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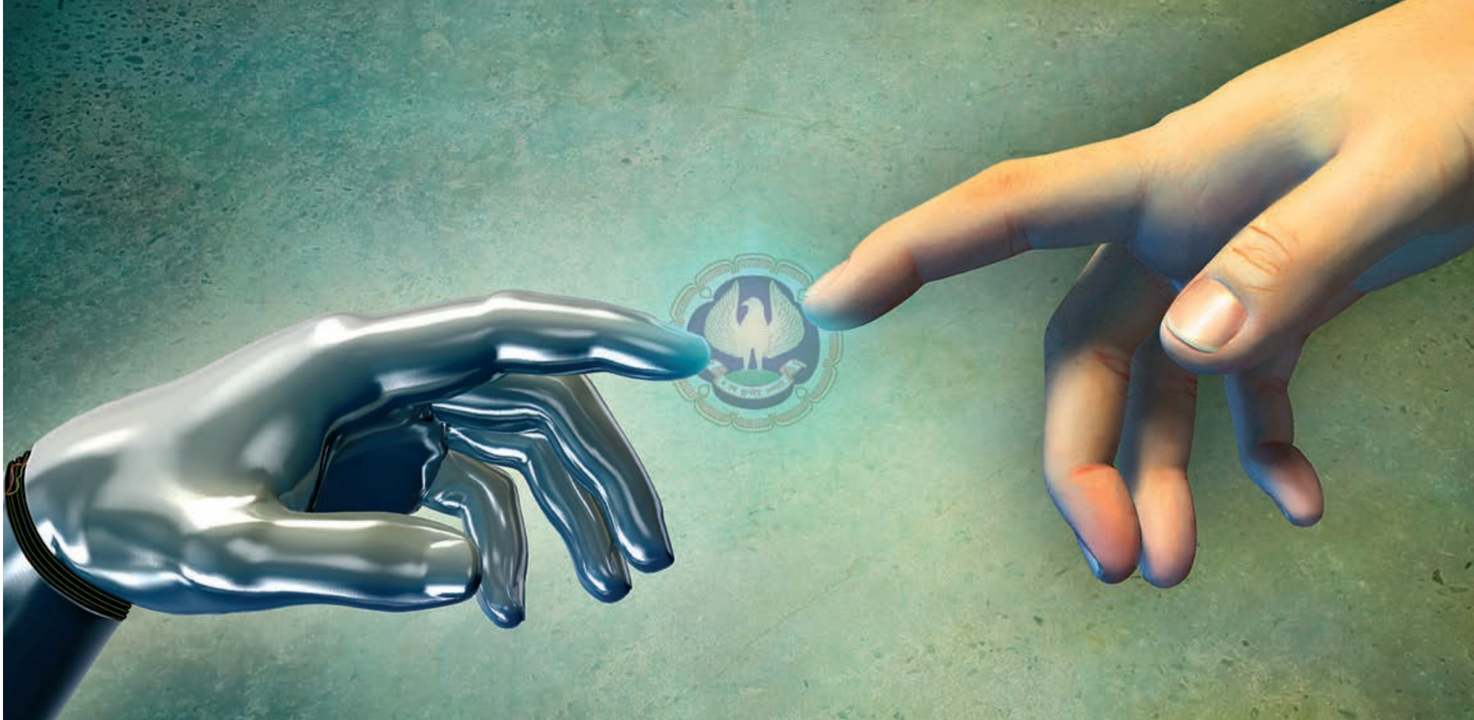
THE CHARTERED ACCOUNTANT JOURNAL

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

Companies Bill 2012
Corporate Governance with Social Responsibility



ICAI
Connecting Excellence with Fiscal Prudence

Values Virtues Vision

VOLUME 61 | No. 11 | MAY 2013
THE CHARTERED ACCOUNTANT
₹ 100

Ushering in a New Indian Corporatism

The company law in India is a composite class of many compartments just like in a train where there are different classes suiting a comfort level of a variety of passengers. It has been a long journey for the law which has been travelling since 1956 through the various corridors and grids of companies, and it has been amended as many 26 times. This long train is the corporate life-link and has always been looked upon with fervour and favour by all kinds of companies ranging from small, medium, big both inland and foreign. No doubt the Companies Act, 1956 is the epitome not only of Corporate India, but the World Inc. International business entities watch with interest and are very eager with anticipation as to whether the law of the land suits them in carrying out their operations and how the rules and regulations are for starting operations in the country.

Today, with the global multinational chain of companies in India, it is much to the credit of the policy makers who have devoted much of the discussion and deliberations with varied interests, whether it be shareholders, stakeholders, investors, promoters, and the corporate at large, as to what they expect from the law and what the law expects from them. The amendments that took place so far were on a piece-meal basis catering to different subject matters, but the current amendment under the name *"Companies Bill 2012"* is truly a sparkling in the twilight that the Lok Sabha has passed the Bill in its wisdom and it awaits clearance from the Rajya Sabha. Slimming by downsizing, compacting by re-characterisation, shifting from principle-based to rule-based law, reduction of governmental control to emphasis on self-regulation through corporate internal control, adoption of best international practices, legalising corporate governance practices, effective enforcement of law through machinery and mechanism and addressing appropriately the concerns of small businesses are the paradigm of the new Companies Bill, 2012.

It is a major leap forward for the corporate world, reform process and inclusive growth agenda in India. The new law is a step forward towards globalisation and is a successful attempt to meet the needs of the changing environment. It is progressive and futuristic in nature, duly envisaging the technological and legal developments. The Minister of Corporate Affairs Shri Sachin Pilot, while steering the long-awaited passage of the Bill in Lok Sabha on December 18, 2012, had rightly said: *"The aim is to protect the interests of employees and small investors while encouraging firms to undertake social welfare voluntarily instead of imposing that through 'inspector raj' and make India an attractive and safe investment destination."*

One of the major highlights of the proposed new legislation is that specified companies will have to necessarily spend 2% of their average net profits made in the immediately preceding three financial years towards Corporate Social Responsibility (CSR). The enactment of Companies Bill 2012 will make India the only country that has mandated CSR spend through statutory route. *"Private companies, while maximising their growth, also have responsibility towards society besides equitable and sustainable growth of the country,"* Shri Pilot rightly said while moving the Bill.

It might be a ponder to predict the outcome of the Bill, 2012 yet, but the Government's conscious efforts in bringing a thorough change are going to redefine and usher in a new Indian Corporatism in line with the best international principles and practices. New Concepts and definitions, redefining corporate governance and democracy, paving way for shareholders' activism, ensuring proper role and responsibilities for auditors, directors and whistle-blowing mechanism and suits under class action are the highlights which should usher in a new Indian Corporatism.

In this issue of the journal, we have highlighted many aspects of the Companies Bill, 2012 from the perspective of professionals besides other features. So read on...

-Editorial Board

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THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
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COMPANIES BILL 2012

ACCOUNTING

SPECIAL AUDIT

TAXATION

INTERNATIONAL TAXATION

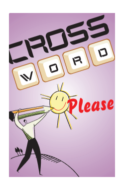
GLOBAL PERSPECTIVE

INFORMATION TECHNOLOGY

MANAGEMENT

CAPITAL MARKET

GENERAL



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CA. Subodh Kumar Agrawal, President, ICAI

Dear Friends,

Ethics is all about our becoming and feeling responsible about everything that is around us. We are responsible only when we appreciate everything that is ethical and denounce all that is not ethical around us. I would like our membership to ensure that they always go for the stricter interpretation, foregoing the liberal one wherever and whenever they realise a presence of two interpretations on a matter of professional interest, despite both being legal. Such a courageous display of moral conduct will inspire not only generations of our professionals, but also those from other walks of life.

Thomas More, in his *Utopia*, raises the same question when he asks: *Having distinguished between three types of 'good', psychological, physiological, and environmental, they proceed to ask whether the term is strictly applicable to all of them or only to the first*. Our past-President Shri R. C. Cooper also echoes More while writing the first preface to the ICAI's *Code of Ethics: …practice of professional ethics is largely a matter of conscience and the determination of members to distinguish between what is right and wrong. Ethics is a state of the mind*. He goes on to explain: *…there may be some acts which, though may not strictly fall under one of the items of the Schedule, may be one which may not be proper by any moral or ethical standards*. Very intimately and yet with sincere concerns, he advises all of us to act *in the larger interests of the Institute*, and *to search* our *hearts and conscience whenever in doubt.*

Let me assure our young members who have recently joined or are going to join the profession that the *Code of Ethics* being an appeal to act with conscience in the larger interests of our society, is there for all to inspire our ardour, good intention and enthusiasm. Let us present more ethical examples before our nation.

Recently, the Union Finance Minister Shri P. Chidambaram, while warning corporate giants against willful defaults, had asked the banks to constitute a board-level committee to monitor loan recoveries, and expressed his faith in our disciplinary mechanism when he said: *We have also told banks to lodge formal complaints with the ICAI, if the auditors of the borrower have been negligent or deficient in their auditing*. I assure him that we have been taking strict measures and we will do everything to keep the ethical values of our profession intact.

Another CSR Initiative Advanced

In deference to the CSR initiative of the Ministry of Corporate Affairs, recognising its social obligations as a partner-in-nation-building, the ICAI Council has decided at its recent meeting that the ICAI, through its dedicated network at the Regional and Branch-level centres, will seek volunteers from amongst its eligible members for offering free audit services to at least 100 auditable entities, to start with, viz. to undertake *pro bono* and *gratis* and complete audit in terms of applicable Generally Accepted Accounting Principles. It has been decided that the target beneficiaries would be selected from amongst those engaged in micro and small enterprises, located in tribal, remote and rural areas, belonging to underprivileged/disadvantaged sections of our society, differently abled and deserving but deprived classes. The ICAI will soon invite applications from its interested members/firms for necessary empanelment, which will then be submitted to the Ministry of Corporate Affairs.

Consensus Needed on Indian Financial Code Bill Proposal

The Government-appointed Financial Sector Legislative Reforms Commission (FSLRC) headed by Justice B. N. Srikrishna has finally given its long-awaited report proposing an Indian Financial Code Bill containing 450 clauses and six schedules, which mainly seeks to merge the SEBI, the Forward Markets Commission, the IRDA and the PFRDA under one Unified Financial Agency (UFA) among other sweeping measures. Further, it also proposes to limit the role of the RBI to monetary management. Explaining why the vast changes in the system of financial regulation and management is necessary, the report said: *The Commission is mindful that over the coming 25 to 30 years, Indian GDP is likely to become eight times larger than the present level, and is likely to be bigger than the United States GDP as of today... The aspiration of the Commission is to draft a body of law that will stand the test of time.* The inherent aim is to reform financial sector regulations for the longer term in keeping with systemic risks involved in financial management. The proposed Bill puts consumer protection at the centre of all regulations.

However, the move has stirred a lot of debate on its pros and cons in the Indian financial world. Though the intention and objectives of the proposed Bill are to be appreciated, the proposed wide-ranging re-engineering of financial regulatory framework needs to be debated and analysed threadbare in the public domain before it is concretised and taken to Parliament.

Meeting with Union Finance Minister

I recently attended the first meeting of the reconstituted Central Direct Taxes Advisory Committee, which was chaired by Hon'ble Finance Minister Shri P. Chidambaram. Minister of State (Revenue) Shri Namo Narain Meena, Advisor to Finance Minister Shri Parthasarathi Shome, and CBDT Chairperson Dr. Poonam K. Saxena, among other senior officials of CBDT were also present. Representatives from FICCI, ASSOCHAM, Federation of Association of Small Industries of India, Trade Commerce and Industry, etc., also attended the meeting.

At the meeting, I on behalf of ICAI submitted a detailed note suggesting measures for developing and encouraging mutual understanding and co-operation between tax payers and the Income Tax Department and removing administrative and procedural difficulties of a general nature. I also specifically highlighted ICAI's views relating to Tax Accounting Standards, need for an online grievance mechanism for e-filing and TDS and changes desired in ITR forms and Form No. 3CD pursuant to change in the revised Schedule VI.

Sincerely for the Cause of Membership

I would again appeal all our members and other stakeholders of our profession to contribute in matter and spirit in order to empower our sincere initiative for the cause of our membership, *Chartered Accountants Benevolent Fund*, which provides fiscal aid and assistance to all our members-in-distress for support and sustenance. Therefore, at present, all we need to do is to strengthen and build up the Fund's corpus. As you know, contributions to CABF are exempted under Section 80(G) of the Income-tax Act, 1961. Help us help our accounting fraternity in need and bring back some relief in their life.

Creativity and Innovation Must for Actual Success

According to a recent IBM survey, creativity and innovation is the most sought-after trait in leaders today. Most people are born creative, and remain so, particularly as children. Give a child a paper and pencil and he/she will immediately get down to 'create'. But overtime, as we grow, because of socialisation and formal education, a lot of us start to stifle the creative impulses. Most of us professionals are no exception to this phenomenon. As such, I, as the leader of accountancy profession in India, would like to see my professional fraternity to rediscover its creative confidence—the natural ability to come up with new ideas and courage to try them out. To do this, what we all need is to get past four fears that hold most of us back: *fear of messy unknowns, fear of being judged, fear of first step and fear of losing control*. You might argue that it is easier said than done. But, for sure, it is possible. To begin with, we may break challenges down into small steps and then build confidence by succeeding one after another. Creativity to me is something you practice. The process may feel a little uncomfortable at first but later on the discomfort quickly fades away and is replaced with new confidence and capabilities. Do try it out to make a difference to what we do as professionals.

Life is more than accumulation of things money can buy. Life is more than collecting rewards and accolades competing with others. Life is more than gaining attention and admiring glances when you are with people. Life is more than playing a game of one-upmanship. Instead, life is about 'creating something special'. There are enough people who believe the ultimate objective of life is to accumulate enough wealth and fame, create a safety nest for their immediate family and live life happily. This is what most people define as success. But if you take it from me, the goal of life should never be this 'success'. It should be ‘significance.’ And the more we create, the more we are significant. Otherwise, we are in a mirage called success. While success is 'produced', impact is 'created'. So, let’s come forward and create an impeccable impact as professionals, singularly as well as collectively.

Reporting of Foreign Currency Gains and Losses

We have suggested making it mandatory for companies to report foreign currency gains and losses separately in their financial statements. Companies will now have to separately state the impact of foreign exchange fluctuations in their balance sheets. This change will help a reader of the financial statement understand as to how much impact the foreign currency has had on the company. The move will help avoid divergence in accounting and bring more transparency in reporting of numbers. From now on, companies should show the Foreign Currency Monetary Item Translation Difference Account (FCMITDA) separately, under which they have to show foreign currency fluctuations "under the 'Equity and Liabilities' side of the balance sheet under the head 'Reserve and Surplus'.” These changes were approved at our last Council meeting. Further, we have suggested changes in reporting of gains or losses with regard to hedging instruments related to long term foreign currency items. It is suggested that Exchange difference related to the hedging instrument obtained to cover the exchange risk on long term foreign currency monetary items should also be separately shown in the balance sheet.

Requirements Arising from SEBI Circular

Members may note that the SEBI had issued a circular CIR/CFD/DIL/7/2011 dated October 5, 2011, regarding certain amendments to the Equity, IDR and SME Equity Listing Agreements. Paragraph 2(a)(ii) of the circular requires that "Listed entities shall also submit the last quarter results along with the audited annual results." This requirement has also been incorporated into the format of the listing agreement, in paragraph 41.I.(d) which reads: *The company shall submit audited financial results for the entire financial year, within sixty days of the end of the financial year. The company shall also submit the audited financial results in respect of the last quarter alongwith the results for the entire financial year, with a note that the figures of last quarter are the balancing figures between audited figures in respect of the full financial year and the published year to date figures up to the third quarter of the current financial year.*

This requirement was subsequently deferred, but will apply for financial years ended March 31, 2013 and thereafter. This amendment, therefore, requires companies to submit the audited financial results for the last quarter, which would be derived as the balancing figure between the full year's results, and the published year-to-date figures up to the end of the third quarter of the financial year. Members are advised to please take note of this requirement.

Submission of Post-Budget Memoranda 2013

The Finance Bill 2013 has given the country the direction for inclusive and sustainable growth with fiscal consolidation. To further the grand objectives and efficacy of Finance Bill 2013, and to make it more practical and people

& economy-friendly, we have given a number of suggestions in our Post-Budget Memoranda on Direct and Indirect Taxes to the Ministry of Finance for their consideration. These memoranda have also been hosted on our website. In these memoranda, we have suggested certain amendments, which would greatly help the Government to achieve the desired objectives besides making tax laws simple, fair and transparent so as to avoid litigation.

Representation to CBDT with regard to Specified Domestic Transactions

As the members are aware, the Finance Act, 2012 amended the provisions of Chapter X to encompass within its ambit certain specified domestic transactions. Consequently, changes have been made in the various provisions including section 92E, which now requires every person who has entered into an international transaction or specified domestic transaction to obtain a report from a chartered accountant in a prescribed format within specified time i.e., due date of filing of return under section 139(1). Further, Rule 10E provides that such report shall be in Form No. 3CEB. In order to incorporate the amendment made by the Finance Act, 2012, Form No. 3CEB is yet to be amended or a separate form is to be notified, as the case may be, in which report of an accountant is required to be furnished in respect of specified domestic transactions. As the report is to be issued by the chartered accountants, ICAI has requested CBDT to allow it to participate in the process of preparation of the aforesaid revised format. ICAI has further suggested exemption from applicability of Domestic Transfer Pricing provisions for certain transactions.

May 2013 Examinations, e-Learning and GMCS

I wish all our students all the best for their May 2013 Examinations, as I am sure they must have prepared hard for them. The key is to prepare and write examinations intelligently rather than stressing yourselves out, and with an enlightened mind.

Our e-learning for Common Proficiency Course and Intermediate (IPC) Course has helped a lot of you so far, which could be ascertained from 20,000+ student registrations, 84,000+ e-Learning Hours by Students, 2,00,000+ Visitor Count. Today, students qualifying our Chartered Accountant examinations are more confident in communication skills, including presenta-tions, by undergoing GMCS courses during their article training. These courses help them in improving their intelligence in this global competitive environment. I would urge the students to complete the GMCS courses as early as possible, which will help them in changing their outlook and transform them into more confident and competent personalities.

More Facilities in Mobile Version of Journal

We have incorporated the podcast and bookmark facility in the mobile compatible (on iOS, Android, tablet platform) version of e-Journal. Members can now also listen to the textual material instead of reading and can make optimum use of their time while travelling.

*****

Acclaimed poet John Milton hails the present month of May, since it inspires, mirth and youth and warm desire in us to act—to do something for us, our people and our society. May is also here to warn for two reasons—first, we are about to cross the year's first half and, second, the Summer is at our doors. Therefore, it is time to introspect and prepare; it is time to assess and act; it is time to recall what we have promised at the start.

I assure all of you to be there with you always in action and spirit, while you enjoy your life and feel the gladness of the May, with your heart.

Best wishes

S K Agrawal

CA. Subodh Kumar Agrawal
President, ICAI
New Delhi, April 23, 2013

Meeting with Indian Finance Minister

ICAI President CA. Subodh Kumar Agrawal along with Union Finance Minister of India Shri P. Chidambaram. (April 12, 2013)

Meeting with Indian High Commissioner to Singapore

ICAI President CA. Subodh Kumar Agrawal presents a memento to the Indian High Commissioner Dr. T. C. A. Raghavan in Singapore. (April 19, 2013)

NRIC Annual Prize Distribution

ICAI President CA. Subodh Kumar Agrawal addresses the awardees and other members of the northern region; Vice-President CA. K. Raghu shares the dais with the Chief Guest and Member of Parliament Dr. Ashok Tanwar and Central Council members CA. Sanjay "Voice of CA" Agarwal, CA. Vijay Kumar Gupta, CA. Sanjiv Chaudhary and CA. Naveen N. D. Gupta, among others, in New Delhi. (April 1, 2013)

ICAI President CA. Subodh Kumar Agrawal and Chief Guest and Member of Parliament Dr. Ashok Tanwar presents certificate to an awardee, while Vice-President CA. K. Raghu, Central Council member CA. Vijay Kumar Gupta and NIRC Chairman CA. Vishal Garg among others celebrate. (April 1, 2013)

Financial Services Secretary at 324th ICAI Council Meeting

Financial Services Secretary of Govt. of India, Shri Rajiv Takru, unveils an ICAI publication while ICAI President and Vice-President CA. Subodh Kumar Agrawal and CA. K. Raghu along with ICAI Central Council members share the occasion. (March 25, 2013)

Meeting with Union Minister for Petroleum & Natural Gas

ICAI President CA. Subodh K. Agrawal presents a bouquet to Union Minister for Petroleum and Natural Gas Dr. M. Veerappa Moily in New Delhi, while ICAI Vice-President CA. K. Raghu shares the joy. (March 28, 2013)

Union Minister for Petroleum and Natural Gas Dr. M. Veerappa Moily looks over an ICAI publication, while ICAI President and Vice-President CA. Subodh Kumar Agrawal and CA. K. Raghu look on. (March 28, 2013)

IFRS Conference in Sao Paulo

ICAI President CA. Subodh Kumar Agrawal and IASB Chairman Hans Hoogervorst meet during the Conference, while ICAI Central Council member CA. Sanjeev K. Maheshwari and ICAI Technical Director Dr. Avinash Chander join them. (April 15-16, 2013)

Orientation Programme in Chennai

ICAI President CA. Subodh Kumar Agrawal addresses the newly-qualified chartered accountants; ICAI Vice-President CA. K. Raghu along with Central Council members CA. Vijay Kumar Gupta, CA. G. Sekar, CA. Tarun Jamnadas Ghia and CA. Babu Abraham Kallivayalil, among others, share the dias. (March 5, 2013)

Campus Placement Orientation Programme in Mumbai

ICAI President CA. Subodh Kumar Agrawal addresses the newly-qualified chartered accountants while Central Council members CA. Prafulla P. Chajed, CA. Vijay Kumar Gupta and CA. Tarun Jamnadas Ghia, and WIRC Chairman CA. Mangesh Kinare among others share the dais. (March 6, 2013)

Orientation Programme in New Delhi

ICAI Vice-President CA. K. Raghu addresses the newly-qualified chartered accountants, while Central Council member CA. Vijay Kumar Gupta looks on. (March 12, 2013)

SAFA BPA Awards Ceremony in Colombo

ICAI President and SAFA Vice-President CA. Subodh Kumar Agrawal lights the lamp to inaugurate the function, while CMA Sri Lanka President Prof. L. R. Watawala, CA Sri Lanka President Mr. Sujeewa Rajapakse and Vice-President Arjuna Heerath and ICAB President Md. Abdus Salam observe. (March 22, 2013)

ICAI President and SAFA Vice-President CA. Subodh Kumar Agrawal with CA Sri Lanka CEO/ Secretary Aruna Alwis, among others, presents certificate to an awardee. (March 22, 2013)

CA Sri Lanka President Mr. Sujeewa Rajapakse presents a memento to ICAI President and SAFA Vice-President CA. Subodh Kumar Agrawal. (March 22, 2013)

Bangalore Branch Felicitates ICAI Vice-President

Bangalore Branch Chairman CA. Ravindranath S. N. presents memento and felicitates the ICAI Vice-President CA. K. Raghu, while other members and office bearers of the Branch celebrate. (March 21, 2013)

ICAI President and Vice-President in Kolkata

ICAI President and Vice-President CA. Subodh Kumar Agrawal and CA. K. Raghu along with senior chartered accountants in Kolkata. (April 9, 2013)

Members' Meet in Ahmedabad

ICAI President and Vice-President CA. Subodh Kumar Agrawal and CA. K. Raghu along with Ahmedabad Branch Chairman CA. Purushottam Khandelwal and Secretary CA. Amresh Patel among others on the dias. (April 6, 2013)

ICAI President CA. Subodh Kumar Agrawal addresses the audience while Vice-President CA. K. Raghu shares the dais with Central Council member CA. Dhinal Ashwinbhai Shah and Ahmedabad Branch Chairman CA. Purushottam Khandelwal, among others. (April 6, 2013)

Invitation to Contribute Articles for *The Chartered Accountant Journal*

The Editorial Board has decided to specially focus on certain key topics besides other routine features in the forthcoming issues of The Chartered Accountant Journal. As such, the expert authors in the respective fields are invited to send articles on the following focus issues for consideration of the Editorial Board of the ICAI.

June 2013	Tax Audit+Sustainability & Social Audit+Public Finance
August 2013	Indian Accounting Standards converged with IFRSs
September 2013	XBRL
October 2013	Internal Audit+Forensic Accounting
November 2013	LLP & Accountancy Profession
December 2013	Professional Opportunities (new horizon)
January 2014	Information Technology
February 2014	Bank Audit+Government Accounting

The articles of not more than 3000 words (original and not having been published of hosted anywhere else) with executive summary and authors photographs should be sent at eboard@icai.org at the earliest. The authors are also required to give a declaration of originality and that the article has been published/hosted anywhere else. The guidelines for authors have been hosted on ICAI website in Editorial Board Section on the link: http://icai.org/new_post.html?post_id=2556

Special Issue on Union Budget 2013-14 was Very Informative

The April 2013 special issue on Union Budget 2013-14 was very informative and knowledge enhancing. The key aspects of the Budget were well explained and highlighted. Knowledge packed articles *"Salient Features of Finance Bill, 2013: Direct Taxes'* by our past President CA. Ved Jain, *Impact of Finance Bill, 2013 on Real Estate Sector* by CA. G. Sekar, *Analysis of Budget 2013-2014-Central Excise* by CA. Madhukar N.Hiregange, *Key International Tax Provisions Proposed in Finance Bill,* 2013 by CA. Dhinal Ashvinbhai Shah, Service Tax – Amendments in Finance Act, 1994 & Exemptions by CA. Rajendra Kumar, Service Tax Voluntary Compliance Encouragement Scheme, 2013 by CA. Asok Batra and *Overview of Macroeconomic Aspects of Budget* 2013-2014 by Dr. Pratap Ranjan Jena, were all worth reading while providing valuable updates. The Editorial titled "Budget 2013-2014 for inclusive, Sustainable Growth too was also very well written and explained. We got a valuable update through the write-up *'Revised Auditor's Report Format – An overview (SA 700 Revised, SA 705 and SA 706).* It is to be specially noted that 'From the President' feature authored by President CA. Subodh Kumar Agarwal has become further impressive with brief and to the point information for the Readers. Overall, the journal is getting more impressive month after month.

-CA. Subhash Chandra Podder

Articles Published in Journals Provide Contemporary Updates

The journal of March 2013 was very helpful and informative. I read almost of the articles but articles on 'bank audit' were really superb. The ICAI journal is proving to be very useful for new chartered accountants like me.

-CA Akshay Garg, New Delhi

It has been my monthly routine to read the CA Journal which has been giving lots of information to the practicing CAs. The article on "Comparison of Financial Statements prepared as per IFRS & Indian GAAP" in March 2013 issue has been well presented and the authors have compared the financial statements prepared by certain renowned companies to indicate any significant difference in the reporting of Equity & Net Profit. The article is very good and the Institute should encourage publication of such articles quite often which enhances the professional skills of the CAs.

- CA.Srinivasan Chakravarthy, Nagpur

The articles on the bank statutory audit published in the journal were like a readymade capsule. Congrats to the Editorial Board. Keep sending such readymade capsules every month.

-CA Jomon. C.V, Navi Mumbai

First of all, thank you very much for great efforts put in compiling an informative CA journal. I particularly liked the article *'Women on Boards-the Statistics Speak'* published in the January 2013 issue. I have worked in corporates where I found very few women on top positions. I didn't have satisfactory answer to my queries as to the HR reason behind this. However, this article answered my question. We really need balanced boards with right mix of male and female directors. A good change has been made to have at least one woman director by Companies Bill 2012.

-CA.Jaya Goyal, Mumbai

The article titled 'Taxability of Income from Offshore Supply of Goods to India in a Turnkey Contract' was well conceived and well concluded.

-Vikas Jain, Noida

The article titled 'Taxability of Income from Offshore Supply of Goods to India in a Turnkey Contract' in the January 2013 issue was well written and the sum and substance of the topic was very well covered.

-Ravi Tela

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 eboard@icai.org/nadeem@icai.org or write to:
The Editor, The Journal Section, ICAI, A-29, Sector 62, Noida (UP) - 201309

Ethical Issues in Question-Answer Form

Q. What is the Conceptual Framework Approach?

A. It is a framework that requires a professional accountant to identify, evaluate and address threats to compliance with the fundamental principles, rather than merely comply with a set of specific rules. Professional accountants are required to apply this conceptual framework to identify threats to compliance with the fundamental principles, to evaluate their significance and, if such threats are other than clearly insignificant than to apply safeguards to eliminate them or reduce them to an acceptable level such that compliance with the fundamental principles is not compromised.

Q. What are the threats involved while complying with the fundamental principles?

A. Compliance with the fundamental principles may potentially be threatened by a broad range of circumstances. Many threats fall into the following categories:

(a) Self-interest threats;
(b) Self-review threats;
(c) Advocacy threats;
(d) Familiarity threats; and
(e) Intimidation threats.

Q. What are the available safeguards that may eliminate or reduce the threats at an acceptable level?

A. Safeguards that may eliminate or reduce such threats to an acceptable level fall into two broad categories:

(a) Safeguards created by the profession, legislation or regulation; and
(b) Safeguards in the work environment.

Q. What is Ethical Conflict Resolution?

A. Ethical conflict resolution means to resolve a conflict in the application of fundamental principles while evaluating compliance with the fundamental principles.

Q. What is a Client Acceptance, Engagement Acceptance and Changes in Professional Appointment?

A. Section 210 of Part - A of Code of Ethics deals with Professional Appointment:

(a) Client Acceptance – Under this a professional accountant in public practice should consider, before accepting a new client relationship, whether acceptance would create any threats to compliance with the fundamental principles.

(b) Engagement Acceptance - A professional accountant in public practice should agree to provide only those services that the professional accountant in public practice is competent to perform.

(c) Changes in Professional Appointment - A professional accountant in public practice who is asked to replace another professional accountant should determine whether there are any reasons, professional or other, for not accepting the engagement, such as circumstances that threaten compliance with the fundamental principles. It shall require direct communication with the existing accountant to establish the facts and circumstances behind the proposed change so that the professional accountant in public practice can decide whether it would be appropriate to accept the engagement.

Under all the 3 circumstances, the significance of any threats should be evaluated. If identified threats are other than clearly insignificant, safeguards should be considered and applied as necessary to eliminate them or reduce them to an acceptable level. Where it is not accountant in public practice should decline to enter into the client relationship.

Q. What are the measures available to professional accountants in case conflict of interest arises?

A. A professional accountant in public practice should take reasonable steps to identify circumstances that could pose a conflict of interest. Such circumstances may give rise to threats to compliance with the fundamental principles.

A professional accountant should evaluate the significance of any threats. Depending upon the circumstances giving rise to the conflict, safeguards should ordinarily notify the client / all known relevant parties.

The additional safeguards e.g. the use of separate engagement teams, clear guidelines for members of the engagement team on issues of security and confidentiality, Regular review of the application of safeguards by a senior individual not involved with relevant client engagements should also be considered.

* Contributed by the Ethical Standards Board of the ICAI

Q. Whether a Professional Accountant in Public Practice may pay or receive a referral fees or commission?

A. A professional accountant in public practice may receive a referral fee or commission relating to a client and may pay a referral fee to obtain a client. A professional accountant in public practice should not pay or receive a referral fee or commission, unless the professional accountant in public practice has established safeguards to eliminate the threats or reduce them to an acceptable level.

Q. What are the safeguards available to a Professional Accountant in Public Practice in respect of Custody of Client Assets?

A. A professional accountant in public practice entrusted with money (or other assets) belonging to others should:

(a) Keep such assets separately from personal or firm assets;

(b) Use such assets only for the purpose for which they are intended;

(c) At all times, be ready to account for those assets, and any income, dividends or gains generated, to any persons entitled to such accounting;

(d) Comply with all relevant laws and regulations relevant to the holding of and accounting for such assets.

Q. What is Independence?

A. Independence requires:

Independence of Mind - The state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.

Independence in Appearance - The avoidance of facts and circumstances that are so significant that a reasonable and informed third party, having knowledge of all relevant information, including safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism had been compromised.

Q. What is the Conceptual Framework to Independence?

A. It is to be applied to specific circumstances and relationships. It gives various examples about the threats to independence that may be created by specific circumstances and relationships and also provides how professional judgment is used to determine the appropriate safeguards to eliminate threats to independence or to reduce them to an acceptable level depending on the characteristic of the individual assurance engagement. ■

Letter from DIT (Systems)

Letter from DIT (Systems) - Members to be Cautious While E-Filing Income-Tax Returns

Members may note that ICAI has received a letter from Directorate of Income-tax (Systems) requesting it to impart information regarding correct procedure of e-filing of returns. The following are the major concerns of the Department:-

a) ITR-V is not received or is belated for the assessment year at CPC

b) ITR-V is not signed by the tax payer

Members may note that to eliminate the above mentioned problems, the Income-tax Department has started a drive through media, press release, instructions and chambers to increase awareness among the tax payers. Although, we are sure that the members are aware of the e-filing process, it is our responsibility to bring, the following initiatives taken by the Department in this regard, to your notice:

- A help desk has been set up for information, held or any assistance. The taxpayers can call 1800 180 1961 or 1800 425 2229.
- The taxpayer can visit Income tax website https://incometaxindiaefiling.gov.in for any information.
- They can also know the status of their e-returns through e-filing website under "Know your ITR V status". The status of receipt of ITR-V can be viewed at e-filing website https://incometaxindiaefiling.gov.in. The ITR-V form can be downloaded from the same website.

PNGRB reference on compliance with AS 17

ATTENTION MEMBERS

PNGRB reference on compliance with AS 17 by CGD entities

The Petroleum and Natural Gas Regulatory Board (PNGRB), entrusted with the duties, *inter alia*, of regulating the transportation rate for city or local natural gas distribution networks or common or contract carrier pipelines, has recently informed the Institute that in the course of their consultation process, they have come to know that CGD entities i.e. entities engaged in the activities of laying building, operating or expanding city or local natural gas distribution networks are not adhering to the requirements of segment reporting on the ground that they operate in only one segment of business and therefore Accounting Standard 17 (Segment Reporting) that contains provisions for segment reporting does not apply to them.

Upon consideration of the matter, the PNGRB has directed all the CGD entities to ensure compliance with the requirements of AS-17 by reporting their transportation and marketing activities as separate segments for their accounts for the year 2012-2013 and succeeding years.

Against the above background, the PNGRB has requested our Institute to apprise Members of the Institute associated with the preparation of financial statements as well as those who perform the statutory function of audit of accounts of the concerned entities about the stand taken by them as aforesaid.

Attention of Members concerned are accordingly invited to the text of the communication dated 1st March, 2013 (Ref. No. PNGRB/M(C)/42/2013) of PNGRB which is hoisted in the Institute's Website i.e. www.icai.org at What's New.

Legal Decisions[1]

Income-tax Act

LD/61/81
CIT-9
Vs.
Regalia Apparels Pvt. Ltd
March 7, 2013 (BOM)
[Assessment Year 2004-05]

Section 37(1) of the Income-tax Act, 1961 - Business expenditure – Allowable as

Forfeited bank guarantee by Apparel Export Promotion Council for not utilising export entitlement, is allowable as business expenditure in hands of garment manufacturer

The assessee is a manufacturer of garments. The Apparel Export Promotion Council (APEC) granted to the assessee entitlements for export of garments. In consideration for export entitlements the respondent assessee furnished bank guarantee in support of its commitment that it shall abide by the terms and conditions in respect of the export entitlements. In view of the fact that the respondent was incurring losses, it decided not to utilise the export entitlement which led APEC to encash the bank guarantee. The assessee claimed deduction under Section 37(1). The Assessing officer did not accept the same and concluded that the forfeiture was in the nature of penalty and disallowed the expenses under Section 37(1) in view of the *explanation* thereto.

The Bombay High Court held as follows:

The assessee took a business decision not to honour its commitment of fulfilling the export entitlement in view of loss being suffered by it. The Assessing Officer did not dispute this fact nor did he doubt the genuineness of the claim of the expenditure being for business purpose. The assessee had not contravened any provisions of law and thus the forfeiture of bank guarantee was compensatory in nature under Section 37(1).

LD/61/82
CIT, Rohtak
Vs.
Shri Jagtar Singh Chawla
March 20, 2013 (P&H)
[Assessment Year 2007-08]

Section 54F of the Income-tax Act, 1961 - Capital gains - Investment of, in case of residential house

Where assessee has proved payment of substantial amount of sale consideration for purchase of a residential property within extended period of limitation of filing of return and acquired a residential house before end of next Financial Year in which sale has taken place, assessee would not be liable to pay any capital gain

The assessee sold his agricultural land and residential house for ₹2,16,00,000/- and ₹8,25,000/- respectively, *vide* sale deed dated 20.6.2006. On the same date, the assessee claims to have written a letter to the Bank to deposit the said amount in the capital gain account, but it appears that the said amount was not deposited in the capital gain account. However, the same was deposited in a “Flexi General Account”, which is a saving as well as fixed deposit account. The assessee purchased a residential house from the sale proceeds so received.

The Revenue disallowed the claim of the assessee under Section 54F and added a sum of ₹76,85,829/- under the head `long term capital gains’. The said order of the Assessing Officer was upheld by the Commissioner (Appeal. However, in further Appeal, the Tribunal set aside the order of the Commissioner (Appeals), on the ground that the assesee has purchased the residential house within the period prescribed under Section 139 and thus, the addition was not sustainable.

The Punjab and Haryana High Court held as follows:

The assessee has proved the payment of substantial amount of sale consideration for purchase of a residential property on or before 31.3.2008 that is within extended period of limitation of filing of return. Only a sum of ₹24 lacs was paid out of total sale consideration of ₹Two Crores on 23.4.2008, though possession was delivered to the assessee on execution of the power of attorney on 30.3.2008.

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

Since the assessee, has acquired a residential house before the end of the next Financial Year in which sale has taken place, therefore, the assessee is not liable to pay any capital gain.

LD/61/83
Court on its Own Motion
Vs.
CIT
March 14, 2013 (DEL)

Section 139 of the Income-tax Act, 1961 - Return of income

In respect of Central Processing of Income Tax Returns, directions are issued for removing numerous difficulties faced by income-tax assessees with respect to uploading of wrong or fictitious demand, adjustment of refund contrary to the mandate of section 245, credit of tax deducted at source (TDS), etc.

In respect of Central Processing of Income Tax Returns, in a PIL, it was alleged that the numerous difficulties are faced by the income-tax assessees country wide due to the faulty processing of the income tax returns and the TDS deducted at source and request that certain directions be issued by this Court so that lakhs of tax payers are saved from the harassment in filing revised returns/rectification petitions every year.

There were allegations with respect to (i) uploading of wrong or fictitious demand, (ii) adjustment of refund contrary to the mandate of section 245, (iii) credit of tax deducted at source (TDS), etc.

The Delhi High Court disposed the matter as follows:

(i) Directions were given regarding maintenance of register for applications under Section 154, receipt of the said applications and their disposal

In the affidavit filed, the department has stated that they have "recently" prescribed a register for receipt of rectification applications. The said register has various columns namely, date of disposal, date of service of rectification application, demand/refund etc. This is the right step but it must be ensured by the Board that the registers are made available to all Assessing Officers or at the dak counters. The said registers will be made available to the dak counters and the Assessing officers within two months, if not already provided. The Board will also issue instructions that all Assessing Officers and dak counters shall henceforth in the said register, enter and allocate a serial number on the rectification applications and the date of receipt and the serial number will be mentioned on the acknowledgement, which is issued to the assessee. Uploading of the details of the said registers as stated in the affidavit should be made online preferably within a period of six months. This, would be in accordance with the mandate of the Citizen Charter of the Department which states that the department believe in equity and transparency.

In the counter affidavit filed on 5th March, 2013, it is stated that Aayakar Seva Kendras provide for single window service to tax payers for receipt of Dak/grievance and paper returns and applications under Section 154 are also within the scope of Aayakar Seva Kendras. Information in this regard will be disseminated and informed to the assessees, who can take advantage and benefit of the same. It is stated that there are already 75 Aayakar Seva Kendras and 57 more such Kendras are being set up in the current year. Similarly, it is stated that Sevottam Aayakar Seva Kendras are being set up in 112 income tax offices.

Each application under Section 154 has to be disposed of and decided by a speaking order. This is the mandate of the Act. The order has to be communicated to the assessee and there is a relevant column to be filled in the register, which is now required to be maintained. The Board should issue specific directions to ensure that there is full compliance of the said requirements and directions by the Assessing Officers, Dak counters and Aayakar Sewa Kendras.

(ii) The interim directions given by the order dated 31st August, 2012 were affirmed

When a return of income processed under Section 143(1) at Central Processing Unit at Bengaluru, the computer itself adjusts the refund due against the existing demand, i.e., there is adjustment but without following the two stage procedure prescribed in Section 245. In these circumstances, the following interim order was passed on 31st August, 2012:

> "The department shall in future follow the procedure prescribed under Section 245 before making any adjustment of refund payable by the CPU at Bengaluru. The assessees must be given an opportunity to file response or reply and the reply will be considered and examined by the Assessing Officer before any direction for adjustment is made. The process of issue of prior intimation and service thereof on the assessee will be as per the law. The assessees will be entitled to file their response before the Assessing Officer mentioned in the prior intimation. The Assessing Officer will thereafter examine the reply and communicate his findings to the CPC, Bengaluru, who will then process the refund and adjust the demand, if any payable. CBDT can fix a time limit for communication of findings by the Assessing Officer. The final adjustment will also be communicated to the assessees."

The said interim order is confirmed. The department has taken remedial steps to ensure compliance of Section 245 as they now give an option to the assessee to approach the Assessing Officer. The interim order passed in the writ petition dated 31st August, 2012 has been implemented.

(iii) With regard to past adjustments where procedure under Section 245 has not been followed, directions are issued

In spite of the opportunity given to the Revenue to take steps, prescribe, adopt a just procedure, to correct the records, etc., nothing has been done and they have not taken any decision or steps. The affidavits filed subsequently after 31st August, 2012, are silent on this specific point. In cases where returns have been processed by the CPC Bengaluru and refunds have been fully or partly adjusted against the past arrears while passing or communicating the order under Section 143(1), without following the procedure under Section 245, it is directed that:

> "A. All such cases will be transferred to the Assessing Officers; B. The Assessing Officers will issue notice to the assessee which will be served as per the procedure prescribed under the Act; C. the assessees will be entitled to file response/reply to the notice seeking adjustment of refund; D. After considering the reply, if any, the Assessing Officers will pass an order under Section 245 of the Act permitting or allowing the refund; E. The Board will fix time limit and schedule for completing the said process."

There are three reasons why the said directions have been issued. Firstly, the department accepts and admits the position that wrong and incorrect demands have been uploaded in the CPC Bengaluru. Secondly, the department has not followed the mandate and requirement of Section 245 before making the adjustment. The two stage process with the opportunity and right of the assessee to submit a reply before the adjustment is made, has been denied. CPC Bengaluru did not entertain or accept any application of the assessee questioning past arrears uploaded in their system as they are not custodian of past records. CPU Bengaluru entertain on-line applications but do not entertain physical or hard copy applications. Assessing Officer similarly did not entertain any application by the assessee on the ground that the order under Section 143(1) was passed by the CPC Bengaluru and they do not have the files/return with them. Thus, the problem was created and caused by the department who did not realise the effect and impact of incorrect and wrong arrears being uploaded in CPU Bengaluru and did not follow the statutory requirements of Section 245.

The aforesaid directions are only applicable to cases where two stage procedure under Section 245 has not been followed and not to cases where procedure under Section 245 was followed.

(iv) With regard to the interest under Section 244A, directions are issued that interest should be paid when the assessee is not at fault

In the affidavit filed on 29th January, 2013, the department has stated as under:

> "Where an assessee makes a mistake in the claim of TDS in the e-return and the return is processed and a demand is raised and subsequently the assessee rectifies the mistake in the claim and files an online rectification application, the same is processed and on any excess TDS refunded, the interest under section 244A is granted as per the I.T. Act after excluding the period of delay attributable to the assessee in terms of sub-section 2 of section 244A."

An assessee can be certainly denied interest if delay is attributable to him in terms of sub-section (2) to section 244A. However, when the delay is not attributable to the assessee but due to the fault of the Revenue, then interest should be paid under the said Section. False or wrong uploading of past arrears and failure to follow the mandate before adjustment is made under section 245, cannot be attributed and treated as a fault of the assessee. These are lapses on the part of the Assessing Officer i.e. the Revenue. Interest cannot be denied to the assessees when the twin conditions are satisfied and in favour of the assessee. However, even in such cases Assessing officer may deny interest for reasons to be recorded in writing if the assessee was in fault and responsible for the delay.

(v) With regard to uncommunicated intimations under Section 143(1), directions are given

The grievance of the assessee is with regard to the un-communicated intimations under Section 143(1) which remained on paper/file or the computer of the Assessing Officer. This is serious challenge and a matter of grave concern. The law requires intimation under Section 143(1) should be communicated to the assessee, if there is an adjustment made in the return resulting either in demand or reduction in refund. The un-communicated orders/intimations cannot be enforced and are not valid. Department in the counter affidavit has not dealt with this problem on the assumption that the Assessing Officer who had manually processed the returns and passed the order/intimations under Section 143(1) would have necessarily followed the statute and communicated the said orders/intimations. In case the said orders/intimations under Section 143(1) were communicated or dispatched to the assessees, the directions given below would not be a cause for any grievance and will not be a matter of concern for the Revenue.

Where an order under Section 143(1) was sent and communicated to the assessee but could not be served due to non-availability/change of address or other valid reasons, should not be treated at par with cases where there is no communication or no attempt is made to serve the order whatsoever. But when there is failure to dispatch or send communication/intimation to the assessee consequences must follow. Such intimation/order prior to 31st March, 2010, will be treated as non est or invalid for want of communication/service within a reasonable time. This exercise, it is desirable should be undertaken expeditiously by the Assessing Officers. CBDT will issue instructions to the Assessing Officers.

The onus to show that the order was communicated and was served on the assessee is on the Revenue and not upon the assessee. In case an order under Section 143(1) is not communicated or served on the assessee, the return as declared/filed is treated as deemed intimation and an order under Section 143(1). Therefore, if an assessee does not receive or is not communicated an order under Section 143(1), he will never know that some adjustments on account of rejection of TDS or tax paid has been made. While deciding applications under Section 154, or passing an order under Section 245, the Assessing Officers are required to know and follow the said principle. Of course, while deciding application under Section 154 or 245 or otherwise, if the Assessing Officer comes to the conclusion and records a finding that TDS or tax credit had been fraudulently claimed he will be entitled to take action as per law and deny the fraudulent claim of TDS etc. The Assessing Officer, therefore, has to make a distinction between fraudulent claims and claims which have been rejected on ground of technicalities but there is no communication to the assessee of the order/intimation under Section 143(1). In the later cases, the Assessing Officer cannot turn around and enforce the demand created by uncommunicated order/intimation under Section 143(1).

(vi) With regard to unverified TDS under the heading 'U' in Form 26AS, directions have been issued for verification and correcting unmatched challans within a time period, which should be fixed by the Board keeping in mind the date of filing of return and processing of return by the assessing officer

Another problem highlighted relates to the use of alphabets "U", "M" and "P" in Form 26 AS. The said alphabets stand for "unmatched challan", "matched challan" and "provisional booking". It is stated that "provisional booking" is applicable for DDOs, i.e., Government deductors and shall be shortly discontinued. "Unmatched challans" relate to challans where the reports by the deductor in the TDS statement are not found available in the OLTAS data base (OLTAS stands for Online Tax Accounting System). The department will fix a time limit within which they shall verify and correct all unmatched challans. This will necessarily require communication with the deductor and steps to rectify. The time limit fixed should take into account the due date of filing of the return and processing of the return by the Assessing Officer. An assessee as a deductee should not suffer because of fault made by deductor or inability of the Revenue to ask the deductor to rectify and correct. Once payment has been received by the Revenue, credit should be given to the assessee. Board will issue such suitable directions in this regard.

(vii) With regard to credit of TDS to an assessee when the tax deducted has been deposited with the Revenue by the deductor, directions have been given

The Act empowers and authorises the Assessing Officer to verify the contents of the return and notices can be issued to a third party, i.e. the deductor, to furnish information and details. The deductor, the principal officer or person responsible for making deduction, once issued notice to appear, in most cases, would like to comply with the statutory requirements and also furnish details with regard to TDS deducted from the income of the assessee. The statutory powers given to the Assessing Officer are sufficient and should be resorted to and the assessee cannot be left to the mercy or the sweet will of the deductors. Therefore, when an assessee approaches the Assessing Officer with requisite details and particulars, the said Assessing Officer will verify whether or not the deductor has made payment of the TDS and if the payment has been made, credit of the same should be given to the assessee. These details or the TDS certificate should be starting point for the Assessing Officer to ascertain and verify the true and correct position. The Assessing Officer will be at liberty to get in touch with the TDS circle in case he requires clarification or confirmation. He is also at liberty to get in touch with deductor by issuing a notice and compelling him to upload the correct particulars/details. The said exercise must be and should be undertaken by the Revenue, i.e. the Assessing Officer as an assessee who suffers in such cases is not due to his fault and can justifiably feel deceived and defrauded.

The stand of the Revenue cannot be accepted that they can only write a letter to the deductor to persuade him to correct the uploaded entries or to upload the details. Power and authority of the Assessing Officer, cannot match and are not a substitute to the beseeching or imploring of an assessee to the deductor. If required and necessary, the income tax authorities can obtain prior approval from the Director or the Commissioner. The authorities can also examine whether general approval can be given. The said exercise is to be undertaken by the Assessing Officer while verifying or examining the return. Section 234E will also require similar verification by the Assessing Officer. In such cases, if required, order under Section 154 may also be passed. Circular No. 4 of 2012 will be equally applicable.

Patent Act

LD/61/84

Novartis AG
Vs.
Union of India
April 6, 2013 (SC)

Section 3 read with Section 2

of the Patents Act, 1970 – What are not Inventions

Where it was not shown as to how beta crystalline form of cancer drug Imatinib Mesylate will produce an enhanced or superior therapeutic efficacy on molecular basis than what could be achieved with already existing drug Imatinib free base, claim for patent for beta crystalline form of Imatinib Mesylate would only appear as an attempt to obtain patent for already existing drug Imatinib Mesylate

The following questions arose for consideration:

- What is the true import of section 3(d) of the Patents Act, 1970 (the Act)?
- How does it interplay with clauses (j) and (ja) of section 2(1)?
- Does the product for which the appellant claims patent qualify as a "new product" which comes by through an invention that has a feature that involves technical advance over the existing knowledge and that makes the invention "not obvious" to a person skilled in the art?
- In case the appellant's product satisfies the tests and thus qualifies as "invention" within the meaning of clauses (j) and (ja) of section 2(1), can its patentability still be questioned and denied on the ground that section 3(d) puts it out of the category of "invention"?

On the answer to these questions depends the answer to the question as to whether the appellant is entitled to get the patent for the beta crystalline form of a chemical compound called Imatinib Mesylate which is a therapeutic drug for chronic myeloid leukemia and certain kinds of tumours and is marketed under the names "Glivec" or "Gleevec".

The Supreme Court held as follows:

In case of chemicals and especially pharmaceuticals, even if the product for which patent protection is claimed is a new form of a known substance with known efficacy, even then the subject product must pass, in addition to clauses (j) "invention" and (ja) "inventive step" of section 2(1), the test of enhanced efficacy as provided in section 3(d) read with its *explanation*.

The patent applicants have to meet the standard of Section 3(d) before they can get patents under the Indian law.

On a combined reading of causes (j), (ac) and (ja) of section 2(1), in order to qualify as "invention", a product must satisfy the following tests: (i) It must be "new"; (ii) It must be "capable of being made or used in an industry" (iii) It must come into being as a result of an invention which has a feature that: (a) entails technical advance over existing knowledge; or (b) has an economic significance And (c) makes the invention not obvious to a person skilled in the art.

The Act, dealt with "invention" and "patentability" as two distinctly separate concepts. For grant of patent the subject must satisfy the twin tests of "invention" and "patentability".

Something may be an "invention" as the term is generally understood and yet it may not qualify as an "invention" for the purposes of the Act. Further, something may even qualify as an "invention" as defined under the Act and yet may be denied patent for other larger considerations as may be stipulated in the Act.

The amended portion of section 3(d) clearly sets up a second tier of qualifying standards for chemical substances/pharmaceutical products in order to leave the door open for true and genuine inventions but, at the same time, to check any attempt at repetitive patenting or extension of the patent term on spurious grounds.

The drug Gleevec directly emanates from the Zimmermann patent and comes to the market for commercial sale. Since the grant of the Zimmermann patent, the appellant has maintained that Gleevec (that is, Imatinib Mesylate) is part of the Zimmermann patent. It obtained drug approval for Gleevec on that basis. It claimed extension of the term of the Zimmermann patent for the period of regulatory review for Gleevec, and it successfully stopped another pharma company NATCO Pharma Ltd. from marketing its drug in the UK on the basis of the Zimmermann patent. Not only the appellant but the US Board of Patent Appeals, in its judgment granting patent for beta crystalline form of Imatinib Mesylate, proceeded on the basis that though the beta crystal form might not have been covered by the Zimmermann patent, the Zimmermann patent had the teaching for the making of Imatinib Mesylate from Imatinib, and for its use in a pharmacological compositions for treating tumours or in a method of treating warmblooded animals suffering from a tumoral disease. This finding was recorded by the US Board of Patent Appeals, in the case of the appellant itself, on the very same issue that is now under consideration. The appellant is, therefore, fully bound by the finding and cannot be heard to take any contrary plea.

From the published articles in medical journals also Imatinib Mesylate cannot be said to be a new product, having come into being through an "invention" that has a feature that involves technical advance over the existing knowledge and that would make the invention not obvious to a person skilled in the art. Imatinib Mesylate is all there in the Zimmermann patent. It is a known substance from the Zimmermann patent.

That Imatinib Mesylate is fully part of the Zimmermann patent is also borne out from another circumstance. It may be noted that after the Zimmermann patent, the appellant applied for, and in several cases obtained patent in the US not only for the beta and alpha crystalline forms of Imatinib Mesylate, but also for Imatinib in a number of different forms. The appellant, however, never asked for any patent for Imatinib Mesylate in non-crystalline form, for the simple reason that it had always maintained that Imatinib Mesylate is fully a part of the Zimmermann patent and does not call for any separate patent.

Thus, there is no force in the submission that the development of Imatinib Mesylate from Imatinib is outside the Zimmermann patent and constitutes an invention as understood in the law of patent in India.

In light of the discussions made above, the appellant's case that Imatinib Mesylate is a new product and the outcome of an invention beyond the Zimmermann patent is to be firmly rejected. Imatinib Mesylate is a known substance from the Zimmermann patent itself. Not only is Imatinib Mesylate known as a substance in the Zimmermann patent, but its pharmacological properties are also known in the Zimmermann patent and in the article published in the *Cancer Research* journal. The consequential finding, therefore, is that Imatinib Mesylate does not qualify the test of "invention" as laid down in section 2(1)(j) and section 2(1)(ja).

The subject product, that is, beta crystalline form of Imatinib Mesylate, is thus clearly a new form of a known substance, i.e., Imatinib Mesylate, of which the efficacy was well known. It, therefore, fully attracts section 3(d) and must be shown to satisfy the substantive provision and the *explanation* appended to it.

All the pharmacological properties of beta crystalline form of Imatinib Mesylate are equally possessed by Imatinib in free base form or its salt, there is no question of the subject product having any enhanced efficacy over the known substance of which it is a new form?.

It may also be stated here that while going through the Zimmermann patent one cannot but feel that it relates to some very serious, important and valuable researches. The subject patent application, on the other hand, appears to be a loosely assembled, cut-and paste job, drawing heavily upon the Zimmermann patent.

On going through the subject application, the impression one gets is that the beta crystalline form of Imatinib Mesylate is derived directly from Imatinib free base. This may, perhaps, be because once the beta crystalline form of the methanesulfonic acid salt of Imatinib came into being, the Imatinib free base got seeded with the nuclei of Imatinib Mesylate beta crystalline form and, as a result, starting from Imatinib one would inevitably arrive directly at the beta crystalline form of Imatinib Mesylate. But all this is nowhere said in the subject application.

The physical properties of the Free Base and imatinib mesylate differ in that the Free Base is only very slightly soluble in water while imatinib mesylate is very soluble in water. That being the position, the appellant was obliged to show the enhanced efficacy of the beta crystalline form of Imatinib Mesylate over Imatinib Mesylate (non-crystalline).

There is, however, no material to make any comparison of efficacy, or even solubility, between the beta crystalline form of Imatinib Mesylate and Imatinib Mesylate (non-crystalline).

In whatever way therapeutic efficacy may be interpreted, this much is absolutely clear: that the physico-chemical properties of beta crystalline form of Imatinib Mesylate, namely (i) more beneficial flow properties, (ii) better thermodynamic stability, and (iii) lower hygroscopicity, may be otherwise beneficial but these properties cannot even be taken into account for the purpose of the test of section 3(d), since these properties have nothing to do with therapeutic efficacy.

In whichever way section 3(d) may be viewed, whether as setting up the standards of “patentability” or as an extension of the definition of “invention”, it must be held that on the basis of the materials brought before this Court, the subject product, that is, the beta crystalline form of Imatinib Mesylate, fails the test of section 3(d), too, of the Act.

The subject product, the beta crystalline form of Imatinib Mesylate, does not qualify the test of Section 3(d) but that is not to say that Section 3(d) bars patent

The Institute of Chartered Accountants of India

(Set up by an Act of Parliament)

Industrial Training

CA Regulations, 1988 provide scope for Industrial Training as a part of CA Course curriculum facilitating articled assistants real life exposure in office workings at industry and service organizations in order to develop their professional acumen. On account of Industrial Training ICAI produces highly trained and accustomed professionals as per specific needs of Industry and Service Organizations.

The period of Industrial Training may range between nine months to twelve months during last year of the prescribed period of Practical Training under CA Course and can be given to an articled assistant who have completed Intermediate (Integrated Professional Competence) Examination/Intermediate (Professional Competence) Examination/Professional Education (Examination-II)/ Intermediate Examination of the Institute.

For the purpose, a financial, commercial, industrial undertakings and Organization fulfilling eligibility requirements of the Service Sector including Government Department (please see eligibility details on Institute website) may get registered with the regional offices of ICAI for imparting Industrial Training to CA Course students. A serving CA employee in such organization can impart Industrial Training upon eligibility depending on total period of service with the organization.

Interested Organizations / Members serving in such organizations are requested to apply to ICAI along with copy of Organizational Profile and list of Chartered Accountant(s) serving with them. Detailed information and prescribed application forms are available on ICAI website www.icai.org as well as may be obtained from concerned regional offices of ICAI.

protection for all incremental inventions of chemical and pharmaceutical substances. It will be a grave mistake to read this judgment to mean that section 3(d) was amended with the intent to undo the fundamental change brought in the patent regime by deletion of section 5 from the Parent Act. That is not said in this judgment.

Section 2(1)(j) defines "invention" to mean, "a new product or …", but the new product in chemicals and especially pharmaceuticals may not necessarily mean something altogether new or completely unfamiliar or strange or not existing before. It may mean something "different from a recent previous" or "one regarded as better than what went before" or "in addition to another or others of the same kind"1. However, in case of chemicals and especially pharmaceuticals if the product for which patent protection is claimed is a new form of a known substance with known efficacy, then the subject product must pass, in addition to clauses (j) and (ja) of section 2(1), the test of enhanced efficacy as provided in section 3(d) read with its explanation.

In the US, the drug Gleevec came to the market in 2001. It is beyond doubt that what was marketed then was Imatinib Mesylate and not the subject product, Imatinib Mesylate in beta crystal form. It is also seen above that even while the appellant's application for grant of patent lay in the "mailbox" awaiting amendments in the law of patent in India, the appellant was granted Exclusive Marketing Rights on November 10, 2003, following which Gleevec was marketed in India as well. On its package1, the drug was described as "Imatinib Mesylate Tablets 100 mg" and it was further stated that "each film coated tablet contains: 100 mg Imatinib (as Mesylate)". On the package there is no reference at all to Imatinib Mesylate in beta crystalline form. What appears, therefore, is that what was sold as Gleevec was Imatinib Mesylate and not the subject product, the beta crystalline form of Imatinib Mesylate.

If that be so, then the case of the appellant appears in rather poor light and the claim for patent for beta crystalline form of Imatinib Mesylate would only appear as an attempt to obtain patent for Imatinib Mesylate, which would otherwise not be permissible in this country.

In view of the findings that the patent product, the beta crystalline form of Imatinib Mesylate, fails in both the tests of invention and patentability as provided under clauses (j), (ja) of section 2(1) and section 3(d) respectively. ■

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. You are requested to please submit your feedback and suggestions on the column at **eboard@icai.org**.

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

A. Notifications

1. Amendment in Notification No. SO 2685(E), dated 6-11-2012 relating to Specified companies authorised to issue tax-free, secured, redeemable, Non-convertible bonds during F.Y.2012-13 for the purpose of exemption of interest under section 10(15)(h)(iv)

Notification No. 46/2012 dated 6-11-2012 authorised certain specified companies to issue tax-free, secured, redeemable, Non-convertible bonds during F.Y. 2012-13 subject to certain specified conditions. Amongst other requirements, one of the conditions was that the issue size for the purpose of private placement of such bonds shall be limited to five hundred crores for each tranche. The Central Government has, through this notification omitted this condition. The said notification shall take effect from its date of publication in the Official Gazette.

[Notification No. 23/2013 dated 22-3-2013]

2. Double taxation Agreement – Agreement for exchange of Information with respect to taxes with Gibraltar

In exercise of the powers conferred by section 90 of the Income-tax Act, 1961, the Central Government has through this notification directed that all the provisions of the Agreement between the Government of the Republic of India and the Government of Gibraltar for the exchange of information with respect to taxes shall be given effect to in the Union of India with effect from 11th March, 2013.

[Notification No. 28/2013 dated 1-4-2013]

The details of the said notification can be downloaded from the link below: http://www.taxmann.com/directtaxlaws/topstories/104010000000040077/india-gibraltar-tiea-is-effective-from-march-11-2013.aspx

3. Second Protocol for amending the Agreement for avoidance of double taxation and prevention of fiscal evasion with UAE

In exercise of the powers conferred by section 90 of the Income-tax Act, 1961, the Central Government has signed the second protocol for amending the agreement between the Government of the Republic of India and the Government of the United Arab Emirates for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital. The said protocol shall be given effect to in the Union of India with effect from the 12th day of March, 2013.

[Notification No. 29/2013 dated 12-4-2013]

The details of the said notifications can be downloaded from the link below: http://www.taxmann.com/servicetaxlaws/topstories/104010000000040111/protocol-amending-the-india-united-arab-emirates-dtaa-to-be-effective-from-march-12-2013.aspx

B. Circulars

1. Clarification regarding computation of Arm's Length Price by application of Profit Split Method

In anticipation of the need of a clarification for selection of profit split method (PSM) as most appropriate method, the Central Board of Direct Taxes has issued this circular. The Central Board of Direct Taxes has, through this circular, clarified certain points which may be kept in mind while selecting Profit Split method as the most appropriate method.

[Circular No. 2/2013 dated 26-03-2013]

2. Clarification on functional profile of development centres engaged in contract R&D services with insignificant risk with regard to conditions relevant to identify such development centres

In order to clarify and settle the divergent views amongst the field officers and the assessees regarding functional profile of development centres engaged in contract R&D services with insignificant risk for the purposes of transfer pricing audit, the Central Board of Direct Taxes has issued this circular. The CBDT has through this circular clarified that a development centre in India may be treated as a contract R&D service provider with insignificant risk provided the conditions specified by it in this circular are cumulatively complied with.

[Circular No. 3/2013 dated 26-3-2013]

The details of the said circulars can be downloaded from the link below: http://law.incometaxindia.gov.in/DIT/Notifications.aspx

C. Press Releases

1. An agreement and a Protocol between India and Malta for avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income

In order to bring the agreement between India and Malta in line with international standards, change in domestic laws and changed economic scenario, India and Malta have signed the new Double Taxation Avoidance Agreement (DTAA) at Valetta, Malta on 8th April, 2013 for avoidance of double taxation and for the prevention of fiscal evasion with respect to taxes on income.

[Press Release, dated 15-4-2013]

The complete details of the text of the Press release can be downloaded from the link: http://www.taxmann.com/topstories/104010000000040113/india-malta-inks-new-dtaa.aspx

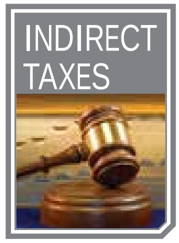
D. Letters

1. Procedure prescribed under section 245 to be followed for set off of Refunds against tax remaining payable

The said letter provides that as per the directions of Hon'ble Delhi High Court order dated 14-3-2013, the Department is required to follow the procedure prescribed under section 245 before making any adjustment of refund payable by CPC, Bengaluru. Accordingly, the assessee will be given an opportunity to file response to the Assessing Officer. The Assessing Officer, after examining the reply, will communicate his findings to CPC, Bangaluru, for processing the refund and adjusting the demand, if any.

[Letter dated 21-3-2013]

The complete details of the text of the Letter can be downloaded from the link: http://www.taxmann.com/topstories/104010000000040038/it-respite-to-taxpayers-aos-to-follow-mandamuses-of-delhi-hc-before-making-adjustment-of-refund.aspx



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

A. Service Tax

1. Erection of pandal or shamiana is liable to service tax - CBEC clarifies

The Central Board of Excise and Customs has clarified that the activity of providing pandal and shamiana along with erection thereof and other incidental activities is a declared service [section 66E(f)] liable to service tax and not deemed sale involving "transfer of right to use goods".

The Board has explained that such an activity is a service of preparation of a place to hold a function or event as the effective possession and control over the pandal or shamiana remains with the service provider, even after the erection is complete and the specially made-up space for temporary use handed over to the customer.

[Circular No. 168/3/2013 ST dated 15.04.2013]

2. Due date for filing ST-3 Return for the period July-Sept'12 extended till 30th April, 2013

Due date for filing of service tax returns in Form ST-3 for the period 1st July, 2012 to 30th September 2012 was extended from 15th April, 2013 to 30th April, 2013.

Considering the difficulties in filing returns, causing inconvenience to the assessee, the CBEC had revised the due date of filing ST-3 Return.

[Order No. 02/2013 ST dated 12.04.2013]

B. Excise

1. Installing new plant and machinery at a distant plot cannot be construed as expansion of existing unit for the purpose of area-based exemption from excise duty

Notification Nos. 49/2003 and 50/2003 both *dated 10.06.2003* provide area based exemption from the excise duty. *Circular No. 960/03/2012-CX dated 17.02.2012* clarified that exemption would continue to be available for the residual period of exemption, if an exempted unit acquires adjacent plot of land and installs new plant and machinery on such land. Such an expansion was considered as akin to expansion by way of installing new plant and machinery inside the existing plot/premises.

It has been further clarified that term 'adjacent' used in the above mentioned circular would **not** include a plot which is at some distance away from the exempted unit. In other words, exemption would continue to be available only when the exempted unit undertakes expansion by acquiring the adjoining plot with **at least one common boundary** with the exempted (existing) unit and the same is merged to make it one unit.

[Circular No.968/02/2013-CX dated 01.04.2013]

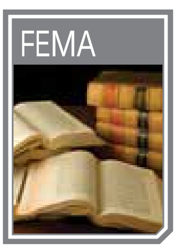
2. New Forms for filing appeal to CESTAT

CBEC has revised the forms for filing appeal in the CESTAT. Amended new forms for Central Excise (E.A.-3, E.A.-4, E.A.-5), Customs (C.A.-3, C.A.-4, C.A.-5) and Service Tax (S.T.-5, S.T.-6, S.T.-7) have been notified vide *Notification Nos. 6/2013-CX (N.T.), 37/2013-Cus (N.T.) and 5/2013-ST, all dated 10.04.2013* respectively. These forms have been made effective from 01.06.2013 though they would be optional till 31.08.2013. Therefore, all appeals filed in the Tribunal on or after 01.09.2013 would be in the new form being prescribed.

These forms have been revised to ensure quick disposal of cases. Additional information sought would lead to faster communication between the Tribunal Registry and the appellant, bunching of cases and would also facilitate creation of a comprehensive database.

[Circular No. 969/03/2013-CX dated 11.04.2013]

The text of the above notification/circulars is available at www.cbec.gov.in



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

A. Simplification of procedure for "Write-off" of unrealised export bills

A.P. (DIR Series) Circular No.88 dated March 12, 2013

With a view to further simplifying and liberalizing the procedure and for providing greater flexibility to all exporters as well as the Authorised Dealer banks, RBI has decided to effect, subject to the stipulations regarding surrender of incentives prior to "write-off" adduced in the A.P. (DIR Series) Circular No. 03 dated 22 July 2010, the following liberalization in the limits of "write-offs" of unrealised export bills:

a) Self "write-off" by an exporter (Other than Status Holder Exporter -5%*

b) Self "write-off" by Status Holder Exporters -10%*

c) "Write-off" by Authorised Dealer bank -10%*

*of the total export proceeds realised during the previous calendar year.

The above limits will be related to total export proceeds realised during the previous calendar year and will be cumulatively available in a year. The above "write-off" will be subject to the following conditions:

(i) The relevant amount has remained outstanding for more than one year;

(ii) Satisfactory documentary evidence is furnished in support of the exporter having made all efforts to realize the dues;

(iii) The case falls under any of the categories specified in the circular.

(iv) The exporter has surrendered proportionate export incentives (for the cases not covered under A. P. (DIR. Series) Circular No.03 dated July 22, 2010), if any, availed of in respect of the relative shipments. The AD Category – I banks should obtain documents evidencing surrender of export incentives availed of before permitting the relevant bills to be written-off.

(v) In case of self write-off, the exporter should submit to the concerned AD bank, a Chartered Accountant's certificate, indicating the export realization in the preceding calendar year and also the amount of write-off already availed of during the year, if any, the relevant GR/SDF Nos. to be written off, Bill No., invoice value, commodity exported, country of export. The CA certificate may also indicate that the export benefits, if any, availed of by the exporter have been surrendered.

However, the following would not qualify for the "write off" facility:

a) Exports made to countries with externalization problem.

b) GR/SDF forms which are under investigation by agencies like, Enforcement Directorate, Directorate of Revenue Intelligence, Central Bureau of Investigation, etc. as also the outstanding bills which are subject matter of civil/criminal suit.

The respective AD banks may forward a statement in form EBW, in the enclosed format, to the Regional Office of Reserve Bank under whose jurisdiction they are functioning, indicating details of write-offs allowed under this circular.

AD banks are advised to put in place a system under which their internal inspectors or auditors (including external auditors appointed by authorised dealers) should carry out random sample check/percentage check of "write-off" outstanding export bills.

Cases not covered by the above instructions/ beyond the above limits, may be referred to the concerned Regional Office of Reserve Bank of India.

B. Revision in Money Transfer Service Scheme (MTSS) Guidelines

A.P. (DIR Series) Circular No.89 dated March 12, 2013

RBI has revised MTSS guidelines applicable to all Authorised Persons who are Indian Agents under MTSS, in consultation with the Government of India. The revised MTSS Guidelines is available on RBI website at: http://rbi.org.in/scripts/NotificationUser.aspx?Id=7887&Mode=0

These guidelines would also be applicable mutatis mutandis to all Sub Agents of the Indian Agents under MTSS and it will be the sole responsibility of the APs (Indian Agents) to ensure that their Sub Agents also adhere to these guidelines.

C. Maintenance of Collateral by Foreign Institutional Investors (FIIs) for transactions in the cash and F & O segments

A.P. (DIR Series) Circular No.90 dated March 14, 2013

RBI has, in consultation with the Government of India and the Securities and Exchange Board of India (SEBI), permitted FIIs to use, in addition to already permitted collaterals, their investments in corporate bonds as collateral in the cash segment and government securities and corporate bonds as collaterals in the F&O segment.

With the proposed changes coming into effect, henceforth, FIIs will be eligible to offer government securities/corporate bonds (acquired by FIIs in accordance with provisions of Schedule 5 to Notification No. FEMA 20 dated May 3, 2000), cash and foreign sovereign securities with AAA ratings in both cash and F & O segments.

D. Foreign investment in India by SEBI registered FIIs in Government Securities and Corporate Debt

A.P. (DIR Series) Circular No.94 dated April 1, 2013

RBI had, vide A.P. (DIR Series) Circular No.80 dated January 24, 2013 revised the limit for investments by FIIs and long term investors in Government securities to USD 25 billion and for corporate debt to USD 51 billion (including sub-limit of USD 25 billion each for bonds of infrastructure sector and non-infrastructure sector and USD 1 billion for QFIs in non-infrastructure sector).

In order to simplify the existing limits, RBI has now decided to merge the existing debt limits into two broad categories as under:

(i) ***Government Debt limit:*** Government securities of USD 25 billion by merging the existing sub-limits under Government securities [(a)USD 10 billion for investment by FIIs in Government securities including Treasury Bills and (b) USD 15 billion for investment In Government dated securities by FIIs and long term investors]; and

(ii) ***Corporate Debt Limit:*** Corporate debt of USD 51 billion by merging the existing sub-limits of Corporate debt [(a) USD 1 billion for Qualified Foreign Investors (QFIs), (b) USD 25 billon for investment by FIIs and long term investors in non-infrastructure sector and (c) USD 25 billion for investment by FIIs/QFIs/long term investors in infrastructure sector].

Revised position is summarised below:

Instrument/s	Limit	Eligible Investor	Remarks
Government securities including Treasury Bills	USD 25 billion	FIIs, QFIs and Long terms investors registered with SEBI – Sovereign Wealth Funds (SWFs), Multilateral Agencies, Pension/ Insurance/ Endowment Funds, Foreign Central Banks	Eligible Investors may invest in Treasury Bills only upto USD 5.5 billion within the limit of USD 25 billion
Eligible instruments as referred to in Schedule 5 of Notification No. FEMA 20/2000-RB dated 3rd May 2000	USD 51 billion	FIIs, QFIs, Long terms investors registered with SEBI - SWFs, Multilateral Agencies, Pension/ Insurance/ Endowment Funds, Foreign Central Banks	Eligible Investors may invest in Commercial Papers only upto USD 3.5 billion within the limit of USD 51 billion

The Non-Resident Indians were not subject to any limit for investment in Government Securities as well as corporate debt. They will continue to be regulated as per extant guidelines.

The above changes will come into effect from April 1, 2013. The operational guidelines in this regard will be issued by SEBI.

E. Review of all-in-cost ceiling for Trade Credits for imports into India

A.P. (DIR Series) Circular No. 98 dated April 9, 2013

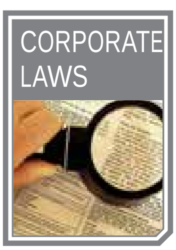
RBI had revised the all-in-cost ceiling for trade credits for imports into India vide A. P. (DIR Series) Circular No. 44 dated November 15, 2011 which was applicable upto March 31, 2012. This said limit was extended till September 30, 2012 vide A.P. (DIR Series) Circular No.100 dated March 30, 2012 and further till March 31, 2013 vide A.P. (DIR Series) Circular No.58 dated December 14, 2012. It has now been decided to continue the said all-in-cost ceiling till June 30, 2013 subject to review thereafter.

F. Consolidated Foreign Direct Investment (FDI) Policy effective from April 5, 2013

Circular 1 of 2013 dated April 05, 2013

The Department of Industrial Policy and Promotion (DIPP) has, on April 05, 2013 issued Consolidated FDI Policy - Circular 1 of 2013 which is effective from April 05, 2012. This circular subsumes and supersedes all Press Notes/Press Releases/Clarifications/Circulars issued by DIPP, which were in force as on April 04, 2013, and reflects the FDI Policy as on April 05, 2013.

The circular is available on DIPP's website at: http://dipp.nic.in/English/Policies/FDI_Circular_01_2013.pdf



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

MCA (www.mca.gov.in)

1. Amendment to Companies DIN Rules on Cancellation or Deactivation of DIN

The MCA has issued Notification No. F. No. 5/80/2012-CL V dtd. 15.03.2013 amending the Companies (Directors Identification Number) Rules, 2006 by inserting rule 8 whereby now the Central Government or the Regional Director (Northern Region), Noida or any officer authorised by the Regional Director, upon being satisfied on verification of particulars of proof attached with the application received from any person seeking cancellation or deactivation of DIN, in case (a) the DIN is found to be duplicate, (b) the DIN was obtained by wrongful manner or fraudulent means, (c) of the death of the concerned individual, (d) the concerned individual has been declared as lunatic by the competent Court, (e) if the concerned individual has been adjudicated an insolvent, then the allotted DIN shall be cancelled or deactivated by the respective authority. It is also stated that before cancellation or deactivation of DIN under clause (b), an opportunity of being heard shall be given to the concerned individual. The amendment also defines the "wrongful manner" to mean if the DIN obtained without legally established documents. The term "fraudulent means" is also defined to mean if the DIN obtained unlawfully to deceive any other person or any authority including the Central Government. One may refer to the above citation for further details.

2. Relaxation of Additional Fees and Extension of Last Date in Filing of various Forms

The MCA has issued Circular No. 07/2013 on 20.03.2013 extending the the time limit for filing and relaxation of additional fee on forms has been extended till 31-03-2013. It is explained that where the due date was falling before 17-01-2013, however, additional fee increased due to non-filing of documents between 17-01-2013 and 28-02-2013 (both days inclusive). The affirmative step based on the ticket raised by ROC and the additional fee mentioned therein, will be :

- Change of additional fee applicable against respective SRN in the database;
- Regeneration of challan with revised additional fee;
- Extension of validity period of the challan till 7 days from the date of change;
- Sending an e-mail along with challan to the user requesting him to pay the amount as per the revised challan. (User may also download the challan from FO Portal)

It is also explained that where all the documents which have expired on or after 17-01-2013 due to non-submission/re-submission, the PUCL (pending for user clarification) will be restored back. The validity of tickets raised till 24-3-2013 will be entertained and users will be given the time to file the documents within seven days of intimation to user. In case of failure to file the form within seven days, the form will be marked as NTBR and no further relaxation will be granted. It is also clarified that fee payable for forms on/till 16-01-2013 will remain payable along with additional fee and relaxation of any additional fee will be considered for forms on or after 17-01-2013. One may refer to the above citation for further details.

After issuance of this Circular, the MCA issued Circular No. 08/2013 on 10.04.2013 extending the time limit for filing and relaxation of additional fee on forms has been extended till 15-04-2013. It is clarified that fee payable for forms on/till 16-01-2013 will remain payable along with additional fee and relaxation of any additional fee will be considered for forms on or after 17-01-2013. One may refer to the above citation for further details.

3. Amendment to Companies (Acceptance of Deposits) Rules, 1975

The MCA has issued Notification No. F.NO. 11/2/2012-CL-V-(A) dated 21-03-2013 amending the Companies (Acceptance of Deposits) Rules, 1975 to align it with the Revised Schedule VI requirements. The definition of 'deposit' is amended to exclude any amount raised by the issue of bonds or debentures secured by the mortgage of any fixed assets referred to in Schedule VI of the Act (earlier immovable property was referred) excluding intangible assets of the company or with an option to convert them into shares in the company. In the case of such bonds or debentures secured by the mortgage of any fixed assets referred to in Schedule VI of the Act excluding intangible assets, the amount of such bonds or debentures shall not exceed the market value of such fixedassets. For defaults in acceptance or refund of deposits to be cognizable, complaints can be made by the Regional Director or the Registrar of Companies or any other officer of the Central Government under sub-section (2) of the section 58AAA of the Act (earlier only Regional Director was allowed. One may refer to the above citation for further details.

SEBI (www.sebi.gov.in)

1. Sharing of Information regarding Issuer Companies between Debenture Trustees and Credit Rating Agencies

The SEBI has issued General Circular No. CIR/MIRSD/3/2013 on 15.03.2013 stating that presently the SEBI (Debenture Trustee) Regulations, 1993 require the Debenture Trustees (DTs) provide for sharing of information regarding the issuer company clients with Credit Rating Agencies (CRAs) so as to enable CRAs to perform their obligations effectively. The DTs have expressed the need to receive relevant information on issuer companies from CRAs and hence in consultation with DTs and CRAs, SEBI has now required that registered DTs and CRAs shall share information with each other as specified in the Annexure to this circular. DTs and CRAs may share any other information from time to time in respect of issues/issuer companies which would help them in effective discharge of their duties. The DTs and CRAs shall assign designated email addresses for sending and receiving such information and ensure appropriate action, if any, based on the information received. One may refer to the above citation for further details and the annexure which details the inter se sharing of information between DTs and CRAs.

2. Product Labeling in Mutual Funds

The SEBI has issued Circular No. CIR/IMD/DF/5/2013 dtd. 18-03-2013 so as to address the issue of mis-selling and for which purpose the Committee set up to examine the system of Product Labeling to provide investors an easy understanding of the kind of product/scheme they are investing in and its suitability to them, has issued its recommendations which are accepted. Now, all mutual funds shall 'Label' their schemes on the parameters as mentioned under:

- Nature of scheme such as to create wealth or provide regular income in an indicative time horizon (short/ medium/ long term).
- A brief about the investment objective (in a single line sentence) followed by kind of product in which investor is investing (Equity/Debt).
- Level of risk, depicted by colour code boxes as under:
  - Blue – principal at low risk.
  - Yellow – principal at medium risk.
  - Brown – principal at high risk.
- The colour codes shall also be described in text beside the colour code box.
- A disclaimer that investors should consult their financial advisers if they are not clear about the suitability of the product.
- Few samples of product label for different schemes are illustrated at Annexure I.

The product label shall be disclosed on the front page of initial offering application forms, Key Information Memorandum (KIM) and Scheme Information Documents (SIDs), and on the common application form – along with the information about the scheme. The product label shall be placed in proximity to the caption of the scheme and shall be prominently visible. This circular shall be applicable with effect from 1 July, 2013, to all the existing schemes and all schemes to be launched on or thereafter. However, mutual funds may choose to adopt the provisions of this circular before the effective date. One may refer to the detailed requirements provided in the above Circular.

3. FIIs permitted to offer Corporate bonds and Government securities as collateral

The SEBI has issued Circular No. CIR/MRD/DRMNP/9/2013 on 20-03-2013 stating that currently FIIs are permitted to offer, as collateral, cash and foreign sovereign securities with AAA rating in F&O segment and cash, foreign sovereign securities with AAA rating and government securities in cash segment. Based on the Finance Minister's statement during his speech for the Union Budget for 2013-14, to permit FIIs to use their investment in corporate bonds and Government securities as collateral to meet their margin requirements towards their transactions on the recognized Stock Exchanges in India, the RBI had permitted FIIs to use, in addition to already permitted collaterals, their investment in corporate bonds as collateral in the cash segment and government securities and corporate bonds as collaterals in the F & O segment. SEBI has now clarified that henceforth FIIs will be permitted to offer collaterals relating to government securities, corporate bonds, cash and foreign sovereign securities with AAA ratings, for their transactions in both cash and F&O segments. In this regard, the stipulations specified by SEBI and RBI with regard to the acceptance of various collaterals shall be adhered to. It is also clarified that clearing corporations while enabling the framework for acceptance of corporate bonds as collateral for transactions of any entity in the cash and F&O segments, shall ensure that the bonds shall have a rating of AA or above (or with similar rating nomenclature) by recognised credit rating agencies and shall be in dematerialized form. The bonds shall be treated as part of the non-cash component of the liquid assets of the clearing member and shall not exceed 10% of the total liquid assets of the clearing member.

Also, the bonds shall have a fixed percentage based or VaR based haircut. A higher haircut may be considered to cover the expected time frame for liquidation. To begin with the haircut shall be a minimum of 10%. One may refer to the above citation for further details.

4. Usage of Electronic Payment Modes for Making Cash Payments to the Investors

The SEBI has issued Circular No. MRD/DP/10/2013 dated 21-03-2013 relating to usage of ECS (Electronic Clearing Services) facility and warrants for distribution of dividends or other cash benefits to the investors. Based on the advancements in the field of electronic payment systems in the last decade which has made available various other modes of electronic funds transfer viz. National Electronic Funds Transfer (NEFT), Real Time Gross Settlement (RTGS), etc., it has been decided to modify the framework as under :

- For making cash payments to investors, companies whose securities are listed on the stock exchanges shall use, either directly or through their RTI & STA, any RBI approved electronic mode of payment such as ECS [LECS (Local ECS)/RECS (Regional ECS)/NECS (National ECS)], NEFT, etc.
- In order to enable usage of electronic payment instruments, companies whose securities are listed on the stock exchanges (or their RTI & STA) shall maintain requisite bank details of their investors. For investors that hold securities in demat mode, companies shall seek relevant bank details from the depositories. For investors that hold physical share/debenture certificates, companies or their RTI & STA shall take necessary steps to maintain updated bank details of the investors at its end.
- In cases where either the bank details such as MICR (Magnetic Ink Character Recognition), IFSC (Indian Financial System Code), etc. that are required for making electronic payment are not available or the electronic payment instructions have failed or have been rejected by the bank, companies or their RTI & STA may use physical payment instruments for making cash payments to the investors. Companies shall mandatorily print the bank account details of the investors on such payment instruments.

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

5. Amendment to SEBI Takeover Regulations tightening open offers by promoters

The SEBI has issued Notification No. LAD-NRO/GN/2012-13/36/7368 dated 26-03-2013 stating that a public announcement for a proposed acquisition of shares or voting rights in or control over the target company shall be made on the date of first acquisition, provided the acquirer discloses in the public announcement the details of the proposed subsequent acquisition which can be through a combination of an agreement and any one or more modes of acquisition. Hence, the relevant date for making the public announcement and determination of offer price would be the earliest date on which obligations are triggered. SEBI has also stated that an acquirer may acquire shares of the target company through preferential issue or through the stock exchange settlement process, other than through bulk deals or block deals, subject to such shares being kept in an escrow account and the acquirer not exercising any voting rights over such shares kept in the escrow account. SEBI has also stated that an acquirer shall not withdraw an open offer pursuant to a public announcement even if the proposed acquisition through the preferential issue is not successful. SEBI has also stated that any entity or person acting in concert that holds more than five per cent shares or voting rights in a target company, is required to disclose this even if such change results in shareholding falling below five per cent if there has beenchange in such holdings from the last disclosure made and such change exceeds two per cent of total shareholding or voting rights in the target company. One may refer to the above citation for further details.

6. Arbitration Mechanism through Stock Exchanges – Introduction of Common Pool and Automatic Process of selection of arbitrators

The SEBI has issued Press Release 34/2013 dated 04.04.2013 clarifying that based on inputs received from investors regarding functioning of arbitration mechanism at the stock exchanges, all stock exchanges having nation-wide trading terminals have been advised to pool the list of arbitrators and create a 'common pool', instead of having exchange-wise pools of arbitrators. This pooling of arbitrators is done centre-wise.The selection of arbitrators by stock exchanges as done currently, is now replaced by an 'automatic process'. In order to bring more transparency and fairness the 'automatic process' entails a randomized, computer generated selection of arbitrator, from the list of arbitrators in the 'common pool'. The 'automatic process' sends a system generated sms or email to all entities involved in the particular case. This process has come into effect from 1 April, 2013.Currently, arbitration facilities at Stock Exchanges with nation-wide trading terminals is available at 8 centres viz Ahmedabad, Chennai, Delhi, Hyderabad, Indore, Kanpur, Kolkata and Mumbai. It is intended to extend the arbitration facility to more cities during the course of the current financial year.One may refer to the above citation for further details. One may also refer to SEBI Circular No. CIR/MRD/ICC/ 8 /2013 dtd.18 March 2013 for more information.

RBI (www.rbi.gov.in)

1. Guidelines for Entry of core investment companies (CICs) into Insurance

The RBI has issued Circular No. RBI/2012-13/466/ DNBS(PD) CC.No.322/03.10.001/2012-13 dated 01-04-2013 stating that presently, NBFCs venturing into insurance are guided based on an earlier to NBFC Regulations which contains the 'Guidelines for entry of NBFCs into Insurance'. In view of the unique business model of CICs, RBI has now issued a separate set of guidelines for their entry into insurance business.While the eligibility criteria, in general, are similar to that for other NBFCs, no ceiling is being stipulated for CICs in their investment in an insurance joint venture. It is clarified that CICs cannot undertake insurance agency business. It is also clarified that CICs exempted from registration with RBI do not require prior approval provided they fulfil all the necessary conditions of exemption as provided under/ in the earlier RBI Circular of 5 January, 2011. Their investment in insurance joint venture would be guided by IRDA norms. The Guidelines are enclosed to this Circular for meticulous compliance. Some features of the guidelines are extracted below :

- Any CIC registered with RBI and which satisfies the eligibility criteria as per this Circular will be permitted to set up a joint venture company for undertaking insurance business with risk participation, subject to safeguards.
- The maximum equity contribution such a CIC can hold in the joint venture company will be as per IRDA approval.
- The eligibility criteria for joint venture participant will be as per the latest available audited balance sheet.
- The owned funds of the CICshall not be less than ₹500 crore;
- The level of net non-performing assets shall be not more than 1% of the total advances;
- TheCIC should have registered netprofit continuously for three consecutive years;
- The track record of the performance of the subsidiaries, if any, of the concerned CIC should be satisfactory;
- The CIC shall comply with all applicable regulations including CIC Directions, 2011. CICs-ND-SI are required to maintain adjusted net worth which shall be not less than 30% of aggregate risk weighted assets on balance sheet and risk adjusted value of off-balance sheet items.

One may refer to the above citation for further details and the detailed guidelines. ■

Companies Bill, 2012 – Facts and Emerging Impact

The new law has many facets bringing positive impact for integrating India Inc at par with World Inc. With the presence and emergence of vast international corporate entities vying to set up their units in India, it has addressed issues of transparency, shareholders' activism, corporate democracy, enhancing minority rights, ensuring accountability of the Board and to inculcate a sense that corporate houses are not only profit and wealth creation units but also socially responsible. The attempts of the Government in reshaping, tweaking and slimming the age old company law is a Bold and Golden step to place India on a global platform. This article overviews some of the sensitive changes made in relation to accounts and audit by way of its facts and emerging impact. Read on…

Dr. P. T. Giridharan

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The Company Law of a country is the epitome of economic growth, signifying and signaling how far the rules of a business game should be in sync with international best practices. Restructuring, reshaping and regulating such a business law of a country is a journey towards excellence with no destination. Compacting 32 Chapters into 27, Reducing 658 sections to 470 and Slimming from XVI Schedules into VII as a finer fit (if not a slim fit) of an aged law is an uphill task for the Government. The Companies Act, 1956, though amended 26 times, the time taken to get across the various stakeholders' table, tabling before the House of the Parliament and to get its passage has always been a pedaling hurdle. An illustrative amendment attempt that was taken way back in 2002 for constitution of National Company Law Tribunal (NCLT) resulted in only amendment in law and yet NCLT could not be formed. After the amendment in 2002, it was followed by the Companies Bill as 2008, 2009, 2011 and 2012. After 10 years, the Companies Bill, 2012 could see some light as it got the passage of the Lok Sabha on the night of 18th December, 2012 and is now awaiting the clearance by Rajya Sabha. The new law will be administered mostly by Rules. The words *'as may be prescribed'* has been used at 303 places in various provisions, where Rules have to be framed for around 180 sections and are yet to be open for public discussion. The new law has many facets bringing a positive impact for integrating India Inc at par with World Inc. With the presence and emergence of vast international corporate entities vying to set up their units in India, it has addressed issues of transparency, shareholders' activism, corporate democracy, enhancing minority rights, ensuring accountability of the Board and to inculcate a sense that corporate houses are not only profit and wealth creation units but also socially responsible. As many as 36 new definitions (see box) have been incorporated in the Bill and other 36 existing definitions have been modified. The attempts of the Government in reshaping, tweaking and slimming the age old company law is a Bold and Golden step to place India on a global platform.

New Definitions incorporated in Section 2 of the Bill, 2012

Associate company, Auditing standards, Authorised capital or nominal capital, Books of account, Called up capital, Charge, Chartered Accountant, Chief Executive Officer, Chief Financial Officer, Company Liquidator, Control, Cost Accountant, Expert, financial statement, Global depository receipt, Independent Director, Indian depository receipt, Issued capital, Key managerial personnel, Notification, One Person Company, Ordinary or Special Resolution, Paid-up Share Capital or share capital paid-up, Postal ballot, Promoter, Register of companies, Related party, Serious Fraud Investigation Office, Small company, Subscribed capital, Tribunal, Turnover, Unlimited company, Voting right, Whole-time director

Constitution of National Financial Reporting Authority – NFRA (Section 132)

The Bill, 2012 provides for the very first time constitution of a new authority, namely the National Financial Reporting Authority. The earlier Bills (of 2008, 2009) did not contain/mention/provision about NFRA. Even the Parliamentary Standing Committee on Finance which examined the Companies Bill is silent on the aspect. The terms of reference for NFRA are significantly different, setting a new tone and tenor for regulating accounting profession in India.

Terms of Reference for NFRA

- *Make recommendations to the Central Government on the formulation and laying down of accounting and auditing policies and standards for adoption by companies or class of companies or their auditors, as the case may be;*
- *Monitor and enforce the compliance with accounting standards and auditing standards in such manner as may be prescribed;*
- *Oversee the quality of service of the professions associated with ensuring compliance with such standards, and suggest measures required for improvement in quality of service and such other related matters as may be prescribed; and*
- *Perform such other functions relating to the above as may be prescribed.*

The National Financial Reporting Authority shall consist of a Chairman and such other 15 members consisting of part-time and full-time members. It is not mentioned as to the percentage of full-time and part-time members and their duties and responsibilities. The Chairperson and full time members are restricted to associate with any audit firm (including related consultancy firms) during the course of their term and two years after ceasing to hold such appointment. This is similar to restriction laid by the Competition Act 2002 on its Chairperson and other members for

Considering NFRA is a new set-up and is extending its arm's length towards accounting and auditing, one hopes that spirit of NFRA should enhance the Financial Regulatory system in India and 'Not For Regulating Accountant'. Clause 132 (4) is an non-obstante clause providing a bar on any other body or institute in initiating or continuing the proceedings in case of matters relating to misconduct as referred in the Chartered Accountants Act, 1949. It is to be seen as to how far these 'embargoes' on the powers of other institute/body already enacted under an Act of Parliament hold and behold the spirit of the accounting profession in India.

a period of two years from the date on which they cease to hold office, to accept any employment in any enterprise which has been a party to a proceeding before the Commission under the Act.

Powers of NFRA

- Power to investigate, either *suo moto* or on a reference made to it by the Central Government, for such class of bodies corporate or persons, in such manner as may be prescribed into the matters of professional or other misconduct (as referred in Section 22 of the Chartered Accountants Act, 1949) committed by any member or firm of chartered accountants, registered under the Chartered Accountants Act, 1949.
- Once NFRA initiates or continue any proceedings under the Act, no other institute or body shall initiate or continue any proceedings.
- NFRA shall have same powers as are vested in a Civil Court.
- Apart from imposing penalty it can debar the member or the firm from engaging himself or itself from practice as member of the Institute of Chartered Accountants of India for a minimum period of six months or for such higher period not exceeding ten years as may be decided by the National Financial Reporting Authority. Any person aggrieved by the order of NFRA can appeal before the Appellate Authority.

The constitution of NFRA poses certain concerns and issues:

- Is NFRA a replacement of National Advisory Committee on Accounting Standards (NACAS)?
- Is NFRA an autonomous and independent regulator?
- Clause 132 (4) is an *non-obstante* clause providing a bar on any other body or institute in initiating or continuing the proceedings in case of matters relating to misconduct as referred in the Chartered Accountants Act, 1949. It is to be seen as to how far this 'embargo' on the powers of other institute/body already enacted under an Act of Parliament hold and behold the spirit of the accounting profession in India.
- The structure and hierarchy of NFRA and the time limits within which it shall dispose of the investigation proceedings is not known.
- Considering NFRA is a new set-up and is extending its arm's length towards accounting and auditing, one hopes that the spirit of NFRA should enhance the Financial Regulatory system in India and 'Not For Regulating Accountant'.

Rotation of Auditors (Section 139)

The Bill provides for the system of rotation of auditors and audit firms. This is the first time in the history of company law in India that auditors shall be subject to rotation after certain specified number of years. Though rotation of auditors has not been an encouraging success internationally, in its wisdom and to restrict the lineage and linkage of relationship of the auditor and the auditee, the Bill provides that no listed companies or class of companies shall appoint or reappoint an individual as an auditor for more than one term of five consecutive years and audit firm as an auditor for more than two terms of five consecutive years. This is further subject to the provision that in case of audit firm, members may resolve to provide for such intervals of rotation for audit team and its partners and providing for audit by more than one auditor (joint auditor). The system of rotation of auditor and audit firm is to take effect retrospectively (as on the date on which the Act may come into force) and the period of office of auditor completed earlier will be taken into account in calculating the term of five and two terms of five years respectively for individual auditor and for the audit firm. A transition period of 3 years from the commencement of the Act has been prescribed for the companies existing on or before the commencement of the Act, to comply with the provisions relating to rotation of auditors/audit firm.

The issues relating to rotation are laudable and debatable for its efficacy and efficiency. On the one hand, it delinks the longer relationships of auditor vis-à-vis the auditee. On the other hand, it takes time for the new auditor to understand the business unit and its industry practices. An auditor should not only remain independent but be seen as independent. Does rotation bring independence? In a country where there are thousands of Small and Medium Practitioners, it is difficult to realign their proprietary into a firm for getting the scope of being auditor for two terms of five years.

Cap on Audit Assignments

The Bill disallows an auditor or an audit partner from auditing more than 20 companies. Earlier the limit was 30 excluding that of private companies. It is to be further seen from the Rules that whether private companies, small company, one-person company are excluded in calculating the prescribed limit of 20.

Removal of auditors (Section 140)

If the Tribunal on *suo moto* or an application from Central Government or any person concerned is satisfied that the auditor of a company has acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to the company or its directors or officers whether directly or indirectly, it can direct the company to change the auditor. Such auditor shall not be eligible for appointment as auditor for a period of 5 years against whom the order has been passed by the Tribunal and he shall also be liable for action under section 447 which deals with punishment for fraud. The liabilities will also extend in case of firm and that of every partner or partners.

Qualifications and Disqualifications of Auditors (Section 141)

In addition to the disqualifications provided in the existing Act, the Bill further provides that the auditor himself or his relative or partner shall not hold any security or is indebted or has provided any guarantee in the company or its holding or subsidiary or associate company except that the relative may hold security or interest in the company of face value not exceeding ₹1,000 or such sum as may be prescribed. Further it provides that a firm where majority of the partners practicing in India are qualified for appointment may be appointed by its firm name as auditor of the company. More than his qualifications as an auditor, he should be aware and beware that he knows who are all his relatives and the fact of their holdings in the companies in which he is appointed as an auditor.

Remuneration of Auditor (Section 142)

The remuneration of the auditor of a company shall be fixed in its general meeting or in such manner as may be determined. Such remuneration shall also include the expenses incurred by the auditor in connection with the audit of the company and also any facility extended to him.

Powers and Duties of Auditors (Section 143)

Apart from the powers that are already provided in the Act, 1956, the auditor in his report is to include any qualification, reservation, or adverse remark relating to the maintenance of accounts and other matters connected therewith and also to state whether the company has adequate internal financial control systems in place and its operating efficiency. Further, the auditor is required to provide reasons in the auditor's report for any negative remarks or with a qualification. Also any qualifications, observations or comments on financial transactions or matters which have adverse effect on the functioning of company mentioned in the auditor's report shall be read before the company at its general meeting. Further, auditor or his representative who shall also be qualified to be the auditor shall mandatorily attend all the general meetings of the company. The auditor is now required to comply with the auditing standards.

Penalty for Auditors for Contravention (Section 147)

The clause provides that in cases of contravention of appointment, powers, duties, services, signing of auditors report, the auditor shall be punishable with fine which shall not be less ₹25,000 and may extend to ₹5 lakh. In case of willful contravention and with intention to deceive the company/shareholders/creditors/tax authorities, he shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than ₹1 lakh and which may extend to ₹25 lakh or both. In case he contravenes the provisions relating to his powers and duties, rendering of services and attendance of meetings, the penalty shall be that he shall be required to refund the remuneration received from the company and to pay the damages to the company, statutory bodies, or authorities or to any person arising out of loss out of misleading or incorrect information.

The list of onerous duties and responsibilities of an auditor does not end. He is also expected to be a whistle-blower. Section 143(12) casts the duty on the auditor to report to CG any offence involving fraud committed against the company by officers or employees of the company. Further he is also subjected to class action suits.

The new Bill is going to change the way companies are incorporated, raise money, interact with stakeholders, govern themselves and contribute to nation-building. On the one hand, the Bill has brought out several new concepts and opens up various professional opportunities and on the other hand burdens the corporates and professionals with lots of duties and responsibilities. Nevertheless, the Bill, 2012 is expected to usher vistas and vision for the Indian corporate environment in line with the best international practices. The journey from 1956 to 2012 brought in several experiences and the law which was a goliath finally went into a gym for its trimming and slimming its size to turn India into a better place for global business. ■

Companies Bill 2012[1] With Respect to Chartered Accountants, Audits and Auditors

The Lok Sabha has passed the much awaited Companies Bill 2012 and the Bill, pending its passage in Rajya Sabha, is just two more steps away to be enacted as an Act of Parliament. There are many improvements in all areas which will be witnessed when the Act comes into force. Provisions related to Chartered Accountants, Audits and Auditors have undergone many changes when compared to the existing Companies Act, 1956. In order to strengthen their powers and make auditors more responsible, the Bill has introduced changes including new provisions, revision of old provisions and removal of redundant provisions. This article attempts to summarise those provisions.

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The Companies Bill 2011 was introduced in Parliament in December 2011 and was referred to the Parliamentary Standing Committee on Finance for its review and suggestions. The Parliamentary Standing Committee headed by Mr. Yashwant Sinha submitted its report in June 2012 and based on its recommendations and suggestions, amendments were made to the Companies Bill 2011. Then it was introduced as Companies Bill 2012 (the Bill) and was passed by the Lok Sabha on 18th December 2012. The Bill has 470 clauses distributed in 29 Chapters and contains 7 Schedules.

[1] *As passed by the Lok Sabha on 18th December 2012. The Source document Companies Bill 2012 is sourced from the MCA website. http://www.mca.gov.in/Ministry/pdf/The_Companies_Bill_2012.pdf*

Key Amendments: Bill 2011 Vs. Bill 2012

Here are a few key amendments introduced in the Bill 2012, compared to the Companies Bill 2011.

1. Key Managerial Personnel includes Whole time director; [Cl.2(51)(iii)[2]]
2. Reopening of books of accounts is permitted only on application to an order by a competent court having jurisdiction or by the Tribunal [Cl.130(1)]
3. The provisions regarding the constitution of the National Financial Reporting Authority and its power, authority and responsibilities have undergone a big change. The same has been discussed in detail later in this article.
4. A new proviso has been inserted in Cl.135(5) to mandate companies to give preference to the local areas and the areas around where it operates to spend the funds earmarked for CSR activities. A new explanation is also inserted to clarify that calculation for "average net profits" is to be made in accordance with the provisions of S.198
5. Every company at the first annual general meeting appoint an individual or a firm as an auditor who shall hold the office from the conclusion of the first annual general meeting till the conclusion of the 6th annual general meeting. *But it has to place the matter relating the appointment of auditors for ratification at every annual general meeting.[New proviso to Cl.139(1)]*
6. Existing companies are given one year time to comply with the requirements of the provisions of Cl.149(1) relating to having Board of Directors as specified. [Cl.149(2)][3]
7. Another noteworthy point is that Electronic form of book keeping and documentation is now recognised under the Bill 2012. [Proviso to Cl.128]

Constitution of National Financial Reporting Authority

The major changes introduced in the amended Bill 2012 with respect to the NFRA are hereunder:

1. The persons employed full-time with the National Financial Reporting Authority (NFRA) shall not be associated with any audit firm, including related consultancy firms, during the course of their appointment and two years after ceasing to hold such appointment.[3rd proviso to Cl.132(3)][4]
2. NFRA's power to levy, when professional misconduct is proven, a penalty of ₹100,000 in case of individuals and a penalty of ₹10,00,000 was proposed in the Old Bill 2011. Now the provisions are amended to impose and imply penalty of up to 5 times the sum received as fees in case of individuals (minimum ₹1 lakh) and upto 10 times the sum received as fees in case of a firm (minimum ₹10 lakh) [Cl. 132 4(C)(A)(i) & (ii)]

The key amendments introduced in the Bill 2012, compared to the Companies Bill 2011 include that 'Key Managerial Personnel now includes whole time director,' 'Reopening of books of accounts is permitted only on application to an order by a competent court having jurisdiction or by the Tribunal,' and 'a big change in the provisions regarding the Constitution of the National Financial Reporting Standards Authority and its power, authority and responsibilities'.

Audit and Auditors

Chapter X of the Companies Bill 2012 deals with Audits and Auditors of the Company. For the purposes of this Chapter, appointment includes reappointment. This Chapter contains Clauses 139 to 148 and covers a wide range of topics such as:

1. Clause 139: Appointment of auditors
2. Clause 140: Removal, resignation and giving of Special notices
3. Clause 141: Eligibility, qualifications and disqualifications of auditors
4. Clause 142: Remuneration of auditors
5. Clause 143: Powers and duties of auditors and auditing standards
6. Clause 144: Auditor not to render certain services
7. Clauses 145 – 148: Auditor to sign audit reports, etc.; auditors to attend general meetings; Punishment for contraventions, etc.

Appointment of Auditors:

Cl.139 of the Bill deals with the appointment of auditors. It enumerates the provisions for appointment of auditors for both

a. Government or Government controlled Companies and
b. For every other company.

Provisions related to Government or Government Controlled Companies:

In case of a Government Company, or any other company owned or controlled, whether directly or indirectly, individually or together, by the Central

[2] *Newly inserted in the Bill 2012.*
[3] *New subClause inserted in the amended Bill 2012*
[4] *Newly inserted proviso in the amended Bill 2012.*

or State Government(s) [Government controlled Company], the auditor shall be appointed by the *Comptroller and Auditor General of India, (C&AG).*

First Auditor:
The first auditor of a Government or Government controlled Company shall be appointed by the C&AG within 60 days from the date of registration of the company. If the C&AG does not appoint the auditor, the Board of Directors shall appoint the auditor within the next 30 days. And if the Board fails to appoint such auditor(s), it shall inform the members of the company, who shall appoint the auditor within the 60 days at an Extra-Ordinary general meeting.

Regular appointment of Auditors
In respect of any financial year, the C&AG shall appoint the auditor, who is qualified as per the provisions of this Act, within 180 days from the commencement of the financial year and the auditor so appointed shall hold office till the conclusion of the Annual General meeting (AGM).

Filling up of Casual Vacancy
In case of any casual vacancy in the office of an auditor so appointed by the C&AG will be filled in only by the C&AG within 30 days. In case the C&AG does not fill up such casual vacancy within the stipulated time, the Board of Directors shall fill such vacancy within next 30 days.

Provisions related to every other company:
At the first Annual General Meeting (AGM), every company (other than Government or Government controlled Company) shall appoint an individual or a firm as auditors. For the purposes of this Chapter, the word 'Firm' includes a Limited Liability Partnership (LLP). Such auditors shall hold office from the conclusion of the said AGM till the conclusion of the 6th AGM i.e., for a period of 5 consecutive years. The Bill provides for a term of 5 consecutive years without rotation of the individual or firm, as the case may be, as an auditor. The conditions are:

1. At each AGM thereafter, the matter related to such appointment shall be placed for ratification by the members of the company
2. A written consent to such appointment and a certificate that the appointment is in accordance with the prescribed conditions should be obtained from the auditor before such appointment is made.
3. The certificate should state whether the auditor satisfies the criterion set out in Clause 141, which is essentially the eligibility, qualifications and disqualifications of auditors.
4. The company has to inform the auditor concerned about the appointment and also notify the Registrar within 15 days of such appointment.
5. Listed or Specified Company or a class of companies cannot re-appoint an individual for more than one term of consecutive 5 years. In case of a firm of auditors, these companies cannot re-appoint them for more than two terms of consecutive 5 years. Also, after completion of the said one term or two terms as the case may be, they are not eligible for re-appointment for five years from the completion of such term(s). That is, in case of auditor being
   a. Individual – he is not eligible for re-appointment from the 6th to 10th year from completion of one term of five years;
   b. A Firm – It is not eligible for re-appointment from the 11th to 15th year from completion of two terms of five years, in case it is re-appointed for a second term.
6. The company cannot appoint a firm as auditor, if as on the date of appointment, it has a common partner or partners, whose other audit firm(s) was appointed as an auditor in the company and its tenure had expired in the immediately preceding financial year.
7. In case of casual vacancy (other than by resignation by the auditor), the Board of Directors should fill the vacancy within 30 days. If the vacancy is due to resignation by the auditor, then such appointment should be approved by the company at a general meeting convened at the recommendation of the Board. The auditor so appointed as above shall

Chapter X of the Companies Bill 2012 deals with Audits and Auditors of the Company. For the purposes of this Chapter, appointment includes reappointment. This Chapter contains Clauses 139 to 148 and covers a wide range of topics such as 'Clause 139: Appointment of auditors,' 'Clause 140: Removal, resignation and giving of Special notices,' 'Clause 141: Eligibility, qualifications and disqualifications of auditors,' 'Clause 142: Remuneration of auditors,' 'Clause 143: Powers and duties of auditors and auditing standards,' 'Clause 144: Auditor not to render certain services,' 'Clauses 145 – 148: Auditor to sign audit reports, etc.; auditors to attend general meetings; Punishment for contraventions, etc.'

hold office till the conclusion of the next AGM.

The Bill gives the existing companies a cooling off period of three years from the date of commencement of the Act, when passed, for implementing the provisions of sub-clause (2) of Cl.139 [points 5 & 6 above].

It also provides that nothing in the sub-clause shall mean to prejudice the Company's right to remove the auditors or the auditor's right to resign from such office.

The members of the company are given a right to resolve to rotate the auditing partner and his team of an audit firm so appointed at such intervals as they deem fit. Also, they can resolve to have the audit done by more than one auditor.

The Central Government may prescribe the manner in which companies can rotate the auditors enumerated as above.

A retiring auditor shall be reappointed at an AGM unless

- He is disqualified for re-appointment
- He has given a notice in writing of his unwillingness to be re-appointed
- A special resolution is passed at that meeting appointing someone else or providing explicitly not to re-appoint the retiring auditor.

If no new auditor has been appointed or reappointed at any AGM, the existing auditor shall continue to be the auditor of the company.

Where a company has constituted an Audit Committee under S. 177 of the Act (to be enacted), all appointments including filling up of casual vacancy should be made after taking into account, the recommendation of such committee.

Removal, Resignation of Auditors and Giving of Special Notices

Removal:

The Auditor appointed under clause 139 may be removed from his office before expiry of his term. For this, the company should

1. Get prior approval of the Central Government on that behalf, in the prescribed manner and
2. Pass a Special Resolution.

To safeguard the interest of the auditor, the Bill provides that before taking any action under clause 140(1), the auditor should be given a reasonable opportunity to be heard.

Sub-clause (9) and (10) provides emphasis on the auditing standards and it mandates that every auditor must comply with the auditing standards. While the Central Government prescribes the Auditing Standards or addendums thereto, it shall consult with and take recommendations of the ICAI and the NFRA. Till such **time the Auditing Standards are notified by the Central Government, the auditing standards specified by the** ICAI are deemed to be the auditing standards.

Resignation:

An auditor who resigns from the company shall file a statement in the prescribed form, with the company and the Registrar and in case of Government or government controlled companies, with the C&AG too, indicating the facts, reasons and other relevant information pertaining to his resignation, within 30 days from the date of resignation. If the auditor fails to comply with the above, he shall be punishable with a fine between ₹50,000 to ₹500,000.

Special Notices

1. Special notice is required for a resolution to appoint another auditor in place of the retiring auditor or to provide expressly that the retiring auditor shall not be re-appointed. This provision is not applicable where the auditor is retiring after completing his tenure of 5 years or 10 years, as the case may be.
2. On receipt of such special notice, the company should send a copy thereof to the retiring auditor.
3. Where such a notice is given about such a resolution and the retiring auditor makes a representation in writing to the company with respect to such notice and requests it to be notified to the members, the company should, unless it is too late to do so,
   a. in the notice of the resolution, state the fact of the representation being made and
   b. Send a copy of the representation to the members of the company to whom the notice of such resolution was sent, irrespective of whether the notice was sent before or after the receipt of the representation.
4. If the copy of the representation was not sent as aforesaid, either because it was too late to do so or because of company's fault, the retiring auditor may require the representation to be read out or exercise his right to be heard orally at the meeting.
5. If a copy of the representation is not sent aforesaid, it can be filed with the Registrar.

Powers of the Tribunal with respect to Removal, etc.

The Company Law Tribunal (the Tribunal) has the following powers:

1. If the Tribunal is satisfied that the auditor is abusing his powers under Clause 140(4) [points 1-5 under the heading Special Notices], then the representation need not be sent or read out at the meeting.
2. If it is satisfied that the auditor has acted in a fraudulent manner or abetted or colluded in any fraud by or in relation to the company, its directors or officers, whether directly or indirectly, then it can, by order, direct the company to change its auditors.
3. It can exercise the aforesaid power either *suo motu* or on application by the Central Government or any concerned person.
4. If the Central Government applies for and satisfies the Tribunal that the auditor needs to be changed, then the Tribunal shall make an order within 15 days of such application that he shall not function as auditor and the Central Government shall appoint the auditor in his place.
5. If a final order is passed against an auditor, individual or firm, by the Tribunal under this Clause 140, then that person is not eligible to be appointed as an auditor of any company. He is liable for action under Cl.447 [Punishment for fraud]

Eligibility, Qualifications and Disqualifications and Remuneration

Clause 141 of the Bill deals with the eligibility, qualifications and disqualifications of the auditors. Clause 142 deals with the remuneration to them.

1. Only a Chartered Accountant (as defined in S.2(1)(b) of the Chartered Accountants Act, 1949 and holding a valid certificate of practice thereunder S.6(1)) can be appointed as an auditor of the Company.
2. A firm of Chartered Accountants can be named as auditor by its firm name if the majority of the partners practicing in India are qualified for such appointment.
3. If a firm (including a LLP) is appointed as aforesaid, only the partners, who are Chartered Accountants, are authorised to act and sign on behalf of the Firm
4. The following persons are not eligible for appointment as auditors:
   a. A body corporate other than a LLP registered under LLP Act 2008;
   b. An officer / employee of the company
   c. A person who is a partner or an employee of an officer or employee of the company

A member in practice is prohibited by the ICAI to write or offer book-keeping services, where he is appointed as an auditor of the client. The ICAI, through various **notifications has prohibited rendering of certain** services while accepting appointment as an auditor, failing which the member shall be deemed to be guilty of professional misconduct, to ensure independence of auditors. (Compendium of Guidance Notes, 2012). Now the Companies Bill 2012 tries to incorporate these in the Act itself, to strengthen the independence of Auditors.

   d. A person (or his relative or a partner) who,
      i. Is holding any security of interest in any of the following namely, [the entities for the limited purpose of this point (d)]
         1. The Company;
         2. Its Holding;
         3. Its subsidiary or associate;
         4. Its Holding's subsidiary

      (The relative can hold interest in the company for face value not exceeding ₹1,000 or a sum as prescribed)
      ii. Is indebted to any of the above entities, in excess of prescribed limit
      iii. Has given a guarantee or provided any security for indebtedness of any third person to any of the entities, for such amount as may be prescribed
   e. A person or a firm who is having a business relationship with the entities or an associate of the holding company (whether directly or indirectly)
   f. A person whose relative is a director or is in employment with the company as a director or key managerial personnel
   g. A person who is in full time employment elsewhere
   h. A person or a partner of a firm who holds appointment as an auditor of more than 20 Companies
   i. A person convicted by a court of an offence involving fraud and a period of 10 years has not lapsed from the date of conviction
   j. Any person whose subsidiary or associate entity is engaged in consulting and specialised services provided in Cl.144 [services like book keeping, internal audit, implementation of information systems, management services, actuarial services, investment advisory or

investment banking services etc.].

5. If, after being appointed an auditor, an auditor incurs any of the disqualifications detailed under point 4 above, he should vacate his office as an auditor and such vacation will be a casual vacation in the office of an auditor.
6. The remuneration to the auditors of a company can be fixed in its general meeting or in a manner as determined in such meeting. The remuneration of the first auditor may be fixed by the Board of Directors.
7. Remuneration includes fees payable to the auditor, any expenses incurred by him in relation to the audit; any facility extended to him. But it does not include any remuneration paid to him for any other services provided by him at the request of the company.

Powers and Duties of Auditors and Auditing Standards[5]

Clause 143 covers the powers and duties of the auditors and the Auditing Standards. This clause contains almost the same provisions of the Companies Act, 1956.

Powers of Auditor

1. Every auditor of a company has rights to access to the books of account and vouchers of the company at all times whether they are kept at the Registered Office or at any other place.
2. He is entitled to inquire from the officers of the company information and explanations as he thinks necessary to perform his duties as auditor.
3. He shall inquire into the following matters:
   a. Whether Loans and Advances made by the company are properly secured and not detrimental to the interests of the company or its members
   b. Whether book entry transactions are prejudicial to the interests of the company
   c. Where assets consist of shares, debentures or other securities, whether they are sold at lesser than the purchase price. [This is not applicable to an investment company or a banking company]
   d. Whether loans and advances made by the company are shown as deposits
   e. Whether personal expenses are charged to revenue account
   f. Where it is stated in books and documents of the company that any shares have been allotted for cash, whether cash has actually been received. If not received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.
4. The auditor of a holding company has access to the books of all of its subsidiaries for the purposes of consolidation of financial statements with that of the subsidiaries.

Duties of the Auditor:

5. The auditor has to make a report to the members of the company on the accounts examined by him and on every financial statement which is required to be laid in the general meeting.
6. The Audit report should take into consideration the provisions of this Act, the Accounting and Auditing standards and matters which are required under this Act or rules made thereunder.
7. The Audit report should state that to the best of his (auditor's) *information and knowledge*[6], the said accounts and financial statements give a true and fair view of the state of the company's affair as at the end of the financial year and the profit or loss and the cash flow for the year and such other matters as may be prescribed[7].
8. The auditor's report shall also state other details such as, whether he has sought[8] and obtained all information and explanations necessary to do his job etc. This sub-clause (3) of Clause 143 is almost the same as to the subsection (3) of Section 227 of the Companies Act, 1956. Only wherever Balance sheet and Profit and Loss account are referred to in the Act, 1956, is now referred to as Financial Statements in the Bill, 2012. Also, where the Act, 1956 requires the Qualification of Adverse remarks in thick bold type and italics, the Bill, 2012 does not require such qualifications to be set differently from other contents. Also, the auditor has to state whether the company has adequate internal financial control systems in place and the operating effect thereof and such other matters as may be prescribed. It is interesting to note that the words "whether in his opinion" are missing to state whether the company has adequate internal financial control system in place.

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5 *Auditing Standards is given reference in the heading itself of the new Bill 2012.*
6 *As against 'in his opinion and to the best of his knowledge'*
7 *Only Balance sheet and Profit and Loss account are covered in the Companies Act, 1956*
8 *It is a newly added word in the Bill 2012, compared to the Companies Act 1956.*

Clause 146 of the Bill 2012 mandates that the auditor should attend general meetings. All notices of and communication related to any general meeting shall be forwarded to the auditor of the company and the auditor shall, ***unless specifically exempted by the company,*** attend such meetings either by himself or through his authorised representative.

9. In case of government companies, the C&AG shall appoint the auditor under sub-clauses (5) or (7) under clause 139 and direct him as to the manner in which the books are to be audited. Then the auditor shall submit a copy of his report to the C&AG which includes, *inter-alia*, the directions by the C&AG, the actions taken thereon and its impact on the accounts and financial statement of the company.
10. The C&AG, within 60 days upon receipt of the audit report aforementioned, shall order a supplementary audit to be conducted by person or persons authorised in this behalf.
11. The C&AG has a right to direct to furnish such information/additional information to such authorised person(s). He has a right to comment upon or supplement such audit report. Such comments shall be sent to every person entitled to copies of audited financial statements under Cl.139(1). The comments should also be placed before the AGM at the same time and same manner as the audit report.
12. The C&AG, for companies covered under Cl.139 (5) or (7), may order for test audits for such companies, if he deems fit. The provisions of S. 19A of the Comptroller and Auditor-General's (Duties, Powers and Conditions of Service) Act, 1971 shall apply to such test audit reports.

Audit of Branches of Company:

The provisions related to audit of branches of a company that was dealt with in a separate section (S.228) in lengths and breadths under the Companies Act, 1956 had been trimmed and the redundancies and out-dated provisions had been replaced with a single new sub-clause (8) of Clause 143. Accordingly, a branch can be audited by

1. The company's auditor; or
2. Any other person, qualified to be and appointed as an auditor as per the provisions of the Act (to be enacted) as branch auditor; or

3. In case of foreign branch, by the company's auditor or a competent person appointed in accordance with the prevailing laws of the foreign country.

The branch auditor shall prepare a report on the accounts of the branch examined by him and the company's auditor shall deal with such report in his audit report in a manner as he considers necessary. The duties and powers of the company's auditor and the branch auditor shall be such as may be prescribed.

Emphasis on Auditing Standards

Sub-clause (9) and (10) of Clause 143 provides emphasis on the auditing standards and it mandates that every auditor must comply with the auditing standards. While the Central Government prescribes the Auditing Standards or addendums thereto, it shall consult with and take recommendations of the ICAI and the NFRA. Till such time the Auditing Standards are notified by the Central Government, the auditing standards specified by the ICAI are deemed to be the auditing standards.

Other matters to be set therein..

The Central Government may, in consultation with the NFRA, direct that the auditor's report shall also include a statement on such matters with respect to certain class or description of companies, as may be specified in the direction.

Interesting addition to the duties of the auditor is that, if an auditor, during the course of the performance of his duties as an auditor to the company, has reasons to believe that an offence involving fraud is being or has been committed against the company by its officers or employees of the company, he should immediately report the matter to the Central Government within such time and in such manner as may be prescribed. Protection is given to the auditor by providing that the aforementioned reporting shall not be considered as a breach of duty, if it is done in good faith. The provisions of Clause 143 applies *mutatis-mutandis* to Cost Accountants in practice conducting Cost Audit under Clause 148 or the Company secretary in practice conducting secretarial audit under clause 204. If any auditor, cost accountant or company secretary in practice fails to comply with the provisions of Cl.143(12) [reporting of an offence involving fraud], they will be punished with a fine of minimum ₹100,000 and up to ₹25,00,000.

Prohibition for Auditor to render certain Services:

The new addendum to the Act is that the auditors are explicitly prohibited to carry out certain services, while being appointed as an auditor of the company.

Already a member in practice is prohibited by the ICAI to write or offer book-keeping services, where he is appointed as an auditor of the client. The ICAI, through various notifications has prohibited rendering of certain services while accepting appointment as an auditor, failing which the member shall be deemed to be guilty of professional misconduct, to ensure independence of auditors. (Compendium of Guidance Notes, 2012)

Now the Companies Bill 2012 tries to incorporate these in the Act itself, to strengthen the independence of Auditors. Some of such services, whether rendered *directly or indirectly* to the company or its holding company or its subsidiary, listed are

- Accounting and book keeping services;
- Internal audit;
- Design and implementation of any financial information system;
- Actuarial services;
- Investment advisory or investment banking services;
- Outsourced financial services;
- Management services, etc;

As the members of the ICAI may be aware, most of the services are already prohibited by the Institute under its Act or Rules, Regulations made thereunder for a practicing chartered accountant to ensure

If the auditor of the company contravenes any provisions of Cl.139 [appointment / reappointment] or Cl.143 [powers and duties] or Cl.144 [restriction on rendering of other services] or Cl.145 [signing of audit reports, documents etc] the auditor shall be punishable **with a fine of not less than** ₹ 25,000 and up to ₹5 lakh. But if the auditor contravenes the provisions willfully or knowingly with the intention to deceive the company or **its shareholders or the creditors or tax authorities, he** shall be punishable with imprisonment up to one year **and a fine ranging between** ₹1 lakh and ₹25 lakh.

independence as auditor.

The Bill 2012 provides for a cooling off period stating that an auditor or a firm, if performing a non-audit service on or before the commencement of the Act (to be enacted) shall comply with the provisions under this Clause 144, before the closure of first financial year from the date of such commencement.

The term *"directly or indirectly"* is explained to include rendering of services by an auditor –

- In case of an individual: either himself or through his relative or any other person connected or associated with such individual or through any other entity, in which such individual has significant influence or control or whose name or trade mark or brand is used by such individual.
- In case of a firm: either itself or through any of its partners or through its parent or subsidiary or associate entity or through any other entity, in which the firm or any partner has significant influence or control or whose name or trademark or brand is used by such firm or any of its partners.

This Clause 144 tries to bring absolute independence on the part of an auditor, thereby strengthening and enabling the auditor to be more focused and integrated while discharging his duties as an auditor.

Auditor to Sign Reports, etc.

Clause 145 provides that the auditor shall [in accordance with Clause as 141(2)],

- sign the audit report and
- sign or certify any other document.

Any qualification, observations or comments on financial transactions and matters, which has an adverse effect on the functioning of the company, mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

A person who is or has been an employee or a **proprietor or a partner of an audit firm, which had been** appointed as auditors of the company or its holding, subsidiary or associate in any of the preceding three years cannot be appointed as an independent director. [Cl.149(6)(e)(ii)]

Auditor to Attend General Meeting

Clause 146 of the Bill 2012 mandates that the auditor should attend general meetings. All notices of and communication related to any general meeting shall be forwarded to the auditor of the company and the auditor shall, unless specifically exempted by the company, attend such meetings either by himself or through his authorised representative. The authorised representative should be qualified to be an auditor. He has a right to be heard at such meeting on any part of the business which concerns him as the auditor.

Punishment for Contraventions

Clause 147 provides for a detailed punishment for non-compliance or contravening of Clauses 139 to 146 for both the company and the auditor, unlike the shorter version - Sections 232 and 233 – of the Companies Act, 1956. The Bill 2012, provides that if any of the provisions of Cl. 139 to Cl. 146 (both clauses inclusive) is contravened

- the Company shall be punishable with a fine of minimum ₹25,000 and up to ₹5 lakh
- Every officer of the company who is in default shall be punishable with imprisonment for a term of not less than one year or a fine of about ₹10, 000 up to ₹1 Lakh or both

If the auditor of the company contravenes any provisions of Cl.139 [appointment / reappointment] or Cl.143 [powers and duties] or Cl.144 [restriction on rendering of other services] or Cl.145 [signing of audit reports, documents etc] the auditor shall be punishable with a fine of not less than ₹25,000 and up to ₹5 lakh.

But if the auditor contravenes the provisions willfully or knowingly with the intention to deceive the company or its shareholders or the creditors or tax authorities, he shall be punishable with imprisonment up to one year and a fine ranging between ₹1 Lakh and ₹25 lakh.

If the auditor is convicted under Cl.147(2), then he shall be liable to

- Refund the remuneration received by him, to the company AND

- Pay for the damages to the company or statutory bodies, or authorities or to any other person for any losses arising out of incorrect or misleading statements of particulars made in his audit report.

The Central Government shall by notification specify any statutory body, or authority or an officer for ensuring prompt payment of damages to the company or the aggrieved persons mentioned above. Such notified person who ensures that the damages are duly paid shall file a report with the Central Government in respect thereof in the prescribed manner.

Where it is proved that, in case of audit of a company by a firm, the partner or partners have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to or by, the company or its directors or officers, the liability for such act, whether civil or criminal, as provided in this Act (to be enacted) or under any other law for the time being in force, shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally.

In short, no matter what, if proved guilty in relation to the audit of a company, BOTH the concerned partner(s) of the audit firm and the firm are liable for action for any such fraudulent actions detailed under this Act (to be enacted) or any other Act for the time being in force.

Other Related Provision

A person who is or has been an employee or a proprietor or a partner of an audit firm, which had been appointed as auditors of the company or its holding, subsidiary or associate in any of the preceding three years cannot be appointed as an independent director. [Cl.149(6)(e)(ii)]

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One Person Company in Companies Bill, 2012

The game-changing Companies Bill, 2012 ('Bill') which was passed by the Lok Sabha in December 2012, viewed holistically, is a mixed bouquet of proposals. Whilst it incorporates creditable efforts towards streamlining existing provisions and weeding-out obsolete provisions, it also introduces a few interesting new-age concepts. One such concept which is presented in this article is that of One Person Company ('OPC'). Captured all-in-the-name, it relates to a corporate entity which has just one shareholder. An accepted concept internationally, OPCs are an option in many developed and developing jurisdictions, namely China, United Kingdom, Australia, Singapore, etc. Several states in the United States of America allow the formation of single member limited liability companies. In India, a country where entrepreneurship culture is ingrained from generations and with more than 95% of the commercial and business enterprises being sole-proprietorships, it is a step in the right direction to introduce the OPC vehicle.

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The benefits of limited liability can now be reaped by the largest section of the enterprising class. Though a lot of dots remain to be joined in this endeavour, especially in relation to taxation, conversion of existing proprietorships, banking recognition, FDI, government companies, etc. the ball is now in motion for a fresh change.

This new vehicle called One Person Company (OPC) will provide an opportunity to Indian entrepreneurs, to enter into the corporate framework along with enjoying the benefits of limited liability. The question of 'perpetual succession of a company' has also been appropriately addressed in the Bill.

Definitions and Concept:

Presently the Companies Act, 1956 *('56 Act')* requires at least two persons to register a company under the '56 Act'. The passage of Bill will pave the way for entities that have just a single shareholder.

Clause 2(62) of the Bill defines OPC as *"One Person Company"* that means a company which has only one person as a member.

OPC can be formed by a single person subscribing the name of such one person to the memorandum and complying with the requirements of the Bill in respect of registration. As regards the name of an OPC, the Bill provides that the words 'One Person Company' shall be mentioned in brackets below the name of such company, wherever its name is printed, affixed or engraved.

The word person would normally mean and deem to include a company also. Hence, a company should also be able to form an OPC which would be its 100% subsidiary. Unless specified, the word person would deem to mean and include a 'natural person' and a 'legal person'. This fact though needs to be seen in conjunction with the rules which would be issued by the Ministry of Corporate Affairs.

OPC shall be a private limited company in all respect except OPC can be formed by a single subscriber to the MOA. The memorandum of OPC shall indicate the name of the other person, with his prior written consent in the prescribed form, who shall, in the event of the subscriber's death or his incapacity to contract become the member of the company.

The written consent of such person shall also be filed with the Registrar at the time of incorporation of the One Person Company along with its memorandum and articles.

Subscriber can also change the nominee by giving prescribed notice. Upon changing the nominee, member shall give intimation to company and company in turn shall inform to registrar within time limit, to be prescribed by rules made in this behalf.

The Chinese company law regulations, interestingly, bar a person from opening more than one OPC. The Bill has no such provisions.

Whether the OPC will have a separate status under the provisions pertaining to taxation of the OPC remains unclear as of now. In various developed jurisdictions, the OPC, if formed by a natural person would not be considered as a separate person for taxation purposes.

Types of Companies formed as OPC:

Other than specifically provided or exempted for under the Bill, all provisions as applicable to a Private Limited Company shall be applicable to an OPC. Three types of companies can be formed as an OPC:

1. Company limited by shares
2. Company limited by guarantee
3. Unlimited company

Requirements of Directors:

A minimum of one director is required in an OPC. However, there is no bar on appointment of more than one director. The Member and the Director can be the same individual. Until director(s) are appointed, the individual being member shall be deemed director of the company.

In the case of an OPC having only one director, the compliance with provisions of conducting of Board Meeting would merely be a formality and be frustrated for all practical purposes, hence the Bill does not mandate Board Meeting requirements for an OPC having a single director. The business which is required to be transacted at board meeting shall be sufficiently transacted if the resolution is entered into the minute book, signed and dated. Such date shall be deemed to be the date of meeting of board of directors for the purposes of the Bill. Ancillary provisions with relation to minimum number of board meetings shall also not apply to such an OPC.

In case OPC has more than one director, the Bill provides for a relaxed requirement that, it shall conduct at least one board meeting in each half year and time gap between the two meetings should be minimum 90 days.

Relaxations & Exemptions:

Conceptualised and tailor-made for the sole-proprietor entrepreneur, the Bill proposes some relaxations and exemptions to OPCs. Some of them are as under:

1) OPCs have been given the option to dispense with the requirement of holding a General Body Meeting including Annual General Meeting. All such requirements which pertain to shareholder consents and meetings have been dispensed with e.g. Notice of meeting, quorum, proxies, postal ballot, etc.
2) In the case of a company other than OPC, Annual Return should be signed by the Company Secretary (CS) appointed by the company. If not then, it should be signed by Company Secretary in Practice (PCS). In case of OPC, Annual return should be signed by Company Secretary (CS) appointed by the company, if not, then it should be signed by Director.
3) The financial statement, including consolidated financial statement of an OPC can be signed by one director.
4) The Bill requires companies to mandatorily prepare a cash-flow statement as a part of their financial statements. An OPC is specifically exempted from the requirement of preparation of a cash-flow statement. Relaxations given to an OPC are that there is no need to prepare a cash-flow statement.

Perpetual Succession and Nomination:

Every person incorporating an OPC needs to mandatorily appoint a person as his nominee. The person has to nominate a name with that person's written consent as a nominee to the OPC. This person will be the default and ad hoc member in case of the existing sole member's death or disability. This provision will ensure perpetuity and continuity to the life of the Company.

The model Articles of Association that form a part as a schedule to the Bill state that on the death of the member of an OPC, the person nominated by such member shall be the person recognised by the company as having title to all the shares of the member and shall be entitled to the same dividends and other rights and liabilities to which such sole member of the company was entitled or liable.

Where an OPC limited by shares or by guarantee enters into a contract with the sole member of the company who is also the director of the company, the company shall, unless the contract is in writing, ensure that the terms of the contract or offer are contained in a memorandum or are recorded in the minutes of the first meeting of the Board of Directors of the company held next after entering into contract.

The company shall inform the Registrar about every contract entered into by the company and recorded in the minutes of the meeting of its Board of Directors under section 193(2) sub-section (1) within a period of fifteen days of the date of approval by the Board of Directors.

Experts feel the key challenge for such a company will be to ensure that supporting legislations also recognise such a company as an entity and not just an extension of a sole proprietorship.

Whether the OPC will have a separate status under the provisions pertaining to taxation of the OPC remains unclear as of now. In various developed jurisdictions, the OPC, if formed by a natural person would not be considered as a separate person for taxation purposes. It needs to be seen how the finance minister clarifies the position under the Income Tax Act, 1961 for taxation of OPCs. If the provisions of dividend distribution tax and others continue to apply to OPCs, the same would be a big dampener in large-scale adoption of OPCs.

As per the provisions on financial statement, it may not include the cash flow statement as stated in Clause 2(40). Further, the annual return has to be signed by the company secretary, or where there is no company secretary, by the director of the company. The **Clause 134(1) provides that the financial statement, including consolidated financial statement, if any, has** to be approved by the Board of Directors before they are signed on behalf of the Board only by one director, for submission to the auditor for his report thereon.

Financial Statements

As per the provisions on financial statement, it may not include the cash flow statement as stated in Clause 2(40). Further, the annual return has to be signed by the company secretary, or where there is no company secretary, by the director of the company. The Clause 134(1) provides that the financial statement, including consolidated financial statement, if any, has to be approved by the Board of Directors before they are signed on behalf of the Board only by one director, for submission to the auditor for his report thereon. As per Proviso to Clause 137(1), a copy of the financial statements duly adopted by its member, along with all the documents which are required to be attached to such financial statements, is to be filed within 180 days from the closure of the financial year. For companies other than OPC, the cut-off date for filing is 30 days from the date of AGM.

The Clause 134(4) says that the report of the Board of Directors has to be attached to the financial statement under this section shall, in case of a OPC, mean a report containing explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made by the auditor in his report.

The provisions relating to migration to other forms of companies from an OPC, transferability of shares of an OPC, merger & acquisition provisions, winding-up provisions, ancillary procedures, etc. will also be clear once the rules are issued under the New Act. Though in the current form there seems no express restriction for any of these provisions.

Having provisions for OPC in a major Bill looks good, but that's about the only thing that one can expect from it now, till collateral legislation embraces the concept. ■

New Publications

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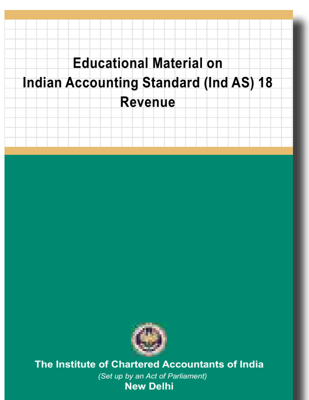

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Companies Bill 2012 and Independent Directors-Enhanced Role & Responsibilities

After a very long wait and sustained efforts of the Government of India, the new Companies Bill, 2012 has been passed in the Lok Sabha. The Bill provisions seem to be more progressive and futuristic. The Bill emphasises on each and every section of India -- be it investor, company, director or the general public and above all, the weaker sections of the Indian population. It is a very optimistic and progressive step to include mandatory provisions of Corporate Social Responsibility (CSR). Besides, there are many provisions giving due emphasis on more transparency and Corporate Governance. It has tried to fill up the loopholes of The Companies Act, 1956. In this regard, the provisions with respect to Independent Directors are worth taking note of. This article deals with the aspect of Independent Directors in Companies Bill 2012.

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A notable provision of the Companies Bill 2012 is the detailed procedure relating to appointment of "Independent Director", wherein a complete definition with procedure has been mentioned. The structure and process of appointment and cessation of Independent Directors will help to improve more transparency in the performance of the Company. It can be concluded that Independent Directors have been given a social duty to maintain transparency.

Another significant provision in the Bill is to include a woman director in certain class of companies. This provision will surely help to improve woman empowerment and to remove gender bias.

With a view to adopt 'Total Corporate Governance,' it has been stated that Subject to the provisions of section 152, an Independent Director shall hold office for a term up to five consecutive years on the Board of a company, but shall be eligible for reappointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report. Moreover, notwithstanding anything contained, no Independent Director shall hold office for more than two consecutive terms, but such Independent Director shall be eligible for appointment after the expiration of three years of ceasing to become an Independent Director, provided that an independent director shall not, during the said period of three years, be appointed in or be associated with the company in any other capacity, either directly or indirectly. It implies that Independent Director shall not be financially or in any way interested with the Company. The provision relating to retirement by rotation shall not be applicable to Independent Director. The Bill casts an onerous responsibility on Independent Directors who now require to hold an important position in CSR Committee. The listed companies would be required to have at least one-third of the total number of directors as Independent Directors and the Central Government may prescribe the minimum number of Independent Directors in case of any class or classes of public companies.

The Bill casts onerous responsibility on Independent Directors who now require to hold an important position in CSR Committee. The listed companies would be required to have at least one-third of the total number of directors as Independent Directors and the Central Government may prescribe the minimum number of Independent Directors in case of any class or classes of public companies.

It has been clearly defined that an Independent Director in relation to a company, means a director other than a managing director or a whole-time director or a nominee Director and

(a) who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience;

(b) (i) who is or was not a promoter of the company or its holding, subsidiary or associate company;

(ii) who is not related to promoters or directors in the company, its holding,subsidiary or associate company;

(c) who has or had no pecuniary relationship with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year;

(d) none of whose relatives has or had pecuniary relationship or transaction with the company, its holding, subsidiary or associate company, or their promoters, or directors, amounting to 2%. or more of its gross turnover or total income or fifty lakh rupees or such higher amount as may be prescribed, whichever is lower, during the two immediately preceding financial years or during the current financial year;

(e) who, neither himself nor any of his relatives—

(i) holds or has held the position of a key managerial personnel or is or has been employee of the company or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed;

(ii) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of—

(A) a firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary or associate company; or

(B) any legal or a consulting firm that has or had any transaction with the company, its holding, subsidiary or associate company amounting to 10%. or more of the gross turnover of such firm;

(iii)holds together with his relatives two per cent. or more of the total voting power of the company; or

(iv) is a Chief Executive or Director, by whatever name called, of any non-profit organisation that receives 25% or more of its receipts from the company, any of its promoters, directors or its holding, subsidiary or associate company or that holds two per cent. or more of the total voting power of the company; or

(f) who possesses such other qualifications as may be prescribed.

(6) Every independent director shall at the first meeting of the Board in which he participates as a director and thereafter at the first meeting of the Board in every financial year or whenever there is any change in the circumstances which may affect his status as an independent director, give a declaration that he meets the criteria of independence as provided in sub-section (5).

Subject to the provisions contained in the bill, an independent director may be selected from a data bank containing names, addresses and qualifications of persons who are eligible and willing to act as independent directors, maintained by any body, institute or association, as may by notified by the Central Government, having expertise in creation and maintenance of such data bank and put on their website for the use by the company making the appointment of such directors, provided that the responsibility of exercising due diligence before selecting a person from the data bank referred to above, as an Independent Director shall lie with the company making such appointment. The appointment of Independent Director shall be approved by the company in the general meeting as provided in sub-clause (2) of Clause 152 and the explanatory statement annexed to the notice of the general meeting called to consider the said appointment shall indicate the justification for choosing the appointee for appointment as Independent Director. As a strict provision, it has been mentioned that no person shall be appointed as an alternate director for an independent director unless he is qualified to be appointed as an Independent Director under the provisions of this Act. The role of an Independent Director can be analysed with this statement that has mentioned, that a meeting of the Board may be called at shorter notice to transact urgent business subject to the condition that at least one Independent Director, if any, shall be present at the meeting: Provided further that in case of absence of Independent Directors from such a meeting of the Board, decisions taken at such a meeting shall be circulated to all the directors and shall be final only on ratification thereof by at least one Independent Director, if any.

Some of the important codes for Independent Directors are as follows:

It can be stated that the concept of Independent Director has been placed in order to provide more & more transparency and corporate governance. Overall, it seems that the Bill will lead to overall development of India and also provide investor friendly environment.

Guidelines of professional conduct:

An Independent Director shall:

(1) uphold ethical standards of integrity and probity;

(2) act objectively and constructively while exercising his duties;

(3) exercise his responsibilities in a bona fide manner in the interest of the company;

(4) devote sufficient time and attention to his professional obligations for informed and balanced decision making;

(5) not allow any extraneous considerations that will vitiate his exercise of objective independent judgment in the paramount interest of the company as a whole, while concurring in or dissenting from the collective judgment of the Board in its decision making;

(6) not abuse his position to the detriment of the company or its shareholders or for the purpose of gaining direct or indirect personal advantage or advantage for any associated person;

(7) refrain from any action that would lead to loss of his independence;

(8) where circumstances arise which make an independent director lose his independence, the Independent Director must immediately inform the Board accordingly;

(9) assist the company in implementing the best corporate governance practices.

Role and functions:

The Independent Directors shall:

(1) help in bringing an independent judgment to bear on the Board's deliberations especially on issues of strategy, performance, risk management, resources, key appointments and standards of conduct;

(2) bring an objective view in the evaluation of the performance of board and management;

(3) scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance;

(4) satisfy themselves on the integrity of financial information and that financial controls and the systems of risk management are robust and defensible;

(5) safeguard the interests of all stakeholders, particularly the minority shareholders;
(6) balance the conflicting interest of the stakeholders;
(7) determine appropriate levels of remuneration of executive directors, key managerial personnel and senior management and have a prime role in appointing and where necessary, recommend removal of executive directors, key managerial personnel and senior management;
(8) moderate and arbitrate in the interest of the company as a whole, in situations of conflict between management and shareholder's interest.

III. Duties:

The Independent Directors shall—
(1) undertake appropriate induction and regularly update and refresh their skills, knowledge and familiarity with the company;
(2) seek appropriate clarification or amplification of information and, where necessary, take and follow appropriate professional advice and opinion of outside experts at the expense of the company;
(3) strive to attend all meetings of the Board of Directors and of the Board committees of which he is a member;
(4)participate constructively and actively in the committees of the Board in which they are chairpersons or members;
(5) strive to attend the general meetings of the company;
(6) where they have concerns about the running of the company or a proposed action, ensure that these are addressed by the Board and, to the extent that they are not resolved, insist that their concerns are recorded in the minutes of the Board meeting;
(7) keep themselves well informed about the company and the external environment in which it operates;
(8) not to unfairly obstruct the functioning of an otherwise proper Board or committee of the Board
(9) pay sufficient attention and ensure that adequate deliberations are held before approving related party transactions and assure themselves that the same are in the interest of the company;
(10) ascertain and ensure that the company has an adequate and functional vigil mechanism and to ensure that the interests of a person who uses such mechanism are not prejudicially affected on account of such use;
(11) report concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct or ethics policy;
(12) acting within his authority, assist in protecting the legitimate interests of the company, shareholders and its employees;
(13) not disclose confidential information, including commercial secrets, technologies, advertising and sales promotion plans, unpublished price sensitive information, unless such disclosure is expressly approved by the Board or required by law.

Separate meetings:

(1) The Independent Directors of the company shall hold at least one meeting in a year, without the attendance of non-independent directors and members of management;
(2) All the Independent Directors of the company shall strive to be present at such meeting;
(3) The meeting shall:
   (a) review the performance of non-independent directors and the Board as a whole;
   (b) review the performance of the Chairperson of the company, taking into account the views of executive directors and non-executive directors;
   (c) assess the quality, quantity and timeliness of flow of information between the company management and the Board that is necessary for the Board to effectively and reasonably perform their duties.

Conclusion

To conclude, it can be stated that the concept of Independent Director has been placed in order to provide more & more transparency and corporate governance. Overall, it seems that the Bill, after becoming an Act, will lead to overall development of India and also provide investor friendly environment.■

India Inc's Evolving Corporate Social Responsibility Landscape— From Voluntary to Mandatory

One of the major highlights of the proposed new legislation, the Companies Bill 2012, is that specified companies will have to necessarily spend 2% of their average net profits made in the immediately preceding three financial years towards Corporate Social Responsibility (CSR). *"Private companies, while maximising their growth, also have responsibility towards society besides equitable and sustainable growth of the country,"* said Union Minister of State for Corporate Affairs (Independent Charge) Shri Sachin Pilot, while moving the Bill. The CSR spend would be mandatory for companies that have a net worth of ₹500 crore or more, or turnover of ₹1000 crore or more or a net profit of ₹5 crore or more during a financial year. Where the company fails to spend such amount, the Board shall in its report specify the reasons for not spending the amount. Under the new legislation, companies will be encouraged to create Employees' Welfare Fund. The enactment of Companies Bill 2012 will make India the only country that has mandated CSR spend through statutory route.

Bhuvanesh Sharma

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The Corporate Social Responsibility (CSR) is not a new concept in India. Ever since the inception, corporates like Bharat Petroleum, Birla Group, Hindustan Unilever, Indian Oil, and Tata Group and ITC to name a few are involved in serving the community. Through donations and charity events, many other organisations have also been doing their part for the society. On the other hand, the CSR programmes of corporations like GlaxoSmithKline and a few others focus on the health aspect of the community. They set up health camps in tribal villages which offer medical check-ups and treatment and undertake health awareness programmes.

CSR is the integration of business operations and values, whereby the interests of all stakeholders including investors, customers, employees, the community and the environment is reflected in the company's policies and actions. *"CSR, if it is implemented with sustainability as a focus, enhances business sustainability, provides new opportunities, develops customer loyalty and improves stakeholder relationship,"* said the former President Abdul Kalam on December 20, 2012 at an award function organised by the industry body, the Associated Chamber of Commerce (ASSOCHAM). *"It should become an integral part of corporate strategy, management practices, business operations, product development and conservation of environment,"* he added.

Corporate Social Responsibility (CSR) can be defined as the economic, legal, ethical, and discretionary expectations that society has of organisations at a given point in time. The concept of corporate social responsibility means that organisations have moral, ethical, and philanthropic responsibilities in addition to their responsibilities to earn a fair return for investors and comply with the law. A traditional view of the corporation suggests that its primary, if not sole, responsibility is to its owners, or stockholders. However, CSR requires organisations to adopt a broader view of its responsibilities that includes not only stockholders, but many other constituencies as well, including employees, suppliers, customers, the local community, state, and federal governments, environmental groups, and other special interest groups.

The essence of CSR comprises of philanthropic responsibility, corporation responsibility, ethical responsibility, environmental responsibility, and legal & economic responsibility. Put all together, the alternative synonymous for CSR is People, Planet, and Profit, also known as triple bottom line. CSR is slowly evolving in India and the developed countries have even established standards for CSR. In developed countries, however the law does not stipulate for mandatory CSR contributions. Many European countries have, however, specified that companies must include CSR information in their annual report.

> It is important for government to ensure that its role does not create an extreme situation where its role becomes an interventionist. The whole world is watching India Inc as to how it implements the Government's mandate on CSR.

In India, the evolution of CSR refers to the changes over time in cultural norms of corporations' engagement and the way business managed to develop positive impacts on communities, cultures, societies, and environment in which those corporations operated. Over the time, way back from 1850 during industrialisation, the charity and philanthropy were main matters of CSR. CSR motives changed during the independence movement in India to more of social reforms to encourage empowerment of women and rural development. Then came the era of globalisation and economic liberalisation where, due to increased growth momentum, Indian companies grew rapidly and, therefore, they showed more interest and were able to contribute towards growth of society and for social cause.

In the earlier days till today also, Indian companies were spending on philanthropic activities and whether such activities be construed as CSR activities, the new regulation is not clear. This will definitely affect the sentiments of companies indulging in philanthropic activities keeping in view the government proposal in the Companies Bill 2012 to make CSR activities mandatory with penal provisions for not complying with. It is important for the Government to ensure that its role does not create an extreme situation where its role becomes an interventionist.

As a broad measure of policy, the Government has prescribed certain areas for making expenditure on CSR activities. The activities are as follows:

(i) Eradicating extreme hunger and poverty;
(ii) Promotion of education;
(iii) Promoting gender equality and empowering women;
(iv) Reducing child mortality and improving maternal health;
(v) Combating human immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases;
(vi) Ensuring environmental sustainability;
(vii) Employment enhancing vocational skills;
(viii) Social business projects;
(ix) Contribution to the Prime Minister's National Relief Fund or any other fund set up by the Central Government or the State Governments for socioeconomic development and relief and funds for the welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women; and
(x) such other matters as may be prescribed.

From the view of the Indian companies, meaning of CSR activities could be different from one company to another. For some companies it means providing lunch to its employees and to another it could be about tackling global warming, environmental issues. Indian companies have a tradition of philanthropy but CSR is totally different.

The whole world is watching India Inc as to how it implements the Government's mandate on CSR. CSR is not a new concept in India but has been now discussed and talked upon with more gravity by India Inc due to Companies Bill 2012 which provides for all companies to set aside 2% of net profit for CSR activities. The CSR clause in the Companies Bill 2012 covers all companies that have either net worth in excess of ₹500 crore, or turnover of ₹1,000 crore or more, or net profit of ₹5 crore or more. They have to set aside 2% of the average net profit of the preceding three years for CSR activities.

The Bill clearly spells out about which company to comply, how to calculate 2% and how corporate governance will oversee the spend. However, there are many important questions which are undergoing discussion in India Inc, like: Who in the company will be responsible for implementing CSR activities; who will evaluate the CSR activities and their validity; what are CSR activities under the new law.

From the view of the Indian companies, meaning of CSR activities could be different from one company to another. For some companies it means providing lunch to its employees and to another it could be about tackling global warming, environmental issues. Indian companies have a tradition of philanthropy but CSR is totally different. CSR must relate to conducting the business but not as to giving to the local communities in which business operation are conducted. Corporate philanthropy and CSR are two different disciplines, but the difference gets indistinct. There is a perceptible changeover from giving as an obligation or charity to giving as a strategy or responsibility.

The companies in India have been spending on CSR activities and also doing through it different forms like through trust, foundations and will continue to do so but we will have to wait to see what impact after the mandatory spend on CSR is implemented. Moreover, the amended provisions view the CSR spending as individual company rather than from group perspective. This will adversely affect the promoters having various group companies and have consolidation presentation of their financial statements. For example, if there are 10 companies in group making profits, it implies 20% will be set aside, which can be used for repayment of capital finance, if any, or in new business development.

It is imperative upon the companies as to how to view the government mandate, as tax or as an investment. If the money is spent on philanthropic projects unrelated to the business, then it is just like social tax on profits. However, if companies can use the 2% for philanthropic and shared value projects that create new business opportunities, reduce costs, or strengthen their industry cluster, then the same expenditures would take route of an investment that bring fruits back to the company. "The aim is to protect the interests of employees and small investors while encouraging firms to undertake social welfare voluntarily instead of imposing that through 'inspector raj' and make India an attractive and safe investment destination," Shri Sachin Pilot told the Lok Sabha while moving the Bill.

In addition to setting aside 2%, the regulator had required "business responsibility reporting" as a non-financial reporting which should include environmental, social and governance initiatives, outlined as per National Voluntary Guidelines (NVG) that have been formulated by the Ministry of Corporate Affairs. The mandatory requirement is for top 100 listing companies and these companies are required to submit this reporting along with their annual report for the fiscal year ending on or after 31st December, 2012. However, a majority of the top 100 companies do not seem to be prepared yet in formulating their responsibility reports. A recent study conducted by Carbon Masters, a consulting agency in the field of sustainability, to find the preparedness levels of top BSE-100 companies, indicated that 64% of the top affected companies are not prepared to submit SEBI's prerequisite Business Responsibility (BR) report.

In addition to setting aside 2%, the regulator had required "business responsibility reporting" as **a non-financial reporting which should include** environmental, social and governance initiatives, outlined as per National Voluntary Guidelines (NVG) that have been formulated by the Ministry of Corporate Affairs. The mandatory requirement is for top 100 listing companies and these companies are required to submit this reporting along with their annual report for **the fiscal year ending on or after** 31st December, 2012.

From decades, India business sector generated wealth for shareholders. However, the country continues to grapple with problems of poverty, unemployment, illiteracy and malnutrition. Corporate growth is sometimes seen by regulatory, as widening the gap between India and Bharat (rural India) through its income-skewing competence. The consensus of all the discussions upon CSR happening in corners of India Inc leads to the conclusion that:- 'India needs a new approach to solve social problems and foster growth; Companies have an important role to play; and the Government intends to build companies' capacity to do so.'

The basic objective of CSR is to maximise the company's overall impact on the society and stakeholders keeping in consideration of the following:

Environment: Businesses have a role to play in preserving natural resources and biodiversity while combating pollution and climate change. We are committed to minimising our main impacts on the environment - energy use, business travel and waste management;

Community: Companies need to develop a long tradition of engaging with the communities in which we work by aligning our community involvement with our business activities and client relationships to ensure maximum impact; and

Sustainability: In wider sense sustainability includes both corporate social responsibility and environmental responsibility.

CSR policies, practices and programs are being comprehensively integrated by an increasing number of companies throughout their business operations and processes. A growing number of corporates feel that CSR is not just another form of indirect expense but is important for protecting the goodwill and reputation, defending attacks and increasing business competitiveness.

The Government mantra is that corporates have equal right and duties towards citizens for social upbringing and therefore "Corporate Social responsibility" and "business responsibility reporting" are approaching its way through Companies Bill 2012.■

Exposure Draft: Standard on Assurance Engagement (SAE) 3420

Announcement for the Attention of the Members: Exposure Draft of Standard on Assurance Engagement (SAE) 3420, "Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus" for Comments

The Auditing and Assurance Standards Board of the ICAI has issued the exposure draft of Standard on Assurance Engagement (SAE) 3420, "Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus" for comments. The complete text of the exposure draft can be downloaded from ICAI website at the link: http://220.227.161.86/29615aasb19256.pdf

The comments on this Exposure Draft can be sent latest by **June 03, 2013 to:**

Secretary, Auditing and Assurance Standards Board
The Institute of Chartered Accountants of India
ICAI Bhawan, A-29, Sector-62,
NOIDA, Uttar Pradesh – 201 309
Comments can also be e-mailed at: aasb@icai.org

Capitalisation of Borrowing Costs

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 Government company wholly owned by the Government of India, registered under the Companies Act, 1956, commenced its business in September 1987. The core business of the company is power generation at its power stations located across India. The power is fed into the regional grids and is shared by various states as per the allocation made by the Ministry of Power, Government of India and agreement with beneficiary states.

2. The querist has stated that the borrowing of funds is a centralised function at head office and is not on the basis of specific project appraisal. The borrowing is on the basis of statement of affairs of the company and is made for two or three projects in common and not on the basis of borrowing for one specific project. Sometimes, the loan was raised for a project even after the completion of substantial construction activity in that particular project. The interest is allocated on the actual utilisation of funds for each project. On unutilised funds, the allocation of interest to any specific project is not practical as the quantification of loan amount attributable to each specific project is not workable/possible.

3. The company, during the year, had raised common loans (both domestic and foreign currency) for various projects in general and not specifically for any particular project. Even while raising such loans, amount of loans attributable to a particular project was not known, it was determined only when the loan was actually utilised at the project sites as per level of construction activities undertaken. Sometimes even a portion of the loan was utilised for a project other than the project for which loan was actually taken.

4. The querist has further stated that as the borrowing of funds for the future projects is a corporate function, the interest allocation was made on the basis of actual utilisation of funds for each project for capitalisation of interest during construction. On unutilised funds, the allocation of interest to any specific project was not practical as the quantification of loan amount attributable to one specific project was not ascertainable and the borrowing was made generally for two or more projects in common. Accordingly, the interest cost attributable to unutilised funds was charged to the statement of profit and loss.

5. Till the time, the borrowed funds for the projects were utilised, these were kept at head office in a common pool of funds, which were used for various other purposes. Apart from this, as the company was also having sufficient surplus funds, these funds along with the unutilised funds of project borrowings were invested on short-term and long-term basis keeping in view the future requirement. The interest income earned on these investments was credited to the statement of profit and loss.

6. It may thus be noted that the borrowings made by the company were common for various projects in general and not for a specific project. Loan amount attributable to a specific project was also not identified/quantified in the loan agreements executed with various banks. The utilisation of loans was made progressively based on the construction activities undertaken at various project sites. Till that time, the unutilised loan funds were kept at head office which got mixed up with the common pool of funds which was used for various purposes. Therefore, under such circumstances, it becomes difficult rather impossible to identify a particular project to which the unutilised loan fund relates and the attributable interest cost to a specific project.

7. *Recognition Principle*
The recognition principles as per paragraphs 6 and 7 of Accounting Standard (AS) 16, 'Borrowing Costs', notified under the Companies (Accounting Standards) Rules, 2006 (hereinafter referred to as 'the Rules') are:

> ***"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.***
>
> 7. Borrowing costs are capitalised as part of the cost of a qualifying asset when it is probable that they will result in future economic benefits to the enterprise and the costs can be measured reliably. Other borrowing costs are recognised as an expense in the period in which they are incurred."

As per the recognition principle, 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.

Paragraphs 8, 10 and 11 of AS 16, notified under the 'Rules' further provide the following:

> "8. …When an enterprise borrows funds specifically for the purpose of obtaining a particular qualifying asset, the borrowing costs that directly relate to that qualifying asset can be readily identified."
>
> ***"10.To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings.***
>
> 11. The financing arrangements for a qualifying asset may result in an enterprise obtaining borrowed funds and incurring associated borrowing costs before some or all of the funds are used for expenditure on the qualifying asset. In such circumstances, the funds are often temporarily invested pending their expenditure on the qualifying asset. In determining the amount of borrowing costs eligible for capitalisation during a period, any income earned on the temporary investment of those borrowings is deducted from the borrowing costs incurred."

8. The auditors while conducting the audit of annual accounts of the company have raised a query that as the company borrowed funds exclusively for meeting capital expenditure and not for the working capital or for other purposes, the entire borrowing costs should be charged to the projects and the interest, if any, earned on their temporary investment should be credited to the concerned projects as per paragraph 10 of AS 16.

9. The auditors have further observed that the company had not separately accounted for the interest earned on these funds lying with the head office during the interim period when they were clubbed with other funds.

10. The audit query related to under capitalisation of borrowing cost has been reviewed by the company as per the provisions of AS 16. The justification in support of accounting treatment of borrowing cost made in the books of account for preparation of the financial statements of the company is as under:

> As per paragraph 6 of AS 16, notified under the 'Rules', ***"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."*** Paragraph 7, inter alia, states that borrowing costs are capitalised as part of the cost of a qualifying asset when such costs can be measured reliably.

Paragraphs 8 and 9 of AS 16, notified under the 'Rules' further state as follows:

> "8. The borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are those borrowing costs that would have been avoided if the expenditure on the qualifying asset had not been made. When an enterprise borrows

funds specifically for the purpose of obtaining a particular qualifying asset, the borrowing costs that directly relate to that qualifying asset can be readily identified.

9. It may be difficult to identify a direct relationship between particular borrowings and a qualifying asset… for example, when the financing activity of an enterprise is co-ordinated centrally … and such borrowings are not readily identifiable with a specific qualifying asset. As a result, the determination of the amount of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset is often difficult and the exercise of judgement is required."

Paragraph 12 of AS 16, notified under the 'Rules' further, inter alia, states that, ***"To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation should be determined by applying a capitalisation rate to the expenditure on that asset."***

11. Accordingly, for the measurement of borrowing costs eligible for capitalisation, AS 16 provides two circumstances, one specific borrowing and other when funds are borrowed generally for acquisition, construction or production of a qualifying asset. According to the querist, paragraph 10 of AS 16 applies only when there is a borrowing for a specific project. It may also apply to a new company in a project stage without any commercial operation. Paragraph 12 of AS 16 applies in other cases.

12. It may, however, be seen from the above paragraphs that the system of borrowing adopted by the company is to borrow the funds commonly for various projects in general and not for the purpose of any specific project. Loan amount attributable to a specific project was also not identified/quantified in the loan agreements executed with various banks. The utilisation of loan funds has been made progressively based on the construction activities undertaken at various project sites. Till that time the unutilised loan funds were kept at head office and got mixed in the common pool of funds. Therefore, under such circumstances it becomes difficult rather impossible to identify a particular project to which the unutilised loan fund relates. When it is impossible to identify a particular project to which the unutilised loan fund relates, it is also impossible to measure reliably the related borrowing cost attributable to a particular project. As a result, it was impossible for the company to follow paragraph 10 of AS 16 and quantify the interest (on unutilised funds) attributable to each specific project.

B. Query

13. In the light of the aforementioned facts, the querist has sought the opinion of the Expert Advisory Committee of the Institute of Chartered Accountants of India on the following issues:

(i) whether the accounting treatment carried out by the company, i.e., capitalising the interest on the portion of funds utilised for capital projects as capital expenditure and charging off the balance amount of interest on the unutilised portion of the funds available with the company to the statement of profit and loss, even though these were raised for two to three projects as mentioned above, is correct.

(ii) whether whole of the interest on unutilised portion of funds need to be capitalised even though the funds were not actually utilised on any of the projects under construction.

C. Points considered by the Committee

14. The Committee notes that the basic issues raised in paragraph 13 above of the query relate to capitalisation of interest on the portion of borrowed funds utilised for capital projects as capital expenditure and accounting for the balance amount of interest on the unutilised portion of the funds available with the company. The Committee has, therefore, considered only these issues and has not examined any other issue arising from the Facts of the Case, such as, determination of qualifying assets, determination of point of time when the borrowing costs should cease to be capitalised, treatment of interest income earned from the investment of unutilised portion of the borrowings and its allocation to various projects under construction, determination of capitalisation rate applicable to borrowed funds, accounting for internal surplus funds used for financing the

qualifying asset, accounting for foreign exchange fluctuations on the foreign currency borrowings, etc. The Committee notes from the Facts of the Case that the funds have been borrowed generally and not specifically for any project. Further, these borrowings are only for meeting capital expenditure and not for working capital requirements or other purposes. Accordingly, the Committee has restricted itself to these general borrowings only. The Committee also notes from the Facts of the Case (paragraph 5 above) that "as the company was also having sufficient surplus funds, these funds along with the unutilised funds of the borrowings were invested on short-term and long-term basis keeping in view the future requirement". Since the querist has not raised the issue with respect to determination of expenditure on qualifying assets out of borrowed funds and surplus funds accrued internally, the Committee has not examined that issue and presumed that the issue raised in the query is with respect to borrowed funds only which are being used for construction activities.

15. The Committee notes paragraphs 12 and 14 of AS 16, notified under the 'Rules' as reproduced below:

> ***"12. To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation should be determined by applying a capitalisation rate to the expenditure on that asset. The capitalisation rate should be the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs capitalised during a period should not exceed the amount of borrowing costs incurred during that period."***
>
> ***"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."***

From the above, the Committee notes that to the extent that funds are borrowed generally, (i.e., without specifying any particular project) and *used* for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation should be determined by applying a capitalisation rate to the expenditure on that asset. In the extant case, the company raised common loans for various projects in general and utilisation of loans was made progressively based on the construction activities undertaken at various project sites. Accordingly, it may be difficult to identify exact amount of borrowing funds utilised for a particular project. However, determining to what extent general borrowings have been used for a specific project, is a question of fact and should be determined by exercising the best judgement considering various factors, for example, information related to cash inflows and outflows.

16. The Committee is further of the view that to capitalise the borrowing costs, it is not sufficient that the funds are generally borrowed for meeting capital expenditure and not for the working capital or other purposes, as argued by the auditors; it is also essential that the funds from those borrowings should be *used* for the purpose of obtaining a qualifying asset. The Committee notes from the Facts of the Case that there were general borrowings which were not even utilised for any project of the company during the period. Accordingly, the Committee is of the view that borrowing costs related to only utilised funds for the purpose of any project should be capitalised by applying weighted capitalisation rate as per paragraph 12 of AS 16, subject to the satisfaction of the conditions specified in paragraph 14 of AS 16 and borrowing costs related to unutilised funds should be charged to the statement of profit and loss.

D. Opinion

17. On the basis of the above, the opinion of the Committee on the issues raised in paragraph 13 above is as below:

(i) The accounting treatment carried out by the company, i.e., capitalising the interest on the portion of generally borrowed funds (raised without specifying any particular project) utilised for capital projects as capital expenditure and charging off the balance amount of interest on the unutilised portion of the funds available with the company to the statement of profit and loss is correct provided the conditions as per paragraphs 12 and 14 of AS 16 are met, as discussed in paragraphs 15 and 16 above.

(ii) No, the interest on unutilised portion of funds should not be capitalised as discussed in paragraphs 15 and 16 above.

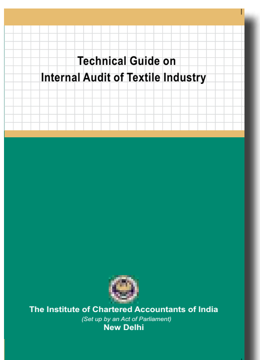
1	The Opinion is only that of the Expert Advisory Committee and does not necessarily represent the Opinion of the Council of the Institute.
2	The Opinion is based on the facts supplied and in the specific circumstances of the querist. The Committee finalised the Opinion on December 26-27, 2012. The Opinion must, therefore, be read in the light of any amendments and/or other developments subsequent to the issuance of Opinion by the Committee.
3	The Compendium of Opinions containing the Opinions of Expert Advisory Committee has been published in thirty volumes. A CD of Compendium of Opinions containing thirty 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.

New Publications

Technical Guide on Internal Audit of Textile Industry

Price:
₹200/-

Pages:
245 (including initial pages)



The Indian Textile Industry is one of the leading textile industries in the world. It is a knowledge based research oriented industry and has been slowly but steadily gaining ground due to reasons, such as, functional requirement, health and safety; cost effectiveness; durability; high strength; light weight; versatility; customization; user friendliness; eco friendliness; logistical convenience, etc.

Considering this, the Internal Audit Standards Board has issued "*Technical Guide on Internal Audit of Textile Industry*" to give an overview of the main activities of the textile industries, the way they work and a perspective from an internal audit viewpoint.

Salient Features of Technical Guide:

- Divided into various chapters that provide guidance on structure, history, regulatory framework, SWOT analysis of the industry.
- Provides guidance on aspects involved in various stages of textile industry, such as, spinning, weaving, apparels, etc.
- Contains internal controls checklist for various processes undertaken in textile industry.
- Describes risks associated with textile industry and issues relating to cost ascertainment.
- Contains illustrative checklist for internal audit of major areas of textile industry.
- Includes glossary of terms used in the textile industry.
- The Guide comes with a CD of the entire Guide to ensure ease of reference and reusability.

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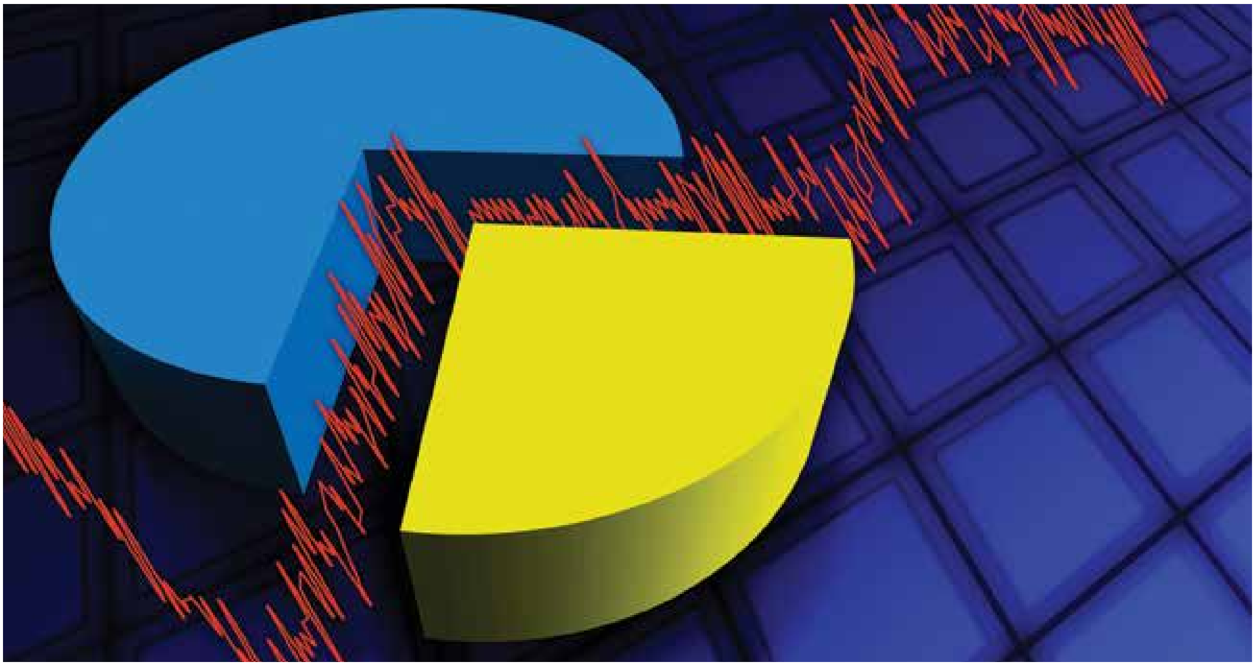
Ind AS 108: Operating Segments



Presently, Indian companies follow Accounting Standard 17: *Segment reporting* as notified under Companies (Accounting Standard) Rules, 2006, that deals with identifying segments and disclose information relating to reportable segments. As India is preparing to adopt Ind AS, Indian version of IFRS compliant accounting standards, there will be a drastic change in segment reporting. Standard equivalent to AS 17 is Ind AS 108: *Operating Segments*. The article focuses on the salient features and requirements of Ind AS 108.

CA. Ankur Bharuka

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I. Core Principle

Core principle states the prime objective that the standard intends to achieve. This principle is important to decide on the information required to be disclosed as per this standard.

The core principle is:
An entity shall disclose information to enable users of its financial statements to evaluate

- the nature and financial effects of the business activities in which it engages; and
- the economic environments in which it operates.

II. Operating Segments

As per the standard, Operating Segment is a component of an entity which satisfies all the following criteria:

1) Engages in business *activity that earns revenue and incurs expenses.*
2) Operating results are regularly reviewed by Chief Operating Decision Maker (CODM) for allocating resources and assessing its performance.
3) Discrete financial *information is available.*

The functions of CODM as specified above are:

1) Allocation of resources to the segment; and
2) Assess performance of segments and company.

> The standard has introduced the 'Management Approach' in determining the segments and related disclosures. This standard has enabled users of the **financial statement to view the entity's results and financial position with the eyes of the management i.e. how the management reviews the result and financial position of the entity. This 4would help users of the financial statements to envisage the** management's future course of action to some extent.

The CODM is decided on the basis of its functions and not on the title. The standard states that often the chief executive officer or chief operating officer or a group of executive directors are jointly responsible to discharge the functions on the CODM.

The standard has introduced the 'Management Approach' in determining the segments and the related disclosures. This standard has enabled users of the financial statement to view the entity's results and financial position with the eyes of the management i.e., how the management reviews the result and financial position of the entity. This would help users of the financial statements to envisage management's future course of action to some extent.

Usually in a company, an operating segment is headed by a segment manager, who is directly responsible for the performance and operation of the segment. He usually would maintain regular contact with the CODM to discuss operating activities, financial results, forecasts, or plans for the segment. A manager may be a segment manager of more than one operating segment. If the criteria of operating segments are satisfied, even more than one component managed by a single manager would qualify for separate operating segments.

One of the important conditions for different segments, is availability of discrete financial information. Financial information generally means balance sheet, profit & loss account and notes. However, standard does not require that all these informations should be available to qualify for a segment. If the information which will enable the CODM to discharge his function is discretely available, then the condition of availability of discrete financial information is deemed to be satisfied.

III. Reportable Segment

Reportable segment are those operating segments or aggregate of operating segments that meets or exceeds any of the following quantitative thresholds:

1) Its reported revenue, including both sales to external customers and inter-segment sales or transfers, is 10% or more of the combined revenue, internal and external, of all operating segments.
2) The absolute amount of its reported profit or loss is 10% or more of the greater, in absolute amount, of (i) the combined reported profit of all operating segments that did not report a loss and (ii) the combined reported loss of all operating segments that reported a loss.
3) Its assets are 10% or more of the combined assets of all operating segments.

Reportable segment can be a single operating segment or an aggregate of operating segments. As per standard, two or more operating segments may be aggregated into a single operating segment if,

1) aggregation is consistent with the core principle as stated above, i.e., it helps in evaluating nature and financial effects of the business activities and the economic environment in which it operates,
2) the segments have similar economic characteristics, and
3) the segments are similar in each of the following respects:
   a) the nature of the products and services;
   b) the nature of the production processes;
   c) the type or class of customer for their products and services;
   d) the methods used to distribute their products or provide their services; and
   e) if applicable, the nature of the regulatory environment, for example, banking, insurance or public utilities.

The standard allows management to report a segment which does not meet the quantitative threshold if in their view information about the segment would be useful to the user.

At least 75% of the entity's revenue shall be from the segments, identified as reportable segment. If this limit is not met, then additional segments shall be reported until at least 75% of the revenue is from reportable segments.

Information of other non-reported operating segments shall be combined and disclosed in an 'all other segments' category.

An operating segment which was reportable segment in the previous year, if it does not satisfy the criteria of reportable segment in the current year, can be reported as a segment, if the management is of the opinion that the segment is of continuing significance and its information is required to be reported separately. In case, an operating segment becomes a reportable segment only in the current year, previous year's information shall be restated for comparability purpose even though the segment did not satisfy criteria of reportable segment in the previous year. The standard has not laid down maximum limit on number of reportable segment, but has stated that if reportable segments are more than 10 then, then entity should consider whether a practical limit has been reached.

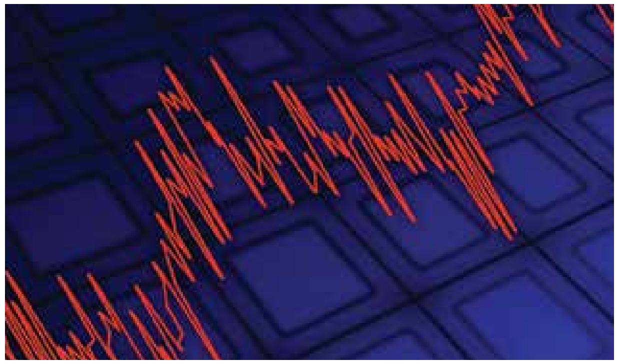
IV. Disclosure

1) As discussed above in the *core principle* paragraph, disclosure shall take into consideration the core principal. Standard requires some general information and some specific information about profit or loss, assets and liabilities of a reportable segment to be disclosed. Some of the disclosures are:
   a) factors used to identify the entity's reportable segments.
   b) types of products and services from which, each reportable segment derives its revenues.
   c) revenues from external customers and from transactions with other operating segments of the same entity;
   d) interest revenue and expenses;
   e) depreciation and amortisation;
   f) material items of income and expense;
   g) the entity's interest in the profit or loss of associates and joint ventures accounted for by the equity method;
   h) income tax expense or income; and
   i) material non-cash items other than depreciation and amortisation.

   Measurement

   The segment items shall be measured at the amount which is reported to CODM. Any adjustment made in revenue, expenses, gains or losses shall be included only if they are included to measure profit or loss reported to CODM.

An operating segment which was reportable segment in the previous year, if it does not satisfy the criteria of reportable segment in the current year, can be reported as a segment, if the management is of the opinion that the segment is of continuing significance and its information is required to be reported separately.



2) **Reconciliations**

   Standard also requires companies to prepare reconciliation of total reportable segment's revenue, profit or loss, assets and liabilities to entity's revenue, profit or loss, assets and liabilities.
3) **Entity-wide Disclosures**

   Certain entity-wide disclosures are required to be made by every company, even if they have only one reportable segment. This information shall be disclosed only if it is available or can be obtained without excessive cost.
   a) Revenues from external customers from each products and services.
   b) Revenues from external customers from domicile country and from foreign country.
   c) Non-current assets other than financial instruments, deferred tax assets, post-employment benefit assets, and rights arising under insurance contracts (i) located in the entity's country of domicile and (ii) located in all foreign countries in total in which the entity holds assets.
   d) Disclose external customers who contribute 10% or more or the entity's total revenue also disclose revenue from such customer.

V. Conclusion

The whole new concept of segments as viewed by management has evolved as compared to business and reporting segments as described by AS 17 – *Segment Reporting*. It would require substantial amount of time and efforts to comply with the requirements of Ind AS 108. But the standard prescribed a good approach and way of communication between management and owners (including other stakeholders). Implementation of the new standard would ensure proper, relevant and sufficient disclosures of segment information. ■

Proposed Special Audit Provisions - Another **Exemplification of Overturning the Settled Law?**

The tax authorities have, on rare occasions, resorted to provisions of Special Audit as contained in section 142(2A) of the Income-tax Act, 1961. However, with some proposed amendments through the Finance Bill 2013, the special audits, which are more or less of investigative nature, may no longer be rare and will have adverse ramifications for the assessee. It will not only leave them stultified and more prone to possible arbitrariness of AO but will also lead to protracted increased litigation. The proposed amendments seem to nullify the landmark judgments pronounced to curb possible arbitrariness of tax authorities, and thus need a very serious review at the earliest. Read on to know more…

CA. Sanjiv K. Chaudhary and CA. Amit Gupta

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An Audit can be of various types – statutory audit, cost audit, quality audit, energy audit, tax audit, etc. But, whatever be the type, an audit is commonly perceived as a cumbersome procedure and a resource-intensive exercise for any corporate. In the taxation world, most common is the tax audit as provided under section 44AB of the Income-tax Act, 1961 ('the Act'). The Act also prescribes Special Audit under the provisions of section 142(2A). This provision, rightly so, has generally not been resorted to by tax authorities, and has been a rare phenomenon until now. However, with recent amendments proposed by

Finance Bill, 2013, will "special audit" still continue to be rare? We shall learn more about special audit and the ramifications of the proposed amendments by Finance Act, 2013 as we go along in this article.

What is Special Audit

Section 142 of the Act provides that for the purpose of making an assessment under the Act, the Assessing Officer (AO) may make necessary enquiry by serving a notice upon the assessee.

Sub section 2A of section 142 of the Act provides that at any stage of the proceedings, if the AO considers it necessary, he may direct the assessee to get the accounts audited by an accountant who is nominated by the Commissioner or the Chief Commissioner. The AO may resort to the above section only in the following circumstances:

- In the opinion of the AO, there is a complexity in the account of the assessee;
- Directing for special audit would be in the interest of the revenue; and
- The AO has taken a previous approval of the Commissioner / Chief Commissioner.

All the above conditions need to be cumulatively satisfied in order to enable the AO to order for a special audit.

What are the Repercussions on Assessee

An assessee undergoes the process of statutory audit each year as per the timelines prescribed under the Companies Act, 1956. Coupled with this statutory annual audit, the Act prescribes tax audit under section 44AB of the Act for all assessees having turnover exceeding Rs. 60 lakhs. It is not only tedious, but also comes to the assessee with its own share of costs (the time cost of auditors, the time / fixed costs of resources of the assessee who are involved in the process and other incidental expenses).

If the assessee is also posited with the process of special audit, the same results in a very tedious exercise of audit being faced multiple times for a single year. To add to the difficulties, since the special audit can be directed only during the course of the assessment proceedings, it would relate to a much earlier year – which creates the problem of fetching old data, information, etc. Special Audit, being more in the nature of investigation, has its own civil consequences. Also, as held by the Apex court in the case of Sahara India1, Special Audit is more or less in the nature of an investigation and in some cases, may even turn out to be stigmatic. Even after the obligation to pay auditor's fees and incidental expenses has been taken over by the Central Government, civil consequences would still ensue on the passing of an order for the special audit. It is on account of these reasons that the recourse to provisions of special audit has to be done only and only if there is complexity in the accounts and the interest of the revenue will be protected if the audit is carried out in a relevant case.

Looking at it from assessee's viewpoint, the special audit may not only be undesirable, but may also leave the assessee stultified.

Legislative Amendments & Judicial Interpretations that Came in to Curb Possible Arbitrariness by Tax Authorities

In the past, several legislative amendments were brought into the section and judicial precedents were pronounced, which clearly conveyed that the AO or the tax department does not have "unbridled powers" to direct special audit for an assessee during the course of assessment. Some of the noteworthy amendments / judicial interpretations are discussed below:

- As per the erstwhile provisions of the Act, the cost of the special audit (including the remuneration of the auditor and other incidental expenses) as was determined by the department, was to be borne by the assessee; However, with effect from June 2007, the section was amended to provide that the cost of the special audit shall be paid by the Central Government. Not only this, even the guidelines for determination of such expenses have been prescribed.
- Earlier, there was no provision in the section which required the AO to accord an opportunity of being heard to the assessee before directing special audit. However, with effect from June 2007, a proviso was inserted in the section so as to provide that the AO shall not direct the assessee to get his accounts audited unless the assessee has been given a reasonable opportunity of being heard. This amendment was done, to give effect to the decision of Supreme Court in the case of ***Rajesh Kumar vs. DCIT (2006) (287 ITR 91).***
- There are various judicial precedents which provide that "nature and complexity in accounts" depending upon which a special audit may be directed, should be interpreted in a very restrictive manner. The direction for special audit should be issued only after careful application of mind:
    - Apex Court in the case of Sahara India[1] held

[1] Sahara India (Firm) vs. CIT (300 ITR 403) (2008)

It is worth reiterating that the proposed amendments in provisions relating to special audit would have very far reaching consequences on the future assessments and tax litigation. All medium to large business entities shall have the sword of special audit hanging as their accounts shall always be voluminous, even if not complex, and an AO can always be skeptical about whatever an assessee does. These provisions, if not reviewed on priority, the term "Special Audit" will become a vernacular term in the corporate world!

that before dubbing the accounts to be complex or difficult to understand, there should be a genuine and honest attempt on the part of the AO to understand the accounts maintained by the assessee, appreciate the entries made therein and in the event of any doubt, seek explanation from the assessee.

The AO should not take recourse to this provision merely to shift his responsibility of scrutinising the accounts of the assessee and pass on the buck to the special auditor.

- Allahabad High Court in the case of Swadeshi Cotton Mills[2] has held that power to direct special audit should not be exercised lightly. The satisfaction of the authorities should not be a subjective satisfaction. The word 'complexity' as used in the section is a nebulous word and all that is difficult to understand should not be treated as complex. What is complex to one could be simple to another. Therefore, special audit should not be directed after having a cursory look at the accounts, but, an honest attempt should be made by the AO to understand the accounts of the assessee.
- Delhi HC in the case of Delhi Development Authority[3] held that the accounts do not become complex merely because there are large number of entries. It is interesting to note what the High Court has observed:

  "Detailed scrutiny of large number of entries by itself, on a standalone basis, will not amount to complexity of accounts. The accounts do not become complex because merely there are large number of entries, e.g. a petrol pump may have substantial sales, to thousands of customers daily at prices fixed under law/Rules, but this by itself will not be the accounts complex. Similarly, an Assessing Officer is required to scrutinize the entries itself and verify them, but this does not require services of a Special Auditor or Chartered Accountant to undertake the said exercise."
- Calcutta High Court in the case of Bata India Ltd[4] has held that mere need for obtaining information not ascertainable from the accounts does not come within the term complexity in accounts; doubts as to correctness cannot be equated with complexity in accounts and special audit cannot be directed on the basis of suspicion.

The aforesaid judicial precedents had settled the position on how complexity should be construed for the purpose of directing special audit, with the intent that there is a captive and judicious exercise of powers by the tax authorities. Once again, the principle laid down by the Apex Court in the case of Sahara India[1] requires a mention. It has been held by the Apex Court that:

> *"The requirement of previous approval of the Chief Commissioner or the Commissioner in terms of the said provision being an inbuilt protection against any arbitrary or unjust exercise of power by the Assessing Officer, casts a very heavy duty on the said high ranking authority to see to it that the requirement of the previous approval, envisaged in the section is not turned into an empty ritual."*

Ironically, amending the law to overturn certain established judicial principles has become newfangled. After witnessing a plethora of retrospective amendments made by Finance Act 2012, which have been enacted to overturn various judicial precedents including the decision of apex court in the case of Vodafone[5], the Finance Bill 2013 has proposed some changes in the provisions of section 142(2A)[6] of the Act that seem to nullify the landmark judgements briefly discussed above.

As per the proposed amendment, AO may direct special audit u/s 142(2A) having regard to nature and

[2] Swadeshi Cotton MillsCo. Ltd. vs. CIT (171 ITR 634) (1987)
[3] Delhi Development Authority vs. Union of India (350 ITR 432) (2012)
[4] Bata India Ltd. vs. CIT (257 ITR 622 @ 631) (2002)
[5] Vodafone International Holdings B.V. vs. UOI and Anr. (341 ITR 1) (2012)
[6] This amendment is proposed to take effect from June 1, 2013

complexity of accounts and in addition, may also consider factors like: **volume of the accounts, doubts about the correctness of the accounts, multiplicity of transactions in the accounts or specialised nature of business activity of the assessee,** and interests of the Revenue.

Voluminous data or accounts are not uncommon in today's corporate scenario. Does this mean that every business which has a voluminous data can be asked to undergo a special audit? Further, all of us would agree and this point does not require any discussion that doubt about correctness of accounts is exceedingly subjective. It will be very easy for the AO to allege that he has doubts about the correctness of accounts produced before him and the assessee will have to get a special audit done.

Can this be the intention of the law makers? Here, it may be important to note what the Hon'ble Finance Minister announced in his Budget Speech at the time of presenting the direct tax proposals in Finance Bill 2013:

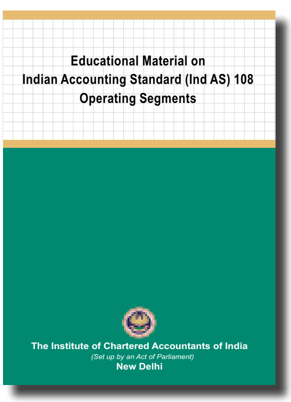
*'When I took over in August, 2012, I made a statement that **"clarity in tax laws, a stable tax regime, a non-adversarial tax administration, a fair mechanism for dispute resolution, and an independent judiciary will provide great assurance." That statement is the underlying theme of my tax proposals,** both on the direct taxes side and on the indirect taxes side'.*

While on one hand, the Government is coming out with new concepts like Safe Harbour Rules, Advance Pricing Agreements, etc. to reduce the tax litigation in line with the above-stated intent, the amendment under section 142(2A) is in complete contrast. The proposed amendment will again confer unbridled powers to the AO/Department to issue directions for special audit and in turn would lead to increase in litigation.

In the above background, it is worth reiterating that the proposed amendments in provisions relating to special audit would have very far reaching consequences on the future assessments and tax litigation. All medium to large business entities shall have the sword of special audit hanging as their accounts shall always be voluminous, even if not complex, and an AO can always be sceptical about whatever an assessee does. These provisions, if not reviewed on priority, the term "Special Audit" will become a vernacular term in the corporate world! It is our view that the settled law in regard to the provisions of special audit needed no amendment.■

New Publications

Educational Material on Indian Accounting Standard (Ind AS) 108, Operating Segments



The Ind AS (IFRS) Implementation Committee of the Institute of Chartered Accountants of India has issued Educational Material on Indian Accounting Standard (Ind AS) 108, *Operating Segments*, to provide gui-dance on the Ind AS. Ind AS 108, *Operating Segments*, requires the entities to follow the management approach to disclose information about operating segments. It requires an entity to disclose information to enable users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environments in which it operates. The purpose of this Educational Material is to provide guidance for proper implementation of the Standard by way of Frequently Asked Questions (FAQs). This publication contains summary of Ind AS 108 discussing the key requirements of the Standard in brief and Frequently Asked Questions (FAQs) on issues which are expected to be encountered while implementing this Standard. The text of Ind AS 108 and significant differences between Ind AS 108 and AS 17 have been included as Appendices to make this publication comprehensive.

Price:
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TDS on Commission Paid To Foreign Agents—Divergent Views!

Over the past few decades, India's contribution to the international trade has increased noticeably. This steep rise in India's share in the international trade could not be possible if the Indian enterprises wish to carry out their operations entirely from India. For better exploitation of the business opportunities available in the overseas markets, the Indian enterprises have increased the appointments of foreign agents who work on commission basis for the Indian businesses. The issue that arises in such type of transactions is that, whether the Indian enterprise is required to deduct, from the payment made to the foreign agent, tax at source under the Income-tax Act, 1961 (the Act). If at all, the tax is required to be deducted, then it has to be deducted under which section of the Act.

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Introduction

Over the past few decades, India's contribution to the international trade has increased noticeably. Just to put the things into perspective: India's total merchandise trade increased over three-fold from US$ 252 bn in FY 2006 to US$ 792 bn in FY 2012. Furthermore, the Exports-GDP ratio increased from 12.3% in FY 2006 to 16.3% in FY 2012[1].

[1] Source: http://www.eximbankindia.com/fore-trade.pdf

In Section 195(1), the crucial expression is 'any other sum chargeable under the provisions of this Act'. It would thus mean that the person making payment to the non-resident would be liable to deduct tax if the payment so made is chargeable to tax under the Act.

This steep rise in India's share in the international trade could not be possible if the Indian enterprises wish to carry out their operations entirely from India. For better exploitation of the business opportunities available in the overseas markets, the Indian enterprises have increased the appointments of foreign agents who work on commission basis for the Indian businesses.

The modus operandi in which this transaction moves forward is that the Indian enterprise appoints a foreign party as its agent for the purpose of soliciting customers for the overseas business of the Indian enterprise. The foreign agent explores the overseas market, finds more and more customers and then forwards the list of such probable customers to the Indian enterprise. Then, the Indian enterprise deals with such probable customer on its own, carries forward the export to such customer and finally, realises the sale consideration from the customer on its own account directly. For the services rendered by the overseas agent, he is paid an export commission by the Indian enterprise.

The Issue

The issue that arises in such type of transactions is that whether the Indian enterprise is required to deduct, from the payment made to the foreign agent, tax at source under the Income-tax Act, 1961 (the Act for short). If at all, the tax is required to be deducted, then it has to be deducted under which section of the Act.

Analysis

Article 265 of the Constitution of India states that no tax shall be levied except by authority of law. There are three stages in imposition of a tax. There is the declaration of liability; that is the part of the statute which determines what persons in respect of what property are liable. Next, there is the assessment. Liability does not depend on assessment that *ex hypothesis* has already been fixed. But the assessment particularises the exact sum which a person liable has to pay. Lastly come the methods of recovery, if the person taxed does not voluntarily pay [*Lord Dunedin in Whitney v. Commissioners of Inland Revenue, (1926) AC 37*, quoted in *Chatturam v. CIT (1947) 15 ITR 302, 308 (FC)*]. It means, for any taxing provision to be levied, there must be a charging prerequisite. In case of payments made to non-residents, Section 195 of the Act deals with the deduction of tax at source from the payments made to such non-residents. The relevant extracts of Section 195 of the Act are reproduced herein for the sake of ready reference:

> *"Any person responsible for paying to a non-resident, not being a company, or to a foreign company, any interest or* ***any other sum chargeable under the provisions of this Act*** *(not being income chargeable under the head "Salaries" shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force:…..."*

A bare perusal of Section 195 clearly shows that any person responsible for paying to a non-resident any other sum chargeable under the provisions of the Act shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash, or by the issue of a cheque, or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force. In Section 195(1), the crucial expression is 'any other sum chargeable under the provisions of this Act'. It would thus mean that the person making payment to the non-resident would be liable to deduct tax if the payment so made is chargeable to tax under the Act. Impliedly, if the payment is not chargeable to tax under the Act, the payer would not be liable to deduct tax at source. The chargeability to tax mentioned in the above provision is directly linked with Section 4 which is the main charging section. In other words, if the charge under Section 4 fails, automatically Section 195 would be inapplicable. Section 195 of the Act will be applicable only if the payment made to the non-resident is chargeable to tax. At this instant, it would be pertinent to refer to the Section 4, the relevant provisions of which are as under:

> *"Where any Central Act enacts that income-tax shall be charged for any assessment year at any rate or rates, income-tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions (including provisions for the levy of additional income-tax) of, this Act in respect of the total income of the previous year of every person".*

Thus, Section 4 makes it evident that the income tax shall be charged for a particular year in accordance with the provisions of this Act. In this regard, Section 5 of the Act which deals with the scope of total income provides, in the case of a non-resident assessee, provides as under:

"(2) Subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which—

(a) is received or is deemed to be received in India in such year by or on behalf of such person ; or

(b) accrues or arises or is deemed to accrue or arise to him in India during such year.

Explanation 1.—Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

Explanation 2.—For the removal of doubts, it is hereby declared that income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India."

The plain language of Section 5 provides that in the case of a non-resident assessee, the total income takes within its ambit two types of incomes: one, the income which is received or is deemed to be received in India; and second, the income which accrues or arises or is deemed to accrue or arise to him in India. In the present case, we are concerned with the latter limb of this scope. Section 9 of the Act provides for the income deemed to accrue or arise in India. This is a fiction created by the enactment which is essential in fixation of the charge under the Act. The relevant extracts of Section 9 are reproduced herein for the sake of ready reference:

"(1) The following incomes shall be deemed to accrue or arise in India:—

*(i) all income accruing or arising, whether directly or indirectly, through or from any **business connection** in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situated in India.*

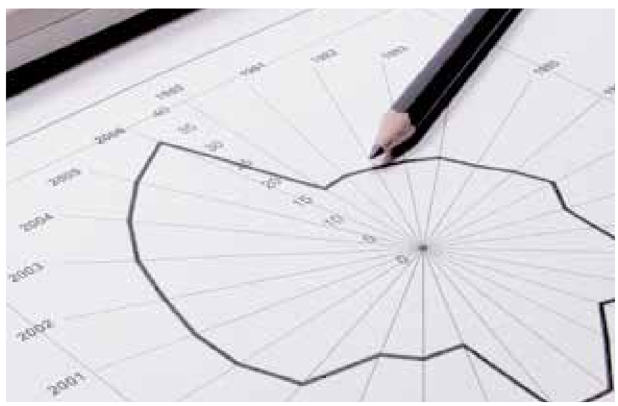
Explanation 2.—For the removal of doubts, it is hereby declared that "business connection" shall include any business activity carried out through a person who, acting on behalf of the non-resident,—

(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident; or

(b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or

(c) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident:

***Provided** that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business:*



The crux of the Circular No. 23 dated 23rd July, 1969 and Circular No. 786 dated 7th February, 2000 has **been that, as regards extent of profits attributable to India, only that portion of the profit, which can** reasonably be attributed to the operations of the business carried out in India, is liable to tax.

Provided further that where such broker, general commission agent or any other agent works mainly or wholly on behalf of a non-resident (hereafter in this proviso referred to as the principal non-resident) or on behalf of such non-resident and other non-residents which are controlled by the principal non-resident or have a controlling interest in the principal non-resident or are subject to the same common control as the principal non-resident, he shall not be deemed to be a broker, general commission agent or an agent of an independent status.

(ii) ...
(iii) …
(iv) …
(v) …
(vi) …
(vii) income by way of ***fees for technical*** *services payable by—*

a. *the Government ; or*
b. *a person who is a resident, except where the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or*
c. *a person who is a non-resident, where the fees are payable in respect of services utilised in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :*

Provided that nothing contained in this clause shall apply in relation to any income by way of fees for technical services payable in pursuance of an agreement made before the 1st day of April, 1976, and approved by the Central Government.

Explanation 1.—……

Explanation 2.—For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries".”

Issuance of Circular No.7/2009 by CBDT (withdrawing Circular Nos. 23 & 786) and the ruling of the AAR in the case of *SKF Boilers* and *Driers Pvt Ltd*, the pandora's box has been opened and the matter has again become an issue for litigation.

Section 9, as aforesaid, creates a legal fiction and provides that certain income shall be deemed to accrue or arise in India. In the present case, we are concerned with clause (i) and clause (vii) of the Section 9(1). Let us analyse each of these clauses one-by-one:

Section 9(1)(i): Business connection

- The plain language of Section 9(1)(i) of the Act provide that all income accruing or arising, whether directly or indirectly, through or from any business connection in India, shall be deemed to accrue or arise in India. Applying the above legal provisions of the Act to the factual matrix of the case, it becomes apparent that the question which needs to be addressed is that whether the income earned by foreign commission agents, whose work is limited to soliciting customers in relation to the overseas business of the Indian enterprise and forwarding the list of such probable customers to the Indian enterprise, accrues or arises from any business connection in India. In other words, does this foreign agents commission have any business connection with India.
- This matter has been the subject matter of various Circulars issued by the Central Board of Direct Taxes (CBDT). The relevant extracts of one such Circular (*Circular No.23 dated 23-July-1969*) is as under:

  “Foreign Agents of Indian Exporters: - A foreign agent of Indian exporter operates in

his own country and no part of his income arises in India. His commission is usually remitted directly to him and is, therefore, not received by him or on his behalf in India. ***Such an agent is not liable to income-tax in India on the commission."***

- The abovementioned Circular No. 23 mentioned that the foreign agents of Indian exporters are not liable to income tax in India on the commission. This Circular was relied by the Honourable Supreme Court of India in the case of *CIT vs. Toshoku Ltd* reported at *(1980) 125 ITR 525 (SC)* wherein the Apex Court held as under:

  "...if no operations of business are carried out in the taxable authorities, it follows that the income accruing or arising abroad through or from any business connection in India cannot be deemed to accrue or arise in India... ***The commission amounts which were earned by the non-resident assessee for services rendered outside India cannot, therefore, be deemed to be incomes which have either accrued or arisen in India..."***

Section 9(1)(vii): Fees for technical services

- If the amount paid by the Indian enterprise to the foreign agent is in the nature of 'fees for technical services' as defined in the Explanation 2 to Section 9(1)(vii) of the Act, then such income in the hands of the foreign agent shall be deemed to accrue or arise in India, and consequently, such foreign agent commission shall be chargeable to tax in India, and consequently, the Indian business enterprise shall be liable to deduct tax at source from such foreign agent commission under section 195 of the Act at the rates in force.
- In this regard, the relevant extracts of the ruling pronounced by the Authority for Advance Rulings (AAR), in the case of *Spahi Projects (P) Ltd.* reported at (2009) 315 ITR 374, are as under:

  "...Explanation 2 to Section 9 contains an inclusive definition of business connection but it applies only to a business activity carried out through a person acting on behalf of a non-resident. That situation does not exist here. Where no business operations are carried out in India by Zaikog, the attribution in terms of cl. (a) of the Explanation is not possible and therefore, no income can be deemed to accrue or arise in India merely because Zaikog promotes the business of the applicant in South Africa. As the income of Zaikog on account of the commission paid to it by the applicant is not chargeable to tax in India by virtue of art. 7 of DTAA and s. 9(1)(i) r/w the Explanation thereto, the applicant is not obliged to deduct the tax at source under s. 195...

  There could possibly be no controversy that Zaikog will not be rendering services of a managerial, technical or consultancy nature and therefore, the liability to tax cannot be fastened on it by invoking the provisions dealing with fee for technical services.."

- Thus, the AAR, in the above case, has categorically stated that the amount paid by an Indian business enterprise to its foreign agent as commission will not be covered in the definition of 'fees for technical services' as defined in the Explanation 2 to Section 9(1)(vii) of the Act.

Judgment of the Supreme Court in the case of *Toshoku Ltd.* is still the law of the land as regards the applicability of TDS provisions to foreign agents' commission paid by Indian exporters.

TDS liability under section 195 of the Act

Once it is established that the amount of commission paid by the Indian enterprise to its foreign agent is not chargeable to tax under the provisions of the Act, it becomes evident that the payer of such commission shall not be required to deduct tax at source under section 195 of the Act from such commission.

This position has been further strengthened by the clarification given by the CBDT in its Circular No. 786 dated 7th February, 2000. The relevant extracts of the said circular are reproduced herein for the sake of ready reference:

"The deduction of tax at source under section 195 would arise if the payment of commission to the non-resident agent is chargeable to tax in India. In this regard attention to CBDT Circular No. 23 dated 23rd July, 1969 is drawn where the taxability of 'Foreign Agents of Indian Exporters' was considered alongwith certain other specific situations. It had been clarified then that where the non-resident agent operates outside the country, no part of his income arises in India. Further, since the payment is usually remitted directly abroad it

cannot be held to have been received by or on behalf of the agent in India. Such payments were therefore held to be not taxable in India. The relevant sections, namely section 5(2) and section 9 of the Income-tax Act, 1961 not having undergone any change in this regard, the clarification in Circular No. 23 still prevails. ***No tax is therefore deductible under section 195*** *and consequently, the expenditure on export commission and other related charges payable to a non-resident for services rendered outside India becomes allowable expenditure."*

A bare perusal of the abovementioned Circular makes it apparent that no tax is required to be deducted by the Indian exporters to their foreign agents since such payments are not taxable in India.

Conflicting Position

The crux of the aforesaid Circulars [Circular No. 23 dated 23rd July, 1969 and Circular No. 786 dated 7th February, 2000] has been that as regards extent of profits attributable to India, only that portion of the profit, which can reasonably be attributed to the operations of the business carried out in India, is liable to tax. Further, the TDS provisions under section 195 of the Act are not applicable on the commission paid by the Indian exporters to their foreign agents. However, subsequently, the CBDT issued Circular No. 7/2009 dated 22nd October, 2009 withdrawing the aforesaid Circulars. The reason mentioned for such withdrawal was that interpretation of the Circular (No. 23 dated 23rd July, 1969) by some of the taxpayers to claim relief is not in accordance with the provisions of section 9 of the Income-tax Act, 1961 or the intention behind the issuance of the Circular (No. 23 dated 23rd July, 1969). As a result, the matter became a subject of opposing views.

Furthermore, the AAR, in the case of *SKF Boilers* and *Driers Pvt. Ltd.* reported at (2012) 248 CTR (AAR) 121, has pronounced the following ruling:

"We are concerned with the source of income of the two non-resident agents who had earned commission from the business activity of the applicant. Sections 5 and 9 of the Act thus proceed on the assumption that income has a situs and the situs has to be determined according to the general principles of law. The words 'accrue' or 'arise' occurring in section 5 have more or less a synonymous sense and income is said to accrue or arise when the right to receive it comes into existence. No doubt the agents rendered services abroad and have solicited orders, but the right to receive the commission arises in India when the order is executed by the applicant in India. The fact that the agents have rendered services abroad in the form of soliciting the orders and the commission is to be remitted to them abroad are wholly irrelevant for the purpose of determining the situs of their income. We follow the ruling of this Authority in [Rajive Malhotra AAR 671 of 2005, 284 ITR 564]. We therefore hold that the income arising on account of commission payable to the two agents is deemed to accrue and arise in India, and is taxable under the Act in view of the specific provision of Section 5(2)(b) read with section 9(1)(i) of the Act. ***The provision of section 195 would apply, and the rate of tax will be as provided under the Finance Act for the relevant year."***

Conclusion

After the above discussion, one thing is certain that post the issuance of Circular No.7/2009 and the ruling of the AAR in the case of *SKF Boilers and Driers Pvt Ltd (supra)*, the pandora's box has been opened and the matter has again become an issue for litigation. Having said that, one thing that still remains in favour of the non-applicability of the TDS provisions under section 195 of the Act is that as on date, the judgment of the Hon'ble Supreme Court in the case of *Toshoku Ltd. (supra)* is still the law of the land as regards the applicability of TDS provisions to foreign agents' commission paid by Indian exporters. ■

CBDT Circulars on Transfer Pricing of Contract R&D Centres: More Questions than Answers?

Characterization of development centers of multinational companies ('MNC') in India has been a vexed issue for a considerable time. While the MNCs contend that they are contract R&D service providers bearing insignificant or risk-free entities, the Transfer Pricing Officers ('TPO's') have been treating them as full or significant risk bearing entities – thus, attributing a higher mark-up for the functional and risk profile borne by them. Given the possibility of the issue of snowballing into a large-scale controversy, the Prime Minister in July 2012 announced the setting-up of Rangachary Committee to review the taxability of development centres. Based on the report of the Committee, the CBDT on March 26, 2013, issued Circulars No. 2 and 3, which seek to provide guidance on the application of Profit Split Method and conditions to identify development centres with insignificant risk respectively. Let us follow the perspective of the author who analyses the CBDT circulars on transfer pricing…

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Profit, the single most buzzword, drives the majority of the industry mandarins. For centuries, businessmen and business houses have aimed towards maximizing the profits of their operations. In the early days of zero or negligible competition, this was achieved by fixing higher prices. As competition begun to increase, margins came under pressure and consequently, businesses started to look outwards towards greener pastures. This cross-border trade sowed the initial seeds of today's globalization.

First movers of the cross-border trades reaped huge profits leading many others to follow suit. However, the economic pressures of various countries and increased competition brought a second wave of stressed-out margins. Due to the increasing economic strength of developed nations and the rising cost of living of their population, the cost of production spiraled in the developed countries and therefore, the cost of products became unviable or margins became thin. Resultantly, many multinational companies moved their production facilities or outsourced the production to under-developed or developing countries where the cost of production was still low compared to developed countries. Typically, as the goods were contract manufactured from entities in developing/ underdeveloped countries, the manufacturer was paid a nominal cost-plus mark-up for the functions performed by it and the low cost of production ensured that the goods retained their competitive edge.

Now, it is a given fact that, in today's highly competitive business environment where consumer is the king, it is necessary that business continuously searches options that lower their cost in order to increase their profit yet retain their competitive edge. In this context, the concept of location savings, i.e. moving certain operations to low-cost jurisdictions (like India) has gained prominence.

Globally, India along with a handful of other developing countries are considered to be an ideal location to avail benefit of location savings due to various advantages like huge pool of skilled yet relatively cheaper workforce, availability of raw materials at competitive rates, cheap infrastructure cost, various tax incentives, etc. India with its booming economy at the turn of the millennium, however, became first among equals.

The initial thought process of various multinational corporations was to avail benefit of the above factors to roll out products at cheap rate. However, multinational companies, especially the software and pharmaceutical majors realized soon that with a huge and young talent pool, even the high value-added services and innovation services could be moved to India. These multinational companies devote huge resources, both in terms of capital as well as manpower to innovate and create better or unique products. Due to higher cost of manpower in developed countries, more and more multinational companies have established captive subsidiaries in India for carrying out product development, software development, performing analytical work, etc.

Typically, the Indian subsidiaries have been positioned as providing routine services and do not employ valuable assets nor bear any significant risks. Resultantly, the Indian subsidiaries have been remunerated using traditional transfer pricing methodology like Cost-Plus Margin ('CPM') Method or Transaction Net Margin Method ('TNMM') so as to ensure that the Indian subsidiary earns a margin on its total costs which is commensurate with that earned by comparable uncontrolled service providers. In this kind of an arrangement, the foreign associated enterprise ('AE'), in most cases the parent company, earns the returns related to intangibles created as well as the benefit of location savings, if any.

The initial round of dispute between the taxpayers and the Indian transfer pricing authorities mainly centered on the level of margins that the captive subsidiaries should earn. For example, the Indian subsidiary engaged in contract R&D may be remunerated at let's say cost plus 18-20%; conversely, the view of the transfer pricing authorities was that the Indian subsidiary should be remunerated at let's say cost plus 30-35%. The mark-up varied depending upon the final list of comparable companies.

However, the controversy has now assumed larger proportions with the transfer pricing authorities contending that the captive subsidiaries/development centers are not rendering routine services but are involved in providing high-level end-to-end services leading to creation of intangibles. Accordingly, it is the contention of the transfer pricing authorities that the Indian subsidiaries should be remunerated for the intangibles which gets created by it.

Detailed discussion on the same can also be found from the India Chapter of the United Nations Practice Manual on transfer pricing issues for developing countries ('UN TP Manual').

India Chapter of UN TP Manual

Paragraphs 10.3.8.8 to 10.3.8.11 of the India Chapter of the UN TP Manual contains the observations of the Indian transfer pricing authorities on the vexed issue of characterization of the captive subsidiaries engaged in providing contract R&D services. The report mentions that typically the parent or the overseas group company positions the Indian subsidiary as a risk-free or limited risk bearing entity and hence, try to justify the low margins of the Indian subsidiary. Correspondingly, the overseas AE is positioned as the entity controlling all the risk and hence, entitled to a major part of the profit accruing as a result of the R&D activities.

The above arguments have been countered by the Indian transfer pricing authorities by stating that based on the detailed functional analysis conducted in course of the transfer pricing assessments, the Indian subsidiaries were found to be bearing significant risk. Further, these subsidiaries undertook detailed strategic decisions, monitoring of the R&D activity and employed substantial assets to conduct the R&D activity. Then the activities of R&D center resulted in creation of unique intangibles whose legal ownership was transferred to the parent company under the contract R&D arrangement. Given the same, the routine cost plus compensation model does not meet the arm's length criteria and additional compensation for development and transfer of such intangibles needs to be given to the Indian subsidiaries.

The contentions made by the taxpayer for characterization of Indian subsidiaries as low-risk contract R&D service provider and the counter claims of the Indian transfer pricing authorities is summarized:

Criterion	Argument of Taxpayers	Argument of Transfer Pricing Authorities
Functions	The parent company designs and monitors all the research programs of the subsidiary	Most multinational companies were unable to justify this claim by filing relevant supporting documents
Funding	Funds for undertaking the R&D program were provided by the parent company	While there is no dispute that funds were provided by parent company and hence, it bears risks related to it, the Indian subsidiary employs various assets like skilled manpower, knowhow for R&D etc. Hence, the Indian subsidiary too bears risk
Budgeting	The parent company prepares, controls and manages the annual budget of the subsidiary for R&D activities	The Indian management decides to allocate budget between different streams of R&D activities. Further, the day to day performance is anyways managed by the Indian management
Strategic decisions	The parent company controls and undertakes all the strategic decisions with regard to core functions of the R&D activity	The Indian subsidiary undertook day to day strategic decisions and monitored the R&D activities. Thus, it bore the operational risk
Risk of unsuccessful R&D activity	The parent company bore the risk of unsuccessful R&D activity	--

A reading of the arguments presented by the Indian transfer pricing authorities suggest that they do not accept the notion that the risk can be controlled remotely by the parent company and the Indian subsidiaries engaged in the R&D activity are risk-free entities. It is the contention of the Indian transfer pricing authorities that as the function of R&D activity is undertaken by the Indian subsidiary, therefore, the important strategic decisions relating to the same would also be undertaken by the management and employees of the Indian subsidiaries. Accordingly, the Indian subsidiary can be considered exercising control over the operational and other risks. Consequently, the ability of the parent company to remotely control the risk from a place where the core functions of R&D are not located is very limited. Hence, it is the Indian subsidiary and not the overseas parent company that assumes the substantial part of the risk, and, hence, should be remunerated accordingly.

Constitution of Rangachary Committee to Review

This divergent view relating to characterization of development centers as low-risk Contract R&D centers or full-fledged risk-bearing R&D service provider has resulted in quite a few high profile adjustments for Multinational companies. Given the prospect of the issue to snowball into huge controversy, the Prime Minister set-up a committee under the aegis of former CBDT Chairman Shri N. Rangachary to look into the issue and suggest the approach to taxation of Development centers. The Rangachary Committee submitted its report on September 14, 2012.

Though, the content of the report has not been released to various stakeholders for consultation, as a follow-up to the constitution of the committee, the CBDT on March 26, 2013, has issued Circular 3/2013 which lays down the conditions relevant to identify development centers engaged in contract R&D services with insignificant risk. Further, Circular 2/2013 deals with application of Profit Split Method ('PSM'), which determines an appropriate return of intangibles on the basis of relative contributions made by each associated enterprise.

Circular 3/2013: Identifying Development Centers with Insignificant Risks

The Circular states that an R&D development centre in India will be characterized as a contract R&D service provider bearing insignificant risks only if the following conditions are cumulatively complied with:

1. *Economically Significant Functions:* The foreign principal performs most of the economically significant functions in the R&D cycle while the Indian affiliate largely performs economically insignificant functions.
2. *Economically Significant Assets:* The principal provides funds/capital and other economically

significant assets including intangible assets to the Indian affiliate for R&D. The Indian affiliate does not use any other economically significant assets in its R&D activity.

3. *Control and Supervision:* The foreign principal performs the core functions; has the necessary "control functions" and actually controls and supervises the R&D activity of the Indian affiliate by undertaking strategic decisions. The Indian affiliate works under the direct supervision of foreign principal.
4. *Economically Significant Risk:* The Indian affiliate does not assume or bear any economically significant risks. Contractual terms will not be recognized if the terms are not consistent with the conduct of the parties. However, the circular has incorporated a deeming fiction to state that where the foreign principal is located in a low or no tax jurisdiction, it will be presumed that the foreign principal is not controlling the risks unless the Indian affiliate can rebut this presumption with appropriate facts before the tax authorities.
5. *Legal or Economic Ownership:* The foreign principal would be the legal and economic owner of the outcome of the research and the Indian affiliate would have no ownership rights on the same.

Further, the Circular states that the satisfaction of the above conditions will be determined primarily by analyzing the conduct of the parties and not merely by the contractual terms.

Going on by the flavor of the Circular, it seems that the CBDT has laid its emphasis on *substance over form* at the level of the foreign parent, as a pre-condition for the Indian R&D centre being accorded a *contract R&D service provider* status. The said is consistent with the views expressed in the Discussion Draft on transfer pricing aspects of intangible property issued by the Organisation for Economic Cooperation and Development ('OECD') in 2012. The draft lays down that while the contractual obligations between the two parties may be considered as a starting point for assessing which entity should be entitled to the returns on the intangible, the ultimate deciding factor should be considered to be the actual conduct between the parties. As per the OECD guidelines too, the entity which stakes its claim to the returns on the intangibles should demonstrate performance of the functions, assumption of risks and utilization of assets for undertaking the R&D activity.

Issuing a circular definitely shows the intent of the legislature to resolve the dispute. However, lot of clarity is required while identifying whether an Indian entity is an independent R&D unit or a contract R&D unit. There could be potential issues on interpretation of certain points like what shall be economically significant functions, who shall be covered under the definition of Principal i.e. whether the entity with whom service arrangement is made or group as a whole, how would one demonstrate performance of core functions i.e. what shall be the parameters, etc which needs clarity. Further, the conditions prescribed under the circular offers very little allowance for consideration of unique facts/ circumstances for qualifying an arrangement as that of a pure contract R&D. Accordingly, it would be advisable that the taxpayers are provided greater flexibility in getting their development centers qualified as contract R&D centers.

Additionally, the Circular does not specify the approach to be followed for benchmarking the transactions once the Indian subsidiary has been characterized as a low risk contract R&D service provider. Clarity on the approach to be followed in such a situation would definitely clear a lot of confusion and potential litigation for various entities qualifying as low risk contract R&D service providers.

Circular 2/2013: Application of PSM

The Circular seeks to provide clarification on use of PSM as the most appropriate method in the context of transfer pricing for R&D centres. The Circular mentions that In the absence of a correlation between the cost of the R&D activities and the return on the intangible developed through the R&D activity, the use of TNMM that seeks to estimate the value of the intangible based on a cost plus model, is discouraged; the circular encourages use of PSM in such cases.

The Circular notes that as per Rule 10B(1)(d) of the Income-tax Rules, 1962 ('Rules'), PSM can be applied in international transactions involving transfer of unique intangibles or in multiple international transactions which are so interrelated that they cannot be evaluated separately for determining the arm's length price on a standalone basis. In such a scenario, PSM which determines the appropriate return on intangibles on the basis of relative contributions made by each AEs would be a better method.

The reiteration of the Circular 2/2013 that PSM would be the most appropriate method to benchmark the transactions involving transfer of unique intangibles and issuance of this Circular along with Circular 3/2013 on Development Centers, seems to suggest that the revenue authorities are seeking to apply PSM as the most appropriate method in case of transactions involving R&D services through the contract R&D service providers where such R&D service providers or the Development Centers do not qualify as contract R&D service providers bearing insignificant risk as specified under the Circular 3/2013. However, the Circular has not clarified in certain terms the approach to be adopted in case of Development Centers which qualify as contract R&D service providers bearing insignificant risks.

Here, it needs to be noted that selection of PSM as the most appropriate method would inter alia depend upon the following factors as specified in Rule 10C(2) of the Rules:

1. Nature and class of international transactions
2. Nature of AEs entering into transactions and the functions performed, assets utilized and the risks assumed by them
3. Availability, reliability and comprehensiveness of the data required for application of the method
4. Degree of comparability between the international transaction and uncontrolled transactions and with the companies adopted as comparable to the tested party
5. Ability and extent to which reliable and accurate adjustments could be made for the differences between the international transactions and comparable uncontrolled transactions
6. Nature, extent and reliability of assumptions required to be made in application of the method.

Given the various factors which affect the selection of PSM as the most appropriate method, even if theoretically it may result in being the most appropriate method, application of the same may not be always possible. Accordingly, determination and application of the most appropriate method would need to be analyzed on case to case basis.

The Circular seems to have recognized this practical challenge and indirectly, provided flexibility to the transfer pricing officers that where PSM cannot be applied due to non-availability of information and reliable data, he may consider other methods like TNMM or comparable uncontrolled price ('CUP') method after giving reasons for non-applicability of PSM. Upon documenting such reasons, other methods may be applied by selecting comparables engaged in IP development in the same line of business and by making appropriate adjustments for value of IP transferred, location savings, etc.

However, the Circular has also reiterated that the onus of maintaining the requisite documentation for application of PSM is on the taxpayer (Rule 10D of the Rules). Accordingly, there should be good and sufficient reasons for the non-availability of such information with the taxpayer. Accordingly, taxpayers would be well advised to ensure that PSM may not be summarily rejected citing lack of data but adequate and convincing reasons may be documented by the taxpayer in support of non-availability of specific information which led to rejection of PSM as the most appropriate method.

Thus, the Circular certainly provides an insight to the thought process of the revenue authorities on the issue of transfer pricing of R&D service providers who do not qualify as the contract R&D service providers bearing insignificant risk. However, it is silent on the approach to be adopted on those contract R&D service providers who qualify as low risk bearing service providers as per the Circular 3/2013. The authorities would be well advised to provide clarity on the same so that scope of litigation related to the same could be avoided.

Concluding Thoughts

Overall, it appears to be a very welcome move on the part of the CBDT in proactively introducing guidelines and clarifications in the form of the above circulars. However, it is uncertain as to how the tax authorities would interpret and apply these circulars during the TP audits.

Though, the Circular 2/2013 provides for the application of PSM, it is essential to note that the CBDT has just reiterated the principles provided in the Rules and no new guidance has been provided. Further, the rejection of TNMM or other methods for transactions involving transfer of intangibles has been based on the premise that there is no correlation between costs incurred on R&D activities and return on an intangible developed through such R&D activities. Thus, while the Circular has sought to clarify the position on application of PSM, the ambiguity has not been adequately dealt with.

Further, as regards the Circular 3/2013 is concerned, it now appears to introduce the concept of substance while determining risk allocation. Thus, the focus of the transfer pricing authorities now seems to be 'substance over form' and it would be prerogative to demonstrate that the arrangement for undertaking the contract R&D services should have some justifiable business or commercial purpose. Accordingly, the transfer pricing authorities are now more likely to check the actual facts of the arrangement rather than go simply by the contractual terms. For example, where the Indian subsidiary is engaged in providing contract R&D services to its overseas AEs which has no R&D setup itself and therefore, in effect the complete R&D process is undertaken by Indian subsidiary itself, the transfer pricing authorities may not accept that the Indian subsidiary is a low or insignificant risk bearing entity doing only low-end contract R&D.

Given the fact that both the circulars have cast the onus of justifying the commercial arrangement and the methodology of undertaking transfer pricing analysis of the contract R&D service on the taxpayers, the taxpayers would be well-advised to undertake a detailed FAR analysis of the international transactions based on the actual functions performed, risks assumed and the assets employed and document its findings in support of its transfer price rather than rely on the contractual provisions alone.

Given the fact that taxpayers are already facing litigation on the issue, taxpayers would be advised to proactively consider the impact of these circulars on their transfer pricing arrangements and seek to adopt ways and means to mitigate litigation including obtaining ruling under the Advance Pricing Agreements route and treaty-based competent authority proceedings. ■

Transfer Pricing for Specified Domestic Transactions – An Insight

Finance Act, 2012 has made sweeping changes to the tax landscape in India. One such change pertains to the application of transfer pricing provisions to 'Specified Domestic Transactions'. In theory, all taxpayers crossing the threshold for specified domestic transactions would now be required to comply with the transfer pricing regulations. However, there are several challenges when it comes to practical application of the transfer pricing regulations to such transactions. This article seeks to hypothecate how transfer pricing would be applicable to specified domestic transactions, analysing some relevant Indian case laws, highlighting key differences and similarities, and noting some practical issues and unanswered questions. Further guidance on areas lacking clarity should help the cause of the taxpayers as well as tax professionals.

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Background

While examining related party transactions between two Indian Companies in the case of *Glaxo SmithKline*[1], the Supreme Court suggested that the CBDT should consider making Transfer Pricing Regulations applicable to domestic transactions. While making this suggestion, the Supreme Court categorically referred to two situations where transfer pricing provisions could be relevant in the context of domestic transactions. The two situations being:

- Transactions between loss-making and profit-making group entities
- Transactions between two related units (of the same taxpayer) having differential tax rates

[1] *CIT vs. Glaxo SmithKline Asia (P) Ltd. (2010) 236 CTR 113 (SC)*

In the case of *CIT vs. Glaxo SmithKline Asia (P) Ltd,* **[2010] 236 CTR 113 (SC), the Supreme Court suggested that the CBDT should consider making Transfer Pricing Regulations applicable to domestic** transactions.

By way of an amendment *vide* Finance Act, 2012, even specified domestic transactions are now required to adopt the arm's length principle.[2] The amendment, however, does not appear to have considered the Honourable Supreme Court's suggestions completely, and has sought to make transfer pricing applicable to all specified domestic transactions.

Until now, in the domestic context, the determination of fair value of transactions with related parties has been governed by the following categories of provisions:

- Specified payments to related parties
- Transfer of goods or services between taxpayer's units eligible for tax holidays, and other units
- Transactions by taxpayer having units tax holiday, with parties having close connection with such taxpayer.

Henceforth, the concept of arm's length price will supersede the notions of fair valuation as per the relevant sections, in respect of specified domestic transactions.

Practical Application of transfer pricing to specified domestic transactions

This section examines the probable manner in which current transfer pricing regulations will be applied to specified domestic transactions, as well as some practical challenges likely to be faced in the process.

Compliance requirements

Essentially, there are two-fold compliance requirements under the Indian transfer pricing regulations.

The first part of the compliance requirements relates to maintenance of robust and contemporaneous documentation. In this connection, Section 92D of the Income Tax Act, 1961 (the Act), read with Rule 10D of the Income Tax Rules, 1962 (the Rules) prescribes stringent documentation requirements on the part of the taxpayer, to justify the arm's length nature of transactions entered into by it, which are subjected to the transfer pricing regulations. Until now, Section 92D dealt with only international transactions. However, the Finance Act, 2012 has also included specified domestic transactions within the ambit of Section 92D.

It is interesting to note that although Section 92D has been amended to include specified domestic transactions, a similar amendment has not yet been made to Rule 10D. As a result, as of now, Rule 10D appears to apply only to international transactions. On a strict conjoint reading of Section 92D and Rule 10D, it appears that the taxpayer subjected to transfer pricing regulations in respect of specified domestic transactions is required to maintain sufficient documentation to prove the arm's length nature of such transactions. However, the documentation does not necessarily need to be in line with Rule 10D requirements.

The second part of the compliance requirements relates to obtaining an accountant's report, and submitting the same with the revenue authorities. Again, the relevant Section (Section 92E) has been amended to include specified domestic transactions, however, the relevant Rule (Rule 10E), and the format of the accountant's report (Form 3CEB) are yet to be amended. In the absence of clarity regarding Form 3CEB, it is not clear whether separate accountant's reports (Form 3CEBs) will need to be filed for international transactions and specified domestic transactions, or a single Form 3CEB will include both these categories of transactions.

Methods for determining arm's length price

Section 92C, which deals with computation of arm's length price specifies the use of five methods, and such other method as may be prescribed. Correspondingly, Rule 10B prescribes the manner of using each of the five specified methods, and Rule 10AB prescribes the sixth transfer pricing method.

Until now, Section 92C was specifically applicable only to international transactions, and has now been extended to also include specified domestic transactions. However, Rule 10B and 10AB currently deal only with situations involving international transactions, and are yet to be amended in order to give practical effect to the amendment to Section 92C.

[2] See Section 92(2A) and 92BA. Several other amendments have also been made to give practical effect to these provisions.

Scrutiny by Transfer Pricing Officer

Section 92CA, which provides for reference to the transfer pricing officer, has also been amended to include specified domestic transactions. However, question arises regarding the applicability of monetary limits for selecting cases for a transfer pricing scrutiny. It may be noted that the CBDT had issued an instruction[3] prescribing the monetary threshold (₹5 crore) for selecting cases for a transfer pricing scrutiny and reference to transfer pricing officer. The question arises regarding the applicability of this threshold to specified domestic transactions. While the current wordings are restricted to only international transactions, it cannot be assumed that specified domestic transactions would not be subjected to scrutiny. On the other hand, if the monetary limit of ₹5 crore is considered to be inclusive of specified domestic transactions, all cases involving specified domestic transactions would be subjected to compulsory scrutiny by the Transfer Pricing Officer, since the threshold for a transaction to be considered as a specified domestic transaction itself is ₹5 crore, which is the threshold prescribed by the above noted Instruction.

The option to approach the Dispute Resolution Panel (DRP) would also be available to a taxpayer where a transfer pricing adjustment in respect of specified domestic transactions is proposed consequent to an Order of the Transfer Pricing Officer.

Allowability of corresponding adjustments

The Indian transfer pricing regulations clearly stipulate that corresponding adjustments would not be permitted in the context of 'international transactions'.[4] In other words, if there is an upward adjustment to the taxable income of the taxpayer, a corresponding downward adjustment would not be allowed to be made to the taxable income of the associated enterprise of such taxpayer.

However, a plain reading of the provision suggests that this would not be automatically applicable to specified domestic transactions.[5] Accordingly, in the absence of any clear provision in this regard, the availability of corresponding adjustments in respect of specified domestic transactions appears to be uncertain.

If corresponding adjustments were denied even in cases involving specified domestic transactions, if the transfer prices in respect of such transactions are found to be inappropriate by the revenue authorities, the same could result in double taxation for the group.[6]

Deadlines for compliance and scrutiny

The due date for tax compliance (including filing of the tax return, as well as transfer pricing documentation and accountant's report) for all categories of taxpayers having international transactions would now become applicable to taxpayers entering into specified domestic transactions also.

Similarly, additional timelines available to the revenue authorities for completion of the scrutiny proceedings would also be extended for taxpayers entering into specified domestic transactions.

Differences between applicability of transfer pricing to international and specified domestic transactions

Broadly, general principles of transfer pricing would now be applicable to specified domestic transactions. However, there are several differences between how transfer pricing regulations were being applied practically to international transactions, and how these will now be applied to specified domestic transactions.

Some key differences are as under:

Threshold for applicability of transfer pricing regulations

By definition, transactions will be considered to be specified domestic transactions, if the sum of various transactions covered within the definition exceeds ₹5 crore, and any domestic transactions

Amendment made in Finance Act, 2012 does not appear to have considered the Supreme Court's suggestions completely, and has sought to make transfer pricing applicable to all specified domestic transactions.

[3] Instruction No. 3 of 2003 dated 20-5-2003
[4] Refer Second Proviso to Section 92C(4).
[5] The second Proviso to Section 92C (4) denies a corresponding adjustment to the 'associated enterprise'. However, 'associated enterprise' is not a relationship covered for the purposes of specified domestic transactions. Also refer Section 3.3 of this article for discussion on the relationships covered for specified domestic transactions.
[6] In fact, in the absence of a specific provision allowing corresponding adjustments, the better view appears to be that such corresponding adjustments will not be allowed even in cases involving specified domestic transactions.

In several cases, it has been held that where two related parties were in the same tax bracket, there was no motive for them to shift profits, and a disallowance under Section 40A(2) is not warranted.

below this threshold would not be covered within the ambit of transfer pricing regulations. On the other hand, there is no such prescribed threshold for international transactions, and transactions worth even a single rupee are subjected to transfer pricing regulations.

Revenue Loss to the Government

Any mispricing in the case of international transaction has the potential to cause revenue loss for the Government.[7] However, specified domestic transactions need not always result in a revenue loss to the Government. For instance, a transaction between two related parties does not result in a tax arbitrage for the group and revenue leakage for the Government, if each of them:

- is subjected to the same tax bracket,
- does not enjoy any special tax holidays or benefits, and
- does not have any carried forward losses eligible for set off.

CBDT Circular No. 6-P, dated 6-7-1968, which explains the provisions of the Finance Bill, 1968 (the year when Section 40A (2) was incorporated in the Income Tax Act), also mentions, in the context of Section 40A (2), as under:[8]

> *"It should be borne in mind that the* ***provision is meant to check evasion of tax*** *through excessive or unreasonable payments to relatives and associate concerns and should not be applied in a manner which will cause hardship in* bona fide *cases". (Emphasis supplied)*

In fact, in several cases, it has been held that where two related parties were in the same tax bracket, there was no motive for them to shift profits, and a disallowance under Section 40A(2) is not warranted.[9]

However, notwithstanding the tax neutrality of such transactions, the same appear to be subject to transfer pricing compliances, scrutiny, and could even result in transfer pricing adjustments[10].

Coverage of relationships

The kind of relationships covered by transfer pricing for international transactions, and that for specified domestic transactions are different. Transfer pricing for international transactions is applicable to transactions between 'associated enterprises' as defined under Section 92A. On the other hand, relationships included for applicability of transfer pricing to specified domestic transactions continue to be as per the particular Sections under which the transactions were being covered until now.

For instance, transactions with an associated enterprise as per Section 92A which is not a related party as per Section 40A (2), will not be considered as specified domestic transactions.[11] Conversely, transactions with entities which are related parties as per Section 40A (2), but not associated enterprises as per Section 92A could now be considered as specified domestic transactions.[12]

Similarly, tax holiday units also cover specific relationships for applicability of transfer pricing, as against 'associated enterprises' for the purposes of international transactions. Inter-unit transfers by tax holiday units to non-tax holiday units of the same taxpayer; or transactions by such taxpayer with a person having close connection with the taxpayer would be considered as specified domestic transactions and subjected to transfer pricing regulations.

Coverage of transactions

The coverage of transactions subjected to transfer pricing is also different between international

[7] There could also be situations where international transactions do not actually result in a revenue loss to the Government. Discussion on such situations is beyond the scope of this article.

[8] Para 74

[9] For instance, refer *CIT vs. Indo Saudi Services (Travel) (P.) Ltd. [2008] 219 CTR 562 (Bom); CIT vs. V.S. Dempo & Co. (P.) Ltd. [2011] 196 TAXMAN 193 (Bom.); Orchard Advertising (P.) Ltd. vs. Addl. CIT [2010] 8 taxmann.com 162 (MUM); DCIT vs. Lab India Instruments (P.) Ltd. [2005] 93 ITD 120 (PUNE)*

[10] Subject to clarity regarding availability or otherwise of corresponding adjustments – refer Section 2.4 of this article for a discussion on this subject.

[11] For instance, payments to subsidiaries (which would be considered as Associated enterprises as per Section 92A(2)(a)), may not be subjected to transfer pricing for specified domestic transactions. Refer *CIT vs. V.S. Dempo & Co. (P.) Ltd. (supra)* in this regard. Entities which fulfill other criteria of Sections 92A(2)(a) to (m) but are not related parties as per Section 40A(2) would also not be covered.

[12] An example of such a situation could be an equity holding of, say 25% by a company in another company. While the threshold for 'associated enterprise' relationship is 26%, as per Section 92A (2)(a), the threshold for a related party relationship is only 20%, as per Section 40A(2)(b) read with the explanation to Section 40A(2).

transactions and specified domestic transactions.

The definition of international transactions is very wide and covers several types of transactions.[13]

However, all transactions are not covered within the ambit of specified domestic transactions. For instance, Section 40A (2) only covers payments to related parties on account of payments for goods, services or facilities. Evidently, receipts from such related parties would not be covered within the ambit of specified domestic transactions.[14] Payment for capital goods also does not appear to be covered.

Further, as regards taxpayers having tax holiday units, specified domestic transactions would cover all inter-unit transfers of goods and services[15]; or all transactions between such a taxpayer with another person having a close connection with the taxpayer.

Similarly, there are transactions which get typically covered within the gamut of specified domestic transactions, but are generally not encountered in cross-border dealings with associated enterprises. Examples of these kinds of transactions include managerial remuneration, rental charges for use of immovable property etc.

Availability of Advance Pricing Agreements

Advance Pricing Agreements (APAs) have been introduced in the Indian transfer pricing regulations by the Finance Act, 2012, to reduce uncertainty and litigation with the revenue authorities.

Section 92CC, which deals with the concept of APAs, reads as under:[16]

> *"The Board, with the approval of the Central Government, may enter into an advance pricing agreement with any person, determining the arm's length price or specifying the manner in which arm's length price is to be determined* ***in relation to an international transaction*** *to be entered into by that person."* (Emphasis supplied)

Accordingly, it is evident that the option of applying for APAs is available only in respect of international transactions, and not in respect of specified domestic transactions—the tax positions which could continue being uncertain.

Section 92C, which deals with computation of arm's length price specifies the use of five methods, and such other method as may be prescribed.

Similarities between pre and post-amendment scenarios

A perusal of some of the relevant judicial precedents would suggest that the principles involved in a transfer pricing analysis have also been considered valid in the pre-amendment scenario. Further, some concepts under the pre-amendment laws would yet continue being applicable even when transfer pricing regulations are made applicable to specified domestic transactions. These include:

Coverage of Relationships and Transactions

As noted above, the coverage of transfer pricing regulations in terms of relationships and transactions covered will continue to be governed as per the respective existing Sections, and would not be replaced by the relationships or transactions as per Chapter X of the Act.

Comparability considerations

On various occasions, the Court had to delve into comparability considerations, to gauge whether the so-called comparable presented before it were indeed comparables, for determining the fair market value of the transactions under consideration. Some relevant principles are summarised hereunder:

FUNCTIONAL COMPARABILITY

The arm's length principle emphasises functional comparability for determination of appropriate comparables. However, even without a mention of the arm's length principle, the considerations of comparability have been upheld by Indian Courts in various decisions.

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[13] A seemingly all-pervasive definition of international transactions as existing in Section 92B (1) has been further expanded by the Finance Act, 2012, by way of an explanation with retrospective effect from 1.4.2002.

[14] For instance, refer *CIT vs. A.K. Subbaraya Chetty & Sons [1980] 123 ITR 592 (Mad); CIT vs. Udhoji Shrikrishnadas [1983] 139 ITR 827 (MP); Durga Rice & Gen Mills vs. AO [ITA No. 360/Chd/2012]*.

[15] A plain reading of the provisions suggests that other inter-unit transfers, for instance, transfer of assets would not be covered within the ambit of specified domestic transactions.

[16] Refer Section 92CC(1)

In the case of *Lab India Instruments*[17], it was held that commission paid @ 20% to sister concern cannot be compared with commission @ 10% paid to third parties, since the functions performed by such sister concern and the third parties were different and not comparable.[18]

Similarly, in the case of *Hive Communication*[19], in the context of Directors' remuneration, it was held that remuneration paid to two directors performing different functions (especially in the context of the industry in which the taxpayer operates), cannot be compared for the purposes of disallowance under Section 40A(2).

EXTENT OF COMPARABILITY

In the case of *Deep-raj Minerals*[20], it was held that transactions purported to be used for determining fair market value for Section 40A (2) purposes need to be comparable to the transactions under consideration, and not necessarily be identical.

Even under the arm's length principle, it is accepted that finding exact comparables could be challenging (especially finding external comparables for the CUP Method). Accordingly, the relevance of other methods which do not require such strict comparability requirements as CUP Method has been emphasised.

COMPARABILITY CONSIDERATION FOR INTEREST ON LOANS

In the case of *Shiv Agrevo*[21], it was held that interest on short term and long term funds can be different and cannot be compared for disallowing expense under Section 40A (2).

Even under the arm's length principle, although sometimes in a different context, it has been held that interest on loans with different characteristics cannot be compared.[22]

The Indian transfer pricing regulations clearly stipulate that corresponding adjustments would not be permitted in the context of 'international transactions'.

GEOGRAPHICAL DIFFERENCES

In the case of *West Coast Paper Mills*[23], the taxpayer had a paper unit and few power units in the state of Karnataka, from which power was supplied to the paper unit. It also had windmills in the state of Tamil Nadu, from which power was supplied to the Tamil Nadu State Electricity Board (TNSEB). For determining the fair value of supply of electricity to the paper unit for Section 80IA (8), the Mumbai Tribunal observed that the cost of production of power was different in the states of Karnataka and Tamil Nadu. Accordingly, it rejected that rate at which the taxpayer sold power to TNSEB, and adopted the rate paid by the taxpayer to Karnataka State Electricity Board for power purchased. It was further held that an adjustment needed to be made to exclude extraneous charges such as electricity duty etc., which were not connected with the taxpayer's business.

Use of appropriate allocation keys for cost allocation

In various cases involving tax holiday units, an appropriate cost allocation for shared resources becomes important, to determine the exact amount of profits available for the tax holiday. Courts have had the occasion to pass judgement on the question of appropriateness of the allocation key used.

In the case of *EHPT India Pvt. Ltd.*[24], the Delhi High Court held that headcount was an acceptable allocation key in the facts and circumstances of the case. In another case of *Controls & Switchgear Co. Ltd.*[25], turnover was held to be an appropriate

[17] *Supra*
[18] Also refer *CIT vs. Computer Graphics Ltd. [2006] 155 TAXMAN 612 (MAD)*
[19] *Hive Communication (P.) Ltd. vs. CIT [2011] 201 TAXMAN 99 (DELHI)*
[20] *Deep-raj Minerals vs. ACIT [2009] 31 SOT 144 (MUM)*
[21] *ACIT vs. Shiv Agrevo Ltd. [2009] 34 SOT 1 (Jp.) (uro)*
[22] For instance, refer *ITO vs. Maharishi Solar Technology Pvt. Ltd. [ITA No. 4561/Del/2009]*, wherein, size, and terms and conditions of the loan were held to be important comparability considerations. Similarly, in *Aithent Technologies Pvt. Ltd. vs. ITO [2012] 134 ITD 521 (DELHI)*, the Delhi Income Tax Appellate Tribunal (Tribunal) observed several comparability considerations for loans, including period of loan amount, currency, interest rate basis etc.
[23] *West Coast Paper Mills Ltd. vs. ACIT [2006] 103 ITD 19 (MUM)*
[24] *CIT vs. EHPT India (P.) Ltd. [2012] 204 TAXMAN 639 (DELHI)*
[25] Controls & Switchgear Co. Ltd. vs. DCIT [2012] 204 TAXMAN 53 (DELHI) (MAG)

Any mispricing in the case of international transaction has the potential to cause revenue loss for the Government. However, specified domestic transactions need not always result in a revenue loss to the Government.

allocation key for allocation of indirect expenses. It would not be out of place to mention that, although in a different context[26], even under the transfer pricing regime, turnover and headcount have been held to be acceptable allocation keys.[27]

Differences between pre and post-amendment scenarios

There are several important differences between the way payments to domestic related parties was examined until now and how such payments would be looked at going forward. The key areas of differences are highlighted below.

Concept

Under the pre-amendment scenario, the valuation of all payments to related parties was required to be justified using 'fair market value'. Similarly, in respect of tax holiday units, inter-unit transfers of goods or services were required to be carried out at 'market value'. Intra-group transactions by taxpayers having tax holiday units were required not to result in 'more than the ordinary profits' for the taxpayer. However, these terms have not been defined under the Act. Divergent interpretations of these terms by taxpayers as well as revenue and judicial authorities have resulted in significant litigation.

After the amendments, the concept used for justification of the fair valuation would be that of arm's length price. Arm's length price has been defined[28] as:

> *"A price which is applied or proposed to be applied in a transaction between persons other than associated enterprises, in uncontrolled conditions."*

The arm's length price is required to be computed using any of the six[29] specified methods, which is the most appropriate method under the facts of the case.

The concept of ALP is more structured as compared to fair market value, and provides some degree of certainty and guidance regarding the computation of the fair valuation of the transaction at hand.

Ad-hoc adjustments

Fair market value being a flexible concept, often resulted in arbitrariness and ad-hoc adjustments without any reasonable basis.

The case of Hinduja Group[30] is a case in point. In this case, the revenue authorities had provided an ad-hoc adjustment to the taxpayer in relation to rent paid by it to its related party, and reduced the amount of disallowance which could have been made otherwise. In a subsequent year, the Mumbai Tribunal, deciding in favour of the taxpayer, insisted that such ad-hoc adjustment should be continued to be provided to the taxpayer, and deleted the disallowance made by the revenue authorities.

There have also been several cases wherein, the Revenue Authorities have disallowed expenses on an ad-hoc basis, and such disallowances have been deleted by the Judicial Authorities[31].

The room for making ad-hoc adjustments appears to be restricted now, given the application of arm's length principle to specified domestic transactions.

Burden of proof

Section 40A (2) reads:

> *"…and the **Assessing Officer is of opinion** that such expenditure is excessive or unreasonable…"* (Emphasis supplied)

Accordingly, it would appear that until now, the burden of proof was placed on the Revenue Authorities for cases involving payments to related parties.[32]

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[26] Cost contribution allocation for centrally provided services

[27] See *Dresser-Rand India (P.) Ltd. vs. Addl. CIT [2011] 47 SOT 423 (MUM)*

[28] Section 92F(ii)

[29] Refer Section 92C read with Rule 10B and 10AB for details of prescribed methods.

[30] *DCIT vs. Hinduja Group India Ltd. [2008] 22 SOT 237 (MUM)*

[31] For instance, refer *Emersons Process Management India (P.) Ltd. vs. Addl CIT [2011] 47 SOT 157 (MUM) (URO); Gujarat Guardian Ltd. JCIT [2008] 174 TAXMAN 151 (CHD)(MAG)*

[32] Decisions of various Courts have also upheld this view. For instance, refer *DCIT vs. Choice Sanitaryware Industries [2011] 9 taxmann.com 120 (RAJKOT); Mittal Metal vs. ITO [2008] 21 SOT 186 (DELHI) (SMC); Marghabhai Kishabhai Patel & Co. vs. CIT [1977] 108 ITR 54 (GUJ.); DCIT vs. Lab India Instruments (P.) Ltd. (supra)*. However, in *CIT vs. Shatrunjay Diamonds [2003] 128 TAXMAN 759 (Bom)*, the burden of proof in cases involving Section 40A(2) was held to be shifted to the taxpayer.

However, after the amendment made by the Finance Act, 2012, the documentation and compliance requirements for specified domestic transactions are in line with international transactions. Accordingly, the burden of proof is placed on the taxpayer for determining the fair transfer price of specified domestic transactions.

Based on the above, it can be said that the obligation is now cast on the taxpayer, to ensure that specified domestic transactions are compliant with the arm's length standards, rather than mere basic reporting requirements prior to the amendment.

Managerial Remuneration

In several cases, payment of a certain amount of managerial remuneration, or increase in managerial remuneration as compared to the last year(s) has been justified considering the increase in sales and profitability of the taxpayer.[33]

However, under the arm's length principle, the amount of remuneration would also need to be justified based on an appropriate comparable benchmark, rather than only qualitatively justifying the validity of payment or increase in the amount of the remuneration.

Interest paid to related parties – nexus with loans given

The approach to determine the fair market value of interest paid on loans taken from related parties in several cases has been that high interest paid to related parties cannot be disallowed if the nexus of such related party loan with a low interest-bearing loan given by the taxpayer cannot be proved.[34]

Under the arm's length principle, the stress is on the comparability of comparable interest rates, rather than on the nexus between loans taken and loans given by the taxpayer.[35]

Use of related party/AE as comparables

There have been divergent Court Rulings in the context of whether payments to other related parties/group companies can be used as valid indicators of the fair market value of the goods/services in consideration.

For instance, in the case of *Diebold Systems*[36], payment to one related party was held as an indicator of fair market value, and used by the Revenue Authorities to make adjustments to the purchase price paid for the same products to other related party. This was also subsequently upheld by the Chennai Tribunal.

Conversely, in the case of *Van Oord Dredging*[37], payments made to one related party were held not to be an indicator of fair market value for making adjustments in prices paid to another related party.

Henceforth, in respect of specified domestic transactions, the stress would be on obtaining third party comparable data, either internal or external; and use of related party data for benchmarking arm's length nature of any payment would not be allowed.[38]

Applicability to tax holiday units/taxpayers

In relation to taxpayers enjoying profit-linked tax holidays, the concept of fair value has been applied to ensure that such taxpayers are not over-stating incomes or under-stating expenses, and thereby, claiming higher profit-linked tax deductions.

In cases where such tax holiday entities have been subjected to transfer pricing provisions, it has been held unanimously in various cases, that arm's length price determined by the Revenue Authorities as per the transfer pricing regulations cannot be considered as the fair market value for disallowing the profit-linked deduction.[39]

The kind of relationships covered by transfer pricing for international transactions, and that for specified domestic transactions are different.

[33] For instance, refer *Jagdamba Rollers Flour Mill Ltd. vs. ACIT [2009] 117 ITD 260 (NAG) (TM); Abbas Wazir (P.) Ltd vs. CIT [2003] 133 TAXMAN 702 (AL.)*.
[34] For instance, refer *Deputy Commissioner Vs. Shripal S. Morakhia [2006] 7 SOT 609 (MUM)*.
[35] Refer, for instance, *VVF Ltd. vs. DCIT [ITA No. 673/Mum/06]; Aithent Technologies Pvt. Ltd. vs. ITO (supra)*
[36] *Diebold Systems (P.) Ltd. vs. ACIT [2006] 8 SOT 585 (CHENNAI)*
[37] *Van Oord Dredging & Marine Contractors BV vs. DDIT [2007] 105 ITD 97 (MUM)*.
[38] In a slight departure from this position, the Mumbai Tribunal, in *Bayer Material Science (P.) Ltd. vs. Addl. CIT [2012] 134 ITD 582 (MUM)* has held that in cases where the type of transaction at hand normally occurs only between associated enterprises, a controlled transaction can also be used as a valid comparable for determining arm's length price, provided that such controlled transaction is at arm's length.
[39] Refer, for instance, *M/s Tweezerman (India) Private Limited vs. Addl. CIT [2010] 4 ITR(TRIB.) 130 (CHENNAI); M/s. Visual Graphics Computing Services (India) Pvt. Ltd. vs. ACIT [2012] 15 ITR(TRIB.) 393 (CHENNAI); Weston Knowledge Systems & Solutions (India) Pvt. Ltd. vs. ITO [2012] 23 taxmann.com 215 (Hyderabad – Trib.)*

However, the concept and definition of arm's length price have now been specifically imposed on the existing concept of fair market value in cases of such taxpayers. Accordingly, the above-mentioned Court Rulings will now be inapplicable in this context.

Way forward for taxpayers

Application of transfer pricing regulations to specified domestic transactions will certainly add to the compliance requirements of Indian taxpayers. This would significantly impact domestic business houses which have several group entities and multiple inter-company transactions.

However, rather than application of transfer pricing to specified domestic transactions, what really appears to have added to the compliance burden of taxpayers, is the shifting of onus of proof from the revenue authorities to the taxpayer.

While the deadline for reporting requirements for specified domestic transactions for Financial Year 2012-13 would be 30th November 2013, documentation for such transactions is required to be contemporaneous, and therefore, the documentation requirements have already triggered.

The approach of the taxpayers will now need to be proactive, and not reactive. Rather than waiting for the closure of accounts, it would be prudent on the part of taxpayers to review their transactional structures and pricing policies at the earliest, and amend such structures and policies to the extent required, in order to be compliant with the arm's length standards. A timely review would provide taxpayers with sufficient time to take corrective actions, if necessary, as well as guide them on the contemporaneous documentation requirements. ■

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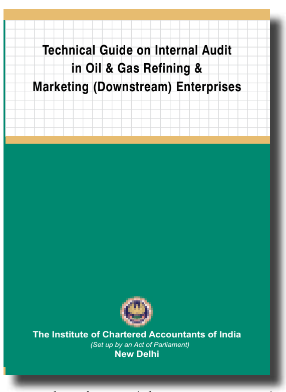

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Designing and Implementing an Effective FCPA and UKBA Compliance Program

As India Inc goes global, compliance with anti-bribery legislations of the developed countries, in particular the United States of America (the "US") and the United Kingdom (the "UK"), may become essential. The Foreign Corrupt Practices Act, 1977 (the "FCPA") was enacted in the US and the Bribery Act, 2010 (the "UKBA") was made effective in 2011 in the UK, to act tough against cases of bribery. An attempt has been made in this article to describe, how an effective compliance program can be designed and implemented, to ensure an adherence to the anti-bribery laws of the US and the UK. Read on…

Paras Kumar Jain

(The author is a Company Secretary, who may be reached at paraskumar.j@nuziveeduseeds.com.)

FCPA and UKBA

Foreign Corrupt Practices Act, 1977 (the "FCPA") was enacted by the US Congress in response to a maelstrom of outrage following the report by the Watergate Special Prosecutor that US corporations were bribing government officials in foreign lands. Following the pressure mounted by the Organisation for Economic Cooperation and Development and the US to act tough against the bribery, the UK Parliament passed the Bribery Act 2010 (the "UKBA") and brought the same into force from 1st July, 2011.

The FCPA prohibits direct or indirect bribing of foreign public officials, political parties or politicians, for the purpose of obtaining or retaining business or securing improper advantage. It also mandates that companies registered with securities exchange commission to maintain accurate books and records of all transactions and an effective internal control system. It applies broadly to the US companies and their foreign subsidiaries, individuals, companies that have issued securities registered in the US, directors, employees and agents of the US businesses, and foreign nationals and businesses that cause prohibited acts in the US.

The UKBA prohibits bribery of both government and private officials, whether in the UK or at any place in the world by a person having 'close connection' [defined under Section 12] with the UK. Close connection is a very widely defined term under the UKBA and includes individual holding UK citizenship or nationality or a body incorporated in the UK. A criminal offence will be committed under the UKBA if an employee or 'associated person' [defined under Section 8] acting for, or on behalf of, 'relevant commercial organisation' [defined under Section 7] offers, promises, gives, requests, receives or agrees to receive a bribe; and if such relevant commercial organisation does not have the defense that it has adequate procedures in place to prevent bribery by its employees or associated persons.

Distinction between the FCPA and the UKBA:

While both the FCPA and the UKBA deal with anti-bribery provisions, following are the key differences:

Particulars	FCPA	UKBA
Type of Bribery	Applies only to bribery of foreign official	Prohibits bribe to 'any person' (including bribe to individual or corporate)
Active and Passive Bribery	Giving bribe is an offence, but receiving the same is not.	Both receiving and giving a bribe is an offence.
Mens rea	It must be proved that person offered the bribe with a "dishonest or corrupt" intent.	It is not required to prove the dishonest or corrupt intent in case of bribery to foreign public officials. The company is strictly liable for failure to prevent acts of bribery.
Facilitation Payment	Allows facilitation payments under limited circumstances, provided such payments are properly reported in the company's financial records.	Facilitation payments are illegal.
Promotional expenses	Allows promotional expenses if it can be demonstrated that they were a reasonable and bona fide expenditure.	No such provision. However Ministry of Justice ("MoJ") has provided some comfort on this aspect in its guidance by stating that hospitality may be legitimate, provided it is reasonable and proportionate for the organisations' business.
Defense	Existence of compliance program is not a defense; however it would be an essential factor for considering prosecution and the terms of settlement.	While relevant commercial organisation is accountable for failing to prevent bribery, it is a statutory defense if it is proved that the relevant commercial organisation had in place "adequate procedures" designed to prevent bribery.
Liability of senior officers	Senior officers (officer, director, supervisor, manager, or another person having "control" over the conduct) may be held liable for offence in their capacity as a 'control person'.	Senior officers (director, manager, secretary or other similar officer of a body corporate) may not be liable if such offence is committed without their consent or connivance.
Penalties	Individual: Bribery. Imprisonment upto 5 years and fine up to US$ 2,50,000 per violation. Penalties may be levied under other laws as well. Accounting Offence. Imprisonment upto 20 years and fine up to US$50,00,000 per violation. Penalties may be levied under other legislations as well. Corporate: Bribery. Fine up to US$ 20,00,000. Penalties may be levied under other laws as well. Accounting Offence. US$ 250,00,000 or twice the benefit sought. Penalties may be levied under other laws as well.	Individual: Imprisonment upto 10 years and unlimited fines. Penalties may be levied under other laws as well. Corporate: Unlimited fines. Penalties may be levied under other laws as well.

Relevance to Indian Companies

a) Under the following circumstances, an Indian company (including its directors, employees or agents) is required to comply with the FCPA and the UKBA :

FCPA	UKBA
1) has principal place of business is US; or 2) is listed on the US stock exchange(s); or 3) is required to file periodic reports with the US Securities and Exchange commission (the "SEC"); or 4) is a branch or subsidiary or a joint venture of the US entity.	1) it carries on a business or any part of a business in the UK;or 2) is listed on the UK stock exchange(s); or 3) is a branch or subsidiary or a joint venture of the UK entity.

b) An Indian company positioning itself to act as an agent, representative, distributor, reseller, consultant, contractor, sub-contractor or as any other service provider, or for merger, joint venture, acquisition, or foreign investment from an organisation, subject to the FCPA and the UKBA (the "covered persons"), needs to ensure that it complies with the FCPA and the UKBA provisions, because the covered persons may:

1) conduct adequate and proportionate due diligence to ascertain past and present compliance with anti-bribery laws;
2) insist on representation, warranties and indemnities in the contracts on past, present and future compliance with anti-bribery laws;
3) insist on the right to terminate the contract or as mandatory 'put option' on the Indian company to exit in the event of violations of anti-bribery laws.

c) **FCPA cases relating to Indian Companies.**

1) *SEC vs. Oracle Corporation:* The SEC charged Oracle Corporation ("Oracle") with violation of the FCPA for failing to prevent its Indian subsidiary from secretly setting aside money off the company's books that was eventually used to make unauthorised payments to phony vendors in India. Oracle without admitting or denying the SEC's allegations paid US$ 20,00,000 to settle the SEC's charges.

2) *SEC vs. Westinghouse Air Brake Technologies Corporation:* The SEC charged Westinghouse Air Brake Technologies Corporation ("WATC") with violation of the FCPA for improper payments that WATC's Indian subsidiary, Pioneer Friction Limited ("Pioneer"), made to employees of the government of India in order to obtain or retain business from the Indian railway.WATC without admitting or denying the SEC's allegations paid approximately US$288,000 to settle the SEC's charges. Similarly, in a related matter, under non prosecution agreement with Department of Justice, US (the "DoJ"), WATC paid a penalty of US$ 3,00,000.

3) *SEC vs. Chandramowli Srinivasan:* The SEC charged Mr. Chandramowli Srinivasan ("Mr. Chandramouli"), the former president of A.T. Kearney India Limited ("ATK") for his role in improper payment. Mr. Chandramowli without admitting or denying the SEC's allegations paid US$70,000 to settle the SEC's charges. In related administrative proceeding under file no. 3-12825 dated 25th September, 2007, Electronic Data Systems Corporation, holding company for ATK without admitting or denying the SEC's allegations paid US$ 4,90,902 to settle the SEC's charges.

4) *SEC vs. The Dow Chemical Co:* The SEC charged Dow Chemical Company ("Dow") with violation of the FCPA for improper payments by its Indian subsidiary to a government official to speed up registration of its product. Dow without admitting or denying the SEC's allegations paid US$3,25,000 to settle the SEC's charges.

Designing and Implementing FCPA and UKBA Compliance Framework

Importance of designing and maintaining a strong compliance program for the FCPA and the UKBA stems from the fact that:

a) it provides assurance to the stakeholders that the company operates ethically and transparently;
b) under the FCPA, in case of violation, it may help in avoiding prosecution or reducing the penalty; and
c) under the UKBA, it acts as full defense against liability if it is established that proper and adequate procedures were in place to prevent bribery.

The DoJ in various cases settled under the FCPA has prescribed best practices for the FCPA compliance program. The MOJ in accordance with Section 9 of the UKBA, on 30th March, 2011, published 'adequate procedures' guidance that relevant commercial organisations can put in place, to prevent their 'associated persons' from committing bribery.

Combined analysis of the compliance programs prescribed under various deferred prosecution agreements and non-prosecution agreements under the FCPA by the DoJ and the guidance of the MoJ on the 'adequate procedures' under the UKBA, reveal that there are several important components to an effective FCPA and the UKBA compliance program ("compliance program"). Following are the practical tips for a company to consider while designing and implementing the compliance program:

1. Top-level Commitment. The tone at the top is fundamental to an organisation's culture and is the foundation for building blocks of compliance program. Like any other important initiative, it is impossible to effectively implement a compliance program without support of the higher echelons. The Board and the senior management should be educated about the anti bribery laws and the vigour of the enforcement agencies. Additionally, it is vital for the success of a compliance program to seek participation and backing from an organisation's various business leaders and stakeholders. The buy-in for a compliance program would only come when the importance of compliance and the value it brings to the organisation is clearly articulated to all concerned. Compliance program with top level commitment would essentially have :
- adequate financial and other resources;
- a senior management member overseeing the development and roll out of compliance program; and ensures that it evolves and functions the way it is designed to work;
- a "zero tolerance anti bribery policy" in every facet of the organisation's operation; and
- explicit message of the consequences that all concerned will suffer in the event they violate the anti bribery policy.

2. Risk Assessment. It is only upon identification of the risks, that efforts and resources can be directed for developing a program for mitigating them. Therefore, it is essential to begin the process with the risk assessment. The risk assessment exercise *interalia* involves review of social and political environment of the geography, business activities, business processes, local business practices and customs, relationships with partners, suppliers, agents, consultants, intermediaries, government bodies and own employees, spot bribery risks inherent in those activities, and try to estimate the probability of the incidence of the risks and its impact on the business.

The risk assessment procedures should be designed keeping in view the nature and size of the organisation, its activities, customers and countries of operation. The risk assessment can be done using various methodologies and tools including reviewing audit reports, customer complaints, employee interviews, surveys, review of targeted accounting records.

Having identified the relevant areas of risk, the next task is to establish relevant and proportionate policies, procedures and controls that address the likely areas of bribery.

3. Proportionate Policies and Controls. The company should establish strong policies and controls to prevent and detect violation of applicable anti corruption laws and the organisation's code of conduct. While the type of policies and procedures may defer from organisation to organisation depending on the nature and size of the business, and the countries of operation, but they all need to be simple and complete. Effective policy is one which explains, what constitutes an improper payment, dos and don'ts, and what to do if improper payment is requested. It is imperative that the policies and procedures should not be just on paper, but should also be implemented in a manner that promotes "ethical conduct" and allegiance to compliance with applicable anti bribery laws. Following policies and controls are relevant for effective implementation of compliance program:

(i) Code of Conduct: Code of conduct is an important element of compliance program as it gives broad guidelines for expected ethical behaviour from all concerned. Code of conduct should detail required standards of behaviour from directors, employees, third parties, viz. agents, representatives, distributors, resellers, consultants, contractors, sub contractors or any other service provider ("business associate").

Following are the best practices in drafting and implementing an effective code of conduct:
- code of conduct should act as a guide to apposite conduct by detailing what is expected from the employees and business associate in their dealings with the company and outside of the company;
- ensure that all concerned understand their responsibilities under the code of conduct;
- consider conduct in relation to the code of

conduct when evaluating employees or business relationships;
- roll out annual questionnaire on code of conduct to be filed by all concerned;
- all concerned to annually affirm compliance with code of conduct; and
- always act to stop violations of the code of conduct.

(ii) Anti-Bribery Policy: Zero tolerance towards bribery, consequences in case of breach, and the company's aim to maintain anti bribery compliance as business as usual rather than as a one-off exercise should be made clear through this policy. Following are the best practices in drafting and implementing an effective anti bribery policy:
- the policy should be commensurate with the company's size, industry, culture and the level of risk the company faces;
- the policy should describe the company's position on anti bribery, outline the process for identifying, reporting and dealing with suspected anti bribery cases;
- ensure that the applicability and procedures are clear and employees and business associate are aware of their responsibilities in terms of managing the risks associated with potential bribery;
- provide real life examples for acceptable and unacceptable practices and how to deal appropriately; and
- specify names of the individual(s) who are charged with the responsibility of enforcing and monitoring compliance of the policy and who can be contacted in the case any guidance or clarification is required.

(iii) Facilitation Payment Policy: It should be made clear through this policy, that none should, on behalf of the company, offer, pay, and promise or provide gifts or anything of value to a government official in exchange for a business advantage. Following are best practices in drafting and implementing an effective facilitation payment policy:
- don't allow payment to be made, except when faced with a imminent threat of, or fear of,violence or loss of liberty to the health, safety or welfare of an employee, family member or co-worker; and
- where payment is determined to be unavoidable and payment is made, this should be completely and timely recorded for in books and records.

(iv) Gift & Entertainment Policy: It should be made clear through this policy, that no gift or entertainment should be given or received if doing so will improperly influence a decision or create a sense of obligation or if there is a risk it could be perceived as doing so. Also limit on receipt or giving of genuine gift & entertainment and the procedure for reporting the same shall be established. Following are best practices in drafting and implementing an effective gift & entertainment policy:
- gift or entertainment should be in line with customary regional practices, business policies, applicable laws and regulations;
- gift or entertainment should be reasonable and appropriate for the event;
- the expense shouldn't impose sense of obligation on the recipient;
- don't allow offer or acceptance of gift or entertainment during the periods when important decisions are to be made by them which will affect the company;
- cash shouldn't be provided as gift;
- identify and exclude *de minimis* items (pen, coffee mugs or other marketing items with the company's logo) from the purview of the policy;
- gift or entertainment shouldn't be lavish ;
- gift or entertainment should be transparent and should be given in a manner that avoids intent and appearance of impropriety;
- gifts offered should be recorded in a separate register; and
- the expense shouldn't exceed the reasonable fixed value and must be completely and timely accounted for in books and records.

(v) Travel Policy: It should be made clear through this policy, that the company will not pay or reimburse third party travel expenses, such as airfare, lodging, boarding and other incidentals, unless such expenses relate to (i) promotion, demonstration, or explanation of the company's products or services, or (ii) execution or performance of a contract, and provided such costs are modest and in accordance with the third party's own travel regulations and restrictions. Following are the best practices in drafting and implementing an effective travel policy :
- should comply with the stricter of any local laws or the company policies;
- the expense should be openly incurred;
- the expense shouldn't impose sense of obligation on the recipient;
- don't select or recommend particular official for travel;
- no side trip shall be allowed;
- avoid cash payments to officials to cover travel and travel-related expenses;

- don't pay for or reimburse travel expenses incurred on designated official's family members or friends;
- preferably pay directly to the third-party service provider or reimburse against valid third party receipts;
- pay incidental and local transportation only when such expense is associated with the official's participation in the relevant activities; and
- the expense is completely and timely accounted for in books and records.

(vi) Political, Charitable Contributions and Sponsorship Policy: Through this policy, guidance should be provided on political, charitable donations and sponsorship, including a clear prohibition of the sponsorship or payment of donations to political parties or charities that are directly linked to obtaining new business or gaining a business advantage. Following are the best practices in drafting and implementing an effective political, charitable contributions and sponsorship policy:

- the expense should comply with the stricter of any local laws or the company policies;
- the expense shouldn't impose sense of obligation on the recipient;
- the expense should not be incurred if it is intended to influence official action or secure an improper advantage;
- payment to private account or in cash shouldn't be permitted;
- should be incurred and given in a manner that avoids intent and appearance of impropriety;
- obtain receipt or acknowledgement for the payment; and
- the expense is completely and timely accounted for in books and records.

(vii) Petty Cash Policy: Following are best practices in drafting and implementing an effective petty cash policy. Petty cash should not be allowed for :

- any gifts, entertainment, travel, political or charitable donations, or other expenses benefitting, or at the request of, a government official;
- payments to, or on behalf of, a government official;
- payments connected to seeking clearance from government departments;
- payment to business associates; and
- other items generally reimbursed through a designated reporting process.

(viii) Whistle Blower Policy: Following are best practices in drafting and implementing an effective whistle blower policy:

- clearly explain the legal position and the rights available to the whistle blower;
- specify reporting mechanism (designated individuals, hotlines, websites, or suggestion boxes) for making disclosure;
- explain how the disclosure will be investigated;
- make clear that disciplinary action or appropriate proceedings will be launched against those who retaliate against whistleblowers;
- encourages culture where all concerned can raise concerns or draw attention to the breaches of the anti-bribery policy;
- management should demonstrate its commitment that it takes seriously any concerns raised in good faith and deal with them appropriately;
- inform progress of the disclosure to the whistle blower; and
- review effectiveness of the policy and procedures on a regular basis.

(ix) HR Process: Thorough and effective system for pre-employment verification should be introduced and regular training and awareness programs should be conducted to ensure the company's values and policies are understood and put into practice at all levels.

(x) Due Diligence. To help employees identify warning signs of potential bribery practices and minimise the risk of potential liability for the actions of a business associate, the company should adopt comprehensive anti bribery due diligence procedures to screen and monitor such business associate prior to engaging them. Some of the steps that may be taken while engaging business associate are :

1) Online Check: Check online using search engines to find out allegations of bribery against the proposed business associate.
2) Reference Check: obtain and verify three references from reputable organisations, and check with industry association or local chambers of commerce.
3) Contracts: The contract with the business associate should include, among other things, the following provisions:

- the business associate's obligation to strictly comply with the applicable anti-bribery laws and strict adherence to the company's policies;
- the business associate's obligation to maintain separate books and records;
- the company's right to audit the business associate's books and records, including documents pertaining to the business associate's interaction with government officials on behalf of the company;
- the business associate shall not assign or sub-

contract work under the contract without the prior approval of the company;

- the business associate shall indemnify the company for any losses that result from the breach of any of the business associate's representations;
- payments shall always be by check or wire transfer; and
- the company's right to forthwith and unilaterally terminate the contract, without penalty or claim for damages, in the event there is credible evidence or reasonable belief that business associate has or may have violated applicable anti bribery laws or the company's anti bribery policy.

4) M&A Due Diligence: The company may be held liable for past anti-bribery violations of the target and there could be potential risk from target's conduct that continues post-closing. Accordingly, the company must review, as part of its M&A due diligence exercise, target's compliance with anti bribery laws and potential exposure stemming from its past activities. The due diligence process should also address whether the target has any weaknesses in accounting, record keeping requirements and internal controls systems. Specific attention should be paid to the following:

- whether the target has ever been accused of violating anti-bribery laws;
- what percentage of target's business is derived from government contracts;
- the involvement of government officials in the target's business (either as owners, directors or employees);
- the types and identities of agents and consultants engaged by the target and their compensation arrangements; and
- the condition of the target's internal controls and books and records.

5) Warning Signals: Employees should be trained to be alert for suspicious circumstances. Examples of common warning signs are:

- the country where the transaction is taking place has a history of bribery;
- the business associate was recommended by a government official;
- the business associate has family or business ties to the relevant government officials;
- the business associate refuses to agree to abide by the anti-bribery policy of the company or refuses to agree to or sign required representations, warranties, or certifications;
- the business associate provides incomplete or incorrect information in required disclosures or refuses to submit the required information;
- the business associate makes unusual requests, such as to backdate invoices;
- the business associate requests that payment be made in cash or that cheques be made out to "bearer" or "cash," or seeks payment by some other unusual means, such as payment be made to a third party or in some other country than where services are being provided;
- the business associate doesn't want to appear with the company official before officials or staff of governmental agencies, embassies or multilateral organisations;
- the business associate requests reimbursement of vaguely described or questionable expenses;
- the business associate makes unusually large or frequent political contributions;
- the business associate appears to lack the adequate resources to perform the services contemplated by the contract or cannot provide references or cannot document its claimed experience; and
- bribery concerns have been raised in the past about similar transactions.

(xi) Accounting and Internal Control: Following are the best practices in maintaining accounting records and internal controls:

- maintain detailed and accurate books and records that reflect the transactions in reasonable detail. Documentation must not only record financial facts related to any transaction, but must also include relevant information alerting the assessor to illegality, if any; and
- maintain system of internal controls commensurate with the size of the organisation and adequate to provide reasonable assurances that, among other things, transactions have been conducted in accordance with management's specific sanction and accounted in accordance with generally accepted accounting principles.

4. Communication and Training: Communication and training help people realise what is expected of them and make them accountable. End result, everyone understands their roles and responsibilities. Thus, effective communication and training throughout the organisation is pivotal to implementation of compliance program. Following are the best practices for effective communication and training:

- training shall be part of the directors and employee's induction process and there should be regular training updates on how to implement and adhere to the policy;

- training where necessary and appropriate, business associates, and prohibition on bribery must be communicated to all business associates at the outset of the company's business relationship with them, and as appropriate during the course of their work for the company;
- training may be given through e-learning tools, face-to-face sessions and team briefings on various aspects of a compliance program, depending on their role;
- communication and training materials should be developed in relevant languages to create awareness of current issues, familiarise all concerned with business conduct expectations, and promote understanding of the company's business values and philosophy;
- introduce "train the trainers" concept by training identified champions who would in turn train and carry anti bribery message within the company;
- create dedicated intranet page which provides information related to the company's compliance program, including anti-bribery policy with supporting guidance. The company's Code of Conduct should be made available in the local languages of relevant markets;
- conduct face to face workshops to enable employees working in high risk areas (such as government relations, procurement and business development) have a realistic understanding of the important issues. These workshops should use real life situations to challenge participants to think about proper courses of action based on the company's policies;
- letters, posters, articles, newsletters, social media posts, and games may be used as communication mediums;
- maintaining records setting out what training was completed and when; and
- seek declarations from all concerned certifying compliance with the training requirements.

5. Monitor, Audit and Evaluate: It is only periodic monitoring and evaluation exercise that would tell whether or not compliance program is on track and whether or not it achieved its objectives. Procedural and substantial compliance should be monitored and audited at regular intervals to identify potential violation, to uncover new risks which have to be addressed and to assess effectiveness and performance in various ways. Frequency and depth of the monitoring and evaluation should be proportionate to the risk associated with the relationship. Following are best practices in monitoring and evaluating effectiveness of compliance program:
   - development of annual anti-bribery compliance audit plan with particular focus on;
     - compliance of policy for engaging business associate;
     - payments to business associate;
     - review of our compliance program;
     - assurance that contracts with business associate have necessary safeguards to protect the company from potential violations of the anti bribery laws;
     - the internal reporting system, follow-up activities, and related investigations;
     - review of the company's books and records pertaining to gift & entertainment, travel and travel related expenditures on behalf of government officials; and
     - review of any charitable contribution or sponsorship or any other corporate social responsibility activities; and
     - submission of compliance reports to the audit committee and the board of directors;
   - designate senior level officer with authority to report matters directly to board of directors or any appropriate committee of the board, to monitor effectiveness of, and ensure there is a review of the implementation of policy, regularly considering its suitability, adequacy and effectiveness, shall have to
   - establish hotline and additional means of communication for reporting and resolution of questions and issues;
   - usage of data analytical tools to identify risk indicators; and
   - monitor and review the records of personnel working in high-risk areas.

Conclusion

Both the FCPA and the UKBA contain a wide range of anti-bribery provisions and empower the regulating agencies to enforce civil and criminal provisions. The expansive and extraterritorial jurisdiction reach of these two statutes encompasses many companies' global operations and sharpens the focus on issues of bribery. For organisations committed to conducting business ethically and lawfully, a robust compliance program acts as a tool, for doing business—the right way. ■

Business of Cloud Computing: Issues in Accounting, Auditing and Taxation

Cloud computing is an innovative IT architecture, which has leveraged users from hardware requirements, while reducing overall client-side requirements and complexities. In this paper, we attempt to demystify the unique security challenges introduced in a cloud environment and clarify issues from a security perspective. *Cloud* is a metaphor for *Internet and cloud computing* that refers to various IT resources (infrastructure, platform, applications) being delivered over the internet as a service. Cloud computing heralds an evolution of business that is no less influential than e-business. By 2015, cloud computing will generate $200 billion to $250 billion in economic activity; in India itself, it will grow at a CAGR of 40%. Given these huge figures and to carve out a niche, it becomes imperative for us to comprehend the term. This paper attempts to conceptualise cloud computing in a non-technical manner, outlining its business model and meticulously deliberate the legal, accounting, auditing and taxation issues relating to it. Read on…

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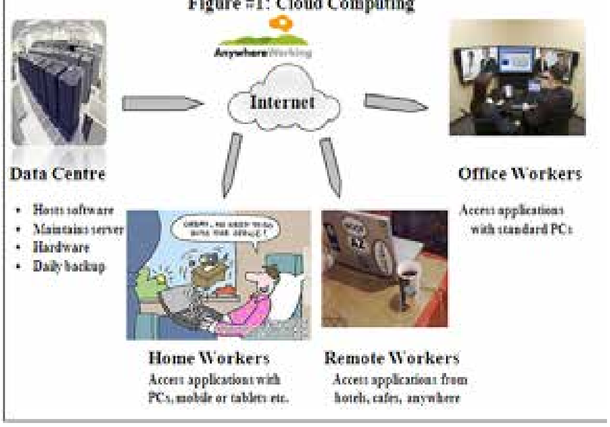
1. Introduction to Cloud Computing

Cloud is the condensed state of vaporised water from the earth; it then comes back to the earth in the form of rains, but in terms of IT, it is used only as a metaphor for the internet. Most probably, it was derived from the diagrams of clouds used to represent internet in the textbooks. *Cloud computing* refers to a range of servers located remotely which not only host computing applications but also deliver software, infrastructure and storage on the internet.

Computing refers to the use of computers to process data and perform calculations. In that sense, *cloud computing* means internet-based computing in which a large group of remote servers are networked so as to allow sharing of data-processing tasks, centralised data storage and online access to computer services or resources.

Figure #1: Cloud Computing



Though the phrase *cloud computing* may appear to be new, in technology, it is not a new concept; it is a culmination of many primary technologies such as grid computing, utility computing, SOA, Web 2.0 and other existing ones. Remote computing has been here since 1960s. What is new is the scale. We are using it without even knowing it. Simplest illustration is an e-mail that we use, e.g. Google mail, Yahoo mail, Hotmail, etc. Also, the use of Google docs in place of MS Word document or MS Excel sheet is also a part of cloud-computing environment. But, everything we use on internet is not cloud computing. When we download a song from iTunes onto our computer, we are using internet but not necessarily the cloud. When we store music in a remote server, such as Amazon's or Google's, and have device dependent access to it, we are using both the internet as well as the cloud.

An expounding and most widely-used definition of the term has been given by Mell and Grance (2009) from National Institute of Standards and Technology, U.S. Department of Commerce: *Cloud Computing is a model for enabling ubiquitous, convenient, on demand access to a shared pool of configurable computing resources (e.g., networks, servers, storage, applications and services) that can be rapidly provisioned and released with minimal management effort or service provider interaction.*

Further, they summarise the five-point essential characteristics of cloud computing:

1. *On-demand self-service*: user can use computing capabilities *as and when required*, that too with no human interaction.
2. *Broad network access*: capabilities are available over the internet and can be accessed through standard mechanisms such as computers, mobile phones and tablets.
3. *Resource pooling*: providers bundle the capabilities to server multiple consumers using a multi-tenant model; different users (tenant) share the same underlying resources without even having knowledge of its location, e.g. resources like storage, processing, memory and network bandwidth.
4. *Rapid elasticity*: capabilities can be easily scaled up and down according to the demand of users; unlimited capabilities are available infinitely for users and these can be apportioned in any quantity at any time.
5. *Measured service*: use of resources is monitored, controlled and reported by employing a metering capability appropriate to the type of service, e.g. storage, processing, bandwidth and active user accounts.

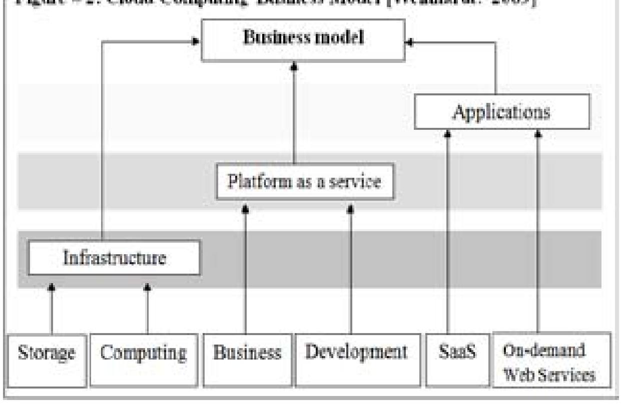
Further, a cloud can be a public cloud or a private cloud—a public cloud is open for use by general public and generally at no or low cost and exists on the premises of the cloud provider; and on the other hand, private cloud infrastructure is for the exclusive use by a single organisation at a certain price to be paid on *pay-as-you-use* basis and may exist on or off premises.

To sum up, *cloud computing* is a way of using computers in which data and software are stored mainly on a central computer (cloud), to which users have access through internet. While definitions, taxonomies and architectures are interesting, it is more important for us to understand the business model for cloud computing. We need to understand how suppliers of cloud technology will come together to deliver on the promise of cloud computing.

2. The Business Model

The first thing is that cloud computing is not a separate sector or industry. In terms of purchase of business processes, it can be called as an advanced stage of outsourcing where IT infrastructure is purchased instead of outsourcing of business processes.

Figure # 2: Cloud Computing Business Model [Weinhardt: 2009]



In terms of delivery mechanism, there can be three types of service models, which can be used to describe various business models for cloud computing:

1. *Infrastructure*: the user enters into an agreement with the cloud service provider for the provision of data *storage* and various other *computing resources* including processing, sharing and networks, where

it can run its software and applications. It is referred to as Infrastructure as a service (IaaS), e.g., Examples are: Amazon web service, EC2, Gogrid, etc.

2. *Applications*: the user is provided with the use of applications running on the cloud infrastructure. Applications are accessed through a thin client interface (like web browser) or a programme interface. It is termed as *Software as a service (SaaS)*. Christof Weinhardt (2009) distinguishes between SaaS applications and the provisioning of rudimentary Web services on demand. The most prominent examples are: Google Docs and sales force.
3. *Platform as a service (PaaS)*: the cloud provider hosts libraries, programming languages, services and tools onto the cloud infrastructure with which the user is able to create or acquire applications. Weinhardt classifies platform as business platform and development platform.

The most important and interesting part of the service models is that the users do not manage or control the underlying cloud infrastructure including network, servers, storage, etc., or even individual application capabilities. They don't even know where their data is stored, but they are using it *as-and-when-required*.

Further, a cloud can be public or private—a public cloud is open for use by general public and generally at no or low cost and exists on the premises of the cloud provider; and on the other hand, private cloud infrastructure is for the exclusive use by a single organisation at a certain price to be paid on pay-as-you-use basis and may exist on or off premises.

While providing the cloud-based services, various actors are involved in the channel, identified as *vendors*—supplying cloud services, service providers—providing connectivity mechanisms, distributors and aggregators—acting as intermediaries for consolidating solutions, systems integrators—building cloud infrastructures (IaaS), VARs (value-added resellers) & MSPs (managed service providers) brokers and managing cloud-customer relationship, and solution providers—implementing cloud applications (SaaS & PaaS).

The biggest technical barrier a cloud auditor may face is they may not be permitted to access systems and data on the cloud; moreover it is often unknown where the data is being stored. This raises various concerns for the auditor and the worst thing is that the professional organisations such as IAASB, AICPA, CICA, ISACA or the corresponding Indian board AASB **of ICAI, still have not define cloud audit requirement specifically, although progress is being made in this** arena.

3. How to Regulate

In relation to cyber laws, regulations in India are still at its nascent stage and a lot of work is to be done. For instance, we do not have data privacy, data security and data protection laws. The only legislation we have is the Information Technology Act, 2000, which is focussed on legal recognition of electronic documents, e-commerce and cyber crime in general and is not a data privacy protection *per se*. Yet, Sections 43, 43A, 65, 66 and 72 of the Act deal with penalty and compensation against breach and misuse of data in India:

Section 43	Damage to computer, computer system etc. Unauthorised copying, extraction, database theft, and digital proofing.	Compensation to the affected person upto ₹ 1 crore
Section 43A	Failure to protect data	Compensation to the affected person
Section 65	Tampering with computer source documents	Imprisonment upto 3 years or fine upto ₹2 lakh or both
Section 66	Hacking with computer system	Imprisonment upto 3 years and fine upto ₹2 lakh or both
Section 72	Breach of Confidentiality and Privacy	Imprisonment upto 2 years or fine upto ₹1 lakh or both

The Supreme Court has time and again equated the *Right to Privacy* with the fundamental Right to "Protection of life and personal liberty". The Apex Court observed that "…*the concept of liberty in Article 21 was comprehensive enough to include privacy…*" Despite this, phone-tapping and e-surveillance is done without a court warrant and beyond the judicial scrutiny. In the cloud computing environment, the police or a government officer can get access to data just by approaching the cloud service provider. In addition to that, there are several other issues that may arise due to the complex business model and involvement of a gamut of intermediaries such as national security—as it involves huge cross-country data flows, localisation rules, jurisdiction, etc.

In a nutshell, the present regulatory framework does not offer a complete solution to the issues that emanate from the business of cloud computing technology. An efficient regulatory framework would give confidence that the service providers will provide the service securely and reliably. But, there should not be a cloud-specific legislation as it could weigh down the potential of the budding cloud computing.

4. Accounting Issues

Traditionally, companies need to invest heavily in IT-architecture, whereas with the use of cloud services they can now manage their IT demands according to the requirement. They exploit the cloud service on pay-per-use basis. This shift from a capital expenditure (CAPEX) model to an operating expenditure (OPEX) model raises various concerns for accounting, e.g., how a transaction is treated, when to recognise the revenue, implications in budgetary process, etc. Answers to these questions need to be answered by a proper authority, undoubtedly, the ICAI; however, in the present scenario, the following treatment could be given to the cloud transaction:

1. Under IaaS model, transaction between the cloud service provider and user can be classified as 'Leases'. Typically, as per AS 19, it is an operating lease and the treatment shall be:
   a) *In the books of user*: Lease payment shall be recognised as expense in profit and loss accounts P & L account on straight line basis over the term of contract.
   b) *In the books of vendor*: Asset shall be recognised and lease income shall be recognised as income in P & L using straight line method. Further, depreciation as per AS 6 shall be claimed.
2. Under PaaS or SaaS model, it would be a *service contract* where a cloud vendor provides multiple services like customisation of the platform, hosting, support, etc. In order to have a classification of the contract, various components of the contract are to be looked into. The vendor shall recognise revenue either by the application of *Proportionate Completion Method* or by the *Completed Service Contract Method*.
   Under IFRS, revenue recognition from each component begins once the initial configuration is completed and delivery of the cloud computing services commences.

5. Auditing Issues

The principal issue in auditing cloud based services is the lack of understanding of how the cloud differs from the traditional enterprise IT. The biggest technical barrier a cloud auditor may face is they may not be permitted to access systems and data on the cloud; moreover it is often unknown where the data is being stored. This raises various concerns for the auditor and the worst thing is that the professional organisations such as IAASB, AICPA, CICA, ISACA or the corresponding Indian board AASB of ICAI, still have not defined cloud audit requirement specifically, although progress is being made in this arena.

Cloud and Numbers:

- Cloud Computing will expand from $46.4 billion in sales in 2008 to more than $150 billion by 2013 [Gartner]
- by 2015 it will generate $200 billion to $250 billion in economic activity [Gartner]
- cloud market in India is expected to cross $1.08 billion by 2015 from $110 million in 2010 [Zinnov]
- cloud computing market in India will grow at a compound annual growth rate of 40 % by 2014
- it will account for 5 % of the total investments in India by 2015 [Gartner]
- the use of the private cloud model by two or more states could result in savings of up to 50% in the ₹1,378 crore allocated for state data centre projects [Govt. of India estimates]

AICPA provides a standard SAS-70, by which a service organisation can demonstrate the effectiveness of their internal controls. Under SAS-70, a certified

Is the offering a taxable or non-taxable service? Is it a data processing or information service? Is it a sale or a lease of tangible personal property? While a **significant number of nations have addressed cloud** services from a SaaS point of view, very few have **addressed tax classification from an IaaS or PaaS** standpoint, and very few have updated their statutes and regulations to address this emerging use of technology.

independent service auditor performs an audit and issues a report that may be shared with audit teams of the service auditor's clients. With effect from 15th June, 2011, a more inclusive statement SSAE–16 has been issued, which provides a more in-depth range of options in their reporting. This SSAE–16 replaces SAS–70. The major difference between SAS–70 and SSAE–16 is that the latter is an attest standard whereas former is an audit standard.

The SSAE–16 is in line with the ISO reporting standard ISAE–3402, issued by the IAASB of IFAC. The IFAC in its second publication of *Guide to Practical Management for Small and Medium Sized Practices* issued a guidance on cloud computing.

The ICAI has also issued standards which are at the level of the standards issued by the IAASB of IFAC. Two of the standards, namely SA–402 *Audit Considerations Relating to an Entity Using a Service Organisation and SAE–3402 Assurance Reports on Controls at a Service Organisation* serve the purpose. SA–402 establishes standard for an auditor whose client uses a service organisation. It also provides types of report of the auditors of the service organisation which may be obtained by the auditor of the client.

The Auditor of the *organisation using the services of a cloud provider* shall:

a) Obtain an understanding of the nature and significance of the services of the *cloud provider*;
b) Assess the effect of the services on the user entity's internal control; and
c) Design and perform the audit procedures responsive to the risk of material misstatements.

If the user auditor is unable to obtain a sufficient understanding from the user entity, the user auditor shall obtain that understanding from one or more of the following procedures:

(a) Obtaining a Type 1 or Type 2 report, if available;
(b) Contacting the service organisation, through the user entity, to obtain specific information;
(c) Visiting the service organisation and performing procedures that will provide the necessary information about the relevant controls at the service organisation; or,
(d) Using another auditor to perform procedures that will provide the necessary information about the relevant controls at the service organisation.

If the user auditor is unable to obtain sufficient appropriate audit evidence regarding the services provided by the service organisation relevant to the audit of the user entity's financial statements, she/he shall modify.

The Auditor of the cloud provider shall:

a) Obtain reasonable assurance about whether, in all material respects, based on suitable criteria:
   (i) The service organisation's description of its system fairly presents the system as designed and implemented throughout the specified period;
   (ii) The controls related to the control objectives stated in the service organisation's description of its system were suitably designed throughout the specified period;
   (iii) Where included in the scope of the engagement, the controls operated effectively to provide reasonable assurance that the control objectives stated in the service organisation's description of its system were achieved throughout the specified period;
b) Report on the matters in (a) above in accordance with the service auditor's findings.

6. Taxation Issues

As per a global cloud survey, *approximately 45% of the respondents are neither evaluating the tax implications of cloud nor do they know if these factors are being evaluated within their organisation*. A major challenge in the taxation of cloud offerings is in the tax classification of cloud services themselves. Is the offering a taxable or non-taxable service? Is it a data processing or information service? Is it a sale or a lease of tangible personal property? While a significant number of nations have addressed cloud services from a SaaS point of view, very few have addressed tax classification from an IaaS or PaaS standpoint, and very few have updated their statutes and regulations to address this emerging use of technology.

It may be difficult to arrive at any concrete conclusion on the appropriate tax treatment of the new business model as it involves multiple (and intricately connected) features or transactions. In certain situations, an argument may be raised that payments for certain forms of cloud computing services may be classified as fees for technical services, the tax implications of which are similar to that of royalty. But in standard structures where the client does not exercise any control over the cloud server and merely procures certain platform, infrastructure or support services, the consideration paid to a foreign service provider should normally be treated as business profits. This would be taxable in India only if the service provider has a permanent establishment (PE) in India.

There are various issues with the emerging technology like nexus of taxation, applicability of service tax, VAT, etc. It is very necessary for the policy makers to ensure that tax and other regulatory factors should not become an impediment to the growth of innovation and technology.

7. Conclusion

Cloud computing in India is estimated to create about one lakh job opportunities for people specialised in cloud computing by 2015. It is poised to become one of the largest revolutions in this era for the IT industry, but yet it is in the budding stage. A lot of work needs to be done, ranging from a proper legal framework to taxation rules and accounting and auditing issues as well. Recently, the Bangalore Branch of ICAI organised a National Conference on Cloud Computing to analyse and understand the impact of cloud computing on the CA profession. Chartered accountants must be familiar with the basics of cloud computing in order to discuss potential risks and benefits with their clients effectively.

In 2012, the telecom regulator TRAI also called for papers on *Regulatory Framework for Cloud Computing* for a conference to explore the various challenges that exists in cloud computing. It has also recommended its National Telecom Policy 2012 where it has suggested a setup of an efficient cloud computing environment. Strategies suggested by TRAI are as follows:

1. Adopt best practices to address the issues related to Cloud Services
2. Create a secure network for cloud computing covering encryption and privacy
3. Create a legal and security frame work covering network security, law enforcement assistance and preservation of cross-border data flows for deployment of Cloud Services
4. TRAI to devise appropriate mechanisms to provide interoperability among cloud computing service providers.

The ball is now in the court of our Government. Let us see how they react to these suggestions. ■

SBU Concept of Business Structure and Management

Strategic Business Units or SBUs have been defined as autonomous divisions or organizational units, small enough to be flexible and large enough to exercise control over most of the factors affecting their long-term performance. They focus on product offering and market segment—having clear marketing plan, campaign and analysis. They have autonomous mission and objective. They inspire the owning empire to respond quickly to changing economic situations. The author has tried to explore the concept of business structure and management from the SBU perspective, while looking at different categories of SBUs, in this article. He has also discussed the management mechanism of the SBUs in details. Read on to understand this crucial perspective…

CA. O. P. Jagati

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What is an SBU?

As a company grows, it gradually adds new products (covers services also) to its basket of business. To start with, the new products are variants or derivatives of the original products, like an automobile company launching new models of cars. Later on, even products of different segment or industry are added, e.g. a heavy engineering company going for software business, etc. However, as the business grows, the management becomes complex and tough. New business divisions are created to ensure better operational efficiency. In the earlier days, the business efficiency of an individual division was measured by the amount of turnover achieved by it. In a nutshell, it was a top line approach.

Profit-making companies were trying to add more and more products to their basket of business without giving much thought to the margin from each such new addition. However, with fierce competition after liberalisation and globalisation of economy coupled with limited resources for expansion, the profit from operation took the center stage. Consequently, turnover concept-based business division was transferred into an SBU (strategic business unit), which is a profit centre focusing comprehensibly on product offering, market creation as well as profit from operation. Efficiency of an SBU is measured on profitability rather than turnover alone.

AS 17 – the Reflection of Performance

Accounting standard on segment reporting, i.e. AS 17, requires reporting of financial information about different types of products and services an enterprise provides, known as *primary reporting*. A business segment is a distinguishable component of an enterprise providing a product or service or group of products or services that is subject to risks and returns that are different from other business segments. A business segment is a reportable segment if (a) revenue from sales to external customers and transactions with other segments exceeds 10% of total revenue (both external and internal) of all segments; or (2) segment result, whether profit or loss is 10% or more of (i) combined result of all segments in profit or (ii) combined result of all segments in loss whichever is greater in absolute amount; or (c) segment assets are 10% or more of all the assets of all the segments. Under primary reporting, each reportable segment should disclose revenue—both external and internal, segment result, amount of segment assets and liabilities, cost of fixed assets acquired during the year, depreciation, amortisation and other non-cash expenses. A company can have more segments than the minimum mandatory requirements under AS 17. Like any financial reporting, the primary segment reporting under AS 17 is a reflection of performance of underlying divisions. However, for a discussion on the effective business management through SBU concept, we need to touch upon various other elements as attempted in this article.

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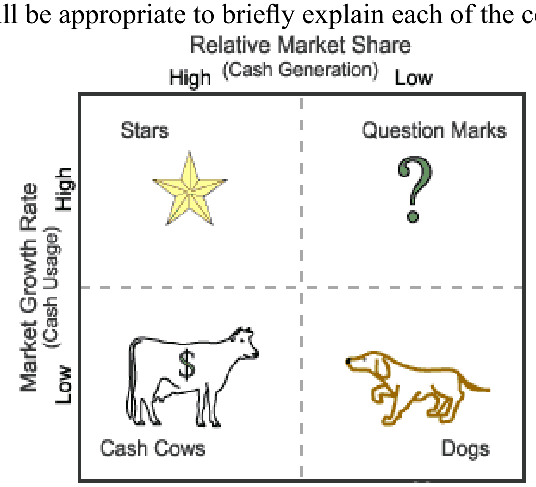
Categorization of SBU

BCG matrix developed by Bruce Henderson of Boston Consulting Group, USA, in 1970 is a popular tool for classifying various SBUs in an enterprise. This matrix has four cells with horizontal axis representing relative market share and the vertical axis denoting market growth rate. Resources are allocated to various SBUs according to their position on the grid. As displayed in the following figure, four cells of the matrix have been named as *cash cows*, *stars*, *question marks* and *dogs*. It will be appropriate to briefly explain each of the cells.



- *Cash cows* are units with high market share in a slow growth industry. These units typically generate cash in excess of the amount of cash needed to maintain the business. Each company would be interested to have as many SBUs as possible in this cell. Literally speaking, these SBUs are to be milked continuously with as little investment as possible.

- *Stars* represent business units having large market share in a fast growing industry. These units generate cash but because of fast growing market, they require high investment to maintain their position. Net cash flow is usually modest. SBUs located in this cell are attractive as they are located in a robust industry and at the same time these units face tough competition. If succeeded, a star SBU will become a cash cow unit when the industry matures.
- *Question marks* represent SBUs having relatively low market share in a high growth industry. They require huge investment to gain market share. Such SBUs need to be analysed to examine their business viability. Question marks are usually new products that have a good commercial prospective.
- *Dogs* represent business units having weak market share in low growth market. These units have weak market share because of high cost, poor quality, ineffective marketing, etc. Such units need to be avoided in an organisation, unless there is some convincing long-term prospect.

It may be noted that the BCG matrix is a tool to help broad categorisation of SBUs. Categorisation may vary from company to company. Each company has to arrive at the categorisation based on its perception about market conditions, future prospect of the industry, company's strategy to acquire market as well as availability of funds for investment. Anyway, for better understanding of the SBUs categorisation, let us take some illustrations from the published annual reports. As per the ITC Limited Annual Report, 2012, FMCG (Cigarettes) Division had a revenue of ₹22,250 crore with profit margin of 31%. This division's revenue share in total business of ITC is 58%. This business has a formidable market share of 72% with only 3 major players in the market, with no one touching 15% market share. This division's profit earning is 82% of total ITC profit. At the same time, the future growth of cigarettes market seems to be between low to moderate in view of social awareness about evil effects of tobacco, statutory restriction regarding smoking at public places as well as increased duty rate. Although there is good margin in this business, there is tremendous entry barrier due to huge investment and stringent statutory compliances. As such, ITC is expected to enjoy its formidable position in this segment of business and earn huge profits in coming years too, although it is not required to invest heavily in this segment. FMCG-(Cigarettes) SBU may be considered as cash cow of ITC. During the year, the company had incurred capital expenditure of ₹721 crore in Hotels Division and ₹594 crore in Paperboards, Paper and Packaging Division, which are the emerging segments. As per the author, these SBUs may be considered as Stars with future investment likely to be funded largely by FMCG (Cigarettes) business. Other 2 SBUs, viz. FMCG (Branded packaged foods, personal care products, stationery products, branded apparel, incense sticks and safety matches) Division and Agri Business Division are having revenue of ₹11,240 crore in aggregate with margin of just 4%. However, these SBUs may be perceived as Question Marks with expectation of high market growth in these segments in the coming days. As such, these businesses may be requiring huge investment for higher market share. Let's analyse the segment reporting of another diversified company, i.e. Titan Industries Limited. As per the Annual Report, 2012, two Divisions of the company, viz. Watches and Accessories Division and Jewellery Division had revenue of ₹1,520 crore and ₹6,990 crore respectively with respective profit margin of 14% and 10%. As per the author, these SBUs may be considered as Stars for the reasons of having good market share, operating in a fast growing market, however requiring high investment to maintain their position in the competitive market. Third SBU of Titan Industries, i.e. Eye Ware Division, may be considered as Question mark in view of relatively low market share in an industry with good commercial prospective. The company needs to examine closely the viability and growth of this SBU and invest accordingly.

Product and process innovation can happen either **by in-house R&D activities or import of technology or both. However, the SBU Head should have the insatiable quest to make "Better than the Best" for** the target customers. It may be in form of better **product, novel product, simple-convenient-less expensive product etc. The ultimate success** depends on 'performance – price point' that the competitors cannot match.

Management Mechanism of SBUs

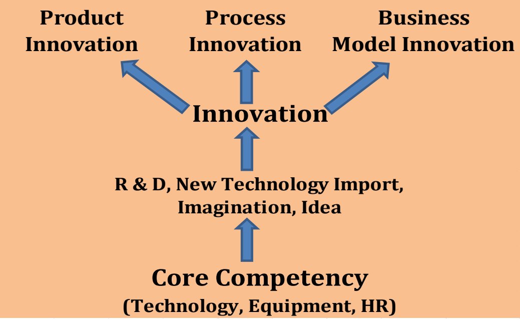
In a multi-SBU company, it requires proper categorisation of SBUs as well as prudent management of each SBU. In this context, a CFO plays a key role in extending necessary functional and advisory support to the individual SBU Heads, and functioning as an

Although SBU managers are expected to be involved in strategic decision making, take calculated risk to achieve greater results, many a times there is a tendency to negotiate for manageable targets that appear to be imposing outwardly but are inwardly comfortable because of advantageous position of the SBU in the particular industry.

effective link with the CEO of the company. In order to make his role clearer, various elements of management mechanism of SBUs have been discussed below.

1. Hand Holding of Core Competency and Innovation

An SBU should try to improve upon its existing products as well as add on new products in order to increase revenue and profit. However, it depends on the innovative attitude and aptitude of the SBU. Many a times, core competency and innovation are considered paradoxical, which in fact is not correct. Core competency of a company acts like a power house of technologies, equipment and human resources for innovative efforts. Innovation can be of various types, viz. product innovation, process innovation and business model innovation. Product and process innovation can happen either by in-house R&D activities or import of technology or both. However, the SBU Head should have the insatiable quest to make "Better than the Best" for the target customers. It may be in the form of better product, novel product, simple-convenient-less expensive product etc. The ultimate success depends on 'performance–price point' that the competitors cannot match. Precision engineering is the core competency of Titan Industries. By blend of precision engineering and product innovation, the company has been able not only to add new model of watches, but also to introduce new products in the field of jewellery and eye ware segments, which have become independent SBUs. Tata Chemicals—the world's second largest producer of soda ash, by process innovation, could filter the hazardous effluents created during production of soda ash and make raw material out of it which is required for production of cement. This has not only reduced the cost of effluent treatment but also given a new product, raw material for cement industry. Later on the company started producing cement taking advantage of in-house produced raw material and it became new division. Apple by introduction of novel and pioneer products in regular interval, e.g. iPod, iPhone, iPad, etc., has been able to increase its product line successfully. In case of business model innovation, Flipkart may be referred to. It is an Indian e-commerce company offering multiple payment methods like credit card, debit card, net-banking, etc. However, the innovative business model of cash-on-delivery adopted by Flipkart has proven to be of great significance since the credit card and net banking penetration is very low in India. The outcome is amazing. Flipkart's reported sales which were ₹40 million in the financial year 2008-09, crossed ₹5 billion during 2011-12.



2. Creation of SBU by Strategy and not by Size

Although AS 17 requires segment reporting based on threshold limit, the company should create an SBU based on market size and growth of the product(s) falling in the division, positional advantage of the company for such products, margin from operation, etc. A product in a niche market may have substantial commercial prospect in future for which the company may exploit its positional advantage. If the product has different market dynamics, it is advisable to make a separate SBU for it. The profit centre concept will drive the SBU to gain expertise for commercial success soon. Fowler Westrup, a Bangalore-based MNC is engaged in the anufacture of various equipments for post-harvest applications in the agri segment. A few years ago, it introduced galvanised steel silos in Indian market which offer scientifically the best and safest solution for storage and handling of grains, cereals and other agri commodities. Although the product was generically falling in the agri segment, the company decided to have a separate SBU for silos, since the niche product had to face challenges and compete with the traditional storage method of gunnysacks in concrete and MS storage structures which is predominantly controlled by government sector. The market dynamics was quite different in comparison to other agri processing equipment. The decision of the company ensured focused approach and yielded affirmative result.

3. Performance Measurement

When a company migrates from a centralised to a decentralised organisational model, it encounters the problem of setting up targets and designing a reward system. Although SBU managers are expected to be involved in strategic decision making, take calculated risk to achieve greater results, many a times there is a tendency to negotiate for manageable targets that appear to be imposing outwardly but are inwardly comfortable because of advantageous position of the SBU in the particular industry. Top management should suitably use its power and influence in convincing the SBU managers for improving the performance and the resultant benefits both to the organisation and employees.

Targets should be well-defined, tough and challenging but achievable. A CFO has to play an important role in preparation of annual budget for various SBUs, the consolidation of which will be the corporate budget for the entire company. He should gather the information on sales forecast, purchase planning, manpower requirement, sales promotion, etc., from the SBU Head. He should collate it with the market size and growth pertaining to the SBU in order to examine the veracity of the sales forecast. In case of capex budget, he should examine the justification by ascertaining the return on investment (ROI) for the proposal. Finally, in consultation with the CEO, the CFO should prepare the SBU budget. For preparation of SBU-wise profit and loss statement, he should evolve a realistic norm of apportionment of common overhead expenses between the underlying SBUs. Every month, actual operating result of the SBU should be compared with the monthly budget and the variance should be analysed, which would help the SBU Head and the CEO for necessary corrective measures. As corporate finance is a centralised function, the CFO has to play a critical role in ensuring requisite funds for operation as well as for expansion of the SBUs. He should closely monitor the funds flow of each SBU and judiciously channelise the surplus fund of one to another SBU having a shortage of fund.

4. Marketing Campaign: Think Differently

Each SBU should develop its own marketing strategy. *Star* category SBU needs to go for well-conceived brand building campaign for its product so as to conquer the confidence of the target customers. Company like Havells manufacturing circuit breakers, electrical wires, etc., (usually purchased through intermediary contractors) could win the confidence of household customers by well-designed and fascinating visual advertisements. It has now become number one in market share from earlier position of number three SBU in *question mark* dealing with niche product should aim to reach the target customers to know their needs, problems and psychological/cultural mindset. It must also find out what the competitors offer and whether there is any gap in the market which could be exploited gainfully. A CFO should examine such marketing campaign proposals with an open mind evaluating the prospective benefits, market study done by the SBU. He may rather try suitably to leverage expenses for such proposals against usual sales promotion expenses with relatively low value addition.

5. Financial Basics for Non-finance Executives

A CFO has the responsibility of enlightening the SBU heads and senior SBU managers about financial basics of business operation. He has to educate them about contribution from sales, operating profit, break even sales, management of working capital, return on investment (ROI) in case of capex proposal, ratio analysis, vendor negotiation for better commercial terms, negotiation of export documents under letter of credit, legal impact of critical clauses in commercial agreements, basic provisions of applicable indirect taxes, etc. Learning process should be simple, example-based, interactive and joyful.

6. Designing Reward System

There should be performance-based incentives to SBU managers based on their functionary role. The calculation mechanism should be linked to KRAs (key result areas). To bring more focus, an individual should have around 3-5 KRAs; each should be tough and challenging, measurable without ambiguity, unconditional and with a definite schedule for execution. Too many KRAs only dilute the focus on performance improvement and complicate the calculation process. KRAs should focus on results and not activities.

Although, the bulk of incentive, say 80%, should be linked to actual performance *vis-à-vis* KRAs fixed for the individual manger, a portion, say 20%, should also be linked to overall company performance, so as to bring collaborative attitude across the company. To bring more clarity, an illustration on reward system has been appended.

7. Effective Training and Career Planning

For the success of an SBU format of business organisation, the management should analyse training needs of the employees and address the issues accordingly. Better trained employees often lead to more satisfied and loyal customers and ultimately improved profitability and cash flow. There should be efforts to attract new talents and retain the existing talents. SBU concept creates a healthy and constructive competition among various divisions to excel better than the others. Further, a successful stint as an SBU head gives opportunity to assume higher responsibility in senior management echelon at a later stage. The CFO gains immense exposure in understanding the nuances of business strategies and coordinating with SBU heads for performance measurement and improvement. This exposure is likely to groom him to assume higher responsibility in general management of the company.

8. Challenges and Conclusion

In India, although there are plenty of qualified graduates in all fields of education, there is certainly dearth of competent manpower with thorough functional knowledge and managerial skill. In the SBU format of business organisation which is run on the principle of decentralised profit centres, the management has the challenge of identifying result-oriented SBU heads with extensive experience in the particular industry. Secondly, at the time of economic slowdown as well as liquidity crunch, the management usually becomes impatient towards newly set up SBUs in niche segment needing relatively longer gestation period before generating profit. Thirdly, organisation having SBUs should have good ERP package so as to ensure data accuracy and sound internal control. Lastly, SBUs should be run on the basis of strategy and not sentiment. There should not be emotional attachment to close down an SBU in case it proves to be commercially unviable. Anyway, it can be concluded that an SBU concept of business management is indispensable for a professionally managed company vying for rapid growth, however, with a strict watch on the investment and returns from each SBU.

Illustration of performance-based incentive calculation mechanism

KRAs of Mr. X, Manager (Marketing), Alpha Limited, working in SBU (ABC) for 2012-13

Sl No.	KRAs	Targets	Points for Actual Performance
1	Invoicing	₹500 crore	If less than or equal to 80%: 0 More than 80%, upto 90%: 20 More than 90%, upto 100%: 25 More than 100%: 30
2	Order Booking	₹750 crore	If less than or equal to 80%: 0 More than 80%,upto 90%: 20 More than 90%,upto 100%: 25 More than 100%: 30
3	Collection	Debtors Days: 30	Debtors Days equal to or exceeding 40: 0 Debtors Days exceeding 30,less than 40: 10 Debtors Days not exceeding 30: 20
4	Customer Base	Number of New Customers: 25	Not exceeding 15: 0 Exceeding 15 but less than 25: 05 Equal to or exceeding 25: 10

For 100% achievement in 4 KRAs, Mr. X will earn 80 points.
Mr. X can earn additional points for more than 100% performance in KRAs of invoicing and order booking.

Company Performance target of Alpha Limited for 2012-13.

a) Company meets budgeted sales : 10 points
b) Company meets budgeted profit: 10 points

Total: 20 points
For 100% achievement in individual KRAs and Company results, Mr. X will earn 100 points.

Incentive Calculation:

Mr. X will get incentive @ 30% of his total salary (CTC) for earning 100 points, to be adjusted upward / downward as per actual points earned. ■

Compliance with Clause 41 (VI) of Listing Agreement: Requirement and Industry Practice

With a vision to enhance investor education & protection and good corporate governance, Clause 41(VI) of the listing agreement notified by SEBI provides for the publication requirements of financial results in newspapers by all listed companies. The spirit of this clause is to enable all stakeholders to know the performance of a company, that too as early as possible. This is made by way of filing/publishing quarterly financials compulsorily in stock exchanges/newspapers/company's website and mandatorily in other sources like press releases. This article is based upon the published results made by the listed companies in leading newspapers. This article is an attempt to study and analyse the publication practice adopted by listed companies.

Pankaj Mundra

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Introduction

Edward Porter Humphrey once said, "True wisdom is to know what is best worth knowing and to do what is worth doing". This is what SEBI has probably desired by incorporating clause 41(VI) of the listing agreement. With a vision to enhance investor education & protection and good corporate governance, clause 41(VI) of the listing agreement notified by SEBI

If we look at the publications of financial results made by the companies in different newspapers/Company's website (or in other sources like press releases), we can easily visualise different colours in compliance practice.

provides for the publication requirements of financial results in newspapers by all listed companies. The spirit of this clause is to enable all stakeholders to know the performance of a company, that too as early as possible. This is made by way of filing/publishing quarterly financials compulsorily in stock exchanges/ newspapers/company's website and mandatorily in other sources like press releases. For this purpose, clause 41 provides an annexure for format of financial results by banks, and companies other than banks, to be disclosed quarterly.

If we look at the publications of financial results made by companies in different newspapers/company's websites (or in other sources like press releases), we can easily visualise different colours in compliance practice. For instance, few companies provide the financial in rupees lakhs compared to rupees crores by other companies. Some companies use the publication requirement as an advertisement and brand building opportunity.

What are the Publication Requirements of Financial Results under Clause 41?

Clause 41 provides for the following compliance requirements with respect to publication of financial results:-

(a) Explanation to variance in case variation in net profit/loss and exceptional or extraordinary items exceeds 10% or ₹10 lakhs, whichever is higher, between the unaudited quarterly (or year to date) results and results amended pursuant to limited review.

(b) Disclosure of any qualification/reservation by auditor and its impact on profit/loss of reportable period.

(c) How auditors' qualification/reservation, if any, in respect of any previous financial year or quarter, resolved and if it is not resolved, steps company intends to take in the matter.

(d) If a company changes its name due to new line of business, company shall disclose net sales/income, expenses and net profit/loss after tax figures pertaining to said line of business separately for three years succeeding the date of change in name.

(e) In case company has not commenced commercial production/operations, amount raised, utilised and remaining for utilisation, description of projects pending completion, expected date of commencement shall be disclosed if company does not submit/publish financial results.

(f) Items of income and expenditure arising out of exceptional transactions shall be disclosed. Item of extraordinary item shall also be disclosed.

(g) Disclosure of change in accounting policy during the period.

(h) Disclosure of seasonal nature of activities in case company's results are subject to seasonal variation.

(i) Disclosure of any material event/transaction which occurred during/before the quarter that is material to an understanding of the results. Examples enumerated include, but not limited to, completion of expansion, diversification program, strikes, lock outs, change in management, capital structure, business combinations etc.

(j) Number of investor complaints pending at the beginning of the quarter, received and disposed of during the quarter and remaining unresolved at the end of the quarter.

(k) If the company has more than one reportable segment in terms of AS-17, company shall disclose the same.

How are Companies Complying with these Requirements?

The general practice adopted while publishing the financial results as a part of compliance to publication requirements under clause 41 as stipulated from (a) to (k) above are as follow:

(a) No such instances are observed.

(b) In rare cases any audit qualification is expressed and dealt in published results.

(c) Again this is a rare case being dealt with by listed companies.

(d) This case is rarely faced by companies. They are giving disclosure whenever they change their name. For new product line/business, information in segment reporting part in published results mostly provides for these requirements.

Some of the companies take quarterly publication requirements as an advertisement and brand building opportunity.

The publication of financial results by companies varies, to small extent, both in format and content. **This primarily suffices the compliance requirement** envisaged under clause 41.

(e) Companies are disclosing information about fund raising and utilisation by way of a note.
(f) Companies are disclosing nature of exceptional/ extraordinary items either by way of a note or by giving detail in respective row for exceptional/ extraordinary items.
(g) Noted the instance when change in accounting policy has been disclosed. These disclosures also include leverages given by any regulatory authorities. For example, disclosure of impact of Ministry of Corporate Affairs' notification dated 29th December, 2011 allowing companies to capitalise foreign exchanges' losses is disclosed by some listed companies.
(h) In most of the cases, no such information has been provided. This is probably due to fact that in most of the cases, the name of company itself describes the nature of the industry.
(i) Companies are disclosing all material/transactions such as merger, amalgamation, any major acquisition, entry into joint ventures, etc.
(j) Companies are disclosing this in their publication. Most of the companies are disclosing this information in tabular format. However, some companies are showing this as a note.
(k) Companies are disclosing this in their publication. In case a company has only one reportable segment, this has been disclosed by way of a note in published results.

What are the Compliance Practices Adopted by Listed Companies?

The compliance practice adopted by listed companies can be summarised as follows:-

Common Notes

Giving notes below the financial results is the most common practice adopted by companies. A closer look reveals that 4 to 8 numbers of notes generally companies give as a part of financial reporting which are common. These common notes are explicit and routine in nature, but vary in language. These common notes are as per Exhibit 1.

Thumb rule for publication of financial results should be the disclosure of all material/significant information/transactions and new developments that occurred during the period to stakeholders.

Exhibit 1

S. No.	Subject	Note generally given in published financial results
1	**Adoption of Financial**	"The above results have been reviewed by the Audit Committee and approved by the Board of Directors at their meeting on -----------------"
2	**Presentation of items**	"Previous period figures have been regrouped/ rearranged/restated/re-casted wherever necessary, to make them comparable."
3	**Presentation of items**	"The figures for the quarter ended ------------ are the balancing figures between the audited figures in respect of the full financial year and published year to date figures up to the third quarter of the relevant previous year."
4	**Exceptional items**	"Exceptional items include ………. " (These are items like voluntary retirement scheme expenses, foreign exchange gains/losses/diminution in value of investments, etc.)
5	**Standalone and consolidated financial**	Company having subsidiaries are giving note on standalone/consolidated results as the case may be.
6	**Dividend declaration**	A note is given as and when an interim or final dividend declared/recommended by Board of Directors.
7	**Investor complaints**	Note is given for the number of complaints outstanding for resolution at the beginning of the quarter, received and resolved during the quarter and pending for resolution at the end of the quarter.

S. No.	Subject	Note generally given in published financial results
8	**Segment Reporting**	Note is given with respect to applicability of segment reporting requirement under clause 41 (read with accounting standard no. 17 on segment reporting is disclosed)

Special Note

Special notes are given by the companies to highlight any significant event/transactions occurred during the period. For instance, all cement manufacturing companies disclosed the notice served by the Competition Commission of India on 20th June, 2012. Matters which are disclosed as special notes are as per Exhibit II.

Exhibit II

S. No.	Special notes given in published financial results
1	Suspension of any operation due to reasons like strike, lockouts etc.
2	Detail of stock option granted under Employee Stock Option Scheme
3	Utilisation of proceeds from initial public offering
4	Stock split and bonus shares issued during the period
5	Any approval, notices, orders, etc., received by government or any other regulatory bodies
6	Winding up of any operation or any subsidiary
7	Fresh investments made in any entity or subsidiary
8	Change in any accounting policy or practices and its impact thereupon on the financial results
9	Suspension of any operation
10	Payment of managerial remuneration above the limit prescribed under schedule XIII.
11	Change in the name of Company

Format and Contents

By and large, the format of published results by listed companies is in line with requirements given in Annexure I and III to clause 41. However, following deviations are observed:-

What are material/significant information/ transactions that need disclosure is a subjective decision of each Company? Looking at the corporate governance framework, this should be left for the Company to decide in consultation with auditor.

(a) Some companies are showing tax expenses in different line items depending upon the nature of its components *viz*. Minimum Alternative Tax, deferred tax, tax for earlier years, etc. However, a few companies preferred to show it in a single line item.

(b) Instead of giving separate line items of earning per shares (EPS, both basic and diluted) before and after the extraordinary items for the period, these are shown in one line item if EPS figures before and after the extraordinary items are same.

(c) Some of the income and expense heads are divided further to give a clearer picture. For instance, finance cost is shown in foreign exchange losses and other finance costs. Other income is shown in interest income and other income.

(d) In most of the cases, sales of products and services are shown as net of excise duty. However, there are instances that excise duty is shown separately in financial as a deduction from gross sales of products and services to arrive at sales of products and services (net of excise duty).

(e) Different nomenclatures are used for income and expenses heads. For instance, Finance cost is shown as Finance and interest charges.

(f) Exceptional and extraordinary items are explained by way of giving description of item in that row. However, a few companies preferred to show these items by way of a note in financial.

(g) Weighted average number of shares is provided separately by a few companies to arrive at basic and diluted earnings per share.

(h) Detail about investor's complaints is given in column format (i.e., the format given under annexure I of clause 41). Contrary to this, a few

Companies should focus on providing information **that make reported financial comparable and easily** understandable.

As a good corporate governance practice, the Company should be encouraged for voluntary disclosure of information.

companies preferred to show this item in a row or by way of a note.

Advertisement and Brand Building

Some of the companies take quarterly publication requirements as an advertisement and brand building opportunity. All companies used their own with holding company's monogram while publishing the results. Contrary to this, a few companies also published:-

(a) Picture of their brands in market.
(b) Punch line.
(c) Product lines.
(d) Product highlights.
(e) Award received during the period.
(f) Major CSR activities undertaken.

Key Highlights

Companies also published their major achievements during the reporting period as key highlights. These highlights included:-

(a) Achievements in production volumes and revenues.
(b) Significant project commissioned/installed during the reporting period.
(c) Major acquisitions made during the period.
(d) Key statistics like key ratios, etc.

Rounding Off

Annexure I and III to clause 41 require publication of financial results in rupees lakhs. Most of the companies are giving financial results up to two decimals of lakh of rupees. Contrary to this, a large chunk of companies preferred giving financial results in crores and some companies in rupees millions as well.

Some Interesting Disclosures

Some interesting disclosures by a few companies are observed. These are as per Exhibit III.

Exhibit III

S No	Company	Period	Disclosure Made
1	Maruti Suzuki India Limited	June 2012	₹ 10 lakhs is equal to ₹ 1 million.
2	HDIL	June 2012	Executive Chairman and Vice Chairman, 7 Managing Director have not taken any remuneration for the quarter under review.
3	Geodesic Limited	June 2012	Company has published 20 number of notes as part of its published results.
4	Nandan Exim Limited	March 2012	Financials are published twice in a newspaper that too in the same edition.

Conclusion

The publication of financial results by companies varies, to a small extent, both in format and content. This primarily suffices the compliance requirement envisaged under clause 41. Moreover, there were no futuristic statements in any publication. Looking at the prevailing practice, we may conclude as follows:-

(a) Thumb rule for publication of financial results should be the disclosure of all material/significant information/transactions and new developments that occurred during the period to stakeholders. This will help all stakeholders to understand the periodic performance of companies.
(b) What are material/significant information/ transactions that need disclosure is a subjective decision of each company? Looking at the corporate governance framework, this should be left for the company to decide in consultation with the auditor.
(c) There is no need of common notes as enumerated above. These are implied ones and may be dispensed with. Instead of this, companies should focus on providing information that make reported financial comparable and easily understandable.
(d) As a good corporate governance practice, the company should be encouraged for voluntary disclosure of information. Refer Exhibit III wherein a few companies have disclosed significant information/transaction/event occurred during the period.
(e) Companies should also be allowed to give 1 or 2 notes giving future outlook perceived by them. ■

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FSLRC's Indian Financial Code Bill Proposes Merging of SEBI, FMC, IRDA, PFRDA into Unified Financial Agency

Aiming to reform financial sector regulations for the longer term in keeping with systemic risks involved in financial management, the government-appointed Financial Sector Legislative Reforms Commission (FSLRC) headed by Justice B. N. Srikrishna has proposed an Indian Financial Code Bill to enable creation of a unified financial agency while limiting the role of the Reserve Bank of India (RBI) to monetary management.

As per the proposed regulatory architecture recommended by the Commission, whose report was put in public domain on Thursday, the unified financial agency (UFA)—and not a unified financial regulator, the commission has asserted—will comprise four existing agencies which will be merged into one. These are the Securities and Exchange Board of India (SEBI), the Forward Markets Commission (FMC), the Insurance Regulatory and Development Authority (IRDA) and the Pension Fund Regulatory and Development Authority (PFRDA).

Envisioning a full transition into a set of small and implementable measures, the FSLRC said the "existing RBI will continue to exist, though with modified functions." In all, the Commission suggested seven agencies and each of them will have distinct functions. Apart from the RBI along with the UFA, the Commission has suggested Financial Sector Appellate Tribunal (FSAT), Resolution Corporation, Financial Redressal Agency, Public Debt Management Agency and FSDC (Financial Stability and Development Council). The existing Securities Appellate Tribunal (SAT), it said, will be subsumed into FSAT and the existing Deposit Insurance and Credit Guarantee Corporation of India (DICGC) will be subsumed into the Resolution Corporation.

While the existing FSDC will continue to exist though with modified functions and a statutory framework, the Commission has recommended two new creations—a Financial Redressal Agency (FRA) and a new Debt Management Office. The draft Indian Financial Code Bill containing 450 clauses and six schedules is to give effect to its recommendations.

Explaining why the vast changes in the system of financial regulation and management is necessary, the report said: "The Commission is mindful that over the coming 25 to 30 years, Indian GDP is likely to become eight times larger than the present level, and is likely to be bigger than the United States GDP as of today... The aspiration of the Commission is to draft a body of law that will stand the test of time."

Implementation of the report, however, is not expected to be smooth. For, apart from the legislative changes required through Parliamentary approval, the fact that the Commission's recommendations are marked by dissenting notes by four members — P. J. Nayak, K. J. Udeshi, Y. H. Malegam and Jayanth R. Varma on a host of specific issues is an indications of the hurdles in the way.

As for capital control, it said the Finance Ministry should make rules for inbound capital flows, while the onus of making rules for outbound capital flows should rest with the RBI. However, one of the dissent notes pertains to this provision.

*(**Source:** www.thehindu.com/)*

Report on Framework for Green National Accounts Released

An expert group under Ministry of Statistics and Programme Implementation (MOSPI), Chaired by Prof. Sir Partha Das Gupta, which was set up to develop a framework for green national accounts, identification of data gaps and preparation of a road map to implement the frame-work, has submitted it Report. The Report was recently released by Prime Minister Dr. Manmohan Singh in the inaugural session of a 2-day International Workshop on 'Green National Accounting for India' on April 5, 2013. The Government of India, in recognition of the emerging need, had set up the expert group in August 2011.

The report "Green National Accounts In India – A Framework" consists of six chapters and dives extensively into the conceptual foundations of economic evaluation providing an outline of what would ideally be needed for a comprehensive set of national accounts. The Report deals extensively with not only the conceptual building up of the system of Green National Accounts , but also deals with the implement ability aspects based on the conceptual framework of Green Accounting Framework using the existing data sets and studies to discuss the framework methodology, valuation techniques, and feasibility of compilation of various sectoral accounting tables.

The National accounts reflect the state of an economy and form the raw material for both performance assessment and policy formulation.

*(**Source:** Press Information Bureau)*

CBDT Streamlines Taxation Rules for IT sector

Seeking to encourage Research and Development (R&D) activities in the IT sector, the CBDT has issued circulars to streamline the taxation rules in line with the recommendations of the Rangachary Committee. The circulars, issued with relation to the applicability of Transfer Pricing rules for taxation of development centres in the IT sector, will help in providing certainty to tax payers, the finance ministry said in a statement. The development centres, it said, should be treated as contract R&D service provider to their foreign principal if the risk attached to such centres is insignificant. The Transfer Pricing officers, while deciding on taxation issues concerning development centres, it said, should look into the conduct of the parties and not on mere contractual terms. With regard to the applicability of Profit Split Method (PSM), the circular said it should be considered as the most appropriate method for the purpose of computing tax liability under the Transfer Pricing. In case of the non-applicability of the (PSM), the circular said the Transfer Pricing officer should record the reason in writing.

*(**Source:** www.thehindubusinessline.com/)*

Income Tax Department to 'Name and Shame' Habitual Tax Evaders

The Income Tax department has decided to name and shame "chronic" tax defaulters by publicising their names and addresses. It is in the process of finalising the procedures of compiling the names and cases pertaining to habitual tax dodgers and subsequently uploading them on its website. "The department would upload the names of such defaulters who have either a huge outstanding tax against their name and are absconding or they have been dodging the taxes for a repeated number of times. The public will be informed against such people," a senior I-T official said.

*(**Source:** http://www.business-standard.com/india/)*

Fin Min Mulls New Intel Wing to Check Service Tax Evasion

Concerned over mounting cases of service tax evasion, the Government is mulling to create a separate intelligence unit to check the menace and stop leakage of revenue. The proposed Directorate of Anti Evasion to check service tax evasion is likely to be set up by the Finance Ministry close on the lines of two other intelligence agencies under it—Directorate General of Revenue Intelligence (DRI) and Directorate General of Central Excise Intelligence (DGCEI), official sources said.

*(**Source:** http://www.business-standard.com/india/)*

High Court Exempts Buses Hired by Road Transport Corporation from Paying Service Tax

A two-judge bench of the AP high court has stayed the collection of service tax from private buses hired by AP State Road Transport Corporation (APSRTC), the state-owned carrier. The bench comprising Justice G Rohini and Justice C Praveen Kumar made the interim order after hearing a writ petition filed by AP Hire Buses Welfare Association complaining that they were being made to pay service tax and value added tax (VAT) even when they were not required to do so. According to the petitioner, RTC had introduced the hired bus system in 2002-03 with a view to cut down its expenditure.

*(**Source:** http://www.economictimes.com)*

CBDT Amends Forms for Filing Appeal in CESTAT

Central Board of Excise & Customs wide Circular No.969/03/2013-CX dated 11th April, 2013 has decided to amend/revise the forms for filing appeal in the CESTAT. Accordingly, new forms for Central Excise (E.A.-3, E.A.-4, E.A.-5), Customs (C.A.-3, C.A.-4, C.A.-5) and Service Tax (S.T.-5, S.T.-6, S.T.-7) have been notified vide Notification Nos 6/2013-Central Excise (N.T.), 37/2013-Customs (N.T.) and 5/2013-Service Tax, all dated 10.04.2013 respectively. These forms have been made effective from 1.6 2013. Therefore, all appeals filed in the Tribunal on or after 1.6.2013 would be in the new form being prescribed. The new forms are expected to ensure quick disposal of cases. Additional information sought would lead to faster communication between the Tribunal Registry and the appellant, bunching of cases and would also facilitate creation of a comprehensive database.

*(**Source:** http://www.expressindia.com)*

Members of the ASAF Hold Inaugural Meeting, sign joint MoU

The members of the Accounting Standards Advisory Forum (ASAF), a technical advisory body to the International Accounting Standards Board (IASB) composed of members of the global accounting standard-setting community, met in London for their inaugural meeting last month. The meeting began with the IASB and members of the ASAF signing a joint Memorandum of Understanding (MoU) that sets out the purpose of the ASAF and its operating activities. The main technical subjects discussed were the IASB's *Conceptual Framework* and the Impairment projects. The meeting was webcast live and a recording of the webcast and corresponding meeting papers is available for downloading, from the meeting page at the IFRS website.

*(**Source:** http://www.ifrs.org/)*

IASB issues Request for Information on Rate Regulation

The International Accounting Standards Board (IASB) has recently issued a request for Information as an early step in its reactivated Rate-regulated Activities research project. The objective of the Request for Information is to identify a range of rate-regulatory schemes to help determine the scope of the research project. The deadline for responses is 30 May 2013. The Request for Information asks specific questions about the objectives of rate regulation and how those objectives are reflected in the rate-setting mechanisms employed by rate regulators. The fact patterns identified through this Request for Information and other research will be used to develop a Discussion Paper that will analyse the common features of rate regulation. The aim of the Discussion Paper is to identify what information about the consequences of rate regulation would be most useful for users of IFRS financial statements and whether the IASB should develop specific guidance for accounting for those consequences. The Request for Information can be downloaded from the IASB's website.

*(**Source:** http://www.ifrs.org/)*

The IFRS Foundation Publishes the 2013 Annual Version of the IFRS Taxonomy

The IFRS Foundation has published the IFRS Taxonomy 2013. The IFRS Taxonomy is a translation of International Financial Reporting Standards (IFRSs) into eXtensible Business Reporting Language (XBRL). The 2013 taxonomy is consistent with Standards as issued by the International Accounting Standards Board (IASB) at 1 January 2013, and contains XBRL tags for disclosure requirements. By providing the IFRS Taxonomy, the IFRS Foundation seeks to address the demand for an electronic standard to transmit IFRS information. The architecture framework of the 2013 taxonomy is consistent with previous versions and consolidates all IFRS Taxonomy interim releases that were published in 2012. In addition, the IFRS Taxonomy 2013 includes concepts that reflect some industry practices. These concepts have been derived from an analysis of financial statements prepared by companies' representatives from the banking, insurance and extractive (mining and energy) industries. In accordance with the IFRS Foundation's due process for its XBRL activities, the IFRS Taxonomy 2013 has undergone a comprehensive review by the XBRL Quality Review Team which is an external advisory committee that supports the IFRS Foundation by reviewing taxonomy drafts. Furthermore, a public review that ended in March 2013 resulted in the submission of comments, which were analysed and, where relevant, integrated into the final version. The IFRS Foundation has published the 2013 taxonomy with the updated IFRS Taxonomy Guide, Feedback Statement and a range of accompanying materials that have been specifically developed to aid understanding and use of the IFRS taxonomy.

*(**Source:** http://www.ifrs.org/)*

IASB Publishes Proposals for Amendments to **IAS 19 Defined Benefit Plans:** Employee Contributions

The International Accounting Standards Board (IASB) recently published for public comment an Exposure Draft of proposed amendments to IAS 19 *Employee Benefits*. The IASB is responding to concerns that were raised about the complexity of applying certain requirements of IAS 19. Specifically the concerns related to the accounting for contributions from employees and third parties to defined benefit plans. The objective of the proposed amendments is to provide a more straight-forward alternative for this accounting when the contributions payable in a particular period are linked solely to the employee's service rendered in that period. The proposed guidance would be applicable, for example, to accounting for employee contributions that are calculated according to a fixed percentage of salary. The issue originated from a submission to the IFRS Interpretations Committee, which recommended that the IASB amend the Standard. The Exposure Draft can be accessed via the project website or on the 'Comment on a proposal' page on www.ifrs.org. The IASB requests comments to these proposals by 25 July 2013.

*(**Source:** http://www.ifrs.org/)*

Small Businesses Want Less Tax Complexity

Complexity and inconsistency within the tax code continue to be a major problem for small businesses, with one out of four small businesses reporting that they need to spend 120 hours or more per year on the administration of federal taxes, or three full work weeks, according to a new survey. The National Small Business Administration recently released its 2013 Small Business Taxation Survey, offering detailed insight on how small businesses are affected by federal taxes. The overwhelming majority of small business owners said they support broad reform of the federal tax code, with both corporate and individual tax reform, in conjunction with a reduction in business and individual deductions. Reducing the deficit is another key issue for small business, and the number one method for doing that supported by small businesses (82 percent) is through tax reform that creates economic growth and generates federal revenues. Underscoring the complexity of the federal tax code is the fact that 84 percent of small-business owners must pay an external tax practitioner or accountant to handle their taxes. Furthermore, when asked to rate the most significant challenge posed by the federal tax code to their business, the majority, 55 percent, picked administrative burdens while 45 percent said financial burdens.

*(**Source:** http://www.accountingtoday.com/)*

PCAOB Plans Forums on Small Business Audits

The annual forums are updated every year with the goal of sharing important information about PCAOB activities with registered public accounting firms that audit clients in the small business community. They also provide an opportunity for PCAOB board members and staff to listen to questions, comments and concerns from auditors. The forums begin on June 6 in Seattle, where the agenda will include several case studies presented by staff from the PCAOB Division of Registration and Inspections, the Division of Enforcement and Investigations, and the Office of the Chief Auditor. Staff from the Securities and Exchange Commission's Division of Corporation Finance will participate with PCAOB staff in discussing the JOBS Act and how it may affect PCAOB standard setting for audits of smaller public companies. SEC staff also will provide an update on recent SEC activities and observations about common financial reporting issues facing smaller public companies. The 2013 agenda will target some of the special challenges that the inspection program has identified in small to mid-size company audits. Each forum is hosted by a member of the PCAOB board and is open to PCAOB-registered firms. There is no fee charged to participate in these events, but pre-registration is required. Attendees also have the opportunity to earn continuing professional education credits. The PCAOB held its first small business forum in 2004 and has continued to hold forums across the country, meeting with more than 5,000 representatives of smaller registered public accounting firms.

*(**Source:** http://www.accountingtoday.com/)*

FASB Previews Framework for Deciding on Accounting Standards Changes for Private Companies

The Invitation to Comment: *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies* seeks feedback from stakeholders on the proposed private company decision-making framework. The framework is supposed to serve as a guide for FASB and the recently established PCC in determining whether and under what circumstances to provide alternative recognition, measurement, disclosure, display, effective date or transition guidance for private companies reporting under U.S. GAAP. To help identify more opportunities to improve the guide, FASB and the PCC are asking to provide input on the Invitation to Comment by June 21, 2013. After the comment period, FASB and the PCC will re-deliberate and are likely to further revise the guide. The Invitation to Comment is available at www.fasb.org. A FASB in Focus document explaining the proposals also is available on FASB's Web site.

*(**Source:** http://www.accountingtoday.com/)*

ACCOUNTANT'S BROWSER

'PROFESSIONAL NEWS & VIEWS PUBLISHED ELSEWHERE'

Index of some useful articles taken from periodicals/newspapers, received during March-April 2013 for the reference of Faculty/ Students & Members of the Institute.

1 ACCOUNTING

Putting Accountants on a "Lean" Diet by Peter C. Brewer and Frances A. Kennedy. *Strategic Finance*, Feb.2013, pp.27-34.

Return on talent & its Accounting-role & challenge for cost & management Accountants (CMAs) by Partha Chatterjee. *The Management Accountant*, March 2013, pp.273-276.

What have IASB and FASB convergence efforts achieved? By Paul Pacter. *Journal of Accountancy*, Feb. 2013, pp.50-59.

2 AUDITING

Clarifying the standard for group Audits by C. William Thomas & Phil D. Wedemeyer. *Journal Of Accountancy*, March 2013, pp.32-39.

Fear factor: Internal Auditors should not be afraid to embrace their role in enterprise risk management and move it ahead in their in their organizations by Neil Baker and Freelance Writer. *Internal Auditor*, Feb.2013, pp.46-53.

Framework for excellence: A Multi-Dimensional assessment tool can help Audit practitioners determine how their department rates along a spectrum of performance levels by Manny Rosenfeld. *Internal Auditor*, Feb.2013, pp.55-58.

3 ECONOMICS

Economic Survey 2012-2013. Company law Journal, Vol.1/1, 2013, pp.152-187.

Educational attainment in India: What drives transition? By Suman Kumar Bhaumik and Manisha Chakrabarty. *Money & Finance*, Feb.2013, pp.95-112.

Global food security through sustainable agriculture by Francis Kuriakose and Deepa Kylasam Iyer. *Facts for You*, Feb.2013, pp.33-35.

Heterogeneous pro-poor targeting in the National Rural employment guarantee scheme by Yanyan Liu and Christopher B Barrett. *Economic & Political Weekly*, Vol.48/10, Mar.9, 2013, pp.46-53.

4 INVESTMENT

Determinants of going-public decision in an emerging market: evidence from India by Manas Mayur & Manoj Kumar. *Vikalpa*, Jan.-March 2013, pp.65-86.

Global foreign direct investment: An Overview by K. Uma. *Facts for You*, Mar.2013, pp.32-34.

Retail investors: How to Boost their participation in the capital market. *Facts for You*, Feb.2013, pp.31-32.

5 LAW

Companies Bill 2012: A Paradigm shift by Manish Kapur and Suvira Agarwal. *CFO Asia*, Feb.2013, pp.20-22.

Consolidated financial statement vs. Companies bill by Dolphy D'Souza. *BCAJ*. Vol.44-B, Mar.2013, pp.83-86.

6 MANAGEMENT

Corporate Governance: Financial regulators & courts need to be on the same page by Anurag K. Agarwal, *Vikalpa*, Jan.-March 2013, pp.1-12.

How to do Business Abroad: A Rising number of small and midsize companies go international by Sabine Vollmer. *Journal of Accountancy*, Feb.2013, pp.40-45.

7 TAXATION & FINANCE

International Taxation: Taxability of Capital Gains in India in respect of transfer of shares of a non-resident entity holding shares of an Indian company, between two non-residents in a Tax treaty situation by Mayur Nayak, Tarunkumar G. Singhal and Anil D. Doshi. *BCAJ*, Mar.2013, pp.39-48.

Stopping Tax identity theft: Practical advice for CPAs and clients by Valrie chambers and Rabih Zeidan. *Journal of Accountancy*, Feb.2013, pp.60-64.

Tax avoidance-what now? By Jim Oulton and Tim Shepherd. *Accountancy*, Mar.2013, pp.12-13.■

Full Texts of the above articles are available with the Central Council Library, ICAI, which can be referred on all working days. For further inquiries please contact on 011-23370154 or by e-mail at library@icai.org

Announcement: FCMITDA

Presentation of Foreign Currency Monetary Item Translation Difference Account

1. In the year 2009, the Ministry of Corporate Affairs amended Accounting Standard (AS) 11, *The Effects of Changes in Foreign Exchange Rates* by inserting Paragraph 46. As per Paragraph 46, in respect of accounting periods commencing on or after 7th December, 2006 and ending on or before 31st March, 2011, at the option of the enterprise, exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, insofar as they relate to the acquisition of a depreciable capital asset, can be added to or deducted from the cost of the asset and shall be depreciated over the balance life of the asset, and in other cases, can be accumulated in a " Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortised over the balance period of such long-term asset/liability but not beyond 31st March, 2011, by recognition as income or expense in each such periods.
2. On 29th December, 2011, the MCA, through the Companies (Accounting Standards) Amendment Rules, 2011, further extended the date of amortisation of the balance in the FCMITDA to 31st March, 2020 instead of 31st March, 2011. The MCA on December 29, 2011, inserted paragraph 46A in the AS 11, *The Effects of Changes in Foreign Exchange Rates* through Companies (Accounting Standards) (Second Amendment) Rules, 2011, on similar lines as paragraph 46.
3. As in the Revised Schedule VI format, no line item has been specified for the presentation of "Foreign Currency Monetary Item Translation Difference Account (FCMITDA)", the Council of the Institute at its 324th meeting held on March 24-26, 2013 at New Delhi, considered the issue regarding the presentation of the FCMITDA in the balance sheet.
4. The Council noted that the Framework on Preparation and Presentation of Financial Statements issued by ICAI, defines an asset as follows:

   "An asset is a resource controlled by the enterprise as a result of past events from which future economic benefits are expected to flow to the enterprise."

Where the balance in FCMITDA represents foreign currency translation loss, it does not meet the above definition of 'asset' as it is neither a resource nor any future economic benefit would flow to the entity therefrom. Accordingly, such balance cannot be reflected as an asset.

Accordingly, the Council decided that debit or credit balance in FCMITDA should be shown on the "Equity and Liabilities" side of the balance sheet under the head 'Reserves and Surplus' as a separate line item.

5. The aforesaid decision of the Council supersedes the following Frequently Asked Question on AS 11 notification – Companies (Accounting Standards) Amendment Rules, 2009 (G.S.R. 225 (E) dt. 31.3.09) issued by Ministry of Corporate Affairs on May 18, 2009, which was issued by the Accounting Standards Board of ICAI on May 18, 2009:

   "(14) How 'Foreign Currency Monetary Item Translation Difference Account' should be presented in the Balance Sheet?

   Response

   The 'Foreign Currency Monetary Item Translation Difference Account' should be shown as a separate line item in the Balance Sheet, in line with treatment given to Deferred Tax Asset/Liability, i.e. after the head 'Investments' or after the head 'Unsecured Loans' as the case may be and separately from current assets and current liabilities."

Study Tour: Sydney & Melbourne

ICAI STUDY TOUR TO SYDNEY AND MELBOURNE SEPTEMBER 18-23, 2013

Australia and India have enjoyed a special bonding in terms of their move to a regional economic operation and in terms of services sector in general and accountancy sector in particular. Both countries share common cultural and linguistic ties as both are part of the Commonwealth of Nations. The Institute of Chartered Accountants of India (ICAI) has recently signed Memorandum of Understanding (MOU) with CPA Australia and the Institute of Chartered Accountants of Australia (ICAA). These MoUs will provide an ample opportunity and recognition to Indian Chartered Accountants in Australia.

In order to promote member to member and firm to firm contact so as to under stand the economic and regulatory environment and better understanding of the economic opportunities and to tap the vast market existing for Chartered Accountants in Australia; the International Affairs Committee of ICAI will be undertaking the tour to selected cities of Australia during **18-23 September, 2013** for members, on self financing basis. The Study Tour is a mix of business meetings and net working.

The study tour would seek to hold discussions with counterpart organisations, stakeholders, members etc. and will have the following basic objectives:-

- Build sustainable capacity by providing participants an opportunity to see and interact with various officials in respective countries
- Facilitate understanding and steps towards networking of the accounting firms in India and respective countries
- Seek association for the research and developmental activities of the Institute in different fields
- Discuss the issues of qualification and ways to facilitate cooperation at firm level
- Develop an understanding to help trade and industry in the respective countries and facilitate inter-country trade and investment

Since, the delegation size would be limited to 50, **registration for the study tour would be on first-come-first-serve basis and ICAI reserves the right to finalise the composition of the delegation.** The package would include the following:

- Economy Class Airfare with applicable taxes Ex-New Delhi
- Visa cost
- All accommodation on twin sharing basis in 4 star hotels or similar to cut down on costs
- All meals (Indian): Breakfast, Lunch and Dinner.
- All transfers by private A/C coach
- Sight seeing activities in Sydney and Melbourne
- Cost of all entrance tickets / fees for the above mentioned sightseeing tours.
- Services of local tour guide and/or tour escort
- All current applicable Hotel & Government Taxes

Complete details reading the itinerary and the amount to be paid will be uploaded on the website www.icai.org shortly. The interested members (spouses are allowed) may write to us at ia@icai.in for any further information.

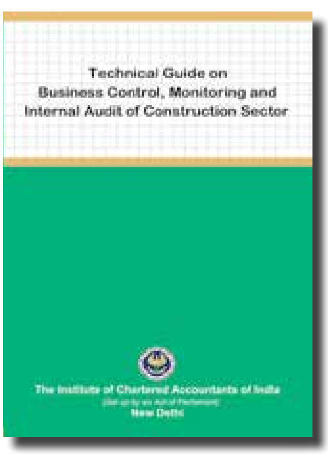
For further details, please contact:
Secretariat of the International Affairs Committee, The Institute of Chartered Accountants of India, ICAI Bhawan, PB No. 7100, Indraprastha Marg, New Delhi – 110 002, India. Ph +91 11 30110443,448, 39893989 (Extn. 443,448), Fax +91 11 30110591.

New Publications

Technical Guide on Business Control, Monitoring and Internal Audit of Construction Sector

Price:
₹250/-

Pages:
276 (including initial pages)



The construction industry in India has been witness to a strong growth wave powered by large spends on housing, road, ports, water supply and airport development. With scale comes complexity, as the global industry and number of players are ever increasing, players navigate a tough political, commercial, regulatory and governance environment, which will test their risk management ability to the maximum extent. As a result, the roles and responsibilities of the members working as internal auditors in construction industry has assumed considerable significance.

1. Keeping this in view, the Internal Audit Standards Board had issued "*Technical Guide on Internal Audit of Construction Industry*" in 2010 that comprehensively dealt with the peculiar aspects of construction industry and provided a step-wise approach for internal audit. In recent times, a number of developments have taken place impacting the construction industry in the country.

Considering this, the Internal Audit Standards Board has issued this "*Technical Guide on Business Controls, Monitoring and Internal Audit of Construction Sector*" which covers more elaborate guidance on internal audit and also covers business controls and monitoring aspects. The focus of this Guide is civil contracting firms, i.e., those organisations which undertake the construction activity on contractual basis; however, it is also relevant for real estate developers and long term infrastructure players.

Salient Features of Technical Guide:

- Describes evolution, benefits, special features, major challenges faced by the construction industry.
- Provides guidance on statutory laws applicable to the industry.
- Provides guidance on aspects involved in various stages of construction industry, such as, tendering, site mobilisation, project execution, project completion with more focus of functional departments like, engineering, stores, human resources, accounts, etc.
- Contains internal controls checklist for various processes.
- Explains detailed procedures to be undertaken by the internal auditors.
- Includes flowcharts to help the readers in understanding the construction environment.
- The Guide also comes with a CD of the entire Guide to ensure ease of reference and reusability.

Ordering Information

The publication can be purchased online. Please refer link: http://www.icai.org/publications.html. The publication is also available at the sales counters of the Institute at New Delhi, Chennai, Mumbai, Kolkata and Kanpur. To order by post, please send a demand draft in favour of "**Secretary**, **The Institute of Chartered Accountants of India"**, payable at New Delhi to:

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Phone: (0120) 3045943
E-mail: postalsales@icai.org

Webcasts for Students

On ICAI WebTV

http://icaitv.com

Introduction

The Board of Studies of the Institute has great pleasure in announcing Webcasts for Students on ICAI TV, the URL given on the LHS.

Students Webcasts are broadly categorized into two categories—Subject Specific and Motivational/ Instructional.

Objective

Provide quality education and development facility anytime and anywhere in an affordable manner through a self learning/ development facility.

Salient Features

- Anytime/ Anywhere Online Learning
- Free Coaching
- Support Students in Small Mofussil Towns and Cities
- Support Poor Students with quality educational inputs
- Take learning and development to the doorsteps of students
- Provide a Self Learning/ Development facility

Webcasts Available

Students are advised to benefit from the following three webcasts of two hours duration each, links for which are available below:

- **Final Direct Tax Laws:** http://icaitv.com/?p=1861
- **Preparing for CA Exams:** http://icaitv.com/?p=1930

Links to the aforementioned webcasts are also available through the Students Learning Management System (LMS) at http://studentslms.icai.org under Announcements Section.

Webcasts Available

The Board of Studies would be organizing Subject Specific Webcasts for the benefit of Students taking the November 2013 Examinations from July 2013.

Director
Board of Studies

The Institute of Chartered Accountants of India
[Set up by an Act of Parliament]

CA Regulations, 1988 provide scope for Secondment of articled assistant facilitating an opportunity for gaining practical experience in multi-disciplinary work and variety of business situations. A principal may second an articled assistant to other member/s with a view to provide him/her training in the areas where the principal/articled assistant may require. Secondment can also be availed during Industrial Training.

Such Secondment can be done under an eligible member whether in practice or in employment. A member can provide secondment to maximum two articled assistants at time. The minimum period of secondment shall be four months and the maximum period shall be one year which may be served with more than one member. During the period of secondment, the member with whom the articled assistant is seconded shall pay stipend at the rates prescribed under CA Regulations. A record of training imparted during secondment will be properly maintained.

For Secondment, a statement in the form containing particulars of training needs to be filed with the Institute within 30 days from the date of commencement of training on secondment.

Members may inform their articled assistants regarding secondment and encourage them to undergo secondment with an eligible member for training in the desired field. Detailed information and prescribed application form of secondment is available on ICAI website www.icai.org as well as may be obtained from concerned regional offices of ICAI.

Overseas Members/Subscribers for Journal Subscription

As per a change in policy, the Postal Department of Government of India is not receiving the Chartered Accountant Journals for posting through Seamail. Hence the Journals are being sent through Airmail only.
In view of the above situation it has been decided to discontinue the Seamail category of sending the journals to the foreign members/subscribers henceforth. As such, all the overseas Members/Subscribers of the Journal are being sent journal by Airmail only. Thus all such members/subscribers are requested to pay ₹2100/- (for One Year) as Airmail surcharge for posting of the Journal.

-Editor

Forthcoming Events[1]

Sl. No.	Title of the Seminar/ Conference	Date	Place	CPE Hours
1.	Certificate Course on Arbitration	11th, 12th, 18th, 19th, 25th & 26th May 2013	ICAI Bhawan, Plot No. 19-B, Scheme No. 78, Part II, Indore (M.P.)	20
Topics	Module I - Introduction to Alternative Dispute Resolution Module II - Allied Laws Module III - Arbitration in India Module IV - Arbitration Procedure Module V - Arbitration Award Module VI - Skills, Ethics and Economics in Arbitration Module VII - Arbitration in Other Countries and Emerging Trends (Including Case Studies/Assignments/Research Paper/ Mock Arbitration/Award writing etc.)			
Contact Person	**Programme Chairman:** CA. Manoj Fadnis, Central Council Member and Chairman, CECL&WTO (M) +91 9826027716, 9302217716, Email: manojfadnis@icai.org **Programme Director:** CA. Prafulla Premsukh Chhajed, Central Council Member and Vice-Chairman, CECL&WTO, (M) +91 9821090612, Email: pchhajed@yahoo.com **Programme Co-ordinator:** CA. Vikas Jain, Chairman, Central India Regional Council of the ICAI, (M) +91 9300099960, Email: vikas_jain_ca@yahoo.com CA. Manoj P. Gupta, Chairman, Indore Branch, CIRC, (M) +91 9827026540, Email: manojpgupta@rediffmail.com; indore@icai.org Secretariat, Committee on Economic, Commercial Laws & WTO Ph: 011 30110499, Mb: 09312085029, E-mail: cecl@icai.in, ctlwto@icai.org			
2.	Seminar on Internal Audit and Risk Management	4th May 2013	ICAI Bhawan, Lucknow	6
Topics	1. Standards on Internal Audit – Codifying the Best Practices, 2. Basic Principles Governing Internal Audit and Planning Internal Audit, 3. Understanding Risk based Internal Audit- Theory, Implications and Practical Issues, 4. Fraud- Internal Auditor's Role in Prevention and Detection of Frauds			
Contact Person	Lucknow Branch of CIRC of ICAI, E-mail: lucknow@icai.org, Phone: +91522-2301524, 3241932			
3.	National Seminar on Direct taxes	18th May, 2013	Hotel Marigold, Greenlands, Hyderabad	6

[1] For more details about the forthcoming events please refer the detailed announcements hosted on the ICAI website www.icai.org

Sl. No.	Title of the Seminar/ Conference	Date	Place	CPE Hours
Topics	1. Issues in TDS provisions, 2. Business deductions – Latest Judicial Trends, 3. Capital Gains & Development Agreements, 4. Domestic Transfer Pricing			
Contact Person	Hyderabad Branch of SIRC of ICAI, ICAI Bhawan , 11-5-398/C, Red Hills, Hyderabad – 500004, Phone: 040-23393182, 23393200, Email id – hyderabadicai.org			
4.	Webinar on “Need for an effective Intellectual Property Eco System in an Innovative Organisation”	13th May, 2013	ICAI Bhawan, Indraprastha Marg, New Delhi	-
Topics	Need for an effective Intellectual Property Eco System in an Innovative Organisation			
Contact Person	Committee Secretariat, Phone: 0120-3045996, e-mail- congos@icai.org, cconpo@icai.in			
5.	Workshop on Capacity Building initiative for Recently Qualified Members in Practice	25th & 26th May, 2013	ICAI Bhawan, 19-B, Scheme No. 78-II, Near New SICCA School, Indore(M.P.)	12
Topics	1. Internals in Internal Auditing: Execution and Areas, 2. Internals in Internal Auditing: Drafting and Reporting, 3. Bird’s Eye view on / Insight to various financing techniques and parameters, 4. Bird’s Eye view on / Insight to Subsidies based Financing, 5. Direct Taxes :Procedural Aspects and TDS, 6. Direct Taxes: How to present your case before Income tax Authority, 7. Marketing yourself within Legal Framework: Dos and Don’t’s of CA Profession and Code of Conduct, 8. Excelling in Non Traditional Areas of Practice: Exploring the Unexplored Area			
Contact Person	**Programme Chairman:** CA. Naveen N.D. Gupta, Chairman, Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI, e-mail: chairman.ccbcaf@icai.org, Mobile: 09810689998 **Programme Co-Chairman:** CA. Shyam Lal Agarwal, Vice Chairman, Committee for Capacity Building of CA Firms and Small & Medium Practitioners, ICAI, e-mail: shyamjpr@gmail.com, Mobile: 9414053163 **Programme Co-Chairman:** CA. Manoj Fadnis, Central Council Member, ICAI, e-mail: manojfadnis@icai.org, Mobile: 09302217716 **Programme Coordinator:** CA. Manoj P. Gupta, Chairman, Indore Branch of CIRC of ICAI, Mobile: manojpgupta@rediffmail.com, Mobile: 09827026540			

What's Your EQ, Mr. Accountant?

The article deals with a subject for which professionals in India are still searching for answers nearly two decades later, after once it appeared on the cover page of a leading magazine in India. It revolves around the subject 'Emotional Quotient'. Emotional Quotient can be expressed as the ability to have command over the emotions in perceiving, controlling and evaluating them. It is the intelligence which allows us to learn from our emotions, and uses them to effectively deal with ourselves as well as others. Emotions drive people and people drive performance. A better predictor of performance than professional skill, knowledge, expertise or even IQ, EQ can be measured and developed unlike IQ which lends itself only for measurement and not for development after a certain age. The article discusses the significance of EQ in depth, IQ getting its due simultaneously. How EQ, in fact supplements IQ and is not a substitute for the latter is well highlighted in the article. Read on to know more…

CA. R. Venkitachalam

(The author is a member of the Institute. He can be reached at venkat_rvc@yahoo.com)

Accountants are the icons of academic brilliance and arguably the finest examples of IQ driven competencies in the business world. To be successful in the world of business, however, an accountant needs some differentiating set of competencies in addition to his intellectual prowess. These leadership competencies are derived from Emotional Intelligence. There is a need to appreciate the importance of these competencies. This proposition has been articulated by various international accounting bodies as well. This makes an attempt to explain the concept of Emotional Intelligence (EQ).

Emotional Quotient

- Why does it matter?
- And what is it, anyway?

I expect the above two questions in return for my article's title query which would in fact justify this article in this Journal. Let me also add the following question of my own, before I try to answer all the three questions, albeit in reverse order in order to be able to commence my discussion from a familiar territory from the point of view of accountants.

- Has it anything to do with IQ?

IQ and the Accountant:

After all, IQ is something all of us know and are familiar with, for it is not only an index of the level of intelligence of a person, but also the most representative character of our profession highlighted by two other alphabets, viz., CA. There are a number of chartered accountants occupying positions in top echelons in the corporate world globally. In fact, many of them are Chief Executive Officers of their respective companies. Being an accountant may have helped them to take the first step towards their journey to the highest positions of power in the organisation; but they are not there for the only reason that they have been successful bean counters. This essentially presupposes certain leadership competencies not acquired through cogitative intelligence, but from some other source. An effort has been made in this article to lay out the source of skill sets required for an accountant to be a successful leader as well.

Beyond the Realm of IQ:

In today's fiercely competitive world for an accountant, or for that matter any other professional, it is not enough to be an ace in his/her own domain of expertise, be it a department, a function or a company. Beyond professional expertise, one needs a unique set of skills and expertise to deal with people and situations which may have nothing to do with knowledge domain. As long as you live in an island relatively isolated from the external world and your functions do not call upon you to interact with people, you may not need any special skills in handling people. Take the case of a research scholar. It may be safe to assume that his or her professional life is not impacted by a lack of any inter-personal skills. However, if his personal life has to be successful and meaningful, he or she has to have skills to handle people that include his or her family. It is therefore virtually impossible to visualise that mythical character called 'the sole performer', who can isolate himself from his environment in which he lives and can still thrive. If ever there is an accountant who is not holding any leadership position and who is not constantly called upon to deal with people, his IQ will of course stand him in good stead as he need not bother about those special skills to influence people. But then, it is indeed difficult to find people of that genre. Instead, the reality for you is that you are constantly surrounded by people, you work in teams and you interact with clients all the time resulting in your influencing others and others in turn influencing you.

The relentless search for that mental ability which can truly be called 'intelligence' made Peter Salovey of Yale University and John Mayer of University of New Hampshire in 1990 to coin the terminology **"Emotional Intelligence" for the first time, thereby** announcing to the world that intelligence is not just about academic brilliance based on numerical abilities and that there is something more to it.

The society sees an accountant almost as a nerd. This perception of the society is changing of late. But is the accountant changing? It is not to say that the accountants as a class suffer from the *Asperger's Syndrome*, a psychiatric disorder characterised by impaired social relations and by repetitive patterns of behaviour. There are accountants and accountants; but only some of them are ready and able to accept the mantle of leadership. It is necessary to go on a journey of discovery to find out the source and sustainability of those competencies which make the accountant a leader – and enters into that intelligence which is not known as intelligence in common parlance. In order to understand this paradoxical statement, we need to discuss the concept of intelligence in itself first.

Concept of Intelligence:

Intelligence means many things to many people. It was always a daunting challenge for the human race not only to understand what it is, but to grade it as well. This quest for measurement of intelligence took Alfred Binet, a French psychologist to develop a construct on intelligence and prescribe a methodology to measure it in the early 1900s. Binet suggested the concept of a mental age or a measure of intelligence based on the average abilities of children of a certain age group. It was during World War I that intelligence tests were used on a large scale. At the outset of the War, the US Army officials were faced with the monumental task of screening large number of army recruits. Robert Yerkes developed two tests known as Alpha and Beta, the former was a written test and the latter was administered orally to deal with army recruits who could not read. It was in 1940 that the American psychologist David Wechsler talked of 'non-intellective' intelligence and he came out with a Wechsler Adult Intelligence Scale. Howard Gardner in 1983 proposed that mere numerical expressions of human intelligence are not a full and accurate depiction of people's abilities. The relentless search for that mental ability which can truly be called 'intelligence' made Peter Salovey of Yale University and John Mayer of university of New Hampshire in 1990 to coin the terminology "Emotional Intelligence" for the first time, thereby announcing to the world that intelligence is not just about academic brilliance based on numerical abilities and that there is something more to it. It was left to Daniel Goleman, a reporter with *The New York Times* who happened to be a psychologist, to popularise the concept of Emotional Intelligence in 1995. With his seminal book titled "Emotional Intelligence" and the work he did in the field, he proved convincingly and beyond doubt that Emotional Intelligence is more a predictor of success in career and life than Intellectual Intelligence. Intelligence is like Money. Money is what money does, so goes the famous economic maxim. So is the case with Intelligence. Intelligence is what intelligence does. It is an enabler whose output is a set of competencies. Those who have high IQ are likely to be good in their respective fields, say mathematics or life sciences. IQ helps one acquire the threshold competencies which by itself is not a great predictor of success. But the other part of intelligence known as Emotional Intelligence (EQ) is what matters most in life, post qualification. IQ may get you selected; but it is EQ that will get you promoted. Such is the power and importance of Emotional Intelligence.

Emotional Intelligence:

Emotional Intelligence is that intelligence which allows us to learn lessons from our emotions, uses our emotions effectively to deal with ourselves and others as well. One can deploy emotions intelligently to influence people and the environment. As quoted earlier intelligence is what intelligence does. This intelligence is the enabler to develop certain competencies from our emotions essential in leadership situations. Meyer and Salovey who coined the term emotional intelligence for the first time defined it thus:

"Emotional Intelligence is the ability to perceive emotions, to access and generate emotions so as to assist thought, to understand emotions and emotional knowledge, and to reflectively regulate emotions so as to promote emotional and intellectual growth."

> "Completing rigorous graduate programmes, passing, testing and gaining credentials ensure that those who pass such hurdles are of above-average intelligence. However, simply having a superior IQ does not guarantee that they will be superior doctors, accountants or leaders"

The focus here is the deployment of emotions on oneself and others for which you need some kind of intelligence which is not present in the IQ domain.

Daniel Goleman defines Emotional Intelligence in the following words echoing more or less the same substance, but with more clarity:

"The capacity for recognizing our own feelings and those of others, for motivating ourselves and for managing emotions well in ourselves and in our relationships."

It is important here to delineate the terminologies used, very often interchangeably, to understand the concepts clearly. Emotional Intelligence is that intelligence which helps us to develop certain competencies which are called Emotional Competencies that are critical for leaders. They are, therefore, called Leadership Competencies and the index of which is called Emotional Quotient (EQ).

Importance of Emotions:

Having understood the critical importance of Emotional Intelligence and the fact that this intelligence operates in the domain of emotions, let us now discuss the importance of emotions. After all, man is a social animal—if I could borrow a clichéd saying. What is implicit in the statement is that though he is behaving the way the society expects him to, he is still an animal by instinct. Animals are driven by base and basic emotions—some of them predatory and many others more moderate. This in a way makes man an oxymoron by design. He is the most rational being on the face of the earth, but is still driven by animal instincts. That in turn makes the task of dealing with the human kind a complex exercise. It may be relatively easy to handle the rational part of the human brain rooted in logic; but dealing with his emotional part calls for a higher level of competency and therein lies the challenge one faces in everyday life. Emotions are who we are. It is necessary to keep in mind that even a new recruit comes to you as a whole package including his emotional baggage. It is as important to deal with his emotional self as it is to deal with his career aspirations. Seen in this light, the age-old refrain that one should keep his or her emotions outside the workplace sounds laughable, if not outright ridiculous. Emotions are real and let us learn to deal with them if we need to be successful in life. Moreover, the ability to use emotions effectively gives us certain critical skills which we need to sustain high performance in an increasingly competitive professional environment. In the past, emotions were considered to be dysfunctional and were branded as

Intelligent accountants famous for their academic brilliance do not often make the grade; yet many others with moderate credentials do. Lower EQ may be the reason.

a weakness in a human being. They were supposed to be chaotic, superfluous, haphazard and above all incompatible with reason. It was generally believed that emotions were largely visceral, resulting from lack of effective mental adjustments. Not anymore. Today, we view emotions differently. They arouse, sustain and direct activities. They are important part of living organisms. It is not in opposition to intelligence, but in a way, it is of a higher order of intelligence in itself.

Emotional Competencies:

Having postulated that emotions are real, let us discuss the tools available to deal with them, for emotions are like loose cannons capable of wreaking havoc at will with unpredictable consequences. We need to have a special kind of intelligence to tell us whether these emotions are capable of producing positive outputs or are they destructive in nature. Should it be of the latter kind, we should be able to have the wherewithal to prevent them from becoming dysfunctional. At the same time, we should effectively use the positive emotions for our benefit. That calls for a special kind of intelligence which we now know and is known as Emotional Intelligence. Simply put in accounting terms, in our Balance Sheet, emotions should become our assets rather than our liabilities. Going a step further, a person gifted with a higher order of emotional intelligence possesses the knack of perceiving the emotions of others and can appropriately tune his or her behaviour to deal with such emotions of others. In a way he is in a position to manipulate the feelings of others, not necessarily in a negative sense.

Like Intellectual Intelligence (read IQ), Emotional Intelligence by itself is not a destination. It is an enabler. By using such intelligence we develop certain competencies. Competencies developed by and through emotions are called emotional competencies. Emotional competencies deployed in leadership situations determine the success or failure of managers or makes star performers as opposed to average ones.

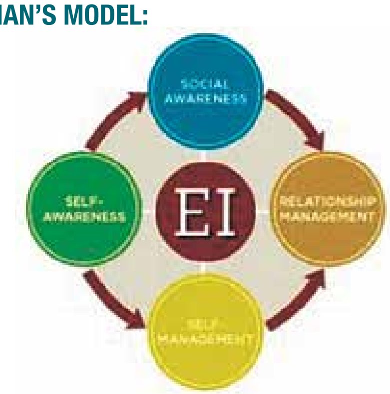
Significance of Emotional Competencies:

Before we go any further and in order to drive home the importance and significance of emotional intelligence, let me quote here some of the research findings to support my argument. It is important to understand that certain critical competencies for success in our lives are derived from this form of intelligence.

- Studies quoted by Daniel Goleman in 1998 lead him to conclude "For all levels of jobs, EI competencies are twice as effective as IQ in determining an individual's success rate. The higher the level of a position in an organisation, the more EI seems to matter. Executive leaders show an 85% correlation between EI competency and success".
- Center for Creative Leadership found that the primary causes of derailment in executives involved deficits in emotional competence which manifest in difficulty in handling change, inability to work in teams and poor interpersonal relations.
- An analysis of over 300 top-level executives from 15 global companies found that 6 emotional competencies distinguished stars from average performers: influence, team building ability, organisational awareness, self-confidence, achievement drive and leadership.
- Daniel Goleman's analysis of 181 jobs in 121 organisations found that emotional competencies were the best differentiators between star performers and typical performers.

Emotional Competencies:

GOLEMAN'S MODEL:



Having discussed the importance of emotions and after having discussed the intelligence to manage them, let me now focus on the competencies that we can develop with emotional intelligence. Daniel Goleman's competency matrix can be captured in the following framework:

With the help of the above framework, let us now take a brief look at the various leadership competencies.

Self Awareness:

- Emotional Self Awareness: Leaders who are high on this dimension are acutely aware of their own mental make-up – how they really feel in a given situation. They are honest and authentic about their own feelings.

- Accurate Self Assessment: Being aware of one's own strengths and weaknesses is a big advantage for a professional in any given situation however grave it might be.
- Realistic Self Confidence: It presupposes that a leader should have self confidence as opposed to over-confidence.

Self Management:

- Self Control: Sometimes called impulse control it is one competency which a Leader cannot do without. Be calm and collected even during an unforeseen crisis.
- Transparency: A leader who does not live by a value system has no hope of heading a successful team.
- Adaptablity: Whether it is leaders or followers, without this virtue there is no hope for them in an ever changing world. Remember, even in the animal kingdom the most adaptable survive the odds than the most powerful.
- Achievement Orientation: Leaders high on this dimension lead their teams even to unchartered territories, but at the same the time not losing focus or control on the environment.
- Initiative and Drive: A leader without a burning desire and drive is a damp squib. He is good enough to lead the team back into history in this dynamic world.
- Optimism: Only an optimistic leader can roll with the punches seeing opportunities or else the entire team would slink away at the first sign of difficulty.

Social Awareness:

- Empathy: This competency makes the leader a people's man. He is able to relate with people better and carry them with him.
- Organisational Awareness: A leader high on this competency dimension would be able to see clearly the cliques and coteries in an organisation, popularly known as organisational politics. This helps him to preempt any political move in the organisation becoming dysfunctional.
- Service Orientation: In an increasingly competitive environment, a leader's ability to relate with his customers assumes considerable significance.

Social Management:

- Inspiration: An ability to inspire people and motivate them is the only effective long lasting weapon a leader has.
- Influence: Leaders are able to ensure buy-in from the employees for their ideas and in the process take them along willingly in any situation.
- Developing Others: Mentoring is a selfless act on the part of the leader and in turn it ensures that his employees work along with him shoulder-to-shoulder.
- Change Catalyst: Leaders make changes happen. They need to have the ability to be a dynamic change agent for the organisation to be vibrant and successful.
- Conflict Management: One of the essential requirements for the leader to be successful is his ability carry everyone and every hue of opinion towards a shared goal.
- Teamwork and Collaboration: Organisations work in teams and leaders have to have the capability to bring in a synergy out of differing views and opinions.

It is possible that some competencies could be present more in a leader than others and that all the above competencies may not be present in equal measure in all the leaders.

Conclusion:

The importance of EI skills in the accounting workplace cannot be over-emphasised. Accountants work both by themselves and in teams. They work in their own professional groups and also as leaders of business entities. A practicing accountant is also called upon to deal with clients, bankers and his or her own staff. His profession is no more isolated from the environment. This in itself justifies the need for the accountant to acquire the necessary leadership competencies. The importance of EI skills in the accounting profession is highlighted by the fact that the American Institute of Certified Public Accountants (AICPA) has identified EI competencies as a critical requirement for accountants. The Institute of Management Accountants (IMA) articulates the issue thus: *"all corporate accountants need good communication and interpersonal skills"*. "Although accounting literature has given little attention to behavioural issues in the past, today many organisations and researchers are recognising that emotional intelligence skills are critical to success" (Akers and Porter 2003). Akers and Porter also reconfirms the fact that a Harvard Business School study of its graduates revealed that little or no significant correlation exists between career success and IQ.

Remember always—emotions drive people and people drive performance. ■

Report on Campus Placement Programme: February-March, 2013

The Committee for Members in Industry (CMII) of ICAI organises Campus Placement Programmes for all levels of Chartered Accountants at frequent intervals throughout the year and is committed to provide world class placement services to the Members and best accounting and finance talents to the industry.

In its endeavor to provide quality Accounting, Finance, Tax, Audit and Management Consultancy personnel to recruiting entities, the Committee has successfully organized one more round of Campus Placement Programme for Newly Qualified Chartered Accountants at thirteen centres viz. Ahmedabad, Bangalore, Bhubaneswar, Chennai, Chandigarh, Coimbatore, Hyderabad, Indore, Jaipur, Kolkata, Mumbai, New Delhi and Pune in February-March, 2013.

Brief summary of the Campus Placement Programme-February-March, 2013 :

Particulars	Campus February-March, 2013
Number of Candidates Registered	7271
Number of Candidates Shortlisted	3597
Number of Interview Teams	116
Number of Organizations	58
Number of Jobs Offered	902*
Number of Jobs Accepted	858
Percentage of Jobs offered vis a vis shortlisted candidates	25.08% approx

Executive Summary

1. Highest salary offered for Domestic posting in the Campus Placement Programme is ₹16.55 lakh Per Annum offered by Bharti Airtel at New Delhi center to 5 candidates.
2. Highest salary offered for International posting in the Campus Placement Programme is ₹21 lakh per annum offered by Alghanim Industries at New Delhi center to 4 candidates.
3. The minimum salary paid by corporate is ₹4.50 lakh per annum and by CA Firm is ₹3 lakh per annum.
4. 902* jobs were offered to the candidates who had participated in Campus Placement Programme.
5. 58 organisations and 116 Interview Teams have participated during the Campus Placement Programme.

Salient Features

1. Candidates were given two chances to meet the recruiting organisations via opting for two centres, first at smaller centres and second (if the candidates has not been selected at smaller centers) at bigger centers.
2. The committee organised Orientation Programme for candidates so as to sharpen their soft skills and to provide them technical updates.

*Status as on 12th April, 2013, 10:00 A.M.

Salary Range

Salary Range (per annum)	Number of Candidates February-March, 2013
₹9,00,000	141
₹7,50,000 ₹8,99,000	136
₹5,00,000 ₹7,49,000	548
₹3,50,000 ₹4,99,000	33$
Total	**858**

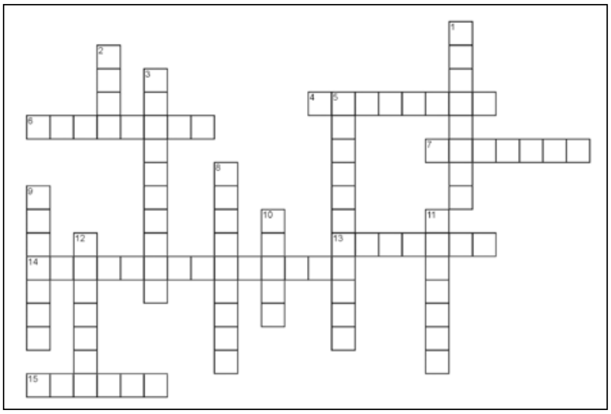
$ A CA Firm has offered the CTC of ₹3 lakh per annum to one candidate.

The following table shows the statistical information of Campus Placement Programme February-March, 2013 at a glance:

S No	Campus interview Centre	Total Number of Candidates registered for Interview	Shortlisted Candidates^	Interview Teams	Jobs Offered	Jobs Accepted
1.	Chennai	603	502	19#	147	145
2.	Kolkata	436	319	10	51	50
3.	Hyderabad	309	114	4	30	29
4.	New Delhi	2707	1470	26	298	293
5.	Mumbai	2227	627	16	101	99
6.	Bangalore	812	505	11	82	65
7.	Pune	948(90+858~)	609	8	102	90
8.	Jaipur	1042(21+1021~)	203	2	21	21
9.	Ahmedabad	828(30+798~)	483	4	32	30
10.	Indore	223(2+221~)	52	2	3	2
11.	Chandigarh	642(10+632~)	35	1	10	10
12.	Bhubaneswar	488(16+472~)	94	2	17	16
13.	Coimbatore	200(8+192~)	97	4	8	8
14.	Rank Holder List					
	Total	**7271**		**116**	**902***	**858**

~ Indicates the total figure of the candidates after merger from the smaller centres.
 # One company has procured database after the Campus Placement Programme.
^ Candidates are shortlisted twice at smaller & bigger centers.

CROSS WORD 083



ACROSS

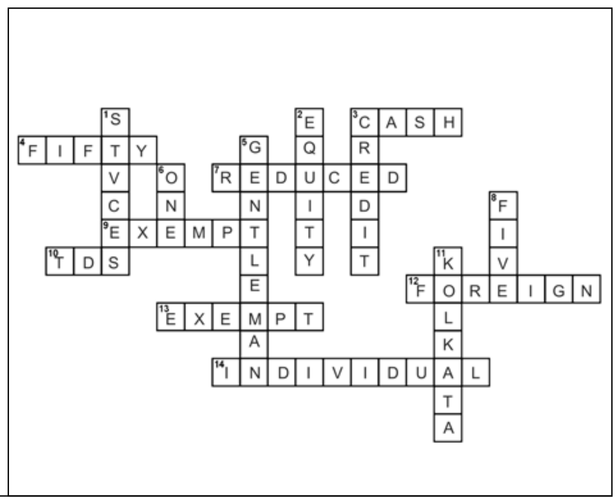
4. The direct materials usage variance and the direct labor efficiency variance are ___________ variances as opposed to price variances.
6. The _____________ rate of return uses discounted cash flows.
7. Manufacturing overhead is commonly referred to as __________ overhead.
13. In the lower of cost or market rule, 'market' means the cost to __________, whether by purchase or production.
14. The government-appointed Financial Sector Legislative Reforms Commission (FSLRC) is headed by Justice __________.
15. The two-way analysis of manufacturing overhead consists of the production volume variance and the flexible-___________ variance.

DOWN

1. The RBI has given a certificate of registration for India _____________Guarantee Corporation, the first mortgage guarantee company to be registered with the regulator.
2. As per Clause 139 of Companies Bill, 2012 there should a Compulsory rotation of individual auditors in every ___________ years and of audit firm in every 10 years.
3. Seeking to encourage Research and Development (R&D) activities in the IT sector, the CBDT has issued circulars to streamline the taxation rules in line with the recommendations of the ____________Committee.
5. A debit to a variance account indicates that the variance is ________________.
8. The name of National Advisory Committee on Accounting Standards has been changed to National Financial ______________Authority.
9. Foreign Corrupt Practices Act, 1977, applies only to ____________of foreign official.
10. High Court exempts hired by AP State Road Transport Corporation (APSRTC) from paying service tax.
11. The depreciation used for tax purposes is relevant because it shelters ____________ income and the resulting outflow of cash.
12. Financial Sector Legislative Reforms Commission (FSLRC) has proposed an Indian Financial Code Bill to enable creation of a __________financial agency while limiting the role of the Reserve Bank of India (RBI) to monetary management.

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 082



Three men: an editor, a photographer, and a journalist are covering a political convention in Miami. They decide to walk up and down the beach during their lunch hour. Halfway up the beach, they stumbled upon a lamp. As they rub the lamp a genie appears and says "Normally I would grant you three wishes, but since there are three of you, I will grant you each one wish."

The photographer went first. "I would like to spend the rest of my life living in a huge house in St. Thomas with no money worries." The genie granted him his wish and sent him on off to St. Thomas.

The journalist went next. "I would like to spend the rest of my life living on a huge yacht cruising the Mediterranean with no money worries." The genie granted him his wish and sent him off to the Mediterranean.

Last, but not least, it was the editor's turn. "And what would your wish be?" asked the genie.

"I want them both back after lunch" replied the editor, "the deadline for tomorrow's newspaper is in about ten hours."