at ways and means to integrate Social Audit components to the existing financial audit to make it more effective.

Role of Chartered Accountants in Social Audit:

At present Social Audit is conducted by various agencies appointed by Central and State Government.

However, Chartered Accountants can play a vital role in the social reporting framework by ensuring the effectiveness of the social audit programme in non-corporate as well as corporate sector, which in turn would contribute positively to the society at large.

A **Social Auditor** is expected to possess certain characteristics, which are as follows:

- (a) **Strong Network:** To conduct Social audit of large public programmes a strong network of Social auditors is required.
- (b) **Independence and Unbiasedness:** The Social Auditor should have no stake in the outcome of the Audit and should be totally independent of management and its system.
- (c) **Expertise and knowledge:** The Social Auditor should be someone who specialises in conducting social audits with the appropriate training and experience.
- (d) **Inquisitiveness and professional skepticism:** Social Auditing requires someone unwilling to accept things at face value and capable of drilling down deeper to uncover issues that are deeper than what appears prima facie.
- (e) **Ability to understand impact of programme/corporate actions in their wider social context:** Social performance must be understood within the context of a diverse stakeholders and a diverse set of perceptions, values, objectives, etc. An effective Social Auditor must be both willing and able to consider a variety of sources and perspectives for an understanding of social performance.
- (f) **Adhere to standards:** The Social Auditor should be able to follow certain standards in their Audit Process and standards on reporting so that the users of Social Audit reports are able to rely on the information contained in those reports.

Chartered Accountant as a Social Auditor

Given the above characteristics, Chartered Accountants are the one of the groups of professionals that is able to understand and to fulfill the objectives and requirement of Social Auditors.

Chartered Accountants with social sector orientation and working collaboratively with social sector professionals are eminently suitable to undertake capacity building and training of human resources who will be involved in undertaking the actual Social Audit.

(a) Professional Training: By professional training in Auditing and being sworn to ethical standards, a Chartered Accountant possesses the required intelligence and independent mindset to deliver Social Audits in India.

(b) Regulatory Mandate: As of date, there is no regulatory mandate for Chartered Accountants to

act as Social Auditors or for any other professional body for that matter; However, creation of appropriate institutional mechanism for training and capacity building will be one of the key deciding factors for pre-eminence in this very critical and emerging area of professional services.

(c) The essential Requisite for Chartered Accountant:

The essential requisites for CAs to become the first choice as Independent Social Auditors are that they should be able to train themselves in two specific aspects, namely:

- (i) Social Auditing and Reporting Standards
 - (ii) Mapping Stakeholders and Social Indicators.
- (i) *Social Auditing and Reporting Standards:* Training on Social Auditing and Reporting Standards is a generic requirement as we all Chartered Accountants are already equipped for that.
- (ii) *Mapping Stakeholders and Social Indicators:* Mapping of Stakeholders and identification of social indicators that can be used for the purpose of Social Audit may vary from engagement to engagement as per the terms of assignment and purpose of the Audit. Chartered Accountants could rely on established Social Indicators that have been formulated by various agencies like United Nations, World Bank, Investment Commission of India, OCED and several others. These Indicators that are relevant for a particular engagement may need to be identified specifically by the Auditor after discussion with the various stakeholders groups who need to be interviewed in the planning phase. There is definitely a case for CAs to collaborate with practitioners of Social Science for Complex Social Audit Projects to add greater value to the users of Social Audit reports.

(d) Social Audit - Supply Side: On the supply side, CA



On the supply side, CA firms have the option of consortium to build capacity and methodologies specifically targeted for Social Audits. On the demand side there

is the need to push for regulatory mandate for Social Audit for Public utility projects undertaken by Government's Social Sector expenditure projects on the lines of MGNREGA. Certain such Projects where Social Audits could be looked at are *Rajiv Gandhi Gramin Vidutikaran Yojana, Sarva Siksha Abhiyan, Pradhan Mantri Gram Sadak Yojana, Pradhan Mantri Gramodyog Yojana, Swarna Jayanti Gram Swarozgar Yojana, Swarna Jayanti Shahari Rozgar Yojana and Bharat Nirman.* ”



firms have the option of consortium to build capacity and methodologies specifically targeted for Social Audits. Specific Training Modules and certification/ accreditation system could be introduced to encourage confidence in the minds of the users of Social Audit services about the quality standards being followed for audit engagements.

(e) Social Audit- Demand Side: On the demand side there is the need to push for regulatory mandate for Social Audit for public utility projects undertaken by government Social Sector expenditure projects on the lines of MGNREGA. Certain such projects where Social Audits could be looked at are as below:

- *Rajiv Gandhi Gramin Vidutikaran Yojana*
- *Sarva Siksha Abhiyan*
- *Pradhan Mantri Gram Sadak Yojana*
- *Pradhan Mantri Gramodyog Yojana*
- *Swarna Jayanti Gram Swarozgar Yojana*
- *Swarna Jayanti Shahari Rozgar Yojana*
- *Bharat Nirman*

An audit process also serves as a means of information to the stakeholders of the organisation to make informed decision. If the information generated and disseminated through the audit process is relevant for decision making, it will be very useful to the stakeholders.

Conclusion

Social Audit is proposed as a supplement to conventional audit to help government department/public agencies/ NGOs understand and improve their performance as perceived by the stakeholders. Chartered Accountants belong to a highly respected and trusted profession and they are committed to maintain the dignity of the profession. As key professionals, CAs can contribute their services towards development of national capacity building as a partner of the Government of India in Social Audit. ■

Assurance on Corporate Sustainability Reports



Global warming, climate change and pollution have raised serious concerns about organisations' sustainability. Since Industrial Revolution in 18th century; mammoth business entities through their activities have continuously been snatching away natural virginity, polluting environment and degrading socio-economic norms. Triple bottom line model of sustainability report takes care of organisational contribution to Planet, People and Profit. In 2004, International Federation of Accountants (IFAC) defined Sustainability Reporting as “a process in which a practitioner expresses a conclusion designed to engage the degree of confidence that intended users can have about the evaluation or measurement of a subject matter that is the responsibility of a party, other than the intended users or practitioner, against criteria”. Assurance on corporate sustainability report increases the level of transparency, authenticity, fairness and acceptability of the published reports. This article provides an insight into assurance on sustainability report and how it is going to be a promising professional opportunity for accountants worldwide.

'Sustainability' was coined from sustainable development. Brundtland Commission (1987) defined sustainable development as that form of development which "meets the needs of the present without compromising the ability of future generations to meet their own needs". Although the word as used in Sustainability Reports has little relation with the planetary 'Sustainability' in true Brundtland's sense, the report, however, allows one to assess the impact that a company has on the environment and on society as well as its economic performance. Therefore, the reports try to embrace economic, social and environmental strategies that contribute to long term organisational success.

Sustainability Report (SR)

A sustainability report refers to a single, consolidated disclosure that provides a reasonable and balanced presentation of performance over a fixed time period (Global Reporting Initiative, 2006). Such reports may include quantitative and qualitative information on their financial/ economic, social/ethical and environmental performance in a balanced way.



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Since 1990s, after the publication of Brundtland's Report, corporate entities have been using 'sustainability report' as an umbrella term for all the non-financial reports comprising triple bottom line (TBL), sustainability, corporate social responsibility (CSR), stand-alone environmental, health and safety, social community and citizenship reports and combination of these (KPMG 2002, 2005).

Assurance on Sustainability Report- An Insight

Over the recent years there has been an inexhaustible interest in the auditing of corporate sustainability reports. "Assurance" is increasingly being used for referring to this kind of audits, because they cannot offer the same level of assurance provided by the financial audits. Assurance is an evaluation method that uses a specified set of principles and standards to assess the quality of a Reporting Organisation's subject matter, such as the Reports and the organisation's underlying systems, processes and competence that underpin its performance. It includes the communication of the results of this evaluation to provide credibility to the subject matter for its users (AccountAbility 1000 Standard, 2003). In 2004, International Federation of Accountants (IFAC) defined it as "a process in which a practitioner expresses a conclusion designed to engage the degree of confidence that intended users can have about the evaluation or measurement of a subject matter that is the responsibility of a party, other than the intended users or practitioner, against criteria". Since there are no mandatory standards to be followed while reporting and assuring, verification of SR is nothing but an assurance given by an assurance provider.

Key Assurance Elements

■ Existence of Three Party Relationship

- (i) **Accountable/Responsible Party:** They disclose information to intended users for exhibiting corporate social responsibility.
- (ii) **Assurance Provider:** Person or organisation who provides independent assurance is called assurance provider. Neither the accountable party nor stakeholders can be an assurance provider. Because he should be independent of responsible party and should exhibit highest standards of ethical and professional integrity achieved through long experience and training.
- (iii) **Stakeholders/key intended Users:** They are the real users of this report which has diverse audiences. Stakeholders are the persons or organisations who influence or are influenced by the activities of the entity.

■ Appropriate Subject Matters and Scope

Subject matters are subject of assurance. They may comprise data, systems, processes and behaviour. Triple bottom line (TBL) reporting which encompasses economic, environmental and social information is the most accepted form of SR. Its scope includes subsidiary or

group companies, divisions, units, types, categories and details of diverse quantitative and qualitative information, etc. Scope of the subject matters is appropriate when it complies with suitable reporting criteria, reported continuously without any omission. Subject matter has to be identifiable, capable of consistent evaluation or measurement against suitable criteria and in a form that can be subject to procedures for gathering evidence to support that evaluation or measurement (IFAC, 2004).

■ Assessment Criteria

Criteria are the standards or benchmark used to evaluate or measure the subject matters of sustainability information and to announce assurance conclusion by the assurance provider. In financial accounting, financial data or transactions are recognised, measured, presented and disclosed with the help of established criteria such as International Financial Reporting Standards (IFRSs) or other Generally Accepted Accounting Principles (GAAPs). But there has been a lack of such internationally or generally accepted criteria for SR. The most widely accepted international, multi-stakeholders standards are first provided by GRI in 1999. While GRI has provided criteria based on TBL, others have concentrated on social and environmental aspects (e.g. Social Accountability 8000) or only environmental aspects (e.g. Public Environmental Reporting Initiative or PERI). Criteria should satisfy the following essential qualities:

- **Relevance** means to assist stakeholders to make decisions and reach conclusions.
- **Reliability** facilitates rational and consistent evaluation.
- **Completeness** addresses all factors related to triple bottom line that affect conclusion reached for each engagement.
- **Neutrality** facilitates to reach unbiased conclusion.
- **Understandability** indicates that criteria should be understandable to three parties involved in the process, facilitates to reach clear and comprehensive conclusion.

■ Collection of Evidence

The assurance provider should *obtain sufficient and appropriate evidence* on which to base his conclusion. Sufficiency is the measure of quantity of evidence. Appropriateness is the measure of quality (relevance and reliability) of evidence. While obtaining evidence, he should consider the cost and usefulness of obtaining evidence and information. However, the expenses or difficulty involved should not be a valid plea for omitting an evidence gathering procedure unless it is impractical. The *reliability of evidence* is affected by source (internal or external), nature (written, oral, and electronic), process, circumstances in which it is obtained including controls over their preparation and maintenance. He should obtain *additional evidence* to resolve inconsistency in the

sources or nature of evidence. He should also exercise professional skepticism at the time of assessing sufficiency and appropriateness of evidence.

He is required to judge the *materiality* of specific engagement and assess the relative materiality of quantitative and qualitative factors. *Risk*, which has a positive correlation with the sufficiency and appropriateness of evidence, is another important factor. Assurance risk is the possibility that assurance provider reaches inappropriate conclusion when sustainability report is materially misstated. Just like financial audit there are three types of risk, viz. inherent risk, control risk and detection risk. For reasonable assurance, the assurance provider reduces assurance risk to an acceptably low level. However, he expresses a limited assurance conclusion when the risk is acceptable but higher than that is required for reasonable assurance.

■ Assurance Report

It consists of statements from assurance provider and his conclusion. Upon completion of assurance engagement, conclusion should be made available to diverse stakeholders through properly formulated assurance report.

Assurance Provider/Assurer:

In India, Companies Act, 1956 gives exclusive powers to Chartered Accountants (CAs) to conduct statutory financial audit of companies. Preparation of SR and its assurance is not mandatory. However, professional accountants like CAs possess enormous skills and experiences in the field of finance, management and corporate governance. They can also prove their supremacy and expertise in the assurance of environmental and social aspects if they acquire proper knowledge, training and experience. Study made by Deegan, Shelly and Cooper in 2003 revealed the following relative market share of different categories of assurance providers for corporate SR:

Country	Percentage of Companies			No. of reporting organisation Surveyed
	Accountants	Environmental Consultants	Others	
Europe (excluding UK)	59.60	19.20	21.20	52
UK	22.90	54.20	22.90	48
Japan	37.50	6.30	56.30	16
Australia	16.70	40.00	43.30	30
Total	36.30	33.60	30.10	146

Another study conducted by Dr. B.K. Basu of Calcutta University in 2003 relating to environmental assurance provider revealed that 55 per cent of population opined in favour of independent audit firm against 45 per cent for multi-disciplinary teams.

Worldwide there is strong backing for accounting professionals for undertaking such type of assignments.

However, such assurance should be conducted by multidisciplinary team comprising experts from finance, accounting, auditing environment science, sociology, engineering and technology, etc. for greater efficiency and effectiveness.

Assurance Approaches

Mainly three approaches are followed worldwide. They are:

- **Structured/ Accounting Approach-** It is inspired by financial audit process and mainly concentrates on collection of evidence, risk perception or analysis of assurance provider. Under this, engaging company provides report to assurance provider who conducts independent assurance/review by applying well-developed standards/guidelines and provides his report based on collection of evidence and objective assessment of risk involved in that engagement. The main criticisms are that it places more emphasis on accuracy of quantitative data and robustness of the accounting systems. Moreover, the assurance has failed to provide reasonable level of confidence to stakeholders and relevance of information disclosed. In India ITC Ltd. followed this approach in 2009-2010.
- **Social Audit Approach-** Social audit is a broad term in which an independent third party report is given without any report from the appointing company. A committee of external experts is formed and they uptake dialogues of external stakeholders with/without cooperation from the company. Sometimes company provides report on which the auditor comments or stakeholders such as NGOs play the role of assurance provider. Main criticisms are that there is lack of perceived neutrality of the assurance function and conflict of interest among the stakeholders. Tata Company follows such approach.
- **Consultancy Approach-** Consultancies do not have a uniform approach. Here the appointing company is benefited by the assistance from external experts. Employees of the company together with expert team conduct the assurance process. The main criticism is that instead of assurance they recommend the features of performance. Royal Dutch Shell Energy followed such approach in 2007.

Standards of Assurance

The organisations generally use the following international standards relating to assurance on SR.

1. International Standard on Assurance Engagements (ISAE) 3000-

ISAE 3000- Assurance Engagement Other Than Audit or Reviews of Historical Financial Information was developed by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC). It is used by the assurance providers of sustainability reports to guide

their assurance engagements.

2. AA 1000 Assurance Standard (AA 1000 AS), 2008-

The AA 1000 assurance Standard was launched in 2002 by UK-based AccountAbility. It was specifically designed to be consistent with assessment criteria developed by the GRI guidelines. AA 1000 AccountAbility Principles Standard (AA 1000 APS) 2008 is used by organisations to develop an accountable and strategic response to sustainability including reporting.

3. The Social Accountability 8000 Standard (SA 8000®)

It is a global work-place standard launched in 1997 that covers key labour rights such as working hours, forced labour and discrimination and crucially certifies compliance through independent accredited auditors. It is based on the core conventions of International Labour Organisation (ILO), the United Nations Convention on the Rights of the Child and the Universal Declaration of Human Rights. The third issue of SA 8000® was released in 2008. By June, 2009, SA 8000 had certified nearly 2,010 facilities in 64 countries representing 66 industries and 11,19,145 employees.

The other international standards are ISO 14010 (provides guidelines for environmental auditing- general principles) and ISO 14011 (Audit procedures and auditing of environmental Management Systems). In addition to these, organisations in different countries are also required to comply with different mandatory and voluntary standards, codes and regulations, etc. relating to environmental and social, ethical aspects of business.

Levels of Assurance

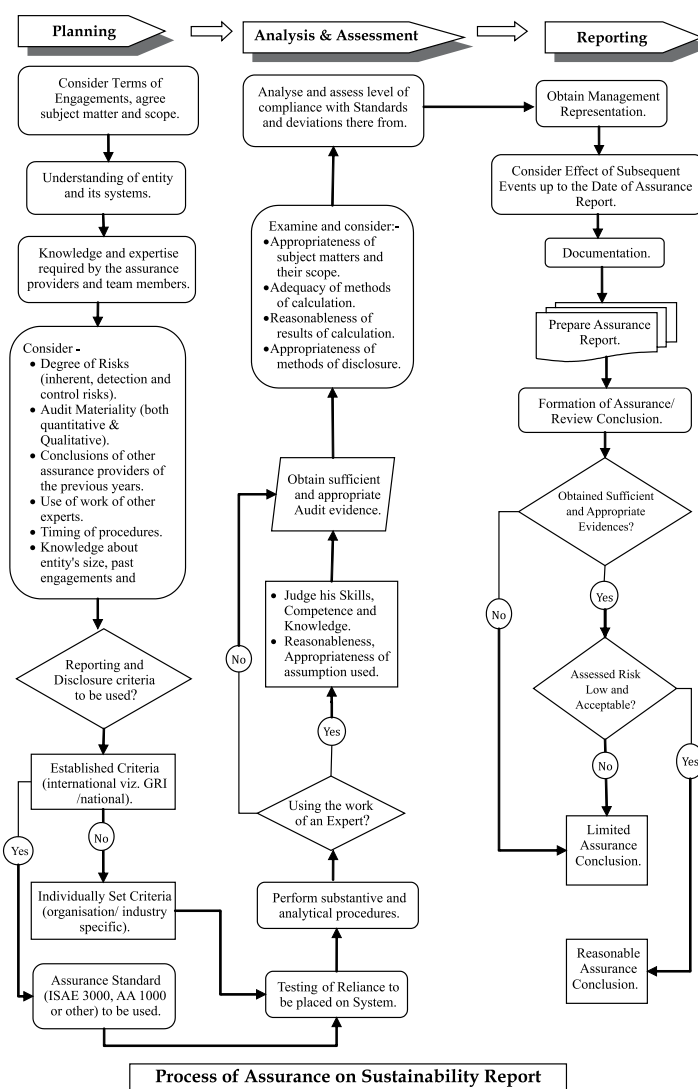
The assurance conclusion may be of the following types:

- **Reasonable Assurance** is provided when assurance providers judge assurance risk (inherent, detection and control risk) to be low. They should either attach conditions or not assign reasonable assurance for lack of sufficient and appropriate evidence. It is similar to a financial statement audit and results in a positive expression of conclusion in their sustainability assurance reports. For example, "In our opinion, ... Ltd's sustainability report is presented fairly in accordance with.....(Standards) Guidelines"
- **Limited Assurance** is assigned if they judge assurance risk to be higher than that for reasonable assurance, provided the risk is acceptable if they use negative expression in their reports. It is provided based on the

conclusion that they will not be able to obtain sufficient and appropriate evidence to assign reasonable assurance. It is similar to financial statement review and results in a negative expression of conclusion. For example, "Based on the procedures described in our report, nothing has come to our attention that causes us to believe Ltd's sustainability report is not fairly presented in accordance with ...(Standards) Guidelines".

Assurance Process

The process followed for assurance on SR is generally same like financial audit. The following diagram shows the process:



Joint Assignment

In case of joint assignment of large entities there should be a clear separation of duties and responsibilities. The report may be signed by both assurers and report should

clearly indicate the fact. In this respect International Standard of Auditing (ISA) 299 on joint auditors may be referred to.

Using the Work of an Expert

In collection and evaluation of evidence, the assurer and the expert should, on a combine basis, possess adequate skills and knowledge regarding the subject matters and criteria to determine that sufficient and appropriate evidence has been obtained. In assessing the sufficiency and appropriateness of evidence, the assurer should evaluate expert's competence, reasonableness of assumptions, methods used including the source of data. ISA 620 provides guidance in this aspect.

Subsequent Events and Assurance

Subsequent events are the events which occur between the date of SR and assurance report. They may affect the sustainability information and assurance report. Therefore, assurance provider is required to evaluate the possibility and impact of the events on the SR and his report. If such events significantly affect the information provided in SR and conclusions of assurance provider, he must consider that they are appropriately disclosed in SR and considered in his report.

Content of Independent Assurance Report

Assurance report generally has two parts- statements in assurance report and conclusion. It may include the following:

- Title to the Report- Specifically state that it is an independent assurance report.
- Addressee
- Brief description of engagement and identification of subject matters
- Preparation or assessment criteria- Whether internally generated/based on national codes, regulations/ international criteria (G3 guidelines of GRI).
- A description of significant, inherent limitations associated with evaluation and measurement of the subject matter against the criteria
- Statement disclosing responsible party, responsibilities of responsible party and practitioner
- Statement disclosing standards under which engagement was performed
- Identification of the report users and the purpose of report
- Practitioner's conclusion- Unqualified, qualified, adverse and disclaimer of opinion
- Report date
- Name of the assurance provider, Firm Name (with Registration No.) and place of issue.

Global Trends of Sustainability Reporting- Emerging Opportunities for CAs

Social and environmental reporting was still considered

to be in fancy just a few decades ago, although its history can be traced back to the 1970s. There has been a clear increase in percentage of the large 100 companies in a number of countries publishing environmental or sustainability report. It was 12 per cent in 1993, 17 per cent in 1996, and 24 per cent in 1999. International Surveys of Corporate Responsibility Reporting 2005 and 2008 by a leading global firm show the following exciting global trends:

	% of Companies					
	2002		2005		2008	
	G 250	N 100	G 250	N 100	G 250	N 100
Standalone Sustainability/ Corporate Responsibility Report	45	23	52	33	79	45
Combined with Annual Report	-	-	12	8	8	9

United Nations Global Compact (UNGC) and Accenture CEO Survey 2010 shows the following:

- 93 per cent of CEOs believe that sustainability issues will be critical to the future success of their business.
- 58 per cent of CEOs identify consumers as the most important stakeholder groups that will impact the way they manage societal expectations and employees were second with 45 per cent.
- 91 per cent of CEOs report that they will employ new technologies to address sustainability issues over the next five years.
- 96 per cent of them believe that sustainability issues should be fully integrated into the strategy and operations of a company.

Joint research survey of AICPA, CIMA and CICA (December 2010) shows that among large companies, 29 per cent include sustainability information in their

United Nations Global Compact (UNGC) and Accenture CEO Survey 2010 shows that 93 per cent of CEOs believe that sustainability issues will be critical to the future success of their business. 58 per cent of CEOs identify consumers as the most important stakeholder groups that will impact the way they manage societal expectations and employees were second with 45 per cent. 91 per cent of CEOs report that they will employ new technologies to address sustainability issues over the next five years. 96 per cent of them believe that sustainability issues should be fully integrated into the strategy and operations of a company.

The numbers of organisations taking care of triple bottom line of sustainability and issuing reports assured by professional accountants are increasing

gradually. However, there are some hindrances such as perceived high cost, no clear cut format, lack of global standards, secrecy and unwillingness, etc. In public sector, Navratnas and others such as, ONGC, SIDBI, Hindustan Paper Mills Ltd etc. are contributing their best efforts towards sustainable development. ”

annual reports, 17 per cent publish separate sustainability reports and 13 per cent do both. Among small and medium sized (SME) companies these are 6 per cent, 8 per cent and 2 per cent respectively. Therefore, independent assurance of SR is going to be budding professional opportunities for accounting professionals like Indian CAs. According to GRI, as on 15th February, 2011 more than 1100 in 2008, 1400 in 2009 and 1700 in 2010 organisations published sustainability reports worldwide. All these show that there has been a growing trend among the corporate entities

globally to include and report sustainability into their agenda. In India there are many organisations which publish such reports assured by auditors. In the coming years the number of companies seeking independent assurance of their SR will obviously increase.

Conclusion

The numbers of organisations taking care of triple bottom line of sustainability and issuing reports assured by professional accountants are increasing gradually. However, there are some hindrances such as perceived high cost, no clear cut format, lack of global standards, secrecy and unwillingness, etc. In public sector, Navratnas and others such as, ONGC, SIDBI, Hindustan Paper Mills Ltd etc. are contributing their best efforts towards sustainable development. Recently the Accounting Research Foundation (ARF) of the Institute of Chartered Accountants of India (ICAI) has taken up a project to formulate a comprehensive standard on sustainability reporting. In near future, it is highly expected that more and more companies will be disclosing their sustainability performances and get their reports assured by independent third party. ■

Enhancement of Value for Corporate Reporting in Current Competitive Era



The fundamental objective of financial accounting is to provide users of financial statements with useful information for the purpose of efficient and effective decision making. Outside of the firm, financial reporting should provide information that is useful to present and potential investors, creditors in making rational investment as well as credit decisions. Within the firm, accounting information is essential for the purpose of efficient managerial decision. But in current competitive and globalised environment traditional reporting of business affairs are not sufficient to fulfil the requirements of shareholders, investors and other interested parties, due to the changes in the nature of transactions, business activities, shifting of focus towards industrial economy to knowledge economy, and growing importance of service sector in the economy. At present stakeholders need qualitative nature of financial reporting, because it includes relevance, faithful representation, comparability and understandability of information. Keeping all these issues in view, this article is an attempt to highlight the important reporting methods which can be used in the preparation of financial statement to enhance the value of corporate reporting for the shareholders, investors, and other stakeholders and also enlarge and widen the usefulness of the annual reports in the globalised and competitive environment. The author has also evaluated the present position of Indian corporate's concerning the adaptation of contemporary reporting practices.

“What is not started today is never finished tomorrow” – Johann Wolfgang von Goethe

This quotation is equally relevant in case of accounting profession also, because whatever latest practice and methods we are adopting today for presentation/reporting of corporate data that leads to the leader in the tomorrow. Financial accounting and reporting practices have traditionally provided a basis for evaluating a company's business performance. The primary objective of financial accounting is to make available the users of financial statements with constructive information for the purpose of competent and valuable decision making. Outside of the firm, financial reporting should provide information that is useful to present and potential investors and creditors in making rational investment and credit decisions. Within the firm, accounting information is essential for the purposes of efficient managerial decision making-as managers need timely and accurate information in order to carry out the budgeting process and implement effective control mechanisms. Consequently, any event that is likely to affect a firm's current financial position or its future performance should be reflected in its annual accounts. Unfortunately, conventional financial statements appear to be rapidly becoming less useful within today's dynamic business environment¹. Exhibit I indicates the shift of value paradigm in the last one century at global level of accounting profession. Especially, in the last twenty years

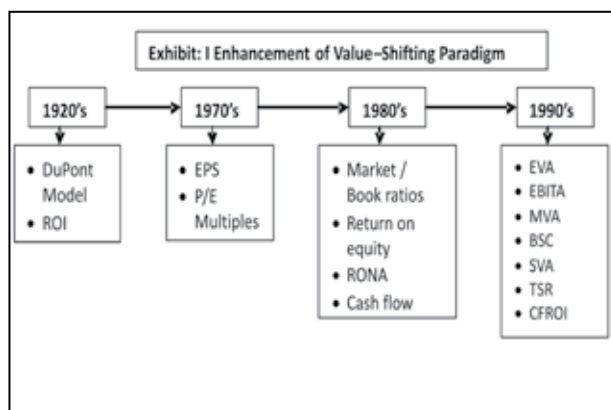


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¹ S. Zambon (2002): "Accounting, Intangibles and Intellectual Capital: an overview of the issues and some considerations" WP4: Accounting, Audit, and

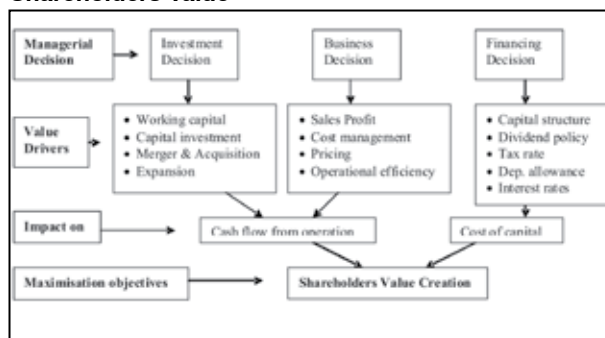
corporate's more focusing on EVA, MVA, SVA, TSR, for enhancement of value reporting in the contemporary environment.



Source: Madhu Sehrawat (2009): *EVA and Performance measurement-text and case studies of Indian companies* pp 9

Disclosure of accounting information is also an important aspect of the globalised environment. Disclosure means information regarding a business unit can be communicated with the help of reports and statements to the stakeholders, interested parties and potential investors will be informed of the strengths and weaknesses of a corporate, related with earning capacity, and activities of the management for the benefits of perspective investors. In regards one example is very appropriate *"UK based one retailer was facing supply issues with milk related products which constitute 9 per cent of sales. When the management information system threw up data (quality of reporting) regarding future challenges in this product strategy, the chain immediately started tying up with UK farmers on how to increase milk yields and address the shortfall²."* It indicate that quality of reporting directly affect the business strategy. As Bushman and Smith³ pointed out "Financial reporting and disclosure is an important component of a corporate governance system since it allows investors and other outside parties to monitor firm performance". In early times accounting was purely concerned with ascertainment of results of business enterprises (as indicated by exhibit II) and main objective of the corporates was to maximise the shareholder value and accordingly they performed various financial managerial activities. However, now a days financial reporting includes useful and other key information which provides the strength and earning capacity of the corporates (which cannot be measured in the money value) also disclosed to meet the users needs and expectations.

Exhibit: II Impact of Managerial Decision on Shareholders Value



Source: Ravi M Kishore (2005): *Financial management text and cases*, pp 224

Significance of Discloser and Reporting

As we know that annual reports are the one of the popular method of reporting since centuries. But, in the current competitive and globalised environment traditional reporting is not sufficient to fulfil the requirements of shareholders, inventors and other interested parties due to the change in the nature of transactions, business activities shifting of focus towards industrial economy to knowledge economy and growing importance of service sector in the economy. However, we have not received more realistic and useful information rather than only accounting information as provided by the companies under Indian GAAP. Therefore, we need voluntary reporting for following reasons:

Firstly, voluntary reporting contributes to reducing the information irregularity between management, shareholders and investors.

Secondly many useful information's /intangibles are not recognised in the financial statement, highly innovative companies where intangibles play a significant role have much greater difficulty attracting investors and banks. In these cases, voluntary disclosure of information can help to reduce the uncertainties of investors and banks and, at the same time, it allows companies to have greater access to funds⁴.

During the last two decades most industrialised economies have progressively moved towards a knowledge-based rapidly changing economy where investments in human resources, information technology, R&D and advertising have become essential in order to strengthen a firm's competitive position and ensure its future viability⁵. Qualitative nature of financial reporting is significant because it includes relevance, faithful representation, comparability and understandability of

² Quality of reporting and transparency- by Charles Tilley, chief executive ICMA, The Hindu business line, 28th October 2010 pp 12

³ Bushman, R. J. and A. Smith. (2001). "Financial Accounting Information and Corporate Governance." *Journal of Accounting and Economics* 32 (1-3): 237-334

⁴ RICARDIS (Reporting intellectual capital to augment research, development and innovation in (SMEs), 2006. Report to the commission of the high level expert group.

⁵ Blair and Wallman (1997).

data and information. Relevance implies providing the right information to the right people. Faithful representation concerns with the financial reports to real world economic situation and assured stakeholders of the verifiability, neutrality and completeness of the information.

Keeping all these issues in view this research article is an attempt to highlights the important methods which can be used in the preparation of financial statement to enhance the value of corporate reporting for the shareholders, investors, and other stakeholders and also increase the usefulness of the annual reports in the globalise and competitive environment.

Tools for Value Enhancement for Corporate Reporting

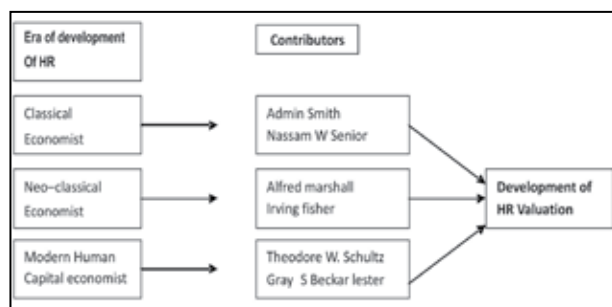
At present corporate financial reporting has taken an important place in the accounting world. There is increasing awareness among the investors about information provided by companies in their financial reports. With the help of the following tools/methods a firm can enhance the value of information for the various stakeholder for the decision making process.

Human Resource Valuation and Reporting

Human resources are one of the key elements of the knowledge economy. The conflict in accounting between human and non-human capital is natural. The latter is recognised as an asset and is, therefore, recorded in the books and reported in the financial statements, whereas the former is ignored by accountants for decades. Exhibit III indicates the different stages for the valuation and reporting for human assets which indicates that human resources are significant part of the corporate reporting but since many years it was ignored by the financial experts at the time of corporate reporting.

The most influential reason for the development of human capital is increase of service-oriented jobs in the economy. The nature of business activity has changed dramatically. Jobs in service-producing industries have increased greatly. At the same time manufacturing, farming, construction and other goods-producing jobs have fallen. We have changed from an economy in which the most significant business was industrial enterprises to one in which service business predominates.

Exhibit III: Era of Development of Human Resource and Valuation



Most of the enterprises, which follow human resource accounting, spare a separate section in their annual reports for a detailed account of their human resources. Human assets reporting in India usually includes a profile of human assets, the compensation pattern, training and development, human asset productivity, human asset value, and the total wealth of the organisation. The distinctive nature of our new economy is the importance of the human capital assets of an enterprise. The knowledge and skills of the employees in an entity, based on their educational development, training and experiential learning are increasingly the determinant of its ultimate success. The Microsoft Chief, Mr Bill Gates, once famously said: "Our primary assets, which are our software and software-development skills, do not show up on the balance-sheet at all". Obviously, he was indicating to his empire- the human skill.

Human Capital Valuation in India: In India HRA is not a new concept. In the 1974-1975's Bharat Heavy Electricals Limited (BHEL) and Steel Authority of India Limited (SAIL) initiated HRA, but unfortunately at that time, the HRA concepts were not in use widely. The concept started becoming popular in the mid 1990s once Infosys Technologies started valuing its employees in the financial years 1995-1996 by using Lev and Schwartz model, there after Satyam Computers, ONGC, HPCL and Reliance Industries introduced HRA in the year 2002. Nearly fifteen companies both public and private sector in India valued the human resources and included them in their annual report.

Exhibit IV: Human Resource Valuation Practices in India

S.N.	Name of the public Enterprises	HRA adopted (Year)	Model adopted	Discount rate applied
1	BHEL	1974-1975	Lev & Schwartz	12 per cent
2	SAIL	1983-1984	Lev & Schwartz	15 per cent
3	ONGC	1981-1982	Jaggi & Lev-Schwartz model	11 per cent
4	HPCL	1981-1982	Lev & Schwartz	11 per cent
5	CCI	1979-1980	Lev & Schwartz	11 per cent
6	NTPC	1986-1987	Lev & Schwartz	15 per cent
7	OIC	1982-1983	Lev & Schwartz	12 per cent
8	MMTC	1982-1983	Lev & Schwartz	15 per cent
9	MELON	1984-1985	Lev & Schwartz	12 per cent
10	EIL	1980-1981	Jaggi & Lev-Schwartz model	13 per cent
11	ELIC	1983-1984	Lev & Schwartz	10 per cent
12	KRL	1987-1988	Lev & Schwartz	12 per cent
13	MRL	1985-1986	Lev & Schwartz	15 per cent

Sources: Consolidated annual review of the companies.

Few companies are providing a separate section in their annual report about the number of employees, their grades, qualifications, remunerations and about the HRD, etc. There are many models for valuation of Human capital; each model has its own negatives and positives when it comes to practical application. In Indian context, present value of future earnings models (the Lev and Schwartz model) has an edge over the other models. This model has been widely adopted by Indian companies. Many Indian companies used the Lev & Schwartz model to compute the value of human resources. Their evaluation is based on the present value of future earnings of employees and on the assumptions such as, (a) employee compensation includes all direct and indirect benefits earned both in India and abroad, (b) the incremental earnings based on group/age have been considered, and (c) the future earnings have been discounted at the cost of capital in different rates.

Human Resource value reporting enables these companies to benchmark their performance and efficiency of their human resources with others. Infosys Technologies Ltd is absolutely providing all the information about its human resource and their valuation. The Human Asset value will disclose the value of human resources handling the organisational productivity and help to interpret return on capital employed properly. They establish a close relationship between workforce management and act as a bridge between the employer and employee. When expenditures on human resource such as recruitment cost, training cost and placement cost linked with return on investment (ROI) it become a vital tool for value addition and cost rationalisation. HRA is equally important for the country like India because our country has more human resource than others. If human resources are properly valued, then it is possible that we can preserve our human capital and with better utilisation we can make our country a developed one, within short period of time.

Brand Valuation and Reporting

Brand is an important element of intangible assets which is very popular in India as well as world in the era of globalisation. That brands are very important for the earning and market share enhancement points to view as to why more and more intentions are given by the shareholders as well as management regarding the valuation and reporting of Brand. Many Indian brands are popular and are leaders in Indian as well as global markets. For many businesses, brands have become critical for shareholder wealth creation. Global brands are still the most powerful and sustainable wealth creators in the business world and will continue to be so in the near future. The task of measuring brand value is a complex

one. Several models are available for valuation of brand but the most widely used is the brand-earnings-multiple model. There are several variants of this model. According to the *Business Week/Interbrand* annual ranking of the world's most valuable brands conducted and published in August 2009, Coca-Cola was valued as the most valued brand in the world for the year 2009 at \$67 billion, when its market capitalisation was \$106 billion. Thus, the brand valuation of Coca-Cola was around 64 per cent of its market cap on the date of valuation. The study goes on to state that even established brands like Coca-Cola and Microsoft have started to recognise the need to nurture stronger ties with the customer⁶. Many Indian companies such as Infosys and Satyam have adapted the Generic brand-earnings-multiple model⁷ to value their brands. They are using the following methodology for valuing the brand is as:

- (a) **Determine brand earnings**-Determine brand profits by eliminating the non-brand profits from the total profits of the company, Restate the historical profits at present-day values, Provide for the remuneration of capital to be used for purposes other than promotion of the brand, Adjust for taxes
- (b) **Determining the brand-strength or brand-earnings multiple**-**Brand-strength multiple** is a function of a multitude of factors such as leadership, stability, market, internationality, trend, support and protection. These factors have been evaluated on a scale of 1 to 100 internally by companies, based on the information available within.

Indian Experience: Brand valuation is a relatively new concept in Indian corporate environment. No specific guidelines have been issued by ICAI on brand valuation other than AS-26. Now AS-26 (Accounting for Intangible assets) is applicable, the brands can be valued if and only if they are purchased and not self generated.

Global brand valuation firm Brand Finance has adopted this method in its India's Top 50 Most Valuable Brands (BF Top 50), presented exclusively by ET. According to BF Top 50, which studied only listed consumer-facing corporate brands, the top brands are spread out evenly across sectors, from software, steel, petroleum, airlines and banking, proving that brands can create significant economic value even outside the traditional consumer goods sector. The valuation was performed by brand finance using the relief-from royalty approach⁸. According to Mohanty B. K. (2010)⁹ this methodology has been used because of two reasons: first, it is the valuation methodology that is favoured by the fiscal and tax authorities because it calculates brand values by reference to documented, third party transactions; and second, because it can be performed on the basis of publicly available financial and

⁶ www.businessweek.com.

⁷ Michael Birkin, "Valuation of Trademarks and Brand Names" Brand Valuation, edited by John Murphy, Business Books Limited, London)

⁸ Relief-from-royalty is another method used by financial analysts. It is based on the concept that, if the company did not have the use of its brand name, it would need to license that right in exchange for a royalty fee. These royalty fees are usually based on a percentage of sales (not profits). The valuation consists of first estimating the fee as a percentage of sales and then projecting that fee over the useful life of the brand.

⁹ Mohanty B. K. (2010): "Role of Branding in Business-Value Proposition" The Chartered Accountant. Vol 58 No 11, May, pp.1847-53.

marketing information. Researchers then estimate brand loyalty rates for each of the India's largest industry sectors. Those rates are then adjusted for each company after having understood its brand strength from poring over market surveys consumer research and investor relations material. Exhibit V indicates a list of top 20 brands. As per exhibit Reliance Industry is the leader the year 2008 as well 2009 with the brand value of 6807 (\$ Mn) and 7844(\$ Mn) respectively. Then followed by SBI, Indian oil and other so on. So on a larger platform; the BF Top 50 list should an important signal for Corporate India to recognise brands as significant assets that drive business value.

Exhibit V: Rank of Top 20 Most Valuable Brands in India

Rank 2009	Brands	Brand Value 2009 (\$ Mn)	Rank 2008	Brand Value 2008 (\$ Mn)	Rating 2009
1	Reliance Industries	7844	1	6807	AA+
2	State Bank of India	5480	4	4215	AA+
3	Indian Oil	4807	3	4509	A
4	TCS	4177	2	4976	AA+
5	TATA Motors	3100	6	3289	AA+
6	BPCL	2620	9	2386	BBB+
7	Bharti Airtel	2512	8	2489	AAA
8	Wipro	2370	5	3295	AA+
9	ITC	2348	10	2204	AA
10	ICICI Bank	2277	7	2929	BBB+
11	HPCL	2274	12	2019	BBB-
12	TATA Steel	2264	14	1825	AAA-
13	L&T	1823	15	1757	AAA-
14	Infosys	1719	11	2117	AA-
15	United Braveries	1718	16	1531	AA
16	Reliance Communication	1436	13	1890	A-
17	Maruti Suzuki	1411	17	1328	AAA-
18	M & M	1335	18	1300	AA
19	Bajaj Auto	1010	20	1001	AA-
20	Hero Honda Motors	859	24	815	AA+

Source: The Economic Times dated 21st November, 2009

Abbreviations used: AAA - Extremely Strong; AA - Very Strong; A - Strong; BBB - Average; BB - Under Performing

Now a days brand and their valuation is important task in the hands of managers and financial experts to indicate the real worth of their hidden assets in the era

of knowledge economy. Shareholders are equally also interested about the tangible as well intangible assets, which are responsible for the shareholders value creation even those who are not included in the financial statements of the companies. At international level Brand contributed more than 60 per cent of the market capitalisation of the leading US companies and out of 50 top rank brands 30 brands alone belong to US-based companies.

In India, brand valuation is not as popular when compared to international level, but few Indian companies are valuing their brands for the benefit of potential investors and their existing shareholders as a part of fair reporting and disclosure practices. Companies such as Infosys Technologies Ltd and Satyam Tech Mahindra are providing information about brand in their annual reports.

Economic Value Added (Eva®) Reporting

EVA® (Economic Value Added) was developed and registered by a New York-based consulting firm, Stern Steward & Co in 1990 to promote value-maximising behaviour in corporate managers¹⁰. It is a single, value-based measure that was intended to evaluate business strategies, capital projects and to maximise long-term shareholders wealth. The concept of Economic Value Added(EVA) is closely related to the concept of residual income of economics. Economic Value Added is a financial performance measure that comes closer than any other measure in disclosing the true economic profit of an enterprise. EVA is a performance measure, which reflects the impact of the performance on the shareholders' wealth. Economic value-added measures the profitability of a company after taking into account the cost of capital. It is the post-tax return on capital employed (adjusted for the tax shield on debt) less the cost of capital employed. Companies which earn higher returns than cost of capital known as value creator, and companies which earn lower returns than cost of capital are deemed destroyers of shareholder value.

Formula $EVA = NOPAT - (WACC \times CE)$

Here, **NOPAT**= Net operating profit after tax, **WACC**= Weighted average cost of capital, **CE**= Capital employed.

As we know that there are various ways to create the shareholder value traditional (EPS, ROI, EPS/DPS analysis) as well as innovative techniques (TSR, EVA, MVA, CVA etc), but EVA is one of the important tools to measure shareholder value creation with the benchmark of the cost of capital

There are many Indian companies which are also using EVA for the different managerial aspect. For instance Infosys is using EVA for the better corporate information system, Marico industries are using it as singling device that capital is important and better utilisation, Dr Reddy's EVA is criterion for various rewards, such as pay hike, stock options and performance bonus. Tata Consultancy

¹⁰ Stern Stewart & Co, 1999, Internet site <http://www.sternstewart.com>.

Services explains the part EVA plays in transforming TCS from an Indian enterprise with a global reach to a truly global organisation. Their first hand experience of the tool was a revelation of the fact that EVA results in an enlarged pie which benefits both the individual and the organisation. For the Godrej Group, EVA has been a tool to measure, motivate, manage and finally, overhaul the mindsets of people.

Exhibit: VI Indian Corporates and EVA Reporting

Company	Usage of EVA
INFOSYS	EVA is used as a tool to tell its clients that the value delivered by Infosys is greater than what the client pays for.
MARICO	As a signalling device to tell its employees that capital is important.
Dr. REDDY'S LAB	As a qualifying criterion to grant rewards such as a variable pay, stock options and performance bonuses.
TCS	Here EVA is linked to compensation and has been implemented in great detail.
BHEL	EVA linked with the companies Business strategy and values along with discharge of economic and social responsibility.
HERO HONDA	EVA linked with the performance appraisal and reward to the employees and analyse value creation process.
HUL	Used EVA as a basis to measure the performance of each of its division. EVA locates performance on the basis of operating profit after charging the cost of capital
GODREJ	EVA is used not only as financial, but also as a way of structuring performance linked variable remuneration. EVA has been a tool to measure, motivate, manage and finally, overhaul the mindsets of people

Source: Compiled from annual reports of the sample companies.

EVA is new tool to measure companies' true earning capacity in the modern competitive era. EVA supported corporate entities to increase the profitability with the help of minimisation of the wasteful activities. It also enhances the good governance and reporting and disclosure practices of the corporate in the information age. To increase EVA, a company can improve its efficiency, reduce its cost of capital, or increase its capital. It's an issue of both quality and quantity.

Over the last one decade, companies in India have paid a great deal of attention to improving their EVA. Many companies they are reorganising Capital employed, their capital structure and sound working capital management. As far as shareholders point of view is concerned, EVA is a new tool to measure their real wealth creation rather than simple profitability and uniform reporting and disclosing

practices of Indian companies create a right environment for transparent reporting practices.

Intangible Assets Score Sheet

Intangible assets score sheet is one of important tool about disclosure and reporting for intangible assets. Many companies published models for valuing two most important intangible assets – human resources and their brand value. This score sheet is developed by Karl-Erik Sveiby¹¹ who believes that such representation of intangible assets provides a tool to the investors for evaluating market-worthiness of the company. The various components of intangible assets score sheet are classified as follows:

External Structure-Our Clients: For any company whether manufacturing, process or service oriented unit, most valuable intangible asset is their client base. Under this form of external structure we include retention and growth of clients every year, repetition of orders, total clients during the year and addition of new clients in the current year. We also include regular clients and their contribution in the total revenue, efficiency includes sales per clients, etc. Clients base and their nationality (belongs to different countries) indicate popularity of product in the different countries and continents. Stability of client business shows repetition of business order important for the revenue growth and earning point of view which directly affects the market capitalisation of the company.

Internal Structure: Internal structure is one of the important intangible assets which differ from company to company. Internal assets are systems, technologies, methodologies, processes and tools that are specific to an organisation. These assets give the organisation a unique advantage over its competitors in the marketplace. It also includes research and development facilities which described as R&D/ total revenue, technological investment and total investment by the firm during the financial years. All these are important to create and maintain intangible assets in the long run.

Competence — People: Competence of an organisation will depend upon the quality of the human resource which is working indirectly or as supporting staff. Quality of people also depends upon the qualifications and their experience with related work. Under the evaluation and reporting of competence the important factors are — total employees, employees added during the years, lateral added, staff education index and employees working from different nationalities. Gender classification such as male and female, stability of employees their age factor, and attrition of employees, etc. Some financial parameters like value added per employees, sales per employees will also be considered under the competence. When we compare all these with similar companies or competitors, we know the strength and competence of people.

Indian companies such as Infosys and Satyam Tech

¹¹ The New Organizational Wealth, Berrett-Koehler Publishers Inc., San Francisco.

Mahindra are providing information about intangible scoresheet in their annual reports as additional information, but many companies are far away from the current trends of reporting and their annual reports are lacking the intangible scoresheet.

Balance Sheet with Intangible Assets

Balance sheet with intangible assets is another way for the reporting and disclosure of overall Intangible assets. Most of the Indian companies are still not incorporating intangible assets in their balance sheet while preparing annual reports. Historically, from the 1840s to the early 1990s, a corporate's value was mainly driven by its tangible assets—values presented in the corporate balance sheet. The managements of companies valued these resources and linked all their performance goals and matrices to these assets such as return on investment, capital turnover ratio, etc. The market capitalisation of companies also followed the value of tangible assets shown in the balance sheet with the difference rarely being above 25 per cent. In the later half of the 1990s, the relationship between market value and tangible asset value changed dramatically. By early 2000, the book value of the assets represented less than 15 per cent of the total market value. In short, intangible assets are the key drivers of market value in this new economy. A knowledge-intensive company leverages know-how, innovation and reputation to achieve success in the marketplace. Exhibit VII explains the balance sheet with intangible assets for the last one decade to know the contribution of the intangible in the total assets of Infosys.

Its clear from the exhibit that intangible assets reserve is consistently increases from ₹7884 crore to ₹134478 crore during the last ten years. Intangible assets of Infosys are in presented in two parts HR value and Brand value. Brand 'Infosys' value significantly increases from ₹5246 crore to ₹32345 crore during 1999-2k to 2008-2009. Similarly HR value also increases from ₹2237 crore to ₹102133 crore during 1999-2k to 2008-2009. When we are comparing value of IA with total assets (Including IA) it is always between 86 per cent and 90 per cent of the total assets during the study period. It clearly describes the strength of IA in the knowledge era as compare to tangible assets.

Indian companies such as Infosys, Satyam Tec Mahindra they are providing information about intangible scoresheet in their annual report as additional information's. There are many effective intangible assets which cannot be recognised by the firm in the current definition and practice due to unstable nature and continuous changes in their structure, shareholders and investors are away from the real potential of the firm other than tangible assets. Due to all these reasons real economic value of the firms not reflected by the traditional accounting system. The practice of the company in the disclosure of these intangible accounting parameters in the Annual published accounts of the company will definitely attract public interest and acts as a confidence building measure in the corporate world. On the basis of such intangible accounting parameters valued opinion about the performance and position of the company could be formed by they various stakeholders.

Exhibit VII: Balance Sheet With Intangible Assets

(Amount in Crore ₹)

Particulars	Amount (2009)	Amount (2008)	Amount (2007)	Amount (2006)	Amount (2005)	Amount (2004)	Amount (2003)	Amount (2002)	Amount (2001)	Amount (2000)
<u>SOURCES OF FUNDS</u>										
Shareholders Funds	286	286	286	138	135	33	33	33	33	33
Share Capital										
Reserves and funds	134478	130684	89069	69552	42487	29325	17905	16796	10500	7484
Capital Reserves – IA	17968	13509	10969	6828	5090	3216	2828	2047	1357	800
Other reserves										
Minority Interest	---	---	4	68	94	94	--	---	---	---
Total	152732	144179	100328	76586	47806	32668	20766	18876	11889	8317
<u>APPLICATIONS OF FUNDS</u>										
Fixed assets	5354	4777	3771	2226	1574	1032	773	718	558	207
INTANGIBLE ASSETS:										
Brand Value	32345	31863	31617	22915	14153	8185	7488	7257	5376	5246
Human Resource	102133	98821	57452	46637	28334	21140	10417	9539	5123	2237
Investments	---	72	25	755	1211	945	33	44	34	14
Deferred Tax assets	126	119	92	65	44	40	37	24	--	---
Current Assets										
Debtors	3672	3297	2436	1608	1322	651	512	337	302	136

Particulars	Amount (2009)	Amount (2008)	Amount (2007)	Amount (2006)	Amount (2005)	Amount (2004)	Amount (2003)	Amount (2002)	Amount (2001)	Amount (2000)
Cash and Bank Balances	9695	6950	5834	3429	1576	1722	1336	772	385	432
Loan and advances	3279	2771	1251	1297	1025	861	873	644	430	210
Less: C/L and provisions Current liabilities	2004	1912	1469	934	656	582	315	126	135	67
Provisions	1868	2279	681	1412	777	1326	388	333	185	99
Net Current Assets	12774	8827	7371	3988	2490	1326	2018	1293	798	612
Total	152732	144479	100328	76586	47806	32668	20766	18876	11889	8317
Percentage of I A/ total assets	88 per cent	90.45 per cent	88.79 per cent	90.82 per cent	88.87	89.77 per cent	86.22 per cent	89.00 per cent	88.31 per cent	89.97 per cent

Value Reporting

Value reporting is another unique feature of reporting and disclosure in the current competitive environment. It is believed that information asymmetry between the Management and shareholders should be minimised. Accordingly, Indian companies should always practise progressive and transparent disclosure. Infosys is the first in Indian companies to adopt US Generally Accepted Accounting Principles (GAAP)¹². Thereafter, it rapidly progressed to additional disclosures that give deeper insights to the way they run business and into value creation. Infosys continues to provide information that is not mandated by law because it believes it will enable investors to make more informed choices about our performance. *The Value Reporting Revolution: Moving Beyond the Earnings Game*¹³, acknowledged the need to go beyond GAAP in providing information to shareholders. The book, *Building Public Trust: the Future of Corporate Reporting*¹⁴, indicates business model and reporting.

To reduce information asymmetry, companies such as Infosys make the following disclosures in addition to the mandated Indian and US GAAP financial statements and supplementary data as required by the relevant statutes such as: Brand valuation, Balance sheet including intangible assets, Economic Value-Added (EVA®) statement, Intangible asset scorecard, Risk management report, Human resource accounting and value-added statement, etc.

These reports are integral to the Annual Report. By adopting similar internal measures to evaluate business performance, their employees are adjudged based on metrics that are additional to the financials. This balances financial and non-financial performance across all levels of the organisation. Accordingly, they seek to align the measures by which stakeholders measure their performance with what results in employee rewards. In fiscal 2005, Infosys adopted and furnished eXtensible

Business Reporting Language (XBRL) data to the United States Securities and Exchange Commission (SEC) for the first time. They are the fourth company worldwide to adopt XBRL.

Exhibit: VIII



Reporting Under Indian GAAP and US GAAP

US GAAP (American generally accepted accounting principles) are the new accounting principles which are followed by all the USA companies as well as, all the international companies who want to raise capital from US capital market. With the international practice large Indian companies like Reliance, Infosys, and Indian Oil also follow US GAAP along with Indian GAAP to take the advantages of US capital and technology available at lower cost of capital. For the Indian companies that are listed on American stock exchanges, there is a growing realisation that the publication of their annual accounts both under Indian and US GAAP adds to the comparability of their profits and financial position.

Besides this accounting as per US GAAP enhances company profile and reputation. In a financial environment

¹² Annual report of Infosys Technologies Ltd 2009

¹³ Authored by Robert Eccles, Robert Herz, Mary Keegan and David Phillips, associated to accounting firm PricewaterhouseCoopers, John Wiley & Sons, Inc., USA, ©2001,

¹⁴ published by John Wiley & Sons, Inc., USA, ©2002 PricewaterhouseCoopers

where the investor is getting increasingly cautious and aware, the companies have begun to understand that the investor will not even touch a company whose balance sheet is even not up to the mark. US GAAP, in this situation, gets that trust stamp of high quality, and makes the company an attractive investment proposition. The stricter disclosure norms do ensure greater transparency and enhance credibility in the capital market. To attract the international investor, thus, US GAAP is almost a must. With most Indian companies heading towards the western financial markets, accounting as per US GAAP has become an essential practice. Indian companies such as Infosys, Satyam Tech Mahindra, Wipro, Patni Computers, Ranbaxy, Dr Reddy's, Dabur, BHEL and RIL are providing information statements under US GAAP in their annual report as additional information, which is useful for the global investor to understand the financial information with their own accounting standards. But still many Indian companies are not disclosing information under US GAAP and they are deprived of the advantages of global investment and technology.

Current Cost Adjusted Financial Reporting

Financial statements are prepared with a view of presenting the financial position of the business on a particular date and displaying the result achieved during an accounting period. These statements are prepared on historical cost (original or acquisition cost) on the assumption that the purchasing power of the money remains the same. But the assumption is not valid as the purchasing power of the rupee goes on changing from time to time on account of changes (up words or down words) - in price level. There is a growing realisation that historical cost based accounting system does not adequately serve the needs if users of accounting information in view of high inflationary pressure. Now it's accepted by the all authorities to include statement of price level changes in annual reports of companies.

There are two popular methods as current purchasing power method (CPP) and current cost accounting methods (CCA). Current cost accounting (CCA) seeks to state the value of assets and liabilities in a balance sheet at their value and measure the profit or loss of an enterprise by matching current costs against current revenues. CCA is based on the concept of 'operating capability', which may be viewed as the amount of goods and services that an enterprise is capable of providing with its existing resources during a given period. In order to maintain its operating capability, an enterprise should remain in command of resources that form the basis of its activities. Consequently, it becomes necessary to take into account the rising cost of assets consumed in generating these revenues. CCA takes into account the changes in specific prices of assets as they affect the enterprise.

The basic purpose of current cost accounting is to provide more useful information than that which is

available from historical cost accounts for the guidance of management of the business, shareholders and other interested parties, matters related with the financial viability of the business, return on investment, pricing policy, cost control, and distribution and capital rearing, etc. In spite of having implementation problems, some of the leading Indian companies are adopting inflation accounting for external reporting purpose, but such number is insignificant. Among public sector undertakings, Hindustan Machine Tools followed Hyde Guidelines and Bharat Heavy Electricals Ltd. followed the CCA method and also Hyde Guidelines in preparing their annual reports. Cement Corporation of India, Steel Authority of India and a few other companies have been taking into consideration the inflation adjusted data and presenting supplementary inflation adjusted accounts in their annual reports.

Value Added Reporting

Value added is a basic and important measurement to judge the performance of an enterprise. It indicates the net value or worth created by the manufacturer during a specific period of time. No enterprise can survive and grow, if it fails to generate wealth. An enterprise may exist without profit, but cannot survive without adding value. Value added reporting is a part of financial reporting that shows value addition by firm during the specific period of time and their application towards employees, government, capital providers for development and expansion activities. Value added is meaningful measure of corporate performance than conventional measures based on traditional financial accounting and can be particularly useful for employee oriented approach, which will allow more fruitful discussion with employees and can be especially useful in productivity arrangements. The value added is a basic and broad standard which comprises investment by shareholders, debenture holders, creditors and specialised financial institutions. If such investment does not create wealth (value addition), it means that is misuse of public funds. Therefore, the concept of value added has a direct linkage with the concept of social responsibility of the business. Value added can be particularly useful to management in comparing the performance of business within group or companies' performance with its industry as a whole. Financial reporting has traditionally concentrated on the needs of shareholders and creditors, but value added statement is important for stakeholders as well as employees for their remuneration point of view.

Generation of Value Added: Value addition is the increase in the market value brought by an alteration in the form, location and availability of a product or services, excluding the cost of brought in material or services used in the product or services. In simple words the value added is an excess of turnover + income from services over the cost of brought in material and cost of the services. Here turnover indicates (Gross sales + sales tax and duties –

(rebate + returns + commission + discount + Goods used for self consumption). In way of formula we can denote as:

$$Va = S + I - C$$

Here, Va means Value addition, S means sales, I mean Income from services and, C Cost of brought in material and services.

Application of Value Added: Value added will be shared by three segments e.g. (1) Employees, (2) Government, (3) Capital providers, and remaining share will be retained by the company for their development and expansion activities. The employees comprise all human resources e.g. workers and staff, the share available to them is salary and gratuity, contribution to the PF, bonus and remuneration to the top managerial persons. The government provides not only the infrastructural facilities, but also conditions encouraging to operational activities; hence the share of value added has also to be given to the government in form of custom duty, excise duty, sales tax, and wealth tax. Share holders are the ultimate claimant of value added. As such a share of the value added is given to them in the form of dividend, from the financial management point of view the profit ploughing back or retained earning also belongs to them. But since they have not yet been paid out they are to be separately distributed under the heading, reinvestment in business. Providers of capital by outsider agencies like bank, financial institutions, and debenture holders will be given in the form of interest.

From better discloser and transparency point of view, some public sector companies such as BHEL, SAIL, NTPC, HPCL and Infosys had started presenting value added statement in their annual reports. Value added reporting enhances the financial reporting which is traditionally concentrated on the needs of shareholders and creditors, but value added statement is important for various stakeholders of the society for social distribution of wealth which is created by corporate in a particular period.

Total Shareholder's Return

Total shareholder's Return (here after TSR) represents the change in capital value of a company over a period of one year, plus dividends, expressed as a percentage of gain or loss of the beginning capital value. TSR is a concept used to compare the performance of different stocks of companies and shares for a particular period. To bring in more accuracy into measuring the TSR, the debt component has been eliminated from the capital value. TSR reflects the gain delivered to shareholders by the company directly and indirectly, directly in the form of the dividend received by them for a year and indirectly in the form of enhancement of capital value by the stock during the financial year. TSR is calculated by deducting the opening market capitalisation from the closing market capitalisation, and adding the dividend paid. It is the gain expressed as a percentage of the opening market

capitalisation. An alternative way of calculating of TSR is to apply the internal rate of return of all cash flows paid to investors during a particular period. However, whichever method we are using to calculate total shareholder return, the result essentially represents an indication of the overall return generated for stockholders, expressed in percentage terms.

Formula $TSR = \frac{CMC - OMC}{OMC} \times 100$, Here, TSR= Total shareholder's Return, CMC= Closing market capitalisation, OMC= opening market capitalisation, D = dividend

If a company is reporting and disclosing about TSR in annual reports, it's significant for the present and potential investors to take appropriate decision about investment. Along with that they can make inter industry comparison about dividend as well as capital appreciation for a particular year. Similarly, this information is equally important to managers for decision making process related with capital structure as well as dividend payout decision as a part of dividend and financial policy.

Market Value Added

Market Value Added (here after MVA) is a supplementary technique used to evaluate a company's performance in stakeholder value creation. MVA is the excess of the market value of the company over the value of investors' capital. In contrast to the economic profit, which is the value added by the company over a given period, the MVA is a measure of the investor's perception of value added. If MVA is positive, the firm has added value, creating value for shareholders. If it is negative, the firm has destroyed value. The amount of value added needs to be greater than the firm's investors could have achieved by investing in the market portfolio. Market Value Added is a modified version of EVA as the value is more related to market. In the ways of formula MVA express as follows:

$MVA = v - k$, where v= Current market value of debt and equity, k= capital invested in the firm (Share capital + Free Reserves + Debt).

MVA is important to know shareholders value creation for a specific period. If companies are providing information about MVA, they attract present and potential investor towards themselves. Outsider/external parties can evaluate the work done by the shareholders agent (directors) with the help of MVA. If MVA is positive during the year, it indicates work done by the Director's are positive and worthwhile for shareholders value creation point of view *vice versa* destroying the of wealth of shareholders.

Market Capitalisation

Market capitalisation is a measurement of the size of a business enterprise (corporation) equal to the share price times the number of shares outstanding of a public company. Market capitalisation is calculated by outstanding shares multiply by market value per share at the particular period (usually companies using last month

data of the financial years). Market capitalisation is a market estimate of a company's value, based on perceived future prospects, economic and monetary conditions.

Market capitalisation is one of the bases for the shareholders value creation. Reporting about the market capitalisation is useful for the various stakeholders. In long term perspective higher market capitalisation indicates higher demand for the shares in the open market due to higher earning/profitability and higher contribution in the business operations. Similarly it also depends upon the long term strategy of the company as to how they are utilising their resources such as manpower, their knowledge, competence and skills to enhance the earning for the shareholders. Market capitalisation can be expressed as follows:

$mc = n \times v$, here mc = market capitalisation, n = number of outstanding shares, v = market value of shares on specific period.

Enterprises Value

Enterprise value (here after EV), is an economic measure reflecting the market value of a whole business. It is a sum of claims of all the security-holders, debtholders, preferred shareholders, minority shareholders, common equityholders, and others. It is an aggregated value of the firm based on the market value of the equity plus market value of the debt minus cash and cash equivalents for a specific period. EV attempts to ascertain the value of the company as on a particular date. EV is one of the fundamental metrics used in business valuation, financial modelling, accounting and portfolio analysis etc. EV is more comprehensive than market capitalisation, which only includes the market value of only equity. We can denote EV as:

Formula: **Enterprises value** = Common equity at market value + Debt at market value+ Minority interest at market value, (if any)–Associate company at market value, (if any)+ Preferred equity at market value– Cash and cash-equivalents.

Voluntary Reporting & Discloser Practices- A Survey of India Corporates

Disclosure and reporting of accounting information is an important aspect of the financial reporting. A comprehensive survey was done by the researcher to know the contemporary reporting practises adopted by the Indian corporates for the enhancement of value of financial statements/annual reports. In this survey, a parameter of 12 independent variables are taken by the researcher such as; Economic Value Added (EVA), Value Added Statement (VAD), Human Resource Accounting (HRA), Brand Valuation (BV), Intangible Assets Scoresheet (IAST), Balance Sheet with Intangible Assets (BS (IA)), Value Reporting (VR), Presentation of financial statement under US GAAP, Current Cost Adjustment Reporting (CCAR), Market Capitalisation (MVA), Enterprise Value (EV) and

Total Shareholders Returns (TSR) to evaluate voluntary reporting practices to enhance the effectiveness and usefulness of financial statement in the competitive era. All the above parameters are not in mandatory nature under the corporate law, but new era companies are using them in financial statement significantly.

For each parameter one point is allocated and total maximum points for all the parameters are twelve, (if a company they reporting with all the above voluntary reporting methods). For this survey 60 leading BSE listed companies are taken to analyse voluntary reporting practice and how they are enhancing the value of financial statement along with other mandatory information's. All the 60 sample companies are categorised as per their nature of business such as; Information Technology industry, Pharmaceutical industry, FMCG industry, Automobiles industry, Tele communication industry, Infrastructure industry, Banking sector industry, and Capital goods industry. Out of the 60 samples companies, only 21 companies are using one or more voluntary reporting parameters in the last five years (refer exhibit X). Other companies are not employing any single parameter of voluntary reporting practices in their reporting statement.

Exhibit IX: Scale for Evaluation of Voluntary Reporting

Score range	Rank
10-12 points	Excellent
7-9 points	Very good
5-6 points	Good
3-4 points	Average
Below 3 points	Poor

After the determining the total score based on above parameters, they have been evaluated on five point scale as state in exhibit IX. Based on evaluation table, Indian companies are ranked as excellent, very good, good, average, and poor. According to reporting table and points scored by the various corporates; Infosys technology a leading (information technology) company score 11 points (they are reporting and disclosing with all parameters) and ranked as excellent. After that 7 points are scored by Satyam Mahindra Tec and secured very good rank for their reporting. Among the public sector companies BHEL is the company scored 5 points with the use of EVA, Value added statement, market capitalisation and presentation of financial statement under US GAAP and enterprises value also and rank as Good for reporting. Dr Reddy's also scored 5 point based on reporting practices and ranked as Good. However, other 16 companies secured less then 3 points out of the 12 points categories as poor performer in the area of voluntary reporting practice.

Similarly, when we analyse the adaptation of a particular method of reporting by the Indian corporates, EVA, Value

Added Statement, MVA or market capitalisation, and presentation of financial statement under US GAAP, these are the popular methods adopted by Indian companies during the last five years. Among the leading Government sector companies EVA, MVA, HRA and Value added reporting are popular as compared to other voluntary reporting methods.

It is clear from the above analysis that as far as voluntary reporting is concerned, Indian companies are not making serious efforts to adopt all such methods as a

part of voluntary reporting practices. For example among the other important factors, brand is one of the popular intangible assets and many independent agencies (such as brand finance, intangible business, etc.) are valuing the brand value for Indian companies but they are not reporting about the brand value in their annual report as in separate section. Similarly, in the knowledge era human resources are the key elements in the service industries, but hardly few Indian companies are using HRA as additional information for the benefit of various stakeholders.

Exhibit X: Voluntary Reporting Methods adopted by Indian Corporates.

Companies	EVA	VAD	HRA	BV	IAST	BS(IA)	VR	USGAAP	CCAR	MVA	EV	TSR	Points
WIPRO	--	--	--	--	--	--	--	Y	--	Y	--	--	2
INFOSYS	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	---	11
TCS	Y	---	---	--	--	--	--	--	--	Y	--	--	2
SATYAM	Y	---	Y	Y	---	Y	---	Y	--	Y	Y	---	7
PATNI COM.	--	--	--	--	--	--	--	Y	--	--	--	--	1
RANBAXY	--	--	--	--	--	--	--	Y	---	--	--	--	1
Dr REDDYS	Y*	--	--	--	--	--	--	Y	--	Y*	Y	Y	5
NICHOLAS	Y	--	--	--	--	--	--	--	---	--	--	--	1
DABUR	--	--	--	--	--	--	--	Y	--	--	--	--	1
HUL	Y	--	--	--	--	--	--	--	---	Y	--	--	2
ITC	--	--	--	--	--	--	--	--	--	Y	--	--	1
MIRCO	Y	--	--	--	--	--	--	--	--	--	--	--	1
HERO HONDA	Y	--	--	--	--	--	--	--	--	Y	--	--	2
EICHER LTD	--	--	--	--	--	--	--	--	--	Y	--	--	1
SAIL	--	Y	--	--	--	--	--	--	--	--	--	--	1
NTPC	--	Y	--	--	--	--	--	--	--	--	--	--	1
ONGC	--	--	Y	--	--	--	--	--	--	--	--	--	1
HPCL	--	Y	Y	--	--	--	--	--	--	--	--	--	2
BHEL	Y	Y	--	--	--	--	--	Y	--	Y	Y	--	5
RIL	--	--	--	--	--	--	--	Y	--	Y	--	--	1
HINDALCO	--	--	--	--	--	--	--	--	--	Y	--	--	1

Source: Compiled from annual reports of the various companies from 2004-2005 to 2008-2009.

*Reporting and disclosure up to the year 2007-2008

Conclusion

After the analysis of current trends of voluntary corporate reporting, it is apparently understood that if a corporate entity adopted latest practices for corporate reporting (annual reports) it will fulfil the needs and requirements of the various stakeholders in the current competitive and knowledge environment. The right information to all stakeholders enhance the quality of reporting, enable effective decision making. Few Indian companies are

applying all these voluntary reporting methods in their annual reports. However, still, a large group of the Indian corporates are away from the current reporting practices, their reporting is based on the traditional system of reporting. Specially, for corporates which are working in the global environment, it is essential to adopt global corporate reporting practices for better understanding of financial transactions, as well as critical information related with the future prospects of the company. ■

Dependent Personal Services – Relieving Dual Taxes on Income from Employment



In today's economic scenario, the world has shrunk and boundaries between countries exist largely only on the land. Countries are increasingly ever becoming dependent on one another and business has grown beyond boundaries of one's country. Consequently, one has witnessed a large scale mobilisation of the basic resources for undertaking business activity viz. capital and labour. The globalised trade of today's times, if at all, has only fuelled this movement of personnel on a scale greater than ever before. Further most countries now have a complex set of taxation rules which seek to tax every income earned on its soil as well as in the hands of its residents. This creates a peculiar situation for such persons who are called to pay tax on their income from employment in the country where employment is exercised as well as the country where such persons is a tax resident (if the two are different). To overcome this scenario, a need was felt to introduce some mechanism whereby the taxing rights of countries to tax such income is adequately defined so that dual taxing of such income could be avoided. With this objective in mind, the Organisation for Economic Co-operation and Development ('OECD') when it introduced the Model Tax Convention, included Article 15 – Dependent Personal Services to allocate the rights and obligations of countries while taxing the employees. A similar article is also present in the UN Model Convention. In 2000, Article 15 was rechristened as 'Income from Employment'. Most of the Double Taxation Avoidance Agreements ('DTAA') entered into by India contains the Article on Dependent Personal Services. This article explains the nuances of the Article dealing with Income from Employment.

Article 15 – Income from Employment ('OECD')

Article 15 of the OECD model convention is reproduced hereunder:

1. *Subject to the provisions of Articles 16, 18 and 19, salaries, wages and other similar remuneration derived by a resident of a Contracting State in*

(Contributed by the Committee on International Taxation of the ICAI. Comments can be sent to citax@icai.org)

respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if:

- a. the recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in any twelve month period commencing or ending in the fiscal year concerned, and
- b. the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State, and
- c. the remuneration is not borne by a permanent establishment which the employer has in the other State.

3. Notwithstanding the preceding provisions of this Article, remuneration derived in respect

of an employment exercised aboard a ship or aircraft operated in international traffic, or aboard a boat engaged in inland waterways transport, may be taxed in the Contracting State in which the place of effective management of the enterprise is situated.

The Article 15 under the UN Model Convention is also on similar lines.

The Model Conventions provide that generally the right to tax the remuneration arising in course of employment would remain with the country where the individual is a tax resident. However, the other country where the income has arose in course of rendering of employment i.e. the source country would also get the right to tax such income if any of the following conditions is fulfilled:

- (a) the person in course of his employment is present in the source country for a period more than 183 days during any 12 months period beginning or ending in a fiscal year; or
- (b) the remuneration is paid to such employee by or on behalf of an employer who is a resident of the source country; or
- (c) the remuneration paid to such employee is borne by the permanent establishment ('PE') of the employer in the source country.

However, one need to bear in mind that the above arrangement would be applicable only in respect of the remuneration which is received by a person who is tax resident of one country and the remuneration is earned by him in course of employment rendered in the other country.

Scope of Article 15 – Income from Employment

Article 15 gets triggered only in cases where an individual has earned remuneration from

rendering employment in a country other than the one of which he is a tax resident. Accordingly, the basic condition for invocation of Article 15 is the presence of employer-employee relationship under which an individual by rendering services to the employer earns remuneration in lieu of the services rendered.

Paragraph 1 of the Article covers salaries, wages and any other similar remuneration earned by a resident of one country in course of rendering employment in other country. Salaries, wages and any other similar remuneration are not defined under the Model Convention. Accordingly, the same needs to be understood in accordance with the domestic law of the respective country (for India, in accordance with the meaning provided under the Income-tax Act, 1961). Given the same, it would cover all forms of remuneration as long as it is connected with the employment exercised, whether received in cash or kind or both, including perquisites like accommodation, motor-car, club membership, ESOPs, etc.

However, as mentioned earlier, it needs to be borne in mind that the source country would only get the right of taxation to the extent such remuneration pertains to the period of exercise of employment in the source country.

The Article, however, carves out exclusion in respect of the fees paid to Directors, income from pensions and government service which are specifically dealt by Articles 16, 18 and 19 respectively.

Threshold of Stay

One of the conditions which enable the source country to tax the income earned by the person from rendering employment is his physical presence in the country for a particular period of time. If the person stays in the source country for more than the specified number

Article 15 gets triggered only in cases where an individual has earned remuneration from rendering employment in a country other than the one of which he is a tax resident. Accordingly, the basic condition for invocation of Article 15 is the presence of employer-employee relationship under which an individual by rendering services to the employer earns remuneration in lieu of the services rendered.

of days, then the source country gets the right to tax income earned from his rendering employment in the source country.

The current Model Convention recommends a physical presence of more than 183 days during any twelve month period beginning or ending in a fiscal year as criteria which would allow the source country to tax the income from employment. However, the threshold provided in various treaties is not uniform and countries often may provide a threshold which may be lower than 183 days.

India has however reserved its right to negotiate on the time threshold provided under the Article and has made the following observation on the same –

“5. India reserves the right to decide the period of stay referred in this paragraph through bilateral negotiations.”

How to compute the presence

The Model Convention provides that the presence ought to be computed with respect to the physical presence of the person in the source country. The method is straightforward and simple to apply. Under the same, the time which is spent outside the source country on account of travel or preparation for the employment is excluded.

However, once the person is physically present in the source country, then period of holidays, relaxation, non-working days due to factors beyond the employee's control are also to be taken into account while computing the threshold.

In this regard, reference may be made to the Model Commentary which provides guidance on how to compute the number of days –

“Under this method the following days are included in the calculation: part of a day, day of arrival, day of departure and all other days spent inside the State of activity such as

When a person goes abroad for employment and then he is shifted back to his home country for the purpose of employment, he should be first considered as resident of the source country and then for the purpose of computing the stay in his home country, only the period he has stayed in the home country after taking employment should be considered.”



Saturdays and Sundays, national holidays, holidays before, during and after the activity, short breaks (training, strikes, lock-out, delays in supplies), days of sickness (unless they prevent the individual from leaving and he would have otherwise qualified for the exemption) and death or sickness in the family. However, days spent in the State of activity in transit in the course of a trip between two points outside the State of activity should be excluded from the computation. It follows from these principles that any entire day spent outside the State of activity, whether for holidays, business trips, or any other reason, should not be taken into account. A day during any part of which, however brief, the taxpayer is present in a State counts as a day of presence in that State for purposes of computing the 183 day period.”

The above view also finds favour with the Indian tax authorities who consider partial presence, however brief, as a day's presence in India.

However, different countries have their own set of tests to compute the said threshold. Ireland applies the test of stay upto midnight. USA takes into account the aggregate of fractional stays on different days and a day's presence is reckoned only when the fractions aggregate to 24 hours period.

Computation of threshold in year of transit

The 2008 update to the Model Convention inserted the following paragraph in the Model Commentary to deal with situations in the year of transition:

“5.1 Days during which the taxpayer is a resident of the source state should not, however, be taken into account in the calculation. Subparagraph a) has to be read in the context of the first part of paragraph 2, which refers to ‘remuneration derived by a resident of a Contracting State in respect

of an employment exercised in the other Contracting State', which does not apply to a person who resides and works in the same State. The words 'the recipient is present', found in subparagraph a), refer to the recipient of such remuneration and during a period of residence in the source State, a person cannot be said to be the recipient of remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State."

What the above paragraph suggest is that when a person goes abroad for employment and then he is shifted back to his home country for the purpose of employment, he should be first considered as resident of the source country and then for the purpose of computing the stay in his home country, only the period he has stayed in the home country after taking employment should be considered. The same can be explained with the help of the following examples provided under the Model commentary -

Example 1: From January 01 to December 01, X lives in, and is a resident of, State S. On 1 January 02, X is hired by an employer who is a resident of State R and moves to State R where he becomes a resident. X is subsequently sent to State S by his employer from 15 to 31 March 02. In that case, X is present in State S for 292 days between 1 April 01 to 31 March 02 but since he is a resident of State S between 1 April 01 to 31 December 01, this first period is not taken into account for purposes of the calculation of the periods referred to in subparagraph a).

Example 2: From 15 to 31 October 01, Y, a resident of State R, is present in State S to prepare the expansion in that country of the business of ACO, also a resident of State R. On 1 May 02, Y moves to State S where she becomes a resident and works as the manager of a newly created subsidiary of

ACO resident of State S. In that case, Y is present in State S for 184 days between 15 October 01 and 14 October 02, this last period is not taken into account for purposes of the calculation of the periods referred to in subparagraph a)."

Remuneration Paid to Employee Borne by PE

One of the other condition that allow the source country to tax the remuneration earned from rendering employment is that the remuneration which is paid to him is borne by the PE that his employer has in the country of source. If this condition is fulfilled, the source country get the right to tax the income earned from employment irrespective of the duration (ie even if the duration is less than 183 days).

The rationale behind this provision is that where the PE bears the expenditure, the remuneration paid to employee is taxed by the source state as a corresponding deduction is allowed to the PE while computing its taxable income. In this regard, one refer paragraph 7 of the Model Commentary which suggests that the expression 'borne by' must be interpreted in the light of this objective. The same is reproduced below -

One of the other condition that allow the source country to tax the remuneration earned from rendering employment is that the remuneration which is paid to him is borne by the PE that his employer has in the country of source. If this condition is fulfilled, the source country get the right to tax the income earned from employment irrespective of the duration (ie even if the duration is less than 183 days).

"The phrase "borne by" must be interpreted in the light of the underlying purpose of subparagraph c) of the Article, which is to ensure that the exception provided for in paragraph 2 does not apply to remuneration that could give rise to deduction, having regard to the principles of Article 7 and the nature of remuneration, in computing the profits of a permanent establishment situated in the State in which the employment is exercised."

"The fact that the employer has, or has not, actually claimed a deduction for the remuneration in computing the profits attributable to the permanent establishment is not necessarily conclusive since the proper test is whether any deduction otherwise available for that remuneration would be allocated to the permanent establishment. That test would be met, for instance, even if no amount were actually deducted as a result of the permanent establishment being exempt from tax in the source country or of the employer simply deciding not to claim a deduction to which he was entitled. The test would also be met where the remuneration is not deductible merely because of its nature (Eg where the state takes the view that the issuing of shares pursuant to an employee stock-option does not give rise to a deduction) rather than because it should not be allocated to the permanent establishment".

The term 'borne by the PE', therefore, means that the PE incurs the expenditure or liability is discharged by the PE. An expense can be treated as borne by the PE if the remuneration is functionally attributable to and has economic nexus with the PE so that the same can be claimed as a deduction in computing the income of PE. Thus, once services are performed for the PE, expense can be regarded as borne by PE irrespective of the fact that -

- (a) The amount is not actually paid by the PE but paid by the head-office outside the source country;
- (b) Amount is not debited in the books of the PE;
- (c) Amount is capitalised in the PE's books;
- (d) The PE does not claim the same as deduction either by choice or due to some exemption.

DTAAs entered into by India with many countries like USA, Canada, Netherlands use similar language as used in the Model Convention. Conversely, DTAAs with UK, Australia, Belgium use the phrase 'deductible in computation of PE income'.

With regard to taxation of expatriates, one of the most controversial issues is the meaning of words 'borne by' vs 'deductible' which is the term used in some of the other treaties. Generally speaking, remuneration can be considered as being 'borne' by a PE if the financial obligation of paying the remuneration is undertaken by the PE. This view is also supported by the ruling of AAR in the case of *Stanley Keith Kinnett v. CIT* (238 ITR 155). In contrast, the word 'deductible' would mean whether the remuneration paid to the employee can be claimed as a deduction in computing the taxable income of the PE. In that regard, it would not be relevant as to whether the liability to pay the remuneration was incurred by the PE or not. It would also not matter as to whether or not, the PE actually claims the remuneration as a deduction in computing its profits. Accordingly, it ought to be interpreted that the meaning of the word 'deductible' is wider than the term 'borne'. However, it is important to note that the OECD Commentary seems to equate the meaning of the term 'borne' with the term 'deductible'.

The country of residence retains the primary right to tax its residents in respect of income earned from exercising employment in the country of source. Thus, India has the right to tax its residents in respect of the income earned by them in rendering employment outside in India as per the provisions of the Act. In such cases, this Article may come to the aid of the Indian employee if such employee satisfies the conditions laid down under the Article are satisfied. ”

Further, the Delhi Tribunal in the case of *Ensco Maritime Ltd. vs. DCIT* (91 ITD 459) has held that there is no distinction in the phrase 'borne by PE' or 'deductible in computation of PE income' which seem to be in line with the view expressed in the Model Commentary.

Presumptive basis of taxation – whether expenditure is borne by PE?

Under the presumptive basis of taxation, income of the PE is computed on the basis of a certain presumption wherein deduction is given on an implied basis for all expenses which can be reasonably presumed to be expended in course of earning of the income by the PE.

In this regard, one may refer to the decision in the case of *Ensco Maritime* (supra) wherein the company had a PE in India for offshore drilling and was taxed in India on a presumptive basis under Section 44BB of the Act. The Delhi Tribunal held that under the concept of presumptive taxation, deduction is impliedly given for all expenditure incurred for the earning the PE income. In view of the same, the remuneration paid to the employee

for performing services for the PE should be taken to have been 'borne by' the PE. Accordingly, the remuneration paid to the employee was held to be taxable in India. The Tribunal here had followed the decision of the Authority for Advance Ruling ('AAR') in the case of *Lloyd Helicopters International Pty Ltd.* (249 ITR 162). Similar view has also been taken by the AAR in the case of *DHV Consultant* (277 ITR 97) and the Delhi Tribunal in the case of *Sedco Forex International Drilling Inc vs DCIT* (2 SOT 175).

However, the Delhi Tribunal in a subsequent decision in the case of *Pride Foramer S.A. vs ACIT* (15 SOT 562) accepted the argument of the employees that finalising assessment under Section 44BB does not prove that remuneration was actually deducted while computing the income of the PE and that the word 'deducted' cannot be equated with the word 'deductible' or interpreted as deemed to be deducted or borne by the PE.

Avoidance of Double Taxation for an Indian Resident

As mentioned above, the country of residence retains the primary right to tax its residents in respect of income earned from exercising employment in the country of source. Thus, India has the right to tax its residents in respect of the income earned by them in rendering employment outside in India as per the provisions of the Act. In such cases, this Article may come to the aid of the Indian employee if such employee satisfies the conditions laid down under the Article are satisfied.

In this context, ruling of the AAR in the case of *British GAS India Pvt. Ltd.* (287 ITR 462) may be referred. In the said case, two employees of Indian company were deputed to a UK group company for a long term assignment. However, they continued to employee of

Indian company and received their salary in India. Indian company recovered the salary paid from the UK company (and thus was borne by the UK company). UK Company further provided accommodation and other allowances to the two employees. During the period of deputation, the two employees paid tax in UK. As the employees were receiving salary in India, such receipt was held to be taxable in India under the provisions of the Act. The employees contended that they had become UK residents under the India-UK DTAA and accordingly under the provisions of Article 16 of the India-UK DTAA the income received by them in course of rendering employment in UK was not taxable in India. The said contention was accepted by the AAR and held that receipt of salary in India would be of no consequence.

However, in the case of *S Mohan (294 ITR 177)*, AAR dealing with the taxability of employee on a short-term deputation had come to a different conclusion. In this case, stay of employee exceeded 182 days in Norway and therefore, exemption was sought in India relying on ruling of *British Gas* (supra). However, AAR did not accept the contention primarily on the basis that the person on a short-term basis cannot be held to have become resident in Norway. Further, as there was no evidence of tax having been paid by the employee in Norway, he was denied benefit under the Article.

Service PE Exposure

It must be kept in mind that where the tax treaties have a Service PE clause due to the presence of the employees in the other state, the presence of employees falling within the ambit of the Article may also constitute a Service PE exposure in the other state for the foreign employer.

Section 10(6)(vi) of the Income-tax Act, 1961 has a 90 day rule which exempts employees of foreign companies for services rendered during his stay in India if the stay does not exceed 90 days. It must be noted that the benefit of the above exemption can be taken by employees who are not citizens of India. ☺☺

Short Stay Exemption under the Income Tax Act, 1961

Section 10(6)(vi) of the Income-tax Act, 1961 has a 90 day rule which exempts employees of foreign companies for services rendered during his stay in India if the stay does not exceed 90 days. It must be noted that the benefit of the above exemption can be taken by employees who are not citizens of India.

Situation of Double Non-Taxation

In case of situation which may result in dual taxation of the same income, the country of residence may give relief on credit basis or on exemption basis. Dual non-taxation may happen where the treaty adopts an exemption basis. For example, the India-Germany DTAA operates on exemption method wherein the DTAA confers the sole right to tax the income to the source country where conditions stated in Article 15(2) are fulfilled. In such a scenario, where a German resident exercises his employment in India and fulfils the conditions specified under Article 15(2), Germany would give up its right to tax the income earned in India. Now in case, such German national qualifies for exemption under the Act, this may result in dual non-taxation. This is because Germany grants the exclusive right to tax the income to

India whereas India does not levy tax by granting exemption.

Provisions for Crew of Airlines, Shipping Companies

Paragraph 3 of the Article provides for provisions relating to remuneration derived by employees rendering employment onboard a ship or an aircraft operating in international traffic. For such crew members due to their frequent traveling in various countries, it is very difficult to determine their country of residence. To overcome the same, the Model provides that for such people, their country of residence would be considered as the country where the place of effective management of the airline or shipping company is located. For e.g. for an employee working with an Indian airline company would always be considered as an Indian resident. Correspondingly, an employee working with British Airways would always be considered as resident in Britain ie the place of effective management

In today's times where the executives are increasingly becoming mobile, the provisions of Article relating to Dependent Personal Services and short stay exemption have assumed great importance. The complex set of taxation rules adopted by various countries today does bring in a lot of complications for the persons resident of one state and exercising employment in another state. And while Article 15 does not provide solutions to all the complications arising in course of cross-border employment, it does provide an effective mechanism to avoid dual taxation of the same income.”

of British Airways.

The point to be noted here is that this provision is only applicable

to those people who work onboard the aircraft/ ship. It does not apply to ground staff who would always have a fixed place or base of work.

Conclusion

In today's times where the executives are increasingly becoming mobile, the provisions of Article relating to Dependent Personal Services and short stay exemption have assumed great importance. The complex set of taxation rules adopted by various countries today does bring in a lot of complications for the persons resident of one state and exercising employment in another state. And while Article 15 does not provide solutions to all the complications arising in course of cross-border employment, it does provide an effective mechanism to avoid dual taxation of the same income. Corporates would be advised to plan their tax costs in advance prior to the deputation of their personnel. ■



Point of Taxation Rules – A Study



Point of Taxation Rules was notified vide Notification No.18/2011-ST dated 1st March, 2011. The Amendment to these Rules was notified vide Notification No.25/2011-ST dated 31st March, 2011. The point of taxation need a close study by every stakeholder i.e. service provider, service receiver, Government as these rules are a change from the past. Any change raises new hopes and expectations and these rules are not exception, for Government the change raises hopes of increased revenue and for the rest it is the much desired clarity in law. In this article, the author analyses the point of taxation rules from professional perspective.



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Unlike goods which can be felt, touched and a trail of transfer can be established, services leave no trail as they are intangible. The necessity to document "point of taxation" rules arises as the payment of tax is shifted from realisation basis to accrual basis. Section 66 of the Finance Act, 1994, the charging section, contains that service tax shall be levied when taxable service as envisaged in Section 65(105) (a) to (zzzzv) is provided. Point of taxation rules contain the provisions

As per Rule 2 of the point of taxation rules the said rules come into force on the 1st April, 2011. However, Rule 9 which contains the provisions for transition provides an option for Services which have been provided in full on or before 30th June, 2011 or where invoices are issued up to 30th June, 2011. In both these instances the option to apply the Rules relating to point of taxation is left with the service provider or receiver as the case may be. ☺

to determine when a taxable service is provided i.e. when and at which point the necessity to levy tax under Section 66 and Section 66A is triggered and once the point of levy is determined the tax shall be paid as per the provisions contained in Rule 6 of Service Tax Rules.

As per Rule 2 of the point of taxation rules the said rules shall come into force on the 1st April, 2011. However, Rule 9 which contains the provisions for transition provides an option for Services which have been provided in full on or before 30th June, 2011 or where invoices are issued up to 30th June, 2011. In both these instances the option to apply the Rules relating to point of taxation is left with the service provider or receiver as the case may be. The service provider or the receiver can treat the point of taxation as the date on which the payment is received or made as the case may be or apply the new set of rules which have been notified with effect from 1st April, 2011. In short the Rule provides an option to deposit service tax on realisation basis for services which are provided in full or where invoices are issued on or before 30th June, 2011 only.

The point when the levy to tax is triggered is contained in Rule 3. As per Rule 3(a) the point of taxation shall be at the time when the invoice for the service provided or to be provided is issued. The proviso to this rule lays down that if the invoice is not issued within 14 days of the completion of the service then the point of taxation shall be the date of completion of the service in question. Sub rule (b) also contains that if any payment is received before the time which is specified in clause (a) then the point of taxation shall be the date on which such payment was received, to the extent of such payment. Explanation to this rule clearly specifies that if any advance is received by the service provider towards the provision of taxable service then the point of taxation shall be date of receipt of such advance. If advance is received on one or more dates then the point of taxation shall be each such date on which the advance is received.

Example:

Date of Completion of Service:	30 th April
Date of Raising of Invoice:	3 rd May
Point of Taxation:	3 rd May
Date of Completion of Service:	30 th April
Date of Raising of Invoice:	16 th May
Point of Taxation:	30 th April
Date of Completion of Service:	30 th April
Date of Raising of Invoice:	13 th May
Date of Receipt of Advance:	₹ 50000 on April 10 th , 25000 on April 25 th .
Point of Taxation:	April 10 th , April 25 th and May 13 th .

Rule 4 contains the rules to determine point of taxation in case of change of rate of tax. The rule begins with the words "Notwithstanding anything contained in Rule 3" which means that when there is a change in rate of service tax it is this rule which is applicable and not Rule 3. When there is a change in rate of service tax the point of taxation shall be determined in the following manner:

- Where a taxable service has been provided before the change in effective rate of tax and the invoice for the said taxable service has been issued and the payment for the same has been received after the change in effective rate of tax then the point of taxation shall be the date of payment or the date on which the invoice has been issued, whichever is earlier.
- Where a taxable service has been provided before the change in effective rate of tax and the invoice has been issued before the change in effective rate of tax but the payment for the same has been received after the change in effective rate of tax then the point of taxation shall be the date on which the invoice has been issued.
- Where a taxable service has been provided before the change in effective rate of tax and the payment for the same is received before the change in effective rate of tax but the invoice has been issued after the change in effective rate of tax then the point

Where a taxable service has been provided before the change in effective rate of tax and the invoice for the said taxable service has been issued and the payment for the same has been received after the change in effective rate of tax then the point of taxation shall be the date of payment or the date on which the invoice has been issued, whichever is earlier. ☺

of taxation shall be the date when the payment has been received.

- Where a taxable service is provided after the change of effective rate of tax and the payment is made after the change in effective rate of tax but the invoice for the said taxable service is issued prior to the change in effective rate of tax then the point of taxation shall be the date of payment.
- Where a taxable service is provided after the change in effective rate of tax and the invoice for the same is issued and the payment for the said invoice is received before the change in effective rate of tax then the point of taxation shall be the date when the payment was received or the date when the invoice was issued whichever is earlier.
- Where a taxable service is provided after the change in effective rate of tax and the invoice is issued after the change in rate but the payment is received before the change in rate of tax then the point of taxation shall be the date when the invoice has been issued.

An Example:

Tax Rate – upto 30-04-2011 – 10.30 per cent

Tax Rate – from 01-05-2011 – 12.36 per cent

Situations	Service Provided	Invoice Raised	Payment Received	Point of Taxation
1	28-04-2011	03-05-2011	10-05-2011	03-05-2011
2	28-04-2011	30-04-2011	10-05-2011	30-04-2011
3	28-04-2011	03-05-2011	30-04-2011	30-04-2011
4	03-05-2011	28-04-2011	05-05-2011	05-05-2011
5	03-05-2011	28-04-2011	30-04-2011	28-04-2011
6	03-05-2011	05-05-2011	28-04-2011	05-05-2011

Rule 5 contains the provisions for payment of tax in case of new services. It is explicitly stated that where a service is taxable for the first time then no tax shall be payable to the extent the invoice has been issued and the payment has been received against such invoice before the said service became taxable.

The word “and” is very important and signifies that mere issuance of invoice is not sufficient; the payment should also have been received before the service became taxable. In other words, all payments realised after the service became taxable shall suffer tax even though invoice has been issued prior to the date when the service was brought within the tax net. Sub rule 5 (b) also states that service tax shall not be payable if the payment has been received before the service became

Where a taxable service is provided after the change in effective rate of tax and the invoice for the same is issued and the payment for the said invoice is received before the change in effective rate of tax then the point of taxation shall be the date when the payment was received or the date when the invoice was issued whichever is earlier.

taxable and the invoice for the said payment has been issued within the period referred to in Rule 4A of the Service Tax Rules i.e. within 14 days from the date of provision of service or receipt of payment whichever is earlier.

Rule 6 deals with “continuous supply of service” (CSS). The following services have been notified as “CSS” vide Notification No. 28/ST-2011 dated 1st April, 2011:

Section 65(105)(zzzx)	Telecommunication
Section 65(105)(zzzq)	Commercial or Industrial Construction
Section 65(105)(zzzh)	Construction of Complex
Section 65(105)(zzzu)	Internet Telecommunication
Section 65(105)(zzzza)	Works Contract

The above services will be treated under the category of “CSS” irrespective of the period for which they are provided or agreed to be provided. All other taxable services shall be treated as CSS only if they are provided or agreed to be provided continuously for a period exceeding three months.

Rule 3, 4 and 8 of the Point of Taxation rules do not apply in case of continuous supply of service. Rule 6 alone applies to CSS. Point of Taxation in case of CSS shall be the time when the invoice for the service provided or to be provided is issued. If the invoice is not issued within 14 days of the completion of the provision of service then the point of taxation shall be the date of completion of such service. However, where any payment is received in advance by the service provider, the date on which such payment was received will be point of taxation to the extent of such payment. In majority of the cases services which are in the continuous supply are governed by a written contract.

Explanation 1 to Rule 6 addresses the issue when terms of contract govern the payment criteria. The explanation clarifies that where the service provided in whole or part is determined periodically on the completion of an event in terms of a contract and upon happening of such an event the service receiver is liable to make payment to the service provider

then the date of completion of each such event will be deemed to be the date of completion of service irrespective of whether payment is received from the service receiver or not. The classic examples in this case are construction related services, works contract, maintenance services, etc. Explanation 2 clarifies that where any advance payment is received by the service provider from the service receiver towards the provision of taxable service, the point of taxation shall be the date of receipt of each such advance payment.

Specific taxable services or persons have been accorded special treatment in determining the point of taxation vide Rule 7. The following taxable services or persons qualify for the privileges contained in this rule:

- a. Services covered by sub-rule (1) of Rule 3 of Export of Services Rules.
- b. Persons who are liable to tax under the reverse charge mechanism i.e. where the recipient of taxable service is liable to deposit service tax as a deemed service provider
- c. Individuals, Proprietary Firms or Partnership Firms who are providing any of the following taxable services: Architect, Interior Decorator, Chartered Accountant, Cost Accountant, Company Secretary, Scientific and Technical Consultancy, Legal Services.

In all the above three instances the point of taxation shall be the date on which the payment is received or made by the service provider or service receiver as the case may be. However, there are three provisos to this rule which prescribe certain conditions to pay service tax on realisation basis. The first proviso provides that with respect to services covered under sub-rule (1) of Rule 3 of Export of Services Rules the payment for such services should be realised within the period specified by the Reserve Bank of India and if the payment is not received within the said specified period then the point of taxation shall be determined as if Rule 7 did not exist at all. Proviso 2 lays down that in respect of services

where the recipient of the taxable service is liable to pay service tax then such recipient should make payment of the value of taxable service to the service provider within six months from the date of invoice and if such payment is not made then it would be deemed that Rule 7 did not exist at all. Hence, if payment is not made within six months then the date of invoice will be the point of taxation and payment of tax will become due which will result in interest outflow along with tax. Proviso 3 of this rule deals with "associated enterprises" taxation. In the case of associated enterprises where the person who is providing the services is located outside India the point of taxation shall be the date of making credit entry for the amount to be paid in the books of account of the person receiving such service or the actual date of making the payment to the service provider outside India whichever is earlier.

Rule 8 deals with royalties, copyrights, trademarks, designs and patents. It may be possible that at the time when these services are provided the whole amount of consideration payable to the service provider may not be ascertainable. In this situation the rule provides that after the service has been provided and the use or benefit of the said service by any person other than the service provider gives rise to payment of any consideration then the service shall be treated as having been provided each time when the consideration is received or an invoice is issued by the service provider whichever is earlier.

Rule 9 contains the transition provisions. The Point of Taxation Rules does not apply to services which are completed or where invoices are issued prior to the date on which these rules came into force i.e. 1st April, 2011. A three month breather from the application of the provisions of these rules is provided in the proviso to this rule. Services which are completed on or before 30th June, 2011 or where the invoices are issued upto 30th June, 2011 the option to follow the provisions of these rules with effect from 1st April, 2011 or treat the point of taxation as the date on which the payment is received or made is at the discretion of the service provider or service receiver, as the case may be.

In conclusion, the point of taxation need a close study by every stakeholder i.e. service provider, service receiver, Government as these rules are a change from the past. Any change raises new hopes and expectations and these rules are not exception, for Government the change raises hopes of increased revenue and for the rest it is the much desired clarity in law. Time will alone answer the question whether these new rules fulfilled the hopes of Government or others or both. ■

Rule 3, 4 and 8 of the Point of Taxation rules do not apply in case of continuous supply of service. Rule 6 alone applies to CSS. Point of Taxation in case of CSS shall be the time when the invoice for the service provided or to be provided is issued. If the invoice is not issued within 14 days of the completion of the provision of service then the point of taxation shall be the date of completion of such service. In majority of the cases services which are in the continuous supply are governed by a written contract. ☺☺

Note: Rule 7 of Point of Taxation Rules, 2011 has been amended vide Notification No. 41/2011 ST dated 27-06-2011 to provide that point of taxation in case of taxable consulting engineer's service would be the date on which payment is received or made. However, if the payment is not made within a period of six months of the date of invoice, the provisions of this rule would not apply.

ESOP Cost Allowability- An Issue for the Indian Companies



In common parlance, we understand ESOPs as schemes floated by the companies for offering shares to their employees. SEBI (Employee Stock Option Scheme and Employee Purchase Scheme) Guidelines 1999, defines ESOPs as “Option given to the whole time Directors, Officers or employees of a company which gives such Directors, Officers or employees, the benefit or right to purchase or subscribe at a future date, the securities offered by the company at a pre-determined price. ESOPs have been popular in India for a long time now. Though companies have been issuing ESOPs since a long time, they face a dilemma in claiming the cost pertaining to the same. There is a lot of ambiguity surrounding the deductibility of the ESOP cost in the hands of the employers. In the absence of any specific provision in the Income Tax Act, 1961, companies have been placing reliance on various judicial precedents to claim these expenses. Read on to know more.

“If I take care of my people, they will take care of the customer,” - Maxine Turner (owner of the Salt Lake City based catering service, Cuisine Unlimited)

The above lines highlight the fact that human assets are one of the most important assets for any company. There are many companies that can attribute their success to their employees. As more and more qualified people find themselves up for grabs by employee-hungry corporates, companies are feverishly striving to retain their own people by hook or by crook. In today's competitive world, it is important that employees' strings are attached to the organisation.

This has inundated companies to accentuate investments in human capital. Unarguably, human assets can increase the organisation value tremendously as opposed to physical assets. Companies have formulated various schemes/plans to reward and retain employees. For instance, in case of Reliance Industries, there is a system of deferred bonuses where all the employees associated with a project are offered a share of the profits it will generate, if they stay till its completion.

With this backdrop, many companies have formulated various incentive schemes, including ESOPs. In common parlance, we



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understand ESOPs as schemes floated by the companies for offering shares to their employees. SEBI (Employee Stock option Scheme and Employee Purchase Scheme) Guidelines 1999, defines ESOPs as “Option given to the whole time Directors, Officers or employees of a company which gives such Directors, Officers or employees, the benefit or right to purchase or subscribe at a future date, the securities offered by the company at a pre-determined price.”

Broadly, the life cycle of ESOPs can be divided into four stages/phases. The first stage is referred to as ‘Grant’, which means issue of option/units to employees under ESOP schemes. The second stage is referred to as ‘Vest’ which means to become entitled to receive incentive (i.e. shares/ cash) upon satisfaction of the specified conditions as agreed under the plan. Date of vesting refers to the date on which the employee has unconditional right to receive cash or shares under the ESOP scheme. Vesting period is the period between the grant date and the vesting date. The third stage is termed as ‘exercise’. It means making of an application by the employee to the employer for issue of shares against the option vested in him. The last stage is characterised by the sale of these shares which entails capital gains tax.

Though companies have been issuing ESOPs since a long time, they face a dilemma in claiming the cost pertaining to the same. There is a lot of ambiguity surrounding the deductibility of the ESOP cost in the hands of the employers. Companies also face an issue as to in which stage the expenses should be claimed by it viz. at the time of grant/vest or exercise of these shares. In the absence of any specific provision in the Income-tax Act, 1961, companies have been placing reliance on various

One of the earliest judicial precedents on ESOP is in the case of **SSI Limited vs DCIT [85 TTJ 1049] (2004) [Chennai Tribunal]**. In this Ruling, the Chennai Tribunal held that the ESOP expenditure booked under the head ‘Staff welfare’ by SSI Limited (the assessee) should be allowed as allowable business expenditure. In this case, the Tribunal referred to SEBI (ESOS and ESPS) Guidelines 1999. The clause (a) of Schedule I (Accounting policies for ESOS) of these guidelines states that “in respect of options granted during any accounting period, the accounting value of the options shall be treated as another form of employee compensation in the financial statements of the Company”. ☺☺

judicial precedents to claim these expenses. The ensuing paragraphs capture the essence of various judicial precedents in this regard.

One of the earliest judicial precedents on the subject is in the case of **SSI Limited vs DCIT [85 TTJ 1049] (2004) [Chennai Tribunal]**. In this Ruling, the Chennai Tribunal held that the ESOP expenditure booked under the head ‘Staff welfare’ by SSI Limited (the assessee) should be allowed as allowable business expenditure. In this case, the Tribunal referred to SEBI (ESOS and ESPS) Guidelines 1999. The clause (a) of Schedule I (Accounting policies for ESOS) of these guidelines states that “in respect of options granted during any accounting period, the accounting value of the options shall be treated as another form of employee compensation in

the financial statements of the Company”. The Tribunal held that for determining the taxability or admissibility, the taxing principle will have to be followed and if there is no such taxing principle, the accounting principle will guide the taxation or allowability of expenditure. For this, a reference was also made to the Supreme Court Judgments of **Chellapalli Sugar Ltd. vs CIT [1974 CTR 309]** and **Tuticorin Alkali Chemicals and Fertilisers Ltd [141 CTR 387]**. Thus, the Tribunal held that in line with the accounting principle laid down by the aforementioned SEBI guidelines, ESOP cost must be considered as another form of employee compensation. Accordingly, the ESOP cost must be treated as an allowable expenditure by SSI Limited.

The Tribunal observed that instead of granting ESOPs to the employees, the employer had the option of paying monies to its employees as compensation for services rendered which could have been used by the employees for acquiring the shares in the Company. In this case, the moneys paid would have been allowed as business expenditure. The mere fact that a different route was chosen by the employer, whereby the shares were issued directly to compensate the employees for services rendered, will not make an otherwise allowable expenditure as an expense of capital nature or one that is notional and fictitious. Further, once the option is given and exercised by the employee, the liability in this behalf is ascertained, so far as the company is concerned. It is not the case of contingent liability depending upon various factors on which the assessee has no control.

Contrary to the above decision is the case of **Ranbaxy laboratories Ltd. vs ACIT [124 TTJ 771] (2009) [Delhi Tribunal]**. The facts in

this case are strikingly similar to the judgement in the case of SSI (supra). In this case also, Ranbaxy (the assessee) had issued its own shares having face value of ₹10/- and market value being ₹738 to its employees at ₹595/- per share. The difference between market price and grant price (₹738 – ₹595) per share was charged in the P&L A/c over the vesting period of five years. Thus, proportionate amount of such amount was charged as deferred employee compensation and claimed as expenses. AO and CIT (A) disallowed the same holding that liability is not certain till employees exercise the option, pay the grant price and get the share. In giving its judgment, the Delhi Tribunal held that issue of shares at below market price does not result into incurring any expenditure rather

it results into short receipt of share premium which the assessee was otherwise entitled to. The receipt of share premium is not taxable and hence any short receipt of such premium will only be a notional loss and not actual loss for which no liability is incurred and such notional losses are not allowable under the provisions of the Income-tax Act, 1961. Further, reference was made to Section 37 of the Income-tax Act, 1961, which requires that there should be an expenditure incurred by the assessee. However, a benefit or income foregone cannot be considered as expenditure. The Tribunal was of the view that the assessee has not incurred any expenditure but has merely received lesser amount of share premium.

The Tribunal pronounced that though the SEBI (ESOS and ESPS) Guidelines 1999 require the assessee to account for short receipt of share premium to employee compensation expense, for claiming such expense as allowable, the assessee has to qualify that expenses are incurred and the same are wholly and exclusively for the purpose of business.

The above judgment has been heavily relied on in recent judgement pronounced by Mumbai Tribunal in the case of *M/s. VIP Industries Ltd.* 2010-TIOL-654. In this case, the Tribunal held that the assessee's case was squarely covered by the decision in the case of Ranbaxy Laboratories Ltd. (supra) and the same squarely covers the issue under consideration against the assessee and in favour of the Revenue.

During the course of the hearing, the Id. Counsel for the assessee pointed out that certain aspects had not been considered by the Delhi Tribunal while rendering its decision in the case of Ranbaxy Laboratories Ltd. (supra) on the similar issue which are business consideration

involved in allotment of shares, SEBI guidelines prescribing the accounting treatment of ESOP cost and the fact that the case of SSI (supra) was not considered as the issue involved was in the context of order by CIT under Section 2663 of the Act.

However, it was held that the said aspects pointed out by the Id. Counsel for the assessee were not material enough to have any direct bearing on the well considered and well reasoned decision rendered by the Tribunal.

Thus in the present case, in lines with the judicial pronouncement of Ranbaxy Laboratories Ltd. (supra), the Tribunal held that any short receipt of share premium would only be a notional loss to the assessee and not an actual loss. It was further held that any benefit or income foregone by the assessee cannot be considered as expenditure and since the assessee had not incurred any expenditure but had merely received lesser amount of premium, the same could not amount to expenditure within the meaning of Section 37 of the Act.

Another judgment that deserves a mention here is the case of *Lowry (Inspector of Taxes) vs. Consolidated African Selection Trust Limited (1940) 8 ITR (Suppl) 88 (HL)*, the House of Lords had an occasion to consider whether the difference between the market value of shares and the price at which it was allotted by the Company was an allowable expenditure. Based on the facts of that case, by a majority judgment, the House of Lords held that the difference between the market price and amount recovered from the employees cannot be allowed as deductible expenditure.

In this case, the assessee Company had issued shares at par to its employees in appreciation of services that employees have rendered i.e. for the past services.

Contrary to the decision in *SSI Limited vs DCIT (2004) case*, is the case of *Ranbaxy laboratories ltd. vs ACIT [124 TTJ 771] (2009) [Delhi Tribunal]*. The facts in this case are strikingly similar to the judgement in the case of SSI (supra). In giving its judgment, the Tribunal held that issue of shares at below market price does not result into incurring any expenditure rather it results into short receipt of share premium which the assessee was otherwise entitled to. The receipt of share premium is not taxable and hence any short receipt of such premium will only be a notional loss and not actual loss for which no liability is incurred and such notional losses are not allowable under the provisions of the Income-tax Act, 1961. ☺

The shares were being quoted at a higher price in the market. It was claimed that the shares were issued at par to further the interest of the Company's trade and to secure a benefit to the Company and the sum representing difference between the market price and that cost recovered by the employees was the sum expended for the purposes of their trade and should be allowed as deductible expense.

The tribunal observation in this regard is reproduced as follows:

"A Company, generally speaking, can issue its shares at any price it likes not being less than par. This is not a trading transaction, and does not in any way affect its gains and profits under Schedule D. In the present instance the shares were issued at par to certain employees in order to give them an interest in the Company, but not in payment of any sum contractually due to them. In these circumstances the respondents have failed to establish that any sum has thus been expended or laid out for the purpose of the trade of the Company."

Thus, the issue of deductibility of ESOP cost in the hands of the employers is not free from litigation. Lack of a specific legislation in this regard and contrary views adopted by the judicial authorities has accentuated the trouble for the companies.

The case of **Accenture Services Pvt. Ltd vs ITO (Mumbai Tribunal) [2010]** is on different footing wherein an Indian company made certain payments to its parent company (which was cross charged by the parent company) for allotment of shares to the employees of the Indian company. The AO disallowed the amount incurred by the assessee on the ground that this expenditure is not the expenditure of the assessee company but that of parent company and the benefit of such expenditure accrues to the parent company and not assessee.

In this judgement, the Mumbai Tribunal gave its findings in consonance with the order pronounced by the CIT (A). The Tribunal held that though the shares of the parent company have been allotted, the same have been given to employees of the Indian company. Since it is an expense incurred to retain, motivate and award the employees of the Indian company and at its behest, it is similar to the salary costs of the Indian company. Accordingly, the same qualifies as business expense of the Indian company.

The above issue pertaining to charge back has also been addressed in Circular 9/2007 dated 20th December, 2007 as well. In reply to question no. 16 to the said circular, it has been specifically mentioned that where the employer purchases the shares and then subsequently transfers such shares to its employees, the expenditure is allowed as a deduction to the employer company. However, if the shares are allotted to the employees from the share capital of the company, no deduction shall be available to the employee.

Thus a principle may be drawn from the above discussion that where the expenses are incurred by the Indian company in terms of purchase of shares for its employees, such expenses are allowed to it and where the shares are being issued from the company's own share capital, the same should not be considered as allowable expenditure.

Another judgment is in the case of **CIT vs Infosys Technologies Ltd. (2008) [297 ITR 167] [Supreme Court]**. This case does not deal directly with the issue of corporate tax deductibility but with the issue of whether the same should be considered as perquisite in the hands of employees or not. The judgment pertains to the AY 1997-1998 to AY 1999-2000, when

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there was no specific provision of perquisite in the Income-tax Act, 1961 ('the Act'). The specific provision that stock options allotted to the employees at discounted price are to be considered as perquisite has been inserted vide Finance Act 1999 w.e.f 1-4-2000 through Section 17(3)(iiia) of the Act

The Supreme Court observed that since the issue pertains to the period when there was no specific provision regarding taxability of ESOP in the hands of employee, these should not be taxed as perquisite in their hands. The Supreme Court held that the benefit which arose on the date when the option stood exercised was only a notional benefit whose value is unascertainable. On the date when the options were exercised it was not possible for the employees to foresee the future market value of the shares.

Another judicial precedent that may be mentioned here is **Eimco K. C. P. Ltd. vs CIT (2000) (242 ITR 659) (SC)**. Though this

Where the expenses are incurred by the Indian company in terms of purchase of shares for its employees, such expenses are allowed to it and where the shares are being issued from the company's own share capital, the same should not be considered as allowable expenditure. ☞

case does not pertain directly to ESOPs, however it may be relied upon to derive an analogy for resolving the issue in hand. Eimco, an American Company, and K.C.P. Ltd., an Indian Company, promoted the appellant-Company. Both the companies agreed to subscribe to shares amounting to ₹4,70,000. Eimco contributed technical know-how towards its share. It valued the know-how, etc., at a sum of ₹2,35,000 and paid the balance in cash as its contribution. The board of directors of the appellant allotted equity shares of ₹2,35,000 being the value of the know-how, to Eimco. In the assessment year 1969-1970, the appellant claimed deduction of ₹2,35,000 as revenue expenditure paid to Eimco towards consideration for the supply of technical know-how.

During the course of litigation, the issue on allowability of such expense travelled up to the Supreme Court. The Apex court held "that what in effect was done by the appellant in allotting equity shares of ₹2,80,000 to Eimco, was to reimburse the contribution made by Eimco in the form of know-how. This could never be treated as expenditure, much less an expenditure laid out wholly and exclusively for purposes of the business of the appellant. It was not a case where after the incorporation, the appellant-Company in the course of carrying on its business,

spent the said amount for acquiring any asset.

An issue that is pertinent in this matter is whether an argument can be taken that ESOP cost is revenue expenditure under Section 37(1) of the Act since the same does not result in any capital asset of enduring nature. At this juncture, it would be important to analyse whether remuneration in kind is expenditure or not. The following decisions may be relied upon to understand the term 'expenditure' envisaged under Section 37(1) of the Act.

- **Indian Molasses Co Pvt Ltd vs. CIT West Bengal (1959) 37 ITR 66 (SC)** held that "the idea of "spending" in the sense of 'paying out or away' money is the primary meaning and it is with that meaning that we are concerned. 'Expenditure' is thus what is 'paid out or away' and is something which is 'gone irretrievably'..... Expenditure which is deductible for income-tax purposes is

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one which is towards a liability actually existing at the time, but the putting aside of money which may become expenditure on the happening of an event is not expenditure".

- In the case of **CIT UP v. Nainital Bank Ltd. (1966) 62 ITR 638 [SC]** the Apex Court held that "In its normal meaning, the expression 'expenditure' denotes 'spending' or 'paying out or away', i.e., something that goes out of the coffers of the assessee".
- In the case of **Madras Industrial Investment Corpn. Ltd. v. CIT (1997) 225 ITR 802 [SC]** the Apex Court held that "expenditure is not necessarily confined to the money which has been actually paid out. It covers a liability which has accrued or which has been incurred although it may have to be discharged at a future date".

It is clear from the aforementioned discussion that even the definition of 'expenditure' has been analysed differently by the same level of authorities, which does not provide a clear picture as to whether ESOP expenses shall be considered as revenue expenditure under Section 37(1) of the Act.

Conclusion

ESOPs have been popular in India since a long time. However, the issue of deductibility of ESOP cost still persists and is not free from ambiguity. It is high time that the Government enact rules/policies to clear the air. Unless the clear laws are laid down, the assessee shall continue to face hardships from the Revenue authorities. All the hopes that one may have laid on Direct Tax Code that it shall bring some respite on the issue, have also turned futile. The Direct Tax Code Bill that has been tabled in the Parliament does not cover this aspect at all. ■

Prize Chit and Money Circulation (Banning) Scheme Act, 1978: Precautions



Prize Chit and Money Circulation (Banning) Scheme Act, 1978 basically bans promotion or conduct of any money circulation and/or prize chit scheme and provides for imprisonment and penalty in case of failure to comply with the provisions. This act bans any prize chit or money circulation scheme or enrolment or participation as members in those schemes or receiving or remitting money under those schemes. This article deals with various aspects of this act with special reference to Multi-level Marketing business in India and gives various related judicial pronouncements in this regard. Multilevel Marketing or Network Marketing has been going on in India for many years. Multilevel marketing or Network marketing are ways to sell the products directly to the consumers in which the salesmen are compensated not only for the work done by them but also for the sales of people who have joined the company through them. These people are usually referred to as the down line and various levels of down line are created. The article also highlights the role and responsibilities of the Chartered Accountant as a statutory auditor or consultant with respect to compliance with this and other laws by network marketing companies.

Introductory Concepts

Multilevel Marketing or Network Marketing (MLM):

Multilevel marketing or Network marketing are ways to sell the products directly to the consumers in which the salesmen are compensated not only for the work done by them but also for the sales of people who have joined the company through them. These people are usually referred to as the down line and various levels of down line are created. The commission which is distributed among the salesmen depends upon the scheme used for division of the commission. These salesmen are known by various

names like distributors, affiliates, dealers, sales consultant, etc.

Pyramid Schemes: A Pyramid Scheme is a non-sustainable business which involves payments to participants primarily to recruit other people into the scheme and there is no real investment or sale of products.

Ponzi Schemes: In a Ponzi scheme the returns are paid to investors from their own money or money of subsequent investors rather than actual profit earned. It is best summarised as “rob peter to pay paul”.



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Legality and Legitimacy of MLM

MLM business operates in over 100 countries including countries like United States of America. Multilevel Marketing or Network Marketing has been going on India for many years and Amway, Oriflame, RCM are some of the companies which have been frontrunners in this field. The Federal Trade Commission of USA which deals with issues of consumer protection and competition jurisdiction clearly states: "Not all multi-level marketing plans are legitimate. Some are pyramid schemes. It's best not to get involved in plans where the money you make is based primarily on the number of distributors you recruit and your sales to them, rather than on your sales to people outside the plan who intend to use the products."¹ Reserve Bank of India in its Notification number RBI/2009-10/158 dated 16-9-2009 has asked all Primary (Urban) Cooperative banks to ensure KYC/AML guidelines in the accounts of multilevel marketing companies and has also given example of seven such Multilevel marketing companies in India. RBI has mentioned in the notification that these companies are luring the depositors by promising huge returns of their investment. In India the pyramid schemes and ponzi schemes are banned under the Prize Chit and Money Circulation (Banning) Scheme Act, 1978.

Prize Chit and Money Circulation (Banning) Scheme Act, 1978

This act basically bans promotion or conduct of any money circulation and/or prize chit scheme and provides for imprisonment and penalty in case of failure to comply with the provisions. This act bans any prize chit or money circulation scheme or enrolment or participation as members in those schemes or receiving or remitting money under those schemes.

In June, 1974, the Reserve Bank of India had constituted a Study Group under the Chairmanship of Shri James S. Raj, the then Chairman, Unit Trust of India, for examining in-depth the provisions of Chapter III-B of the Reserve Bank of India Act, 1934, and the directions issued thereunder to non-banking companies in order to assess their adequacy in the context of ensuring the efficacy of the monetary and credit policies of the country and affording a degree of protection to the interests of the depositors who place their savings with such companies. In its report submitted to the Reserve Bank in July, 1975, the Group observed that the prize chit/benefit/savings schemes benefit primarily the promoters and do not serve any social purpose, and that they are prejudicial to the public interest and affect the efficacy of the fiscal and monetary policies of the country. Ultimately the Group recommended that prize chits or money circulation schemes, by

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whatever name called, should be totally banned in the larger interests of the public and suitable legislative measures should be undertaken for the purpose. Pursuant to the said recommendation, the Parliament enacted the Prize Chits and Money Circulation Schemes (Banning) Act, 1978.

Money Circulation Scheme -Section 2(c):

Any scheme for below mentioned transactions:

- i. Making of quick or easy money or
- ii. Receipt of money or valuable thing as consideration for a promise to pay money on any event or contingency, relative or applicable to the enrolment of members into the scheme.

It is not relevant as to whether the money or thing is derived from the entrance money or periodical subscriptions.

Prize Chit – Section 2(e):

It covers any transaction or arrangement under which a person collects money as –

- i. Promoter
- ii. Foreman
- iii. Agent
- iv. In any other capacity

In any of the below mentioned methods:

- i. Lump sum
- ii. Instalments by way of subscriptions or contributions
- iii. Sale of units
- iv. Sale of Certificates or other instruments
- v. Membership fees
- vi. Admission fees
- vii. Service charges
- viii. Savings, Mutual benefit or thrift

Banning - Section 3:

No person shall promote or conduct any prize chit or money circulation scheme, or enrol as a member to any such chit or scheme, or participate in it otherwise, or receive

¹ "The Bottom line about Multilevel Marketing Plans", FTC, October 2009

or remit any money in pursuance of such chit or scheme.

Penalty:

The act prescribes two types of penalties –

1. Penalty for contravening Section 3 – Imprisonment up to three years or fine up to 5,000/- or both.
2. Penalty of Imprisonment up to two years or fine up to 3,000/- or both, for other offences associated with Scheme like:
 - a. Printing of brochure, tickets, coupons, etc for use in Prize Chit or Money Circulation Scheme;
 - b. Sells or distributes or advertises for selling or distribution of , tickets, coupons, etc for use in Prize Chit or Money Circulation Scheme;
 - c. Prints, publishes or has in possession for the purpose of publication or distribution
 - i. Any advertisement
 - ii. Any list of member, complete or incomplete
 - iii. Any such matter descriptive of or relating to such scheme which may act as inducement to any person
 - iv. Brings or invites any person to send for the purpose of sale or distribution any tickets, coupons etc for use in Prize Chit or Money Circulation Scheme or any advertisement of such scheme;
 - v. Uses any premises or causes or knowingly permits to use any premises for such schemes
 - vi. Causes or procures or attempts to procure any person to do any of the above acts

Offences by Companies:

Every person who is in-charge and was responsible to the company for the conduct of its business, at the time of committing of the offence, and Company itself are liable to be proceeded against provided that in case a person proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence.

In case it is proved that the offence was committed with consent or connivance or is attributable to any neglect on the part of any director, manager, secretary or other officer of the company, such director, secretary or other officer shall also be deemed to be guilty for that offence and shall be liable to be proceeded against and punished accordingly.

Company includes a firm or association of persons and in case of firm the director mean the partners.

This scheme called Multi-level Marketing creates a chain of customers and the long and unbroken chain would ensure larger amount of quick or easy money. The shorter and missed links in the chain would result in earning lesser commission. Therefore, there should be unbroken chain or customers. Secondly, the person does not get the value of the money he pays; thirdly, the companies are collecting service charges as stated above in a sale of goods. No service charges can be collected while the goods are sold. For all these reasons the scheme of so called Multi-level Marketing cannot be said not to violate the provisions of Section 2(c) of the Act. ”

Judicial Pronouncements

These are some of the significant judicial pronouncements on the Prize, Chit and Money Circulation (Banning) Act, 1978

(1) State of Bengal and Ors vs. Swapan Kumar Guha and others, SC, 1982 AIR 949 1982 SCR(2) 121

Background: One Sanchita Investments is a registered partnership firm consisting of three partners with a share capital of ₹7,000/-. In the year 1975 the said firm started its business in finance and investments. On a report given by the Commercial Tax Officer concerned, FIR was registered with the allegations that the firm had been offering 48 per cent interest which was later reduced to 36 per cent and that, therefore, it was involved in money circulation scheme for making of quick or easy money. The firm and its partners filed two writ petitions in the Calcutta High Court under Article 226 of the Constitution of India for quashing the FIR. The High Court allowed the writ petition and quashed the FIR and the State of West Bengal filed appeal by Special Leave in the Supreme Court. After an in-depth analysis of the definition of "money circulation scheme" in Section 2(c) of the Act, the Supreme Court went into the question as to whether the FIR prima facie discloses an offence under Section 4 read with Section 3 of the Act in the light of the requirements of Section 2(c) of the Act.

Decision: In this case the Supreme Court made an in-depth analysis of Section 2(c) of the Act i.e. the section defining money circulation scheme and analysed and interpreted that that any and every activity for the making of quick or easy money by itself would not fall within Clause (c) of Section 2 of the Act and that making of such quick

or easy money must depend upon any event or contingency relative or applicable to the enrolment of members into the scheme. It was held that to hold a person guilty of an offence under Section 4 read with Section 3 and 2(c) of the Act, two conditions must be satisfied: (1) it must be proved that he is promoting or conducting a scheme for the making of quick or easy money; and (2) the chance or opportunity of making quick or easy money must be shown to depend upon an event or contingency relative or applicable to the enrolment of members into that scheme.

Having so analysed the definition of "money circulation scheme", the Supreme Court applied the said definition to the allegations made in the FIR and negated the contention that the scheme attracted the provisions of Section 2(c) of the Act.

(2) *M/s Apple FMCG Marketing Pvt. Limited and Mr. R. Eric vs The Union of India, The State of Tamil Nadu and the Director General of Police, Chennai, Madras High Court, 2005*

Background: In this case, M/s Apple FMCG Marketing Private Limited filed a petition praying for a writ of declaration that selling products through the Network Marketing System is legal and not in contravention of the provisions of the Prize Chits and Money Circulation Schemes (Banning) Act, 1978 or any other law.

M/s Apple FMCG Marketing Private Limited was a company registered under the Companies Act, 1956. It is marketing various products including shampoo, tea, coffee powder, after-shave lotion, etc. under the brand-name 'Joy Eternal' through "network marketing". The marketing process was carried out directly by recruiting

the customers themselves as distributors of the products and services; the company regularly organised business development meetings and seminars, distributors meetings, etc. The participants of the meetings were encouraged to take up the distributorship of the products and were suitably registered if they so desire. There was no service fee for registration as distributor. Any person who was interested was given a product for the price fixed. The distributors were encouraged to enrol more distributors. The commissions were given only as per the volume of sales made by the individual distributor and his team.

Arguments by M/s Apple FMCG Marketing Private Limited

1. So far no complaints have been received against them from any distributor. Therefore, this Multi-level Marketing has not caused any loss to any of the distributors.
2. There is no 'service fee' for registration as distributor.
3. Every distributor gets commission on the basis of the volume of business that is generated by him.
4. No chain of customers in the process.
5. The distributors and the purchasers pay the value of the product that is purchased, therefore, they are not paying any excess amount.
6. They collect only nominal service charge for the service rendered.
7. The surveillance by the respondents violates the petitioners' fundamental right provided under Articles 19(1)(a) and 19(1)(g) of the Constitution of India.
8. Further the Union of India has also clarified that the "Multi-level Marketing" does not infringe the Prize Chits and Money Circulation Schemes (Banning)

Act, 1978 (Hereinafter referred to as 'The Act').

Decision:

1. The scheme, as stated above, creates chain of customers and only when the chain progresses without any break in any of the links, the 'principal distributor' gets more commission. If, for any reason, the chain is broken, at any stage, then the principal distributor's commission would get reduced proportionally to that extent. Therefore, it is not correct to say that there is no chain of customers in the process.
2. The contention that no service charge is collected also does not appear to be correct in view of the fact that every person who purchases a kit has to pay a service charge of Rs.50/- for each kit. Service charges are collected by governmental institutions like Electricity Board and Telephones as they are authorised by the Statutory Rules. No individual can collect any charge as service charges. The collection of service charge is, therefore, not legal.
3. From the very fact that 65 per cent is earmarked for paying as commission to the distributors, it is clear that the value of the product is only 35 per cent of the sale price. That is, when the goods are sold at ₹550/-, the actual value of the goods that are sold is only ₹188/- (calculated at 35 per cent).
4. The progress of the chain of customers, at some point of time, would get saturated and the distributor, who purchases the goods, will not find any purchaser/sub-distributor to sell or enrol afresh. At that time, due to the progress of the chain, in the manner stated above, such persons who would not find new members may be in lakhs

or even millions. Therefore, lakhs or even millions of people are bound to lose their entire money of Rs.550/- (value of one starter kit). At the same time, major portion of 65 per cent of the amount would be a gain to the petitioners-company since there would be no one to share that money.

5. The petitioner submitted that Union of India has made a clarification in an answer to a question in Parliament that Multi-level Marketing does not violate or offend the provisions of the Prize Chits and Money Circulation Schemes (Banning) Act. It is suffice to say that it is not for Union of India or any Member of Parliament to interpret the provisions of any act. The Act has been passed by the Parliament, but the power to interpret the Act is only vested in Judiciary, and that power is not given to the Executive. The statement given by the Union of India or its Officers that Multi-level Marketing does not attract the provisions of the Act cannot legalise an illegal act.

6. This scheme called Multi-level Marketing creates a chain of customers and the long and unbroken chain would ensure larger amount of quick or easy money. The shorter and missed links in the chain would result in earning lesser commission. Therefore, there should be unbroken chain or customers. Secondly, the person does not get the value of the money he pays; thirdly, the companies are collecting service charges as stated above in a sale of goods. No service charges can be collected while the goods are sold. For all these reasons the scheme of so called Multi-level Marketing cannot be said not to violate the provisions of Section 2(c) of the Act.

Role of Chartered Accountants

Chartered Accountants may be associated as Statutory Auditors or Consultants to the network marketing companies. The role and responsibility of the Chartered Accountants would also vary depending on the type of assignment done by the Chartered Accountant.

Role and Responsibility as an Auditor:

'SA 250 Consideration of laws and regulations in an Audit of Financial Statements' deals with the auditor's responsibility to consider laws and regulations when performing an audit of financial statements.

It basically the responsibility of the management to ensure compliance with various laws and regulations during the entity's operation including compliance with provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements.

The SA puts the auditor's responsibility regarding legal compliance as follows:

Legal Requirement type	Auditor's responsibility
The provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements such as tax and labour laws.	The auditor's responsibility is to obtain sufficient appropriate audit evidence about compliance with the provisions of those laws and regulations
Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties; non-compliance with such laws and regulations may, therefore, have a material effect on the financial statements.	Limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial Statements.

In the case of MLM or Network Marketing Companies, if there is any violation of the provisions of the Prize Chits and Money Circulation Schemes (Banning) Act then the direct effect will not be on amounts and disclosures in the financial

statements. The auditor then needs to undertake such specified audit procedures in case of the MLM or Network Marketing Companies so that they are able to identify the non-compliance with this act. In case non-compliance is identified then the auditor is required to undertake specified audit procedures and report as per the requirements of SA 250.

Role and Responsibility as Consultant/Employee:

The role and responsibility of CA as consultant or Employee of the company will be to ensure compliance with the provisions of Prize Chits and Money Circulation Schemes (Banning) Act by the company. The CA may have to play an advisory role and inform the Directors or other person entitled with the management of the company about the various legal provisions and the penalties on contravention of the same. It is also the ethical responsibility of all the members to duly inform any person who wishes to start a network marketing company about all the legal requirements

and ensure compliance with Prize Chits and Money Circulation Schemes (Banning) Act and other applicable laws and regulations. This would help the person greatly in avoiding future legal hassles. ■

Limited Liability Proprietorship



India has introduced the limited liability partnership in 2009 which has been a significant step for facilitating the growth of SME and nurture talent. Though this is a new concept in our country it has been in vogue abroad for quite sometime. Now another new mode called of business in the form of limited liability proprietorship has been introduced in France. Though this is not yet introduced in India, this can be viewed as a new avenue for conducting business and possible introduction in the country as we progress with the reforms. An attempt has been made in the article to examine the structure, regulatory and fiscal aspects governing such business.



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The advent of capitalism has increased the competition in the world, business and commerce have grown to manifest themselves into different forms, beginning with proprietorship, partnership firms, co operative societies, joint stock companies, etc. but these have not been able to cater to the ever growing requirement for newer avenues of conducting business. Of late two further avenues have come to the forefront for conducting business one of them has been Limited Liability Partnership (LLP), this has been a new concept in India and is about to pick up.

However, there is another avenue just opened in another part of the world which is the Limited Liability Proprietorship. Though this is not yet introduced in India, this can be viewed as a new avenue for conducting business and possible introduction in the country as we progress with the reforms.

Limited liability partnership has been in existence for a few decades now across the world, though it has been introduced in India only in 2009 after the parliament passed it and it was approved by the president. Now a new type of business is introduced in France

in the form of Limited Liability Proprietorship.

The French national assembly and the senate have recently approved a bill for a new type of concern known as “**d’entrepreneur individuel responsabilité limitée**” (EIRL) which can be translated for “entrepreneur individual liability limited” in simple language “Limited liability proprietorship”. This was published in the official journal on 16th June, 2010 (Law no 658-2101) and the act comes into force with effect from 1st January, 2011. This provides the much required new avenue for starting a new business by individuals with limited capital resources and risk taking ability. Till now anyone wanting to carry on a business alone and have limited liability needed to get incorporate a single member company “*entreprise unipersonnelle à responsabilité limitée* (EURL). The risk that the personal assets of the individual will be liable for the debts of the business in case of a failure/bankruptcy is totally eliminated and to this effect will give an initiative to start new business and augment the growth engine of the economy.

Any individual (a professional, businessman, trader, farmer, artisan etc) can set up an EIRL by incorporating it with a name with the registrar (this will be followed by EIRL for identification by the public). This new entity thus created can hold assets and incur liabilities in its own name. It can enter contracts and do business just like any other business concern. This mode is available for new businesses as well as for conversion of existing proprietorships. The individual can transfer his personal assets to the new entity and contribute capital which will be used in the business by the entity and belong only to the entity. Put it differently if a person is currently carrying on a business, he can convert it into an EIRL and transfer his own assets

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and liabilities to it on registration, from that point the business of the new entity will be different from the individual.

Creation

An application for registration of the entity has to be made with the registrar. The most important step in the formation is the declaration. An individual who desires to create an EIRL needs to prepare a declaration (**patrimoine d’affectation**) on the property that can be considered as connected to the business and hence is at risk to creditors. This declaration as completed has to be filed with the concerned authority like a Chamber of commerce for people engaged in business, or a court/tribunal handling matters of commerce in case of professionals and others. This is a very important document involved in the creation of the new entity and can be filed either at the time of registration or subsequently.

The declaration contains the description of the property as to the quantity, value and other particulars it will also contain the obligations. Some assets need to be mandatorily included in the declaration as they are inextricably connected with the business like the stock of a trader, finished goods of manufacturer, receivables of a professional etc. While other assets may be included at the option of the entrepreneur like vehicle or furniture used for the business. In case of inclusion of immovable property in the declaration, it has to be registered at the local mortgage office similar to a registrar of properties in India. In case of an asset assigned to EIRL as per the declaration excluding money, if the value thereof exceeds €30,000 a report from an auditor needs to be filed. This will lend authenticity to the assets held by the concern and will form the basis for those dealing with it. It needs to be noted that the assets transferred to EIRL should only be those that would be used in the course of the business and ones which are unrelated to the specific business to be carried cannot be transferred as a part of the declaration.

Any asset that is included in the declaration will form part of the business and in case of a failure only these assets will be liable for attachment or liquidation for satisfying the claims of the creditors. All other assets of the proprietor which are not included in the declaration will automatically get protected. Similarly obligations in favour of the creditors will be enforceable on the entity if they are mentioned in the declaration. It is the duty of the entrepreneur as per the conditions set, that information must be given to the creditors. Any creditor may file his objection thereof within a prescribed time in which case his claim is either settled or provided with a guarantee

and a court will make a ruling in this behalf.

Accounting Requirements

EIRL needs to maintain accounting records in accordance to the nature of business it is in, eg: different accounting records are specified for trading activities, contractors, professionals, etc. and they are simplified as defined by a decree.

The business has to be transacted with an exclusive bank account, different than that of the entrepreneur. Annual accounts or accounts subject to simplified requirements where applicable are to be filed each year with the registrar and will be filed along with the declaration submitted. This will allow the creditors or other interested parties to monitor the operations of the entity.

Taxation

The EIRL can elect to be taxed under the corporate tax structure, *Impôt sur les sociétés* (IS) as per the French fiscal regime; the taxable income will be taxed at

the concessional rate structure as below if the turnover of the entity is less than €7.63 million (excluding VAT).

15 per cent for taxable income upto €38,120.

Income above €38,120 will be taxed at the normal 33 1/3 per cent (which is the normal rate applicable to corporates in France).

This is a benefit available to the EIRL which was earlier available only to corporates, and unifies the tax structures for all SMEs, in essence provides the same benefits to all SMEs irrespective of their legal form. In case of disposal of assets and any capital gains there on will also be taxed under the corporate structure.

The entity may also elect to be taxed under the scheme of Micro BNC, for those with annual revenues of less than €32,000 (Excl VAT). In this case the taxable profit is taken at 66 per cent of the revenues. Subject to certain conditions there are different rates of taxes in this structure. An entity electing this mode is not required to maintain accounting records for tax purposes. It is sufficient if they keep the records of the revenue.

EIRL may pay salary to the proprietor as the two are distinct from each other. This salary will be a compensation for the work done by the person to EIRL, and will be a tax deductible expense in the hands of the entity. The salary so received will be taxed as income from salary for the entrepreneur.

Profits if any generated by the EIRL may be distributed to the entrepreneur, they are treated as dividends and will be subject to tax accordingly. The dividend income will be taxed as the income of the recipient (entrepreneur himself in this case, as he is the sole owner) as per the applicable provisions governing the taxation of dividends by giving an allowance of 40 per

Social security contributions are to be made by an EIRL depending on the tax structure chosen by it. Tax on income (*Impôt sur le revenu*) or Corporation tax (*impôt sur les sociétés*). France is different from other European nations, in a way that social security system is financed mostly from contributions levied on the earned income rather than from taxes. Also the payer of the social security will not get any specific benefits for the part of the social security contributions which represents the General social security contribution (*contribution sociale généralisée* (CSG)) and is like a tax. ”

cent of the amount so received, and rebate available for flat deduction at €1,530 or €3,050 (based on individual being taxed or a couple). The recipient may opt for a flat withholding tax at the rate of 18 per cent to avoid progressive taxation where he finds it to be beneficial.

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contributions can be upto 10 per cent including all components (CSG being the major component accounting for upto 75 per cent of the social security cost payable).

In case a the tax on income is opted social security contributions are to be calculated on total taxable profit of the entity, which is the case in case of normal entrepreneurs and hence there will be no difference in this respect. Although certain minimum contributions like insurance, retirement, death contributions are payable even in case of a loss. For those opting for the corporation tax the contributions are made on the earned income with certain adjustment made by including a part of the distributions in excess of a specified percentage of the value of assets used in the business.

Other Aspects

The act has provided certain provisions to safeguard the interests of the creditors of the EIRL, the tax authorities, and to prevent the abuse of the act. It provides that the sole proprietors will be liable with the totality of their assets in case, they have acted improperly and not observed the obligations and

The concept of EIRL discussed is new and we may wait to observe the kind of impact it creates in the economy or the implementation or operational hurdles it creates before considering introduction in India. More self employed people or professionals may run their business in this mode as it will limit their risk. This will require introduction of a new statute coupled with necessary changes in the tax structure and other related guidelines. ☺

duties cast on them by the statute, like the structure of specified funds or maintenance of separate books of account and other provisions of the governing statute and a court decides the reality of these acts. This provision is similar to the piercing of corporate veil as is found in the companies act to check misuse.

All the business documentation and official communication of the entity shall carry the words EIRL, e.g. on the letter heads, quotes, invoices, receipts etc.

In case of death of the proprietor of the entity the creditors will still enjoy claims on the assets they had prior to the death, also in case of death where a heir/beneficiary comes into the business the same person is marked in the register in place of the original proprietor by the registrar who initially registered the EIRL. The above goes to the effect of making perpetual existence of the entity as long as someone is assigned by the proprietor the legal heir expresses interest to pursue the activity within the prescribed time drafted currently as three months. Provisions have also been made to govern the activities of minors as regards the establishment and operation of EIRL, transfer and recovery of assets.

Conclusion

In India we have embarked on a series of reforms in our fiscal and regulatory frameworks. Progress has been made by initiatives like DTC, Companies Bill, GST, IFRS, LLP, though the speed of these has not been as good as expected. Limited liability partnership (LLP) concept has been started in our country in 2009 after the act by the parliament in this regard; this has been a significant step to help the professionals and other entrepreneurs with limited resources to carry their business with limited risk. However a lot of potential may be unlocked if a new



mode of doing business by one person comes into existence with limited liability.

The government may consider something similar as has been discussed above to provide a fillip to the economic activity, as we want to be an economic power. The concept of EIRL discussed is new and we may wait to observe the kind of impact it creates in the economy or the implementation or operational hurdles it creates before considering introduction in India. More self employed people or professionals may run their business in this mode as it will limit their risk.

This will require introduction of a new statute coupled with necessary changes in the tax structure and other related guidelines. The government has to ensure a hassle free mechanism for creation of business entities devoid of red tape and bureaucracy. Simpler laws, tax incentives, easy credit from financial institutions, arbitration/dispute redressal mechanism and such other measures to ensure that faster economic growth is possible. This hopefully may result in the business moving from unorganised sector into organised and can also be looked at for expanding the tax base both direct and indirect. ■

Basel III: The Mantra of New Economic Order



Capital is scarce resource. Particularly in context of banking industry, any sudden changes in asset quality can quickly wipe out bank-capital. This is the industry where short-term wholesale liabilities fund longer-term assets and any failure to roll over short-term financial paper, or a 'run' on deposits, can lead to de-leveraging and asset sales.ⁱ Therefore, in order to strengthen the soundness of banks and promoting stability of the global banking system; capital adequacy standards have been proposed by the Basel Committee on Banking Supervision, a standing committee under the auspices of the Bank for International Settlements (BIS). This article is an attempt to understand, analyse and explain the development, mechanism and implications of Basel III. The article talks about gaps in Basel I and Basel II accord which led to concentration of bank's loan portfolio towards housing loans. It also highlights the micro and macro prudential measures proposed for strengthening the resilience of the global banking system proposed under the Basel III, and critically analyses the recommendations for achieving financial stability.



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The possibility that banks may adjust capital and asset portfolios to reduce the probability of breach of capital requirements has been highlighted by many researchers. Milne (2001b) had suggested that the Basel committee's January 2001 consultation on revised capital accord overstated the benefits to be obtained from improving the risk-sensitivity of international capital standardsⁱⁱ. Edward Kane (1989) and Rebel A. Cole et al. (1995) document the problem of 'gambling on resurrection' that banks choose a risky asset portfolio that pays out high profits or bonuses if the gamble succeeds but leaves depositors, or

their insurers, with the losses if the gamble fails.ⁱⁱⁱ Hellmann, Murdock and Stiglitz have tried to find the cure of the problem of moral hazard in deposit insurance and stringent capital control^{iv}. They have argued that if banks hold a high amount of capital, they internalise the adverse consequences of gambling and, thus, will choose to invest prudently. While it is possible to combat moral hazard, it can be done only at the cost of profitability.

Introduction

The banks are at the centre of the credit intermediation process. They may play a leading role in the

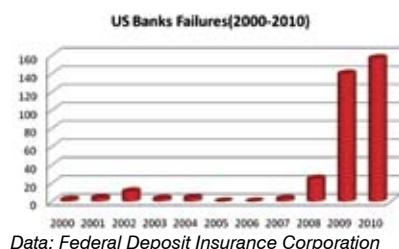
ⁱ Adrian Blundell-Wignall and Paul Atkinson, *Thinking Beyond Basel iii: Necessary Solutions for Capital and Liquidity* OECD Journal: Financial Market Trends – Volume 2010 Issue 1

ⁱⁱ Milne, A (2001b) 'Bank Capital Regulation and the New Basel Accord: A Constructive Critique', *Journal of International Regulation and Compliance*, Nov 2001

ⁱⁱⁱ George A. Akerlof and Paul M. Romer (1993) elaborate on the moral hazard, arguing that banks may use fraudulent lending practices (such as insider lending) to "loot" banks. In this case bank managers extract value out of the banks even if this leads to insolvency.

^{iv} Thomas F. Hellmann, Kevin C. Murdock and Joseph E. Stiglitz, *Liberalization, Moral Hazard in Banking, and Prudential Regulation: Are Capital Requirements Enough?*, *American Business Review*

building up risk of financial crisis, if they start leveraging their balance sheets excessively. They affect the economy, both directly and indirectly, by being lenders, market makers and providers of backstop liquidity and payment services. The collapse of major banks in the United States in 2008 followed by many others in following two years (see chart below) caused significant disruption to the wider financial system and economic activity in the form of recent financial crisis. It has been proved that self regulation under Basel II has not worked and that the depth and severity of the financial crisis was amplified by excess liquidity and weak underwriting standards in the banking sector, which led to too much credit.



Before understanding the nitty-gritty of Basel III, it is first of all important to find out how banking institutions manipulated the requirements of the Basel I and Basel II norms to their benefit, leading to unintended consequences.

Basel I and Basel II: The Road Much Travelled

The first attempt to create global capital adequacy standards for banks was made in 1988, when the Basel I accord was developed. This accord applied relatively crude risk-weightings to different types of lending. The degrees of credit risk exposures were not significantly calibrated to borrowers' default risks, which distorted bank lending decisions away from highly rated borrowers. Banks started treating all types of borrowers under one

risk category irrespective of credit rating.

The regime was refined and made more sophisticated, and the risk weightings made more granular, in 2004 with Basel II, which allowed banks with the appropriate systems and historical data to use an internal ratings-based approach for assessing the risks of particular types of lending. The revised norms for risk-based capital allocation failed to contain any provisions for loading a risk factor for the loan portfolio concentration. This created an incentive for banks to prioritise home lending. As the banks were able to effectively significantly leverage their capital bases they shifted the focus of their balance sheets towards housing loans because of the higher returns on capital available. It is estimated that many banks were generating returns on equity of more than 40 per cent from their home loan books.

The problem with incentives, however – and the Basel Committee's risk weightings provide massive incentives – is that if they are too large and remain in place over the long term, they can produce unintended consequences, like a massive over-exposure to a particular sector or form of lending for which there is no historical experience and a consequent under-pricing of risk^v.

Financial Crisis and Basel III

Sub-prime crises and failure of major banking institutions in the US followed by a crisis situation in the Europe forced the Bank for International Settlements (BIS) to reconsider the risk management system which guides the financial sector behaviour. "Spare the rod, Spoil the child" may be a wrong method of parenting, however, the Basel Committee could not spare the rod of stricter capital requirements to regulate the global

The Basel III framework on the new bank capital and liquidity framework was approved on 12th November, 2010. It is aimed at increasing the resilience of the global banking system by raising the quality, quantity and consistency of bank capital and liquidity, constraining the build-up of leverage and maturity mismatches, and introducing capital buffers above the minimum requirements that can be drawn upon in bad times.

economic and banking order. The purpose was to reduce the ability of banks to damage the economies by taking on excess risk. The pursuit for distorted incentives at the cost of long term financial stability had to be checked.

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Proposed Basel III-The Road Ahead

The Group of Governors and Heads of Supervision, the oversight body of the Basel Committee on Banking Supervision, has developed new global standards referred to as "Basel III" to address the concerns raised during the crisis. It comprises the following building blocks, which address both firm-specific and broader, systemic risks:

^v Bartholomeusz Stephen, *Basel III's missing denominator*, *Business Spectator* 14-15 Sep 2010

Micro prudential, firm-specific reform measures:

I. **Increased Capital Requirements:** The Tier I¹ capital requirement has been increased from 4 per cent to 6 per cent. The core Tier I capital which includes only common equity component has been raised from the current 2 per cent level, before the application of regulatory adjustments, to 4.5 per cent after the application of stricter adjustments. The difference of 2 per cent between the total capital requirement of 8 per cent and the Tier 1 requirement can, however, be met with Tier 2 capital. If we factor in the tougher definition of capital and the better risk coverage, Basel III will lead to around a seven-time increase in the common equity requirement.

II. **Enhancing the Quality of Tier 1 Capital:** Higher quality capital means more loss-absorbing capacity. A key element of the new definition is the greater focus on common equity. The predominant form of Tier 1 capital will be common shares and retained earnings. Goodwill, minority interest (that if a company takes over another with a majority interest and consolidates it into the balance sheet, the net income of the third party minorities can't be retained by the parent as common equity), deferred tax assets, and investments in other financial institutions will not be included in (or will be deducted from) common equity. Tier 2 capital instruments are

Under Basel III, the coverage of the risks has been substantially improved, especially with reference to capital markets activities, securitisations, exposures to off-balance sheet vehicles and counterparty credit exposures arising from derivatives. Trading book exposures shall be subject to a stressed value at risk requirement. Basel III also recommends an additional capital charge against mark-to-market losses associated with the deterioration of counterparty's credit quality. ”

proposed to be harmonised and Tier 3 capital will be completely eliminated. Banks would have less than five years to comply with the minimum ratios (4.5 per cent common equity and 6.0 per cent Tier 1).

III. **Better Coverage of Risk:** The coverage of the risks has been substantially improved, especially with reference to capital markets activities, securitisations, exposures² to off-balance sheet vehicles and counterparty credit exposures arising from derivatives. Trading book exposures shall be subject to a stressed value at risk requirement. Basel III also recommends an additional capital charge against mark-to-market losses associated with the deterioration of counterparty's credit quality.

It is expected that the higher capital requirements for OTC activities will increase incentives to use central counterparties and exchanges. These measures will be introduced at the end of 2011 and will result in about a four-fold increase in trading book capital requirements.

IV. **Minimum Global Liquidity Standards:** Two regulatory standards for liquidity risk have been developed to achieve two separate but complementary objectives. The first objective is to promote the short-term resilience of the liquidity risk profile of institutions by ensuring that they have sufficient high quality liquid resources to survive an acute stress scenario lasting for one month. The Committee has developed the Liquidity Coverage Ratio to achieve this objective. The ratio will be calculated as under:

$$LCR = \frac{\text{High Quality Assets}}{\text{30 Day Net cash Outflows}} \geq 100 \text{ per cent}$$

High quality assets can include, for example, cash, central bank reserves, marketable claims on sovereigns, central banks, the BIS, IMF, etc., and government debt issued in the currency of the country of operation. Corporate and covered bonds may also be eligible – after a quantitative impact study with an appropriate haircut. Cash outflows will be based on the modeling of funding run-offs; stable and less stable deposits; unsecured wholesale funding;

¹ Bank Capital under Basel II was divided into three categories. Tier I ("core") capital included the book value of common stock, non-cumulative perpetual preferred stock and published reserves from post-tax retained earnings. The following items were deducted from shareholders equity, while arriving at capital adequacy ratio: Equity investment in subsidiaries; Accumulated losses of previous years; loss to date in the current year and; other intangible assets. Tier 2 ("supplementary") capital was deemed of lower quality. It included Revaluation Reserves (at a discount of 55 per cent), Investment Fluctuation Reserves and General Provisions and Loan Loss Reserves (upto a maximum of 1.25 percent of total weighted risk assets), long-term subordinated debt (upto 50 per cent of Tier I capital at a discount based on remaining maturity) and cumulative and/or redeemable preferred stock. A maximum of 50 per cent of a bank's capital could comprise tier 2 capital. Tier III capital comprised short-term subordinated debt with lock in clause, which could only be used to cover market risk.

² Trading book exposures under Basel II were based upon a crude value-at-risk (VaR) measure loosely consistent with a 10-day 95 per cent VaR metric.

and secured (collateralised) funding run off.

The second objective is to promote resilience over longer-term horizon by creating additional incentives for banks to fund their activities with more stable sources of funding on an ongoing structural basis. The Net Stable Funding Ratio (NSFR) has been developed to capture structural issues related to funding choices.^{vi} The NSFR will be calculated as under:

$$\text{NSFR} = \frac{(\text{Available Stable Funding } \$)}{(\text{Required Stable Funding})} \geq 100 \text{ per cent}$$

Available Stable Funding is defined as: Tier 1 and Tier 2 capital (100 per cent) + preferred stock not in Tier 2 with maturity $\geq$ one year (100 per cent) + liabilities $\geq$ one year (100 per cent) + stable shorter-term retail and small business funding (with $\leq$ €1m per customer) (85 per cent) + less stable (e.g. uninsured non-maturity) retail and small business funding (70 per cent) + unsecured wholesale funding (50 per cent). Central bank discounting is excluded to avoid over reliance on central banks.

The Required Stable Funding (RSF) is based on balance-sheet and off balance-sheet exposures, and is defined as: Cash, securities $\leq$ one year, loans to financial firms $\leq$ one year (zero per cent) + unencumbered marketable sovereign, central bank, BIS, IMF etc AA or higher with a zero per cent risk weight (20 per cent) + Gold, listed equities, corporate bonds AA- to A- $\geq$ one year, loans to non-financial corporate $\leq$ one year (50 per cent) + loans to retail clients (85 per cent) + all else (100

per cent). Off-balance-sheet exposures to be included are conditionally revocable and irrevocable credit facilities to persons, firms, SPV's and public sector entities: a 10 per cent RSF of the currently undrawn portion. All other obligations will have an RSF set by the national supervisor.

- V. Introduction of a leverage ratio: The Committee has introduced a leverage ratio which will be calculated as under:

$$\text{Minimum equity tier one capital/ assets ratio} \geq 3 \text{ per cent}^{\text{vii}}$$

The objective of introducing this supplementary measure is to contain the build-up of attempts to game the risk based requirements, and help address model risk. The Committee referred to this as a 'backstop' measure. It has proposed a simple leverage ratio based on Tier 1 capital, with a 100 per cent treatment to all exposures net of provisions, including cash and cash-like instruments. Certain off-balance sheet exposures have been included with a 100

per cent credit conversion factor, and written credit protection to be included at its notional value. It is proposed that there be no netting of collateral held and no netting of off-balance sheet derivative exposures (more akin to IFRS treatment than to GAAP). In this way, the leverage ratio would result in a strong treatment for OBS items.

When it comes to the calibration, the Committee is proposing to test the ratio of 3 per cent during the parallel run period. The Committee will use the transition period to assess whether the proposed design and calibration is appropriate over a full credit cycle and for different types of business models. This assessment will include consideration of whether a wider definition of exposures and an offsetting adjustment (i.e. to subtract opposing derivatives positions) in the calibration would better achieve the objectives of the ratio. While there is a strong consensus to base the leverage ratio on the new definition of Tier 1 capital, the Committee will also track the impact of using total capital and tangible common equity. The measure would be fully implemented in 2018.

- VI. Stronger standards for supervision, public disclosures and risk management: Stronger supervision, risk management and disclosure standards have been proposed. The Committee has strengthened the Pillar 2 supervisory review process of the Basel II capital framework, with inclusions in the areas of corporate governance, liquidity risk management, valuation practices, sound compensation practices and stress testing. Pillar 3 disclosure requirements

In Basel III, stronger supervision, risk management and disclosure

standards have been proposed. Pillar 3 disclosure requirements relating to securitisation exposures and sponsorship of off-balance sheet vehicles, among others have been revised. The deficiency of the disclosures as regard to banks' regulatory capital has also been tackled. Banks are expected to comply with the revised requirements by end-2011.

^{vi} Consultative Document on International framework for liquidity risk measurement, standards and monitoring, BIS Publication, December 2009

^{vii} <http://www.ft.com/cms/s/0/ab02375c-aafb-11d1-9e6b-00144feabdc0.html#ixzz1BeB1azcF>

The introduction of liquidity ratios is aimed at providing additional early warning signals to regulators and investors. Taken together, these measures should make the system more stable over the long run. However, the requirement of higher bank holdings of liquid and low return assets coupled with high funding costs will bring additional operating costs that banks will try to pass on to their retail business. It will lead to higher lending rates and tightening lending standards something akin to credit crunch. ”

relating to securitisation exposures and sponsorship of off-balance sheet vehicles, among others have been revised. The deficiency of the disclosures as regard to banks' regulatory capital has also been tackled. Banks are expected to comply with the revised requirements by end-2011.

Macro Prudential Measures

It has been observed that firm-specific approach by itself is not sufficient to promote financial stability. Following broader measures to address procyclicality and to strengthen the resilience of the entire banking system have been considered as equally important by the Basel Committee:

I. **Reducing procyclicality:** The Committee has introduced measures to raise capital levels in good times so that they can be drawn down in periods of stress to reduce procyclicality. Such a capital is called capital buffer as it can be drawn down in periods of stress. Following two kinds of

buffers have been proposed for mitigating procyclicality in the banking and broader financial system:

a) **Capital Conservation Buffer:**

A capital conservation buffer of 2.5 per cent has been introduced, which will bring the total common equity requirement (i.e. core capital) to 7 per cent. The purpose of the conservation buffer is to ensure that banks maintain a buffer of capital that can be used to absorb losses during periods of financial and economic stress. While banks are allowed to draw on the buffer during such periods of stress, the closer their regulatory capital ratios approach the minimum requirement, the greater the constraints on earnings distributions^{viii}.

The capital conservation buffer will begin at 0.625 per cent of RWAs on 1st January, 2016 and increase each subsequent year by an additional 0.625 percentage points, to reach its final level of 2.5 per cent of RWAs on 1st January, 2019.

b) **Countercyclical Capital Buffer:**

A countercyclical buffer within a range of 0 per cent – 2.5 per cent of common equity or other fully loss absorbing capital will be implemented according to national circumstances. Banks that have a capital ratio that is less than 2.5 per cent, will face restrictions on payouts of dividends, share buybacks and bonuses.

This buffer will serve three main purposes: it will help to slow down credit bubbles, make an economy's banks stronger, and offer

a way out of the paradox of capital. The paradox of capital can be explained with an example: let's say that a bank has a minimum capital requirement, and then suffers a series of write-downs. Because the write-downs come straight out of capital, the bank is left below the minimum. So it is forced to raise new capital right at the worst possible time to do so, or else fail. Now with countercyclical capital buffers, banks increase their capital in good times, not in bad times. And then, in bad times, they disappear: regulators can (and indeed are encouraged to) abolish the buffers immediately, if there's some kind of credit crisis. When write-downs eat into bank capital, they eat only into the buffer, which is no longer required^{ix}.

II. **Forward-looking provisioning:**

The Committee has proposed forward-looking provisioning by strongly supporting the IASB principles to base it on the 'expected' (rather than the current 'incurred') losses of banks' existing portfolios. It also proposes to deduct from bank capital any shortfall in these provisions (i.e. to expected losses) to provide an incentive against underprovisioning. The supervisory guidance is also updated to be consistent with the move to such an expected losses (EL) approach. Such guidance will assist supervisors in promoting strong provisioning practices under the desired EL approach.

III. **Addressing systemic risk and inter-connectedness:**

The failure or impairment

^{viii} <http://www.basel-iii-accord.com/>

^{ix} Salmon Felix, Basel III: The incomplete capital buffer proposal, <http://blogs.reuters.com/felix-salmon/2010/07/16/basel-iii-the-incomplete-capital-buffer-proposal/>

of systematically important financial institutions can have negative consequences for other firms and the real economy. For example, a failed bank's creditors can incur losses. And prior to failure, a bank can take actions that help alleviate its problems but can generate costs for other financial institutions. The Basel Committee, in cooperation with the Financial Stability Board, is developing a methodology comprising both quantitative and qualitative indicators to assess the systemic importance of global financial institutions. It is also assessing the magnitude of loss absorbency that global systemic banks should have. It is expected that this additional loss absorbing capacity will be met through some combination of common equity, contingent capital and bail-in debt.

Basel III: Will it be Able to Bring Financial Stability

Will Basel III make the world safer from financial crises? There cannot be a short answer to such a complex question – but the answer is yes, and no, not much either way. The proposals are positive. They represent a fundamental shift in conduct of banking regulation and supervision in future as it fixes not only the shortcomings of micro-level supervision but also gives macro-prudential overlay to the regulatory framework. The recommendations relating to stronger quality and consistency of regulatory capital, increased capital requirements, enhanced risk coverage and implementation of leverage ratio will definitely strengthen banks' resilience to new shocks and improve comparison across banks.

The introduction of liquidity ratios is aimed at providing additional early warning signals to regulators and investors.

Taken together, these measures should make the system more stable over the long run. However, the requirement of higher bank holdings of liquid and low return assets coupled with high funding costs will bring additional operating costs that banks will try to pass on to their retail business. It will lead to higher lending rates and tightening lending standards, something akin to credit crunch. But, it is also not wrong to say that excessive fear of another financial crisis and mistrust of banks by regulators has led to a big penalty in the form of higher equity-capital reserve ratios. The impact is to be borne either by the borrowers in the form of higher interest rates or by the economy in the form of reduced lending. Though, it can also be absorbed by the banks by reducing ROE or reducing operating expenses and increasing non-interest sources of income.

Further, there hasn't been any obvious discussion on the denominator of the capital adequacy ratio. The calculation of a bank's capital adequacy ratio isn't as simple as dividing its capital by its assets. What's important

Looking to the future, it has to be emphasised that the banks that focus on building sound business models underpinned by adequate capital and liquidity, would be the ones that would be able to create sustainable business models. Moreover, at the end of the regulator, a very close look has to be taken to check how banks arrive at their measures of exposure, how they go about risk-weighting their assets, and how they engage in risk mitigation activities. ”

in assessing its adequacy is the relationship of capital to the bank's assets, which is why capital adequacy is expressed as a ratio. An important aspect which is missing in Basel III is the fine-tuning the risk-weightings to reduce the biases to particular forms of lending. Hence, the reference to the denominator, the asset base against which the adequacy of the capital is measured, was very important. During the crisis, the asset bases of most of the big US and European banks imploded. But surprisingly, this aspect has been just covered by a simple leverage ratio – a cap on the relationship between Tier I capital and total assets. At 3 per cent that would allow \$1 of capital to be leveraged 33 times, which is probably around 10 times more than what a good bank's capital is leveraged today.

More than trebling the core Tier I capital ratio to about 7 per cent would, all other things being equal, only collapse the leverage in a bank. Basel I caused massive shifts in the patterns of lending and Basel II exaggerated them. Given the debate about Basel III with a tougher definition and level of capital, undoubtedly there will be pressure on banks to understate their risk-weighted assets and, therefore, the eventual impacts of Basel III as the new measures are phased in, will need to be very closely monitored.

Looking to the future, it has to be emphasised that the banks that focus on building sound business models underpinned by adequate capital and liquidity, would be the ones that would be able to create sustainable business models. Moreover, at the end of the regulator, a very close look has to be taken to check how banks arrive at their measures of exposure, how they go about risk-weighting their assets, and how they engage in risk mitigation activities. ■

Developing IT Strategic Plan and Identifying Areas of Specialisation¹

Information Technology (IT) has become all pervasive and is a key enabler in enterprises of all sizes and this is so even in enterprises providing services. CA firms are impacted by IT in two ways: firstly by automation of their client's operations resulting in most of the client's data turning digital; and secondly CA firms have to use IT in their own offices to provide services. Thus, IT by default rather than by design has become critically relevant for CA firms. Technology deployment by design from a strategic perspective by CA firms could act as catalyst of growth and key differentiator to not only provide current service offerings to existing clients but also develop innovative delivery capabilities for new service offerings to existing /new clients. This can empower CA firms to stay ahead of the curve by enhancing capabilities and transform the way services are provided.

Strategic Planning

Strategy is defined as the long range blueprint of an organisation's desired image, direction and destination what it wants to be, what it wants to do and where it wants to go. Strategic planning is a critical element for articulating a shared vision, and for building the necessary framework necessary to work together on common goals. A good strategic plan will provide clarity on how strategic goals will be achieved. It outlines long-term goals and details the specific strategies and goals that are to be pursued. The strategic planning process has to be iterative and provide a roadmap for transition from the present situation to the future vision.

The Strategic Plan has to be a living document and should be re-visited to review accomplishments against set objectives, so that feedback is provided that will influence future planning and decision making.

Strategy issues

The key issues to be addressed in designing a strategic plan are:

- Who are we? What do we want to be known for?
- Where are we now?
- Where do we want to be and why?
- What needs to be done to get there and how?
- How do we know when we get there?
- How do we keep the momentum going?

IT Strategic Plan

The objective of IT strategic plan is to continuously infuse technology so as to provide better and more efficient service to clients and improve internal processes. The commitment to use of IT has to be key strategy in the firm's business plan. This has to be based not on technology for technology's sake but on an overall understanding that technology can be used to improve staff efficiency and effectiveness and therefore services to the clients.

The IT strategic plan has to be in line with the overall strategic plan and ensure that IT is deployed for meeting business requirements so as to sustain and extend the business strategy. This requires that IT resources are managed and directed in tune with the business strategy and priorities while being transparent

about benefits, costs and risks. A well-developed IT strategic plan improves key stakeholders' understanding of IT opportunities and limitations, requires assessment of current performance, identifies current IT capabilities, capacity and human resource requirements, and clarifies the level of investment required in IT.

The IT strategic planning has to be a standard practice and has to be managed at principal/partner level. The IT strategy has to be linked with the overall strategy of the firm and encompass all key service offerings and designed to build new business and value-added capabilities by leveraging the effective use of IT as required. IT strategic planning has to be documented and regularly updated as per the overall goals of the firm.

The mission statement of the firm would provide the context in which the goals and strategies are formulated, outlines the scope and direction, and provides the framework within which IT Strategic plan would be prepared. Specific technology projects and initiatives would be undertaken accordingly. For example, one of the goals regarding the use of IT in carrying out the firm's mission could be: "We will use appropriate technology to provide effective tools for providing effective timely services to our clients." To achieve this goal we will:

- Encourage office-wide participation in identifying the right type of technology and tools required.
- Enhance the quality of services by appropriate use of technology to facilitate the sharing of information

¹ Contributed by CA A. Rafeeq (The Author is a member of the Institute. He can be reached at rafeeq@vsnl.com.)

within the firm and with the clients as required.

- Provide opportunities for staff to research and develop new approaches and techniques to optimise the use of IT and provide necessary training;
- Develop and maintain an IT plan that encompasses the Technology infrastructure, IT process architecture, applications and relevant best practices for using IT in all key areas of services.

Identifying areas of Specialisation

Based on overall business strategy, the CA firm may decide to specialise in specific areas which offer new opportunities of services. In case of areas of specialisation identified for their future potential, it is necessary to consider in detail the current starting point - existing clients, staff, systems and supporting infrastructure - and to identify the gaps between the current situation and the future needs. Depending on individual circumstances the solutions may involve a drastic change, resulting in replacement of all key systems in a relatively short time scale. In the most of cases, however, a more evolutionary approach will be more appropriate involving replacement and modification of existing systems within a less challenging time scale. In planning for transition to future, it is critical to consider the following key factors:

a) IT Skills and Competencies

An analysis should be made of the current level of IT Skills at both the management and staff level. An inventory of current IT resources of the firm and IT environment of all the major clients has to be made to arrive at the typical IT infrastructure and required skill-sets. The policies, procedures and practices of the firm in various areas of operation need to be evaluated against requirements of client and future direction of the firm's services. The challenge will be to identify the IT Resources, competencies

and the skills needed for the future development of the practice of the firm using IT. IT strategic planning has to be in line with the firm's long term goals and the future strategic requirements. Critical decisions have to be taken on staffing levels, responsibilities and skill requirements.

b) Applications and Data

The existing mechanism of delivering services and related procedures need to be evaluated from the perspective of automation. The types of software applications used and processes in the firm have to be reassessed to confirm whether they are in tune with the future IT strategy. Duplication of jobs needs to be identified so that they could be automated. Care must be taken to develop an integrated timetable for change which takes into account the abilities of staff, IT resources available, IT resources required and practices of the firm. A change management process has to be implemented mapped keeping in mind the overall objective of providing best services at optimal cost.

c) Technology Infrastructure

Based on the requirement assessment of IT of the firm, it is essential to identify areas of development of IT for ensuring appropriate IT solutions for the future. IT resource planning and related budgets need to be carefully assessed considering the rapid technological changes and importance of serving both the present and future clients. The required infrastructure solutions need to be put in place and the staff trained to ensure that services offered meet the client requirements.

d) Delivery of IT Services

The way the firm provides services to clients, internal processes adapted and the means of delivery of such services has to be assessed and new methodologies and means of delivery of services

must be developed in tune with the capabilities of implemented IT. A thorough review of the practices needs to be undertaken to update them in tune with the IT deployment of the firm. It has to be ensured that IT solutions implemented are in tune with the overall IT strategy and goals of the firm.

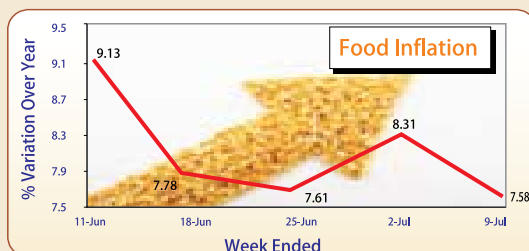
e) User Culture and Training

Developing and implementing identified IT Solutions and services is not just about acquiring the right technology but more about training people in required processes. At all stages in the process it will be necessary to consult as appropriate and to be aware of the extent to which managers and staff are themselves going to have to adapt in order to ensure the success of the implemented strategy. Issues concerning culture, working practices, policies and procedures, documentation and training needs must be an integral part of the IT planning process. The overall aim in reviewing each of these areas is to identify the gap between the current knowledge and skill levels based on present environment and that which has been identified as best suited for the firm serving its future needs in the most cost effective way.

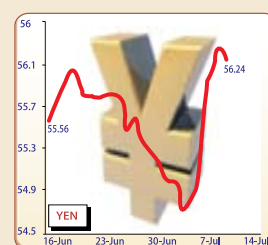
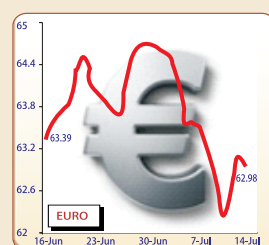
Conclusion

The most critical aspect in developing IT strategic plan in a CA firm is to review the current technology and application infrastructure in terms of future requirements and implement a migration plan by adopting the right strategies. This will require developing the future IT Vision that would deliver needed services to clients which support and align projects with the overall Business Plan and the needs of the firm. Developing IT strategic plan requires investment of time at partner/principal level and involvement of all key staff and identifying areas of specialisation.■

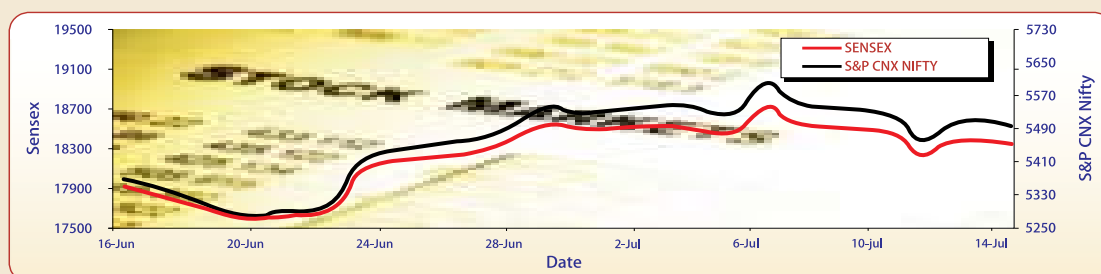
Economic Indicators



Indian Rupee vs. Major Foreign Currencies (June 16, 2011 to July 15, 2011)



Stock Markets



Selected Indicators

(per cent per annum)

Item	2010	2011					
	Jul. 2	May 29	Jun. 3	Jun.10	Jun.17	Jun.24	Jul1..
Cash Reserve Ratio ⁽¹⁾	6.00	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⁾	7.50/8.00	9.25/10.00	9.25/10.00	9.25/10.00	9.25/10.00	9.25/10.00	9.25/10.00
Deposit Rate ⁽³⁾	6.00/7.50	7.75/9.10	8.25/9.10	8.25/9.10	8.25/9.10	8.25/9.10	8.25/9.10
Call Money Rate (Weighted Average) ⁽⁴⁾	5.42	7.40	7.30	7.36	7.40	7.68	7.56

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 ebboard@icai.org.

ACCOUNTANT'S BROWSER

'PROFESSIONAL NEWS & VIEWS PUBLISHED ELSEWHERE'

Index of some useful articles taken from Periodicals/Newspapers received during June-July 2011 for the reference of Faculty/Students & Members of the Institute.

1. ACCOUNTING

Accounting for Jointly Controlled Entities that have Minority Interest, by Dolphy D'Souza. *BCAJ*, June 2011, pp.69.

Effects of SFAS 133 on the Risk Relevance of Accounting Measures of Banks' Derivative Exposures, by Anwer S. Ahmed etc. *The Accounting Review*, Vol.86/3, 2011, pp.769-804.

IFRS – Faulty Framework? by Uday Chitale & Murtuza Vajih. *BCAJ*, June 2011, pp.71.

IFRS: Need for Optimal Choice of Accounting Policies under IND-AS, by Jamil Khatri & Akeel Master. *BCAJ*, June 2011, pp.107-110.

Inflation & Nominal Financial Reporting: Implications for Performance & Stock Prices by Yaniv Konchitchki. *The Accounting Review*, Vol.86/3, 2011, pp.1045-1085.

Principles-based Versus Rules-based Accounting Standards: The Influence of Standard Precision & Audit Committee Strength on Financial Reporting Decisions, by Christopher P. Agoglia, etc. *The Accounting Review*, Vol.86/3, 2011, pp. 747-767.

2. AUDITING

Business Development Skill Builders for Young CPAs: Set Expectations Early to Help Team Members & Your Firm Succeed. By Mark Koziel. *Journal of Accountancy*, May 2011, pp.20-26.

Detection & Severity Classifications of Sarbanes-Oxley Section 404 Internal Control Deficiencies by Jean C. Bedard & Lynford Graham. *The Accounting Review*, Vol.86/3, 2011, pp.825-855.

Internal Audit: Computer-Assisted Audit Tools (CAATS) – Use of CAATS for Operational Review of Plant Maintenance by Deepjee Singhal & Manish Pipalia. *BCAJ*, June 2011, pp.63-68.

Internal Controls & Conditional Conservatism by Beng Wee Goh & Dan Li. *The Accounting Review*, Vol.86/3, 2011, pp.975-1005.

3. ECONOMICS

The Conceptual Dimensions of Good Governance, by Rajbir Singh Dalal. *Indian Journal of Public Administration*, January-March 2011, pp.91-99.

Governance & Risk in a Global Economy, by Fred O'Riordan. *CA Magazine*, June-July 2011, pp.52-59.

Prospects & Policy Challenges in the Twelfth Plan: A Comment on the Risks, by Y. Venugopal Reddy. *Eco. & Pol. Weekly*, June 11, 2011, pp.81-82.

Public Service Ethics in a Globalised World: The Duty to Serve & Responsibility to Care by O.P. Dwivedi. *Indian Journal of Public Administration*, January-March 2011, pp.1-14.

Survey on Computer Software & Information Technology Services Exports: 2009-10. *RBI Monthly Bulletin*, June 2011, pp.941-959.

4. EDUCATION

Liberal Commerce Education & Management Focused Business Education: A Status Report by Jitindra Nath Saikia. *University News*, June 13-19, 2011, pp.14-18.

Problems & Prospects of Indian Higher Education in the Age of Globalisation, by Samhita Chaudhuri. *University News*, June 06-12, 2011, pp.18-21.

What & How to Teach Professional Students for Achieving Short-term & Long-term Goals by M.S. Dhaka. *University News*, June 20-26, 2011, pp.1-2.

5. INVESTMENT

Capital Structure, Cost of Capital, & Voluntary Disclosures by Jeremy Bertomeu, etc. *The Accounting Review*, Vol.86/3, 2011, pp.857-886.

Regulatory Perspectives on Derivatives Markets in India by Subir Gokarn. *RBI Monthly Bulletin*, June 2011, pp.881-884.

6. MANAGEMENT

Corporate Governance Ratings: Towards Achieving True Accountability by Ashish Virmani & J.R. Ram. *Company Law Journal*, Vol.2, 2011, pp.132-138.

The Effect of the Mandatory Adoption of Corporate Governance Mechanisms on Executive Compensation by Constantinos G. Chalevas. *The International Journal of Accounting*, Vol.46, 2011, pp.138-174.

Financial Stability & the Relevance of the Regulatory Disputes Settlement in India by Suvir Sharma & Kanishk Thakur. *Company Law Journal*, Vol.2, 2011, pp.139-152.

7. TAXATION & FINANCE

Can Book – Tax Differences Capture Earnings Management & Tax Management? Empirical Evidence from China, by Tanya Tang & Michael Firth. *The International Journal of Accounting*, Vol.46, 2011, pp.175-204.

Taxation of Charitable Trusts: Role of Business or Profit Making Activity in Taxation of Charity by A.J. Majumdar. *Taxman*, June 11-17, 2011, pp. 103-117.

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

□ New Income Tax Criminal Probe Wing to Toe US Model

The newly created directorate of criminal investigation (DCI) in the income tax (I-T) department is to adopt the functioning and strategies of its American counterpart, the criminal investigation wing of that country's Internal Revenue Service (IRS). A group of senior Income Tax officials would visit the US soon to study the IRS framework and practices in this regard. "We would study the IRS model and accordingly create a system which will suit the Indian context. We will concretise it and present it before CBDT (Central Board of Direct Taxes) for approval," said a senior I-T department official. He added that DCI's primary role would be to handle cases involving money generated through illegal means such as bribery, smuggling, narcotics and terror funding. "The stakes are very high in these cases. The US IRS criminal investigation (wing) has been very successful in handling these cases. Our idea here is to create a specialised agency (DCI) to tackle illegally acquired money, in coordination with other agencies, including the police and enforcement directorate," said the official. He said for cases involving unaccounted income emanating legally but on which tax had not been paid, the departments normal machinery would be utilised, without DCI venturing into this area. DCI will, as mentioned earlier, focus on those cases where criminality is involved. It can operate under the existing framework, as no change is required in the I-T Act to make DCI functional. DCI has been given the mandate to seek and collect information about persons and transactions suspected to be involved in criminal activities having cross-border, inter-state or international ramifications, posing a threat to national security and punishable under the direct tax laws. It will also investigate the source and use of funds involved in such criminal activities and has been given powers to file prosecution complaints in the competent courts under any direct tax law relating to a criminal activity.

(Source: <http://www.economictimes.com>)

□ Now Pay Only 15 Per Cent Tax on Short-Term Gains

There seems to be a dim ray of hope for scores of investors who were asked to pay a higher tax for selling shares within 30 days of purchase. The Income Tax Appellate Tribunal (ITAT) has ruled that profits from the sale of shares held for less than 30 days are eligible to be treated as short-term capital gains, on which 15 per cent tax has to be paid. Tax officials demanded a higher tax of over 30 per cent on the ground that since shares were sold before 30 days from the date of purchase, such gains should be considered as business income and not short-term capital gains. Since tax rules do not spell out the duration of holding and frequency of securities trades for tax treatment, tax officials often use their discretion to arrive at a claim. This has been a source of endless disputes between investors and the tax department. The 15th June ruling by ITAT in Mumbai is the latest in a series of judicial and quasi-judicial decisions on what constitutes short-term capital gains and business income. The ITAT decision in the case of Hitesh Satishchandra Doshi followed two

earlier decisions, where the ITAT drew a 30-day mark to distinguish between business income and short-term capital gains. The Mumbai ITAT, however, held that the statute is clear only as far as the distinction between long-term and short-term capital gains is concerned. For long-term capital gains, shares have to be held for at least 12 months, and the profit from shares held for less than 12 months will be taxed as short-term capital gains. There is no tax on long-term capital gains. The ITAT also observed that the law does not lay down a 30-day mark to distinguish between business income and short-term capital gains. It pointed to the parameters laid down by the Supreme Court for making the distinction between investment and trading in shares. Factors such as intention of the assessee at the time of buying shares, whether the assessee borrowed money to purchase the shares and paid interest, the frequency of such purchases and disposal in that particular item, whether the purchase and sale is for realising profit or purchases are made for retention and appreciation in its value, and how the value of items has been taken in the balance sheet, are critical in determining whether a gain is business income or a short-term capital gain. Therefore, no single factor can be said to be decisive in determining whether the nature of the transaction is trading activity or investment, the ITAT held. Each case needs to be decided on the basis of the facts of the case. Therefore, treating a transaction as investment when the holding period is more than 30 days and treating the income as business income if the holding period is less than 30 days is not correct, the ITAT observed.

(Source: <http://www.thehindubusinessline.com/>)

□ TDS Woes Spilling From TIN

For the first time perhaps the Central Board of Direct Taxes has chosen to consciously undermine a hoary law still extant, the one Parliament has chosen not to repeal. The tax administration has been exhorting taxpayers not to set store by the TDS certificates they receive, but by what appears in the Tax Information Network (TIN) as tax credit available to them by way of advance tax, tax collected at source and deducted at source. What this meant was no matter what the TDS certificates said, the TIN information would be held as final and sacrosanct. And more galling would be a situation where a taxpayer has paid an installment of advance tax, but can't claim credit for the same because the bank with which the amount has been deposited has goofed up. TIN information is compiled out of what the banks with which tax deducted at source is deposited upload into the system and TDS certificates are issued by employers and others obliged to deduct tax at source. The peremptory message is in case of discrepancy between the two, the former would prevail. This was the first step in dethroning of TDS certificates through an administrative fiat without the backing of the Parliamentary approval. Going a step further, the tax administration now has exhorted the tax deductors not to issue Form 16/16A on the basis of their own accounting information, but on the basis of the TIN information. And this time round, the peremptory order is being flashed by the ticker in red appearing on its website. While the ticker might be construed as a belated

attempt to forestall and pre-empt the discrepancy between TIN and TDS certificates by aligning the two peremptorily, the bottom-line is effective marginalisation nay annihilation of the true worth of TDS certificates.

(Source: <http://beta.profit.ndtv.com/news>)

CBDT Plans 11 More Directorates for Tax Exemption Cases

To speed up clearances of tax exemption cases, the Central Board of Direct Taxes (CBDT) will set up 11 more specialised offices in the country. "CBDT plans to have directorate [exemptions] in all the states and to begin with, we will be setting up 10 to 11 new directorates," a revenue official said. However, the official did not specify any timeframe for creation of the specialised offices (directorates). Exemptions are given under the Income-tax Act, 1961, to encourage and fulfill certain social objectives relating to areas such as sports, charity, religion and education. The exemption wing of the Income Tax Department, headed by Director General of Income Tax (Exemptions), currently has seven directorates -- Kolkata, Ahmedabad, Bengaluru, Chennai, Delhi, Hyderabad and Mumbai. When the new directorates are operationalised, the number will increase to 18. The government also allows tax exemptions to various organisations engaged in activities like charity, religious activities and scientific research-related.

(Source: <http://www.hindustantimes.com>)

Government Likely to Roll Back Excise Duty on Branded Garments

In what would come as major relief to garment manufacturers, Centre may withdraw the mandatory 10 per cent excise duty on branded ready-made garments. The duty was imposed in the budget for this financial year on branded apparel sector that is pegged at ₹40,000 crore a year. "I am in the process of taking up the matter with finance ministry. I will write to finance minister by end of this month requesting him to consider the sectors demand for withdrawing 10 per cent mandatory excise duty on ready-made garments as it has led to reduction in retail domestic demand since April, 2011," Textiles Secretary Rita Menon said. Menon is confident that this mandatory excise duty would be withdrawn in next year's budget as it has led to a discernable slowdown in the apparel sector. She was speaking on the sidelines of 47th India International Garments Fair held by Apparel Export Promotion Council. Till now, ready-made garments and made-up textiles were under an optional excise duty regime wherein manufacturer was required to pay excise duty only if he wished to avail Cenvat credit. Over 90 per cent of apparel manufacturers are small and medium enterprises that were not availing Cenvat and, therefore, had never paid excise duty at the factory-level.

(Source: <http://www.indianexpress.com/>)

GST Regime Unlikely From April Next Fiscal; States Oppose Draft Bill

Introduction of indirect tax reforms through the common goods and services tax, or GST, from the next fiscal appears

uncertain with fresh opposition pouring in from BJP-ruled states who claim that it would reduce their status to that of municipalities and corporations. The draft bill for GST was introduced in the Lok Sabha in the last Budget session. It was the fourth draft prepared by the Centre after the first three were rejected by the states, citing autonomy issues. Among the objections raised is the proposal to bring the sales tax in ambit of the GST. The GST would subsume most of the indirect taxes like excise duty and service tax at the central level and VAT on the state front, besides local levies. The implementation of GST, considered to be a major tax reform, has been stuck for years due to differences between the Centre and some states over the new structure.

(Source: <http://www.business-standard.com/india/>)

SEBI Bid to Incentivise MF Sellers

Looking for ways to incentivise mutual fund (MF) distributors, SEBI is mulling to do away with sub-limits within the annual fees that asset management companies (AMCs) are allowed to charge from investors. Instead, the market regulator is weighing options of allowing a consolidated fee structure as per the limits already in place. At present, fund houses are allowed to charge 2.5 per cent annual fee for the first ₹100 crore of equity assets they manage, and this comes down by 25 basis points (100 basis points = 1 per cent) for every additional ₹300 crore assets under management (AUM) with the lower limit capped at 1.75 per cent. However, following SEBI's stand of not charging investors more in any case, the overall limit for annual charges or expenses would remain the same, SEBI sources said. At present, the annual expenses that AMCs charge have sub-limits under different heads like fund management charges, custodian fees, marketing expenses, etc. For example, the limit for annual fund management fee is 1.25 per cent for the first ₹100 crore worth of equity AUM, and 1 per cent for AUM above this limit. The market regulator is now evaluating options of doing away with all these sub-limits to settle for a consolidated fee structure as per the limits already in place, SEBI sources said. Top MF industry officials too said that they have been sounded out unofficially about such a move by the regulator but a final decision will be taken only after a detailed discussion within the SEBI board and industry players.

(Source: <http://www.economictimes.com>)

India Won't Expand FY12 Borrowing Plan, Says Finance Minister

The Indian government will not expand its 2011/12 borrowing programme, Finance Minister Pranab Mukherjee said recently. The government plans to borrow ₹4.17 trillion (\$93.2 billion) rupees in the current fiscal year, with 2.5 trillion scheduled between April and September. The Finance Minister also said the industrial output growth in May was "not encouraging". India's industrial output in May rose 5.6 percent, the slowest pace of growth in nine months, indicating taut monetary policy and high inflation were acting as brakes on the economy.

(Source: <http://timesofindia.indiatimes.com/>)

IFAC Releases Results of Recent SMP Quick Poll

In the second SMP Quick Poll, burden of regulation outpaced economic uncertainty as the most cited "biggest challenge" faced by practitioners' small- and medium-sized (SME) clients. Pace of regulatory change is the aspect of regulation that poses the greatest challenge for both small- and medium-sized practices (SMPs) and their SME clients. About one-quarter of respondents in the poll indicated that economic uncertainty is still the biggest challenge faced by SMEs. Similarly, when asked about the most important issue facing their practices right now, nearly half the respondents cited keeping up with regulations and standards (44 per cent), which was followed by attracting and retaining clients (26 per cent). The aspect of regulation that poses the greatest challenge for both small- and medium-sized practices (SMPs) and their SME clients is pace of change. Two questions were included to inform the work of the International Ethics Standards Board for Accountants (IESBA) SMP/SME Working Group, formed to address the challenges for SMPs and SMEs in complying with the IESBA *Code of Ethics for Professional Accountants*. Asked what guidance they would like to see added to the Code if it were to be expanded, the largest group of respondents said they would like to see additional ethical guidance on tax services; however, about one-third indicated that no further guidance is needed. Nearly 80 per cent of respondents said that case studies on how to apply the Code in specific typical scenarios would be useful or very useful. SMPs continue to generate the largest proportion of their revenue from traditional accountancy services, with nearly 90 per cent of practitioners citing audit and assurance or accounting and compilation as their main source of revenue.

(Source: <http://www.ifac.org>)

New Private Sector Task Force of Regulated Professions and Industries

On behalf of the Private Sector Taskforce of Regulated Professions and Industries, IFAC has submitted the interim report *Regulatory Convergence in Financial Professions and Industries* for consideration by the G20 deputies. This interim report comes ahead of the a final report in September 2011 and focuses on global regulatory convergence, which is a critical issue for capital markets and is a matter on which the private sector has expertise that can assist the G-20 in its objective to achieve a level playing field in relation to regulation, including standards, and to provide comparability and consistency for investors, regulators and market participants.

(Source: <http://www.ifac.org>)

IAESB Proposes Clarified Standard on Practical Experience Requirements for Aspiring Professional Accountants

The International Accounting Education Standards Board (IAESB) has released for public exposure a proposed revision of International Education Standard (IES) 5, *Practical Experience Requirements*. IES 5 currently prescribes the practical experience International Federation of Accountants (IFAC) member bodies should require before qualification as a professional accountant. In addition,

this IES can be helpful to educational organisations, employers, regulators, government authorities, and any other stakeholders who support the practical experience of professional accountants. The revision of IES 5 continues to support the use of practical experience in developing the competence of an aspiring professional accountant, but also proposes greater flexibility in measuring practical experience; permitting supervisors or mentors to direct an aspiring professional accountant's experience; and requiring practical experience to be recorded in a verifiable and consistent form. To access the exposure draft and submit a comment, visit the IAESB's website at www.ifac.org/Education/ExposureDrafts.php. Comments on the exposure draft are requested by 8th October, 2011.

(Source: <http://www.ifac.org>)

New Publication from ISACA and IFAC Helps Organisations Maximise the Value of XBRL

ISACA and the International Federation of Accountants (IFAC)'s Professional Accountants in Business (PAIB) Committee have jointly developed a paper, *Leveraging XBRL for Value in Organizations*, to provide guidance on how to leverage the value of eXtensible Business Reporting Language (XBRL) through effective implementation. XBRL is a universal language of business reporting that is increasingly being used for both external and internal reporting by organisations and is gaining traction worldwide. "Understanding how to embed XBRL within an organisation's information processes can enhance management communication, increasing the value of the information used within an enterprise," said Roger Debrecey, member of ISACA and co-developer of the XBRL paper. "ISACA collaborated with IFAC to develop this paper to provide accounting and assurance professionals with guidance they can rely on from trusted sources to leverage value from XBRL initiatives and compliance requirements." The paper can be downloaded free of charge from the ISACA (<http://www.isaca.org>) and IFAC web sites.

(Source: <http://www.isaca.org>)

Tax Havens Draw 1/3rd of Money Invested Abroad as Outbound Investment

Almost one-third of the money that is invested abroad from India as outbound investments have been in tax havens. Over 80 companies invested in countries like Mauritius, British Virgin Islands and Cyprus - popularly known for their liberal taxation regimes, where usually not many questions are asked about investments to and from these markets. Investments by Indian companies in overseas markets were over \$5 billion in June, according to a Reserve Bank of India release on overseas direct investment, which the central bank has put in public domain for the first time. However, much of these outflows (\$3.9 billion) are in the form of guaranteed issues. Outflows worth \$600 million are in equities and \$900 million is in the form of debt. Most of the investments are in wholly-owned subsidiaries and joint ventures. Put simply, a tax haven is a foreign country that has unique offerings for investors, the primary one being relatively low tax rates in comparison to other countries.

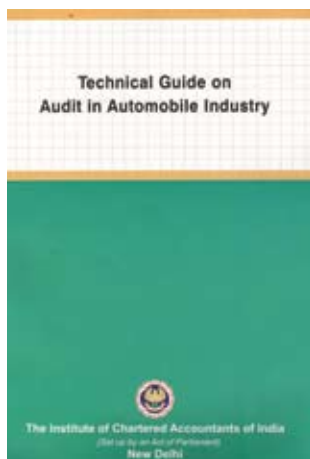
(Source: <http://www.economicstimes.com>)

New Publication from the Auditing and Assurance Standards Board

Technical Guide on Audit in Automobile Industry

Significant features of the Technical Guide are:

- The Guide is written in simple and easy to understand language.
- The Guide contains detailed guidance on various intricacies involved in audit of automobile companies.
- The Guide covers the important aspects of the automobile industry like industry overview, growth and background of the industry, the regulatory environment of the industry etc.
- The Guide comprehensively deals with special considerations relating to revenue, fixed assets, inventories, other assets, loans and advances, current liabilities and provisions, other income in the automobile industry.
- The Guide contains illustrative audit procedures for



various items of financial statements of automobile companies.

- The Guide has been authored by eminent experts in the field of audit in automobile industry.
- The Guide comes with a CD of the entire guide to provide ease of reference.

Price: ₹300/- (including CD)

Ordering Information

The Guide can be purchased directly from the Sales Counters at the ICAI's Regional Offices or at the Head Office. To order by post, please send a demand draft for the price of the publication (plus postage charges as per the desired mode of delivery) in favour of **"The Secretary, The Institute of Chartered Accountants of India, New Delhi"**, payable at New Delhi to the *Postal Sales Department, The Institute of Chartered Accountants of India, ICAI Bhawan, A-29, Sector-62, NOIDA – 201 309, Uttar Pradesh.*

Postal Charges:

Courier (within Delhi):	₹8/-
Courier (rest of India):	₹20/-
Registered Post (all over India):	₹36/-
Unregistered Post (all over India):	₹19/-

Committee on Public Finance and Government Accounting Invitation to Contribute Articles for E-Newsletter

The Committee on Public Finance & Government Accounting of The Institute of Chartered Accountants of India is regularly coming up with its E-Newsletter -'Prudence' featuring various articles on economic issues and measures on bi-monthly basis. The June-July 2011 issue of the E-Newsletter is available at the URL http://www.icai.org/new_post.html?post_id=3825&c_id=241

The Committee invites experts, researchers and writers to contribute articles in different areas of Public Finance and Government Accounting preferably on *Public Debt, Public Expenditure, Fiscal Policy, Monetary Policy, Accounting Reforms, Accrual Accounting, Accounting for Intangible Assets and Restructuring of Chart of Accounts in Accrual System in Public Sector* for publication in the August-September 2011 issue of its E-newsletter. If the article is published, a token honorarium of Rs. 2000/- per article shall be paid. Discretion of the Committee regarding publication /non-publication of the article shall be final and abiding therewith under copyright of the Committee. Material of this E-Newsletter may not

be reproduced, whether in part or in whole, without the consent of Editorial Board of Committee. Authors may only submit original work that has not been appeared elsewhere in any publication.

The articles (500 to 700 words) may be sent to us in the form of soft copy through mail/CD or in printed format through post giving details of the subject matter.

Those desirous may please contact at the following address:

The Secretary
Committee on Public Finance and Government Accounting
The Institute of Chartered Accountants of India
'ICAI Bhawan', A-29, Sector-62,
Noida- 201 309
Phone: 0120-3045950(O)
Email: cpf_ga@icai.org



ICAI- ROC

A MCA-21 Compliance software for Members in practice and 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 a MCA-21 Compliance Software namely ICAI-ROC, for members in practice and CA firms. ICAI-ROC software was launched on 1st July, 2011 by Honourable CA. K. Rahman Khan, Deputy Chairman of Rajya Sabha, Parliament of India.

Salient Features

The ICAI-ROC software provides a complete package to manage secretarial requirements & generates forms as per MCA21 Requirements. It provides the facility to prepare Auto filing of e-Forms, Shares Records/Certificates, Meetings and Minutes, Resolutions/Drafting, Annual Return forms and maintenance of Registers and Reports etc.

- Generates Forms as per MCA 21 Requirement
- Picks Up Data Directly From MCA Site
- Predrafted Resolutions
- Maintains Minute Book
- Calculation of Filing Fees
- Preparation of Memorandum and Articles
- Complete Shareholder Management
- Consolidation/Splitting of Share Certificates
- Share Certificate Printing
- Annual Return Preparation in Minutes
- Preparation of Statutory Registers
- Mortgage and Charges Management
- Manages Unlimited Companies

An Overview of the arrangement of ICAI-ROC

1. About the arrangement

- i) The ICAI-ROC will be provided initial license for free of cost for two years.

Description of the Software	Offer to Members in Practice & CA Firms
ICAI-ROC	Free

- ii) The license renewal charges will be Rs. 1,500/- after 30th September, 2013. Statutory taxes on License Renewal shall be extra as applicable.

2. Downloading the Software:

The ICAI-ROC Software may be downloaded free of cost from the website of Committee for Capacity Building of CA Firms and Small & Medium Practitioners, www.icaai.org.in on request by members.

3. Support on use of Software:

The MDA Softwares Ltd. will provide technical support to the users and renewed customers via Phone, Email and Remote PC access from the date of registering the license.

E-Mail: support@mdasoft.in

Phone No.-09621813973, 09621387418

Chairman

The Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI



www.icaai.org.in

A Exclusive Website for Members in practice and 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 launched its exclusive website www.icaai.org.in for members in practice and CA firms. The website www.icaai.org.in was launched on 1st July, 2011 by Honourable Shri R.P.N. Singh, Minister of State of Corporate Affairs, Government of India.

- **Creating Firm's Website:** In the website www.icaai.org.in, the Firms and Practitioners may create their websites as per the norms laid down by the Council of the Institute of Chartered Accountants of India. The website provides a platform for the CA Firms to upload their firms' details and gives them an opportunity to reach out to the members and CA firms

practicing worldwide.

- **Knowledge Resources:** The website has various downloadable software useful for office management and efficient documentation for the members and CA firms. The website includes e-library facility containing various Knowledge resources such as Guidance Notes, Accounting Standards, Publications, Expert Advisory Opinions etc. for easy reference by the practitioners. This will be helpful in enhancing the knowledge base of the members and CA Firms.
- **Code of Ethics:** The website also contains the Code of Ethics issued by the Council of the Institute of Chartered Accountants of India so that members may be aware of the ethical standards and ensure ethical compliance while rendering their services.
- **Minimum Recommended Scale of Fees:** The

website contains Minimum Recommended Scale of Fees for the Professional Assignments done by the Chartered Accountants, which is about the fee as per the work performed for various professional assignments and the amount quoted under respective heads of professional work for Metro and Non Metro cities separately.

- **Forum for Consolidation:** The website also acts as a forum for consolidation of the members and CA Firms by providing for consolidation measures like Networking, Merger and Corporate Form of Practice. The members may visit portals of other members and firms and like-minded persons may join hands to grow big to compete in the international front. The website also contains a Discussion Forum wherein the members may share their knowledge and experience

gained through their practice.

- **Discussion Forum:** The website also contains a Discussion Forum wherein the members may share their knowledge and experience gained through their practice.
- **Awareness through Website:** The Committee has initiated various measures to strengthen and enhance the portfolio of members and CA Firms and awareness on such measures is being created through this website so that the Practitioners may be benefitted by such endeavors of the Committee.

Chairman,
The Committee for Capacity Building of
CA Firms and Small & Medium Practitioners, ICAI

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ICAI- Tax Suite

A Tax Compliance software for Members in practice and 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 a Tax Compliance Software namely ICAI- Tax Suite for members in practice and CA firms. The ICAI- Tax Suite software was launched on 1st July, 2011 by Honourable CA. K. Rahman Khan, Deputy Chairman of Rajya Sabha, Parliament of India.

SALIENT FEATURES OF ICAI- TAX Suite

ICAI- Tax Suite is a comprehensive package that combines features of Income Tax, Audit Reports, Service Tax, e-TDS, e-AIR, CMA/Project Report, Form manager software and Document manager.

1. Physical ITR Forms (ITR 1 to ITR 7 Including Form Sahaj and Sugam (As per Department Print Specification) and Return Form BA (Wealth Tax)
2. XML File ITR 1 to ITR 6 according to schema provided by the Income Tax Department and Upload of XML File directly from Software without browsing Income Tax Portal manually
3. Computation of Total Income, thereof Tax and Computation Summary along-with comparison of previous assessment year
4. Option to manage the sequence of Set Off of current year losses and unabsorbed depreciation.
5. Tax details import from 26AS.
6. Import from excel is available for various inputs
7. Comparison of Financial Ratios of Current and Previous Assessment years
8. Tax Audit Reports, Company Audit reports, Trial Balance import from Tally, Busy and Excel.
9. Facility to prepare Quarterly, Annual TDS Returns, for form No. 24Q, 26Q, 27Q and 27EQ and correction returns also.

10. Generation of TDS Certificates Form 16/16A/27D.
11. Error locator in TDS.
12. Online TAN Registration, e-Payment, Challan verification and CSI File download.
13. Option to Import New Deductee entries in TDS correction returns.
14. Bulk TDS data Import from Excel /TDS /FVU file.
15. Generation of various MIS Reports for Income Tax and TDS Returns.
16. Preparation of Form ST-1, ST-3 and e-Filing of ST-1, ST-3, GAR 7 Challan & Online Payment and Refund Form R.
17. Enable Client wise documents management for easy listing, storing.
18. Preparation of CMA Project Report with relevant ratios.
19. Preparation of CMA data and calculation of MPBF as per Tandon and Nayak Committee.
20. Approximately 1000 Blank forms and filled forms with Circulars & Notification of Income Tax
21. Facility to Prepare Annual Information Return and e-Filing thereof (with correction statement).

Features of the arrangement

- **ICAI- Tax Suite to CA Members holding COP and Practicing Firms:** ICAI- Tax Suite will provide initial license free of cost with first two years activation for CA members holding COP and Practicing Firms as per the following table:

ICAI-Tax Suite	Income Tax/ Service Tax	Balance Sheet/ AIR	TDS
1 st Year Activation	A. Y. 2011-2012	F.Y. 2010-2011	A.Y. 2012-2013
2 nd Year Activation	A. Y. 2012-2013	F.Y. 2011-2012	A.Y. 2013-2014

- For activation of assessment year immediately next to initial free license, license renewal charges would be ₹ 2,100/-. Software capacity to accommodate 700 returns would be increased to 1000 returns for each assessment year/ financial year.

■ Downloading the software:

The software may be downloaded free of cost from the exclusive website of Committee for Capacity Building of CA Firms and Small & Medium Practitioners (<http://www.icai.org.in>)

■ Technical Support for software:

KDK Software(I) Pvt. Ltd. will provide the technical support to users and renewed customers via phone, email and remote PC access from the date of registering the license.

Phone: (0141) - 4123456,

Email: support@kdksoftware.com

Chairman
The Committee for Capacity Building of
CA Firms and Small & Medium Practitioners, ICAI



Campus Placement Programme for Newly Qualified Chartered Accountants – August-September 2011

The Committee for Members in Industry of the Institute organises Campus Placement Programme for newly qualified Chartered Accountants at various centres all over India. The scheme has been evolved to provide an opportunity both to employing organisations as well as the young professional aspirants to meet and explore the possibility of taking up positions in Industry.

Invitation to Organisations/CA Firms

Campus Placement Programme will be organised at various centres viz. Ahmedabad, Bangalore, Baroda, Bhubaneswar, Chandigarh, Chennai, Coimbatore, Ernakulam, Hyderabad, Indore, Jaipur, Kanpur, Kolkata, Mumbai, Nagpur, New Delhi and Pune.

The schedule of programme is given below.

S No.	Centre	Dates
1	Bangalore, Chennai, Hyderabad, Kolkata, Mumbai and New Delhi	16 th , 17 th , 18 th , 19 th and 20 th August, 2011
2	Bhubaneswar, Coimbatore and Ernakulam	1 st and 2 nd September, 2011

3	Baroda, Chandigarh, Indore, Kanpur and Nagpur	2 nd and 3 rd September, 2011
4	Ahmedabad and Jaipur	5 th , 6 th and 7 th September, 2011
5	Pune	9 th , 10 th and 12 th September 2011

The programme would be organised in the months of August-September 2011 for the candidates who would be passing in the CA Final examination held in May 2011 and also for others who are eligible.

Organisations intending to recruit Newly Qualified Chartered Accountants through the scheme are requested to get in touch with Secretary, Committee for Members in Industry, Indraprastha Marg, New Delhi-110002 and Tel. No. (011) 30110450/548 E-mail: placements@icai.org, mii@icai.org and campus@icai.org.

The complete details of the programme are hosted on www.icai.org and on www.cmii.icai.org.

Chairman
Committee for Members in Industry



CPE Study Circle for Members in Industry

The Committee for Members in Industry has formed three New CPE Study Circle for Members in Industry whose details are as follows:

Name of CPE Study Circle	Location
Vadodra CPE Study Circle	Ahmedabad

Power Sector CPE Study Circle	New Delhi
Worli Mumbai CPE Study Circle	Mumbai

In total, Committee has formed 44 CPE Study Circle for Members in Industry.





Invitation for Research Proposals

Research Committee invites applications for Research Projects from members and others for carrying out research in the field of accounting and other affiliated fields for e.g. accounting in health care industry, accounting for electricity generation and distribution companies, accounting in aviation industry, accounting for shipping companies, management control systems, approaches to social cost-benefit analysis in the Indian context, etc.

The Eligibility Criteria

- (a) The applicant must be a member of the Institute of Chartered Accountants of India with a research aptitude having at least 10 years of post-qualification experience either in the practice of the profession or as an employee with a reputed manufacturing/service organisation; or
- (b) The applicant must be holding a post-graduate degree from a recognised University or an institute of national repute and must have at least 10 years research and/or teaching experience;

Applications from persons having an experience less than as stated above may also be considered on the basis of merit.

The Evaluation Criteria

Only those research proposals will be accepted that result in formulation of guidance material in the form of Technical Guide, Studies, Monographs for the members of the Institute in accounting and allied areas, such as the following:

- the issues on which no accounting standards are available or
- the issues that may arise in the implementation of

accounting standards and other pronouncements in the industry-specific situations.

Duration

The duration of research project should not exceed three months from the date of the approval of the research proposal unless a longer period is otherwise justified.

Documents to be Submitted with the Research Proposal

The proposal should be accompanied by a

- Complete bio-data including experience in the relevant field of interest.
- Synopsis of the project explicitly specifying the objective, scope and issues that would be addressed in the final proposed document. It should also contain a justification for the proposal and the detailed chapter plan.

The proposal should also indicate the estimated expenditure and expected honorarium for this purpose. The amounts in this regard would be remitted on the final acceptance of the draft by the Research Committee.

Research proposals complete in all respects should be sent to the Secretary, Research Committee, at the following address:

The Institute of Chartered Accountants of India,
ICAI Bhawan, Post Box No.7100,
Indraprastha Marg,
New Delhi
E-mail: research@icai.org



Committee on Accounting Standards for Local Bodies

Comments Invited on Exposure Drafts of ASLB 8 'Construction Contracts'

The Committee on Accounting Standards for Local Bodies (CASLB) was constituted as a separate Committee in March, 2005 with the main objective of formulating Accounting Standards for Local Bodies (ASLBs). Moving forward in this direction, the Committee has finalised the Exposure Draft of one ASLBs namely ASLB 8 on 'Construction Contracts'.

ASLB 8 prescribes the accounting treatment of costs and revenue associated with construction contracts. The Standard also identifies the arrangements that are to be classified as construction contracts, provides guidance on the types of construction contracts that can arise in the

local bodies and specifies the basis for recognition and disclosure of contract expenses and, if relevant, contract revenues.

Comments are invited on the Exposure Drafts of the above ASLBs. The text of the Exposure Drafts is available on the website of ICAI i.e. www.icai.org. Comments should be submitted in writing to the Secretary, Committee on Accounting Standards for Local Bodies, The Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi – 110 002, so as to be received not later than **31st August, 2011**. Comments can also be sent by e-mail at caslb@icai.org or tdte@icai.org

Certificate Course on Master in Business Finance

Shape your career in the highly coveted field of Finance

The Committee on Management Accounting (CMA) of ICAI, in the year 2009 launched Master in Business Finance Certificate Course (MBF) at Delhi and Mumbai. Designed to sharpen the competitive edge and acumen of our members with the well researched course curriculum, the course is expected to satiate the members' quest to undertake an MBA or equivalent program. 1st Batch saw an overwhelming response and the 2nd Batch is now commenced.

Course coverage is extensively wide across various topics and tools of advanced financial management viz. Financial Planning & Analysis, Fund Raising, Structuring & International Finance, Financial Markets & Portfolio Management, Forex, Treasury & Risk Management, Valuations, Acquisitions and Risk Analysis, Banking & Trade Finance, with an aim to provide knowledge and skills required for tomorrow's CFO and high end consultancy in finance. The course has the mission to empower our members for the global economy with special emphasis on Indian Market.

Eligibility

The Course is open only to the Members and the Students of the Institute who have passed the CA Final Examination.

Course Duration and Course Hours

Course has a planned duration of little less than one year. Classes will be held in Delhi and Mumbai on alternate (2nd & 4th) Saturdays (2 PM to 8 PM) and Sundays (9 AM to 2 PM).

Faculty

The participants shall have the privilege to interact with best faculty from IIM's, XLRI, MDI, Management Schools of IIT's, Public and Private Sector Banks, Financial Institution, Mutual Funds, ICRA, SIDBI, SEBI, Leaders of the profession and eminent academicians. The committee is exploring possibility to invite faculty from Harvard Business School, Boston and Stern School of Business, New York.

Two Weeks Full Time Residential Programme at COE-HYD

A unique feature of the programme is an inbuilt module

of residential training to provide the participants an opportunity to apply their acquired knowledge in the real life situations. Mandatory participation in 100 hours of dedicated training at ICAI Centre of Excellence, Hyderabad, a residential campus with 3 Star facilities and 24X7 access to eminent faculty, intense brainstorming and projects under expert guidance.

Fee Structure

(a) Prospectus:

₹100 (Rupees One Hundred only) (Not chargeable for the prospectus and from downloaded from the website).

(b) Registration Fee:

Course Registration Fee: ₹30000
(Tea with Snacks will be provided)

Residential Program Fee: ₹20000

(For Two Modules of One Week each. Includes cost of boarding and lodging at ICAI Center of Excellence at Hyderabad. Participants shall make their own arrangements to travel.

(c) 100 CPE HOURS CREDIT.

(d) Well equipped IT enabled library with access to research publications and online data bases. (Open during the class days at ICAI Bhavan, Delhi & Mumbai as well as at COE, HYD).

National Course Director (Dean):

CA. Vinod Jain, FCA
Central Council Member
Mobile No. 9811040004
Email: vinodjainca@gmail.com

Course Coordinator:

Shri A. P. Kar,
Sr. Joint Director of Studies
Mobile No. 09873254833
Email: cma@icai.in, ap.kar@icai.org

Course registration form is available at the following link:

<http://220.227.161.86/22151anno un12514form.pdf>

(Registration for the current year i.e. 2011-12 is closed)

Course Contents are available at the following link:

<http://220.227.161.86/22506 announ12851.pdf>

Committee on Management Accounting The Institute of Chartered Accountants of India



ATTENTION DEPOSITORS OF NBFCs

- Before depositing your money with NBFC, please ensure that the NBFC is registered with Reserve Bank of India as deposit taking company.
- The NBFC whose application for Certificate of Registration has been rejected or cancelled by the Reserve Bank of India can neither accept fresh deposit nor renew existing deposit.®
- The issuance of Certificate of Registration to NBFC by the Reserve Bank of India merely authorises it to conduct the business of NBFC. The repayment of principal amount of deposits or interest thereon is neither guaranteed by RBI nor insured by any official agency.
- Except Equipment Leasing, Hire Purchase Company or Residuary Non Banking Company the NBFC which accepts deposits should have minimum investment grade credit rating granted by an approved credit rating agency for deposit mobilisation programme.
- NBFC cannot
 - o Offer interest at a rate more than the rate prescribed by Reserve Bank of India, which is at present 12 per cent to 5 per cent per annum (on domestic deposits only).
 - o Offer any gift/incentives to solicit the deposit from public.
 - o Accept deposit for a period less than 12 months and more than 60 months.
- Unincorporated bodies, such as individuals, proprietary and partnership firms engaged in the business of loans and advances, leasing and hire purchase cannot accept deposits from public.
- A deposit can be accepted by NBFC* only against issuance of proper receipt bearing name of the company and signed by an authorised official stating the date of deposit, the name of the depositor, the amount in words and figures received by the company by way of deposit, the rate of interest payable thereon and the date of repayment of deposit.
- If a deposit taking NBFC* fails to repay the deposits or interest accrued thereon, the aggrieved depositor can approach the following agencies for the redressal of his grievances:
 - o Consumer Dispute Redressal Forum at district level, or
 - o Regional Bench of the Company Law Board.
- Deposit mobilisation schemes of companies engaged in other activities such as plantation, commodities trading, manufacturing, housing finance, Multi-level marketing companies, nidhis (mutual benefit financial companies) and potential nidhis (mutual benefit company) and companies engaged in collective investment schemes, etc. do not come under the regulatory purview of the Reserve Bank of India.

Issued in Public Interest by
RESERVE BANK OF INDIA
www.rbi.org.in

Notes:

®The list of companies whose application for Certificate of Registration has been cancelled by the Reserve Bank of India is published in Newspapers and available on RBI's website www.rbi.org.in.

*NBFC include a loan company, an investment company, hirepurchase company, an equipment leasing company and Residuary non banking companies.



Invitation of Comments on Draft Policy on Plagiarism

Plagiarism is an intellectual crime that is considered worldwide as violation and infringement of intellectual property rights of others. We have also noticed the growing incidences of such plagiarized submissions for consideration of their publication in our journal. Such cases will be strictly dealt with as they also damage the reputation of our Journal. We are sure our readers will without a doubt agree to this.

We have, therefore, drafted a policy on this issue and the same has been hosted on the ICAI website www.icaai.org.

www.icaai.org for consideration of our readers. You as our valuable readers are requested to go through the draft Policy as hosted on the website and submit your comments by e-mail to eboard@icaai.org or by post at 'The Secretary, Editorial Board, ICAI Bhawan, A-29, Sector 62, Noida – 201309 (U.P.) for consideration of the Editorial Board. The last date for submission of comments is **31st August, 2011**.

----- The Editor

CPE

12

Hours

ALL INDIA CONFERENCE – 2011

On Charter of Chartered Accountants Independency | Transparency | Accountability

On 5th and 6th August, 2011 at Hotel Mayfair Convention, Bhubaneswar**Organised by:** Continuing Professional Education Committee of ICAI**Hosted by:** Bhubaneswar Branch of EIRC of ICAI**Day One: 5th August, 2011 (Friday)****Inaugural Session: 10.00 a.m to 11.00 a.m**

Chief Guest : Sh. Naveen Patnaik, Honourable Chief Minister, Orissa

Guest of Honour : Sh. Prafulla Chandra Ghadai, Honourable Minister Finance & Public Enterprises, Orissa

Distinguished Guest : CA. G. Ramaswamy, President, ICAI

Technical Session I

(11.15 a.m to 12.45 p.m)

Corporate Frauds and Governance

Learning from Satyam Experience

Chairman: CA. B.L.Bagra, Chairman-cum-Managing Director, NALCO

Speaker: CA T. N. Manoharan, Padmashree Awardee, Past

President, ICAI

Technical Session II

(12.45 p.m to 02.15 p.m)

Recent Issues in Income Tax

Chairman and Speaker: CA. Ved Jain, Past President, ICAI

Speaker: CA. Arun Kumar Sabat, Bhubaneswar

Technical Session III

(2.45 p.m to 4.15 p.m)

Journey from Financial Reporting to Business Reporting

Chairman and Speaker: CA. S. Santhakrishnan, Council

Member, ICAI

Speaker : CA. P.R.Ramesh

Technical Session IV

(4.30 p.m to 6.00 p.m)

Auditing and Assurance Standards – Contemporary Issues

Chairman and Speaker: CA. Amarjit Chopra, Past President, ICAI

Speaker: CA. Abhijit Bandyopadhyay, Council Member, ICAI

Two: 6th August, 2011, (Saturday)**Technical Session V**

(10.00 a.m to 11.30 a.m)

Enterprise Risk Management and Internal Audit - Connecting the dots.

Chairman: CA. Subodh Kumar Agarwal, Council Member, ICAI

Speaker: CA. Richard Rekhy

Technical Session VI

(11.30 a.m to 01.00 p.m)

- Show Cause Notice and Adjudication Proceedings under Service Tax

- Intricate Issues in Construction of Residential and Industrial Complexes

Chairman and Speaker: CA. Madhukar N. Hiregange, Council

Member, ICAI

Speaker: CA. V. Sridharan, Lawyer, Supreme Court

Technical Session VII

(02.00 p.m to 03.30 p.m)

CA Practice as an LLP Entity

Speaker: CA. Kamlesh Shivji Vikamsey, Past President, ICAI

Technical Session VIII

(3.00 p.m to 4.00 p.m)

RTI – A Tool to good governance

Chairman: Sri Satyananda Mishra, IAS, Chief Information

Commissioner of India

Speaker: Sri. Taruna Kanti Mishra, IAS, State Chief Information

Commissioner of Orissa

Session on Motivation

(4.00 p.m to 5.00p.m)

Eternal Values in a Changing Society

CA. C. Suresh, Hyderabad

Participation Fees:

Member: ₹2,000/-; Non Member: ₹3,000/- ; Corporate Delegate ₹3,000/-

Seminar Co-ordinators

CA. B. Manoj Kumar Patro

Chairman

Bhubaneswar Branch of EIRC of ICAI

CA. Sumantra Guha

Chairman

CPE Committee, ICAI

Conference Secretariat:

Shri N.K. Bansal

Secretary, CPE Committee

For Registration and further Details, please contact

Bhubaneswar Branch of EIRC of ICAI, ICAI BHAWAN, A-122/1 Nayapalli, Bhubaneswar - 751 012 Orissa.

Phone: 0674-2392391/9861154954/9938014630; Email: bhubaneswar@icai.org; manoj.patro@gmail.com

CPE

12

Hours

Three Days National Residential Seminar on Service Tax

on 12th, 13th and 14th August, 2011 at Uday Samudra Leisure Beach Hotel and Spa, Thiruvananthapuram

Organised by: Continuing Professional Education Committee of ICAI

Hosted by: Trivandrum Branch of SIRC of ICAI

Sessions Details	
Friday, 12 th August, 2011	
Arrival at Thiruvananthapuram 12.00 noon and Inauguration Session 02.30 p.m. to 3.30 p.m. Technical Session I 4 p.m to 6 p.m - Introduction, Levy, Reverse Charge, Framework of Section 65, Classification and Registration. - CA. Divya C. V., ACA, Chennai	
Saturday, 13 th August, 2011	
Technical Session II [10 am to 11.30 am] - Valuation and Valuation Rules - CA. Ashok Batra , FCA, New Delhi Technical Session III [11.45 am to 1.15 Noon] - Rules Relating to Raising an Invoice Payment of Tax and Filing of Returns - CA. Bharath Kumar N. K. , ACA, Chennai Technical Session IV [2.00 p.m to 3.30 p.m] - Interpretation Issues and Export and Import of Services - CA. Ravindra Holani , FCA, Gwalior Technical Session V [3.45 p.m to 5.15 p.m] - Exemptions, Interest and Penalties - CA. Prasanna Krishnan , FCA, Chennai	
Sunday, 14 th August, 2011	
Technical Session VI [9.15 am to 11.15 am] - Show Cause Notice, Reply to SCN, Handling Audit Queries and Appellate Remedies - CA. Rajendra Kumar P. , FCA, Chennai Technical Session VII [11.30 am to 1.30 Noon] - Open House – Questions and Answers on All Taxable Services - CA. Rajendra Kumar P., CA. Bharath Kumar N. K. and CA. Divya C. V.	
Participation Fee:	
Residential (Including accommodation, breakfast, lunch, dinner and course material) Members (on twin sharing basis) - ₹7000/- per participant Non-Members (on twin sharing basis) - ₹7500/- per participant	Non Residential (Including lunch and dinner) Members - ₹3000/- per participant Non-Members - ₹3500/- per participant
Delegate fee by way of Cheque/DD drawn in favour of 'Trivandrum Branch of SIRC of ICAI' payable at Thiruvananthapuram shall be sent to Chairman, Trivandrum Branch of SIRC of ICAI, ICAI Bhawan, P.B. No.416, T.C. 41/401, Pound Road, Thycaud, Thiruvananthapuram – 695014. Phone: 0471-2323789; 2328590 - Email: trivandrum@icai.org	
Seminar Co-ordinators	
CA. Rajendra Kumar P. Central Council Member, ICAI	CA. Sumantra Guha, Chairman, CPE Committee, ICAI
For Registration & further Details, please contact:	
Trivandrum Branch of SIRC of ICAI, ICAI Bhawan, P.B. No.416, T.C. 41/401, Pound Road, Thycaud, Thiruvananthapuram – 695014. Phone: 0471-2323789; 2328590, Email: trivandrum@icai.org	

CPE

6

Hours

NATIONAL TAX WORKSHOP

On 10th August (Wednesday), 2011 (9:45 am to 5:45 pm) at "The Hotel Jehannuma Palace ", Bhopal

Organised by: Direct Taxes Committee of ICAI

Hosted by : Bhopal branch of CIRC of ICAI

Topics to be Discussed	Speakers
1. Taxation of Real estate Transactions including valuation under Section 50C & 55A of the Income-tax Act, 1961. - CA. Jayant P. Gokhle, Mumbai	
2. Recent Amendments on Service Tax & Input Credit - CA. Rajendra Kumar P. , Chennai	
3. M.P. Entertainment & Luxury Tax Act - CA. P.D. Nagar	
4. Deemed Dividend analysis under Section 2(22)(e) of the IT Act and Issues in TDS -Dr. (CA.) Girish Ahuja	
Fees	Members: ₹750/- ; Students: ₹600/-, Non-Members: ₹900/- Cheque/DD to be drawn in favour of "ICAI Bhopal Branch" payable at Bhopal.
Contact Persons and Contact Details	
Workshop Chairman CA. Sanjay K. Agarwal, Chairman Direct Taxes Committee, ICAI	Programme Co-ordinator CA. Manoj Fadnis, Chairman Accounting Standard Board, ICAI
For Registration & further details, please contact	
Bhopal Branch of CIRC of ICAI, 148, Zone - II, M.P.Nagar, Bhopal - 462011. Phone: 0755-2558066; Fax: 0755-2571850; E-Mail: bhopal@icai.org	

CPE

15

Hours

Workshop on Service Tax

(Weekly Evening programme)

Organised by: Committee for Capacity Building of CA Firms and Small & Medium Practitioners**Hosted by:** SIRC of ICAI

Date and Time		Venue
01-10-2011, 08-10-2011, 16-10-2011, 30-10-2011 and 05-11-2011 4.00 p.m. to 7.30 p.m.		P. Brahmayya Memorial Hall ICAI Bhawan, No.122 Mahatma Gandhi Road, Nungambakkam, Chennai - 600034
Theme		
With advent of globalisation and challenges posed by the liberalisation 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 popularising 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 Workshop will concentrate on issues related to Service Tax for enrichment of the Member's Knowledge Base.		
3.30 p.m. to 4.30 p.m. 1 st October, 2011(Saturday)	Registration of Participants and Inaugural Session	
First Session 4:30 p.m. to 7:30 p.m. 1 st October, 2011(Saturday)	Point of Taxation Rules – An Analysis CA. Rajendra Kumar P, Central Council Member, ICAI	
Second Session 4:30 p.m. to 7:30 p.m. 8 th October, 2011(Saturday)	Service Tax and CENVAT Credit Rules – A Study CA. Ashok Batra	
Third Session 4:30 p.m. to 7:30 p.m. 16 th October, 2011(Sunday)	Reading, Drafting of Reply and Adjudication of Show Cause Notice CA. Naveen Raj Purohit	
Fourth Session 4:30 p.m. to 7:30 p.m. 30 th October, 2011(Sunday)	A detailed Study of Service Tax Rules, 1994, Valuation Rules and Rules relating to Works Contract CA. PL. Subramanian	
Fifth Session 4:30 p.m. to 7:30 p.m. 5 th November, 2011(Saturday)	Drafting, Preparation and Filing of Appeals before Commissioner Appeals and CESTAT Dr. Sanjiv Agarwal	
Registration Fees		
DELEGATE FEE	For Entire Course	For Day-wise Regn.
Members	₹ 1,500/-	₹ 350/-
ARS Members	₹ 750/-	₹ 150/-
Non Members	₹ 1,800/-	₹ 400/-
Delegate fee by way of Cheque/DD drawn in favour of 'SIRC of ICAI' payable at Chennai shall be sent to SIRC of ICAI, ICAI Bhawan, No.122, Mahatma Gandhi Road, Nungambakkam, Chennai – 600034. Phone: 044-30210320; Email: sirc@icai.in		
Limited Seats, Registration on First Come First Serve Basis. Advance confirmation of registration is required.		
Programme Director	Programme Co-ordinators	
CA. Vijay K. Garg Chairman, Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI Email: chairman.ccbcaf@icai.org Phone: 094140 41872	CA. Rajendra Kumar P Central Council Member ICAI Phone: 094440 17087	CA. K. Shanmukha Sundaram Chairman SIRC of ICAI Phone: 094433 49727
For further details, please contact: SIRC of ICAI, sirc@icai.in, Phone: 044-30210320 Secretary, CCBCAF & SMP, ICAI, New Delhi, ccbcaf@icai.org, Phone : 011-30110561		

CPE

6

Hours

Workshop on Internal Audit of Labour Lawson 20th August, 2011 (Saturday) at Hotel Orchid, Mumbai**Organised by:** Internal Audit Standards Board of ICAI**Hosted by:** Western India Regional Council of ICAI

Registration, Inaugural Session and Welcome Speech	9:30 a.m. to 11:00 a.m.
Technical Session I	Overview of Labour Laws
Technical Session II	Compliance of Laws related to Social Security and Workmen's Compensation

Technical Session III	Compliance of Laws relating to the Trade Unions
Technical Session IV	Professional Opportunities for Chartered Accountants in Internal Audit of Compliance of Labour Laws
Delegate Fees : ₹1,250/- per Members ₹1,750/- per Non – Members	
(D.D./Pay Order/Cheque should be drawn in the favour of “WIRC of ICAI”, payable at Mumbai. Please mention your name, membership number and contact details at the back of the cheque/demand draft.)	
Registration on First Come , First Serve Basis.	
Seminar Director CA. Rajendra Kumar P. Vice-Chairman, Internal Audit Standards Board Phone:0120-3045 949, 9382303403 Email:cia@icai.org;	Registration on First Come , First Serve Basis. CA. Nilesh S. Vikamsey Central Council Members and Member of Internal Audit Standards Board Phone:0120-3045 949, 9323332552 Email:auditing@icai.org CA. Shriniwas Y. Joshi, Chairman WIRC of ICAI Phone:91-22-39802902, 9821096079 Email:wirc@icai.in; wirc@icai.org

CPE

12

Hours

Training Programme on “An insight on the concepts applicable to Autonomous Bodies”

Organised by: Committee on Public Finance & Government Accounting

Date	Venue
18 th and 19 th August 2011 (Thursday & Friday)	The Institute of Chartered Accountants of India, ICAI Bhawan, A-29, Sector 62, Noida - 201 309
Theme With ever increasing outlays of the Government and changes and complexities introduced in the system of public service delivery, the task of audit has become not only more extensive but also more onerous. This Training Programme is primarily intended for enhancing the quality of financial reporting in Autonomous Bodies and to help the organizations to prepare their financial statements within the stipulated time.	
Day 1-Thursday, 18th August 2011	
9.00 a.m. to 11.00 a.m.	Registration of Participants and Inaugural Session
Technical Session I 11.15 a.m. to 12:45 p.m.	Basic principles of Accounts such as principle of accrual accounting, dual concept, going concern concept and consistency concept
Technical Session II 1:45 p.m. to 3:15 p.m.	Uniform Format Linked with accrual basis, dual concept, going concern concept and consistency concept
Technical Session III 3:30 p.m. to 5:00 p.m.	Uniform Format Linked with accrual basis, dual concept, going concern concept and consistency concept
Day 2-Friday, 19th August 2011	
Technical Session I 9.30 a.m. to 11.00 a.m.	Internal Control
Technical Session II 11.15 a.m. to 12:45 p.m.	Practical Problems related to preparation of annual accounts of Autonomous Bodies
Technical Session III 1:45 p.m. to 3:15 p.m.	Accounting Standards – An overview – AS 1, 4,5,10,6
Technical Session IV 3:30 p.m. to 5:00 p.m.	Accounting Standards: 9, 12, 13, 15, 21, 29 and Introduction of IFRS
Registration Fees: ₹1500/- per Participant DD/Pay order/Cheque should be drawn in favour of ‘Secretary ICAI’ payable at New Delhi and sent to Secretary, Committee on Public Finance & Government Accounting, ICAI Bhawan, A-29, Sector-62, Noida-201 309. Please mention your name, membership number and contact details at the back of the cheque/demand draft.	
Registration on First Come, First Serve Basis.	
Programme Chairman CA. Anuj Goyal, Chairman Committee on Public Finance & Government Accounting, ICAI	Programme Coordinator CA. Shalini Jindal Secretary, Committee on Public Finance & Government Accounting, ICAI
For Registration and further Details, please contact Secretary, Committee on Public Finance & Government Accounting, Phone: (0120) 3045950, 3045968, E-mail: cpf_ga@icai.org, Website: www.icai.org	

CPE

15

Hours

NATIONAL RRC ON**CA Profession towards excellence through Capacity Building**On 11th, 12th and 13th November 2011 at Shree Balaji Seva Sadan, Salasar, Churu(Rajasthan)**Organised by:** Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI**Hosted by:** Jaipur Branch of CIRC of ICAI

Day 1: 11 th November, 2011		
12 p.m. to 2.30 p.m.	Registration and Inaugural Session	
Chief Guest Shri Namo Narain Meena, Union Minister of State of Finance		
Session Chairman CA. Jaydeep N Shah, Vice President, ICAI		
Session- I 2.30 p.m. to 4.30 p.m.	Critical issues in Direct Taxes Session Chairman : CA. S. C. Jain	
	Practical Issues in Income Tax	Dr. Girish Ahuja
	Taxation and accounting in Real estate transactions	CA. Vijay Goyal
Session-II 4.45 p.m. to 6.45 p.m.	Panel Discussion on New Challenges in CA Profession Session Chairman : CA. Amarjit Chopra, Past President , ICAI	
	• CA. Satish Gupta • CA. Ravi Raniwala • CA. Prakash Sharma • CA. Sudhir Bhansali	
Day 2: 12th November, 2011		
Session-III 8.00 a.m to 10.00 a.m	Critical issues in Indirect Taxes Chairman: CA. Ravindra Holani, Council Member, ICAI	
	Practical issues in service tax	CA. Ashok Batra
	Critical Issues in Rajasthan VAT	Shri K B Gupta
Session-IV 10.15 a.m. to 12.15 p.m.	Panel Discussion on Audit Documentations for SMPs Chairman: CA. Rajkumar S. Adukia, Central Council Member, ICAI	
	• CA. K L Jhanwar • CA. Shyam Lal Agarwal • CA. Pawan Goel, Past Chairman CIRC	
Session-V 12.30 p.m. to 2.00 p.m.	Panel Discussion on Profession with Ethics Chairman: CA. Subodh Kumar Agrawal, Chairman, ESB, ICAI	
	• CA. Devaraja Reddy M, Central Council Member, ICAI • Special Address by CA. S S Bhandari, Past Council Member, ICAI • CA. Vimal Chopra, Past Chairman, CIRC	
Day 3: 13th November, 2011		
Session-VI 8.00 a.m. to 11.00 a.m.	Office Management & Corporate form of Practice Chairman: CA. Sanjeev Maheshwari, Central Council Member, ICAI	
	Office Management	CA. Nilesh S. Vikamsey, Central Council Member, ICAI
	Corporate form of Practice	CA. Atul C. Bheda, Vice-Chairman, CCBCAF & SMP, ICAI
Session-VII 11.15 a.m. to 1.45 p.m.	Capacity Building through IT Tools Chairman: CA. Atul C. Bheda, Vice-Chairman, CCBCAF & SMP, ICAI	
	K-Doc & e-Sec	CA. B C Chechani
	ICAI- ROC	CA. Manu Agarwal
	ICAI-Tax Suite	CA. Kapil Goyal
Open House and Valedictory Session 1.50 p.m. To 2.30 p.m.	Chief Guest Shri Rajendra Pareek, Cabinet Minister-Industry, Government of Rajasthan	
	Session Chairman CA. Vijay Kumar Garg, Chairman, CCBCAF & SMP, ICAI	
Registration Fees Particulars	With Accommodation in Rupees	Without Accommodation In Rupees
FCA	3000	2500
ACA	2800	2300
Accompanying Person	1800	1300
Child(3-12 Yr)	1200	700
Child(above 12 Yr)	1800	1300

Note

- Payment may be made by Cheque/Demand Draft in favour of Jaipur Branch of CIRC of ICAI & Should be sent to-Jaipur Branch of ICAI, The Institute of Chartered Accountants of India, ICAI Bhawan, D-1, Jhalana Institutional Area, JLN Marg, Jaipur-302004
- All room are having AC Facility and available on twin sharing basis.
- **Special Attraction:**
 - a) Special Darshan Salasar Balaji(Churu), Rani Sakti Dadi Mandir(Jhuujhunu),Khatu Shyam ji (Sikar), Reengus Bheru Ji
 - b) Bhajan Sandhya and Shekhawati folk Dance
 - c) Pick up & Drop facility from Jaipur (Pickup on 11-11-2011 at 7.00AM from ICAI Jaipur Branch and Drop on 13-11-2011 at 8.00 PM at Jaipur)
- Limited Seats, Registration on First Come First Serve Basis.

Programme Chairman

CA. Vijay Kumar Garg, Chairman
Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI
Email: chairman.ccbcaf@icai.org
Phone: 9414041872 (M)

Programme Convenor

CA. Rakesh Jhalani
Chairman
Jaipur Branch of CIRC of ICAI
Email: rrc.salasarbalaji@icai.org, jaipur@icai.org
Phone:09829064513

For Registration & Information, contact details:

CA. C. L. Yadav, Past Chairman, Jaipur Branch of CIRC of ICAI, Email: clyadav1@yahoo.com, Phone:09829291148
CA. Sunil Mor, Email: mor_sk@yahoo.com, Phone:09414039265

CPE**12****Hours****Two Days Training Workshop on “Revised Schedule VI and XBRL”**

On 3rd & 4th September, 2011 (Saturday & Sunday) at P. Brahmayya Memorial Hall ICAI Bhawan, No.122, Mahatma Gandhi Road, Nungambakkam, Chennai - 600034

Organised by: Continuing Professional Education Committee of ICAI

Hosted by: SIRC of ICAI

Day-1 – Saturday – 03.09.2011 Inaugural Session – 09.30 a.m. to 10.00 a.m. Technical Sessions–1 – 10.30 a.m. to 12.00 noon Highlights of Revised Schedule VI CA. N.R. Govindarajan, Chennai	Technical Sessions–2 – 12.00 noon to 01.30 a.m. Issues in Revised Schedule VI CA. R.G. Rajan, Chennai Technical Sessions–3 – 02.15 a.m. to 05.30 p.m. An overview on XBRL • What is XBRL • XML/XBRL Basic Concepts • Advantages of XBRL • Global XBRL Initiatives CA. Atul Chunilal Bheda, Mumbai
Day-2 – Sunday – 04.09.2011 Technical Sessions–1 – 10.00 a.m. to 11.30 noon • XBRL and ICAI initiatives CA. S. Santhanakrishnan, Chennai Technical Sessions–2 – 11.45 a.m. to 01.15 p.m. XBRL Taxonomies • Structure of taxonomies • Indian GAAP Taxonomy • Attributes/Characteristics of Elements • Dimensions • Tagging CA. P. Selva Moorthy, Chennai	Technical Sessions–3 – 02.00 p.m. to 03.30 p.m. Instance documents - Concept & Practice • Creation of instance documents • XBRL Instance Validation and Viewing • MCA 21 and IFRS perspective CA. R Vittal Raj, Chennai Technical Sessions–4 – 03.45 p.m. to 05.15 p.m. XBRL Tool • Overview of XBRL Generation Process • Taxonomy Editing and Extensions CA. S.D. Packiaraj, Madurai
DELEGATE FEE Members – ₹ 1500/-; ARS Members -₹ 500/-; Non Members –₹ 1800/- Delegate fee by way of Cash/Cheque/DD drawn in favour of ‘SIRC of ICAI’ payable at Chennai shall be sent to SIRC of ICAI, ICAI Bhawan, No.122, Mahatma Gandhi Road, Nungambakkam, Chennai – 600034. Phone: 044-30210320; Email: sirc@icai.in	
Programme Director CA. Sumantra Guha Chairman CPE Committee, ICAI Phone:098310 15331	Programme Co-ordinators CA. Rajendra Kumar P Member CPE Committee, ICAI Phone: 094440 17087 CA. K. Shanmukha Sundaram Chairman SIRC of ICAI Phone: 094433 49727

Advertisement

CPE

6

Hours

Workshop on CARO & TaxationOn Saturday, 20th August, 2011 at ICAI Bhawan, Indore**Organised by:** Continuing Professional Educational Committee**Hosted by:** Indore Branch of CIRC of ICAI

Particulars	Topic
Knowledge Sharing Session I 10.00am to 1.00pm	Issues in CARO CA. Nilesh S. Vikamsey , Central Council Member of ICAI Drafting Notes to Accounts and Qualifications in Auditors CA. Aseem Trivedi
Knowledge Sharing Session II 2.00pm to 5.00pm	International Taxation An Overview CA. Mahesh P. Sarda Central Council Member of ICAI Taxation of Charitable and Educational Institutions CA. N K Poddar, Senior Advocate, Kolkatta Chairman of Session An eminent CA from Indore
Registration Fee : ₹ 600/- Cheque/DD should be drawn in favour of "INDORE BRANCH OF CIRC OF ICAI)	
Programme Chairman CA. Sumantra Guha, Chairman, Continuing Professional Education Committee of ICAI\	Programme Director CA. Manoj Fadnis, Central Council Member, Indore
Programme Co-ordinator CA. Vikas Jain, Chairman, Indore Branch Mobile No. 09300099960	
For Registration & further Details, please contact	INDORE BRANCH OF CIRC OF ICAI ICAI Bhawan Plot no 19-B, Scheme no 78 Near Madhya Pradesh Pollution Board Indore-452010 (India) Telephone Board +91 731 3254900, 4298198

CPE

12

Hours

National Conference on Taxation**Organised by:** Direct Taxes Committee, ICAI**Hosted by:** Eastern India Regional Council of ICAI

Date & Time	Venue
19 th and 20 th August, 2011 (9.30 am to 5.30 pm), Friday and Saturday	"Royal Bengal Room", Block-DC, Sector – I, Citi Centre, Salt Lake, Kolkata
Day-1 - International Taxation & Provisions of GAAR - Taxability of capital receipts with special reference to Section 56 and Cash Credit under Section 68 - Tax deduction for outward remittances under Section 195 of Income-tax Act, 1961 - Taxation of real estate transactions including Valuation under Section 50C & 55A of the Income-tax act, 1961	Day-1 - Contemporary issues in Business Deductions including impact of Sec 14A, Section 94(7) and Deemed Dividend analysis under Section 2(22)(e) of the Income-tax Act, 1961. - Precautions in preparation and filing of Tax Returns & Assessment Proceedings - Service Tax: Point of Taxation Rules 2011 - BRAIN TRUST on - Direct Taxes - Indirect Taxes
Fees Members: ₹1,500/-; Students: ₹1,000/-; Cheque/DD should be payable at Kolkata and drawn in favour of "The Institute of Chartered Accountants of India, EIRC".	
Conference Chairman CA. Sanjay K. Agarwal, Chairman, Direct Taxes Committee of ICAI Phone: 09811080342, Email: agarwal.s.ca@gmail.com	Conference Director CA. Subodh Kumar Agrawal Council Member, ICAI Phone: 09830022848, Email: subodhka@yahoo.com
Conference Convenor CA. Sushil Kumar Goyal, Chairman, EIRC of ICAI Phone: 09830088400, Email: goyalsk@hotmail.com	
For Registration & further details, please contact Assistant Secretary, EIRC Office – Phone: 30211104/33 Email : pradyut.chakraborty@icai.in; eircerevents@icai.in ICAI, ICAI Bhawan, 7, Anandilal Poddar Sarani (Russel Street), Kolkata 700 071 Online payment facility also available at EIRC Website	

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CROSSWORD

062

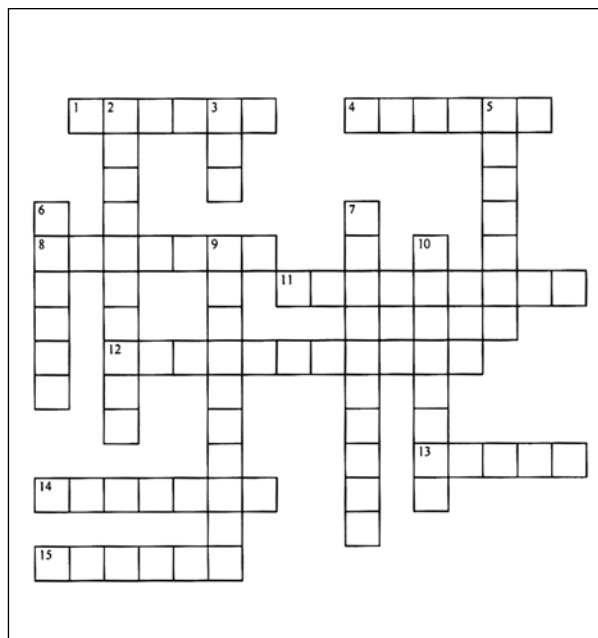
ACROSS

1. Unwritten principles of business conduct. (6)
4. Abbreviation of Earnings Before Interest Tax Depreciation and Amortization.
8. French words *Quotient Cours Benefice* means _____. (2,5)
11. International Bank for Reconstruction and Development is better known as the _____. (5,4)
12. A tax on interest receipts of foreign holders of German Bonds. (11)
13. LIBOR in London is _____ in India. (5)
14. A kind of theft by the cashier. (7)
15. Property by Will. (6)

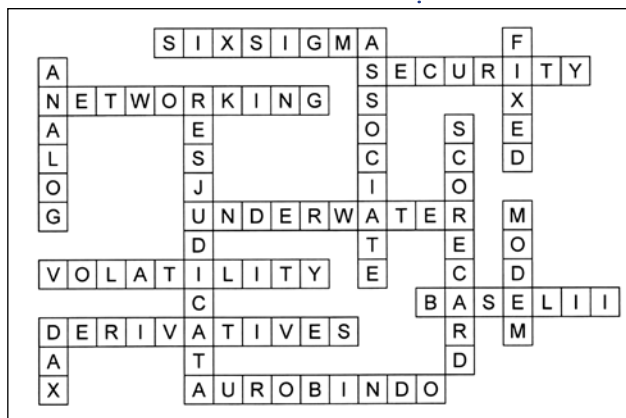
DOWN

2. The rule which prevents an individual being a resident of two countries for the purpose of DTAA. (3,7)
3. Project Management technique which provided the option of adding resources to selected activities to reduce project completion time.
5. _____ signatures are used for e-filing of documents. (7)
6. A derivative that gives the right but not the obligation to execute a specified transaction. (6)
7. Interest rate risk is type of _____. (6,4)

9. Condition when one is unable to pay his debts. (10)
10. Lost time of men or machines (4,4).



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 061



1 Paying in advance

A motorist, driving a car, hit and killed a calf that was crossing the road. The driver went to the owner of the calf and explained what had happened. He then asked what the animal was worth.

"Oh, about ₹2,000 today," said the owner. "But in six years it would have been worth ₹10,000. So ₹10,000 is what I have lost."

The motorist sat down and wrote out a cheque and handed it to the farmer.

"Here," he said, "is the cheque for ₹10,000. It's postdated six years from now."