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Annexe to Insurance Building
Near Income Tax,
Ashram Road
Ahmedabad - 380 014.
Phone : 91 79 27544232
Fax : 91 79 27545442
E-mail : caaahmedabad@gmail.com
Website : www.caa-ahm.org



# CONTENTS

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**Shri Chandrakant F. Patel,** on behalf of Chartered Accountants Association, Ahmedabad, Annexe to Insurance Building, Near Income Tax, Ashram Road, Ahmedabad - 380 014.
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## PROFESSIONAL AWARDS

The best articles published in this Journal in the categories of 'Direct Taxes', 'Company Law and Auditing' and 'Allied Laws and Others' will be awarded the Trophies/ Certificates of Appreciation after being vetted by experts in the profession.

Articles and reading literatures are invited from members as well as from other professional colleagues.

## QUOTES FOR THE MONTH

Happiness is when what you think, what you say, and what you do are in harmony.

**Mahatma Gandhi**

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Try not to become a man of success but rather to become a man of value.

**Albert Einstein**

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# EDITORIAL

## COMPLETE THE CIRCLE….

**CA. Darshan Shah**
*Practising since 1985. He can be reached at das_fca@yahoo.co.in*

In the infancy of carrier, when one meets with some initial success (relatively major compared to the professional standing), one tends to believe that anything can be achieved singlehandedly. At that time the striking things in mind generally are lowest cost and enormous returns. One also considers those others who work in groups as unwise and lacking financial acumen! Why to share the fruits when really no help or support is needed! Why to feed too many from one single source!!!! This is insane, is stupid – time will tell.

True, with unique skills and sound knowledge base, the success came faster to you than to others. The success at one place attracts other opportunities. Precisely at this time, you will start feeling shortage of resources – mental, economical, physical. Need for brain storming, dissemination of work will be severely felt and incapability of multi tasking will be realized.

You should not let your own limitations restrict the work or activities of the whole. What people consider to be limitations is simply a lack of ideas. People do not lack ability to do the work, rather they lack ingenuity and creativity. People who are unable to imagine various possibilities will spend their entire active life doing the same activities. People who put limit on themselves will never become more than they think they are. Remember the maxim "You are what you think".

Remaining present at distant places at a time, doing everything at the same time may be possible for Lord Krishna, as narrated in Mahabharat, but not for we crude sobs!

Once the person at the top has reached the limits of individual abilities, the enterprise for which one is working can expand no further and development will grind to a halt. When a person realizes that now on he is incapable of doing everything on his own, he should turn this knowledge into an advantage. He should offer others the opportunity to do more and create an efficient work force. In the business parlance, this is top down system of management. The leader at every lower top is like a president of a small company. So if you really want to succeed in the world, you have to have other people on your side sharing, supporting and helping you.

There is always a place where the path divides and the outcome will depend on whether you can spot an opportunity and devise ingenious methods.

This precisely is the need of the hour – work in a group. Group of like minded people having expertise on different facets of the profession you are in. Once you learn to work in a group, the shortcomings of working individually as narrated in earlier paragraphs will soon prove to be wishful thinking.

On one side, the developments around also compel you to form groups and work together. At present, many businesses are covered under compulsory audit requirements viz. Cost Audit, Tax Audit, Company Audit, VAT Audit, Bank Branch Tax Audits. Once all these are to be carried out only by Chartered Accountants, the work load in CA's offices will be enormous. It may be very difficult for individual practitioner to satisfy a client on all counts. So the natural solution will be to work in a group.

On the other side, take the example of Bank Branch Audits – as the grapevine goes, proprietor firms and firms with two partners will not be selected to carry out such audits. In order to be eligible for such assignments, one will have to be part of a larger group.

Or consider the new avenues likely to be opened like compulsory Service Tax Audits by Chartered Accountants only, Bank Branch Tax audits (in absence of Bank Branch Audit), VAT Audits handed over to CAs (not a distant possibility). These will open flood gates of opportunities. If one is comfortably placed in a group of one's own choice, the opportunities will be best exploited collectively.

As we all know, working in group and offering varied professional services from one platform will satisfy the service seekers who want all services available from under one roof / banner. These seekers consider such feature as time saving and information protective.

Therefore, make a complete circle instead of scattered dots, how big the single dot may be.

**CA DARSHAN SHAH**

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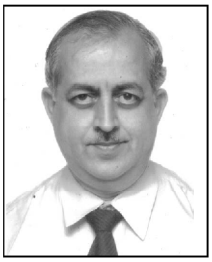
# PRESIDENT'S MESSAGE



**CA. Chandrakant H. Pamnani**
*He can be reached at*
*chpamnani@gmail.com*

**Dear Friends,**

February is the month where the profession is waiting and gearing up for the Union Budget. The elections in five states this year have delayed the presentation of Union Budget to the month of March instead of February. The wait for the debates and discussion on the outcome of Budget will be little bit longer this time.

It is said that in a nation of various states divergent in social and economic structure, the route to Central Government passes through the state of Uttar Pradesh. No national political party can ever take stake at the centre ignoring the electoral mandate of Uttar Pradesh. Now when the state is going for polls for assembly elections with all major political parties in action, two young leaders have been centre of attraction of the media. It is a matter of time when we would learn that a young leader of a national party steals the show or would there be again an emergence of third front led by a young regional party leader from Uttar Pradesh after the election results are out.

Last month the judgment on Vodafone was a matter of hot debate among the fraternity. In fact the decision from the Honourable Supreme Court was welcomed by all the tax practising professionals and more so by the foreign investors because it laid down that Capital Gain Tax on foreign deals do not apply and tax authorities have no jurisdiction in such matter. However it is believed that judgment on Vodafone case will have a short life as Direct Tax Code has specific provisions to tax such transactions. It may also prompt the Government to amend the Income Tax Act, 1961 incorporating the said provisions of DTC in this budget itself, considering the delay in implementing the DTC.

The Indian Cricket team has shown a miserable performance down under. The poor show of the test matches have continued in the One-Day Tri series as well. But as far as the cricket of the Association is concerned it achieved great laurel in the match with Baroda Branch of WIRC last month. The Association won the match by thumping margin and it was first time in the history of Association's cricket that an unbeaten century was scored in a twenty over match by CA Abhishek Jain. Kudos for CA Abhishek and the entire cricket team of the Associaiton.

With regards,

**CA. C.H. Pamnani**
**President**

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ARTICLE...

# FORENSIC ACCOUNTING

**CA. Aditya Gupta**
*The author is practising Chartered Accountant He can be reached at adityagupta003@gmail.com*

Forensic Accounting is an integration of accounting, auditing and investigative skills. The term 'forensic accounting' was coined by Maurice E.Peloubet, in whose words "financial statements have some but not all the characteristics of Forensic Accounting." According to oxford dictionary, the term forensic mean- of or used in 'law court'. Thus, Forensic accounting as a special practice area provides accounting analysis that is suitable to the court and which form the basis for discussion, debate and ultimately dispute resolution. Forensic accounting looks beyond numbers and the focus is on looking at the business reality of the situation.

Companies (Auditor report) order, 2003 requires auditors to report, amongst others, "whether any fraud on or by the company has been noticed or reported during the year. If yes, the nature and amount are required to be indicated." Thus, in the Indian context, forensic accounting has gained importance in this background.

## ☞ AREAS COVERED BY FORENSIC ACCOUNTING:

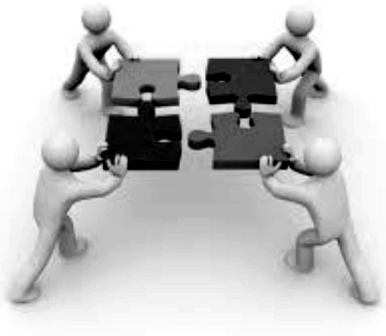

1. Certain engagement related to civil disputes viz. disagreements related to company acquisitions like business valuation, calculating and quantifying losses and economic damages through breach contracts etc.
2. Shareholders and partnership disputes involving detailed analysis of numerous years accounting records to quantify the issues in dispute.
3. Cyber crimes like credit card frauds, ATM card frauds, cyber extortion, cyber stalking, phishing i.e. sending unsolicited e-mails & collection of sensitive information by simple techniques.
4. Forensic accounting also deals with areas of professional negligence claims, involving assessment and reporting on work of other professionals. This involves investigating whether breach of 'generally agreed accounting and/or auditing principles' has occurred.
5. Engagement involving criminal matters, involving assessment of accounting systems and accounts presentation, where forensic accountants are hired by the law enforcement agencies.
6. Business investigations involving fund tracing, asset identifications and recovery, forensic intelligence gathering and due diligence reviews.
7. Employee fraud investigations involving procedures to determine existence, nature and extent of fraud and may involve identification of the clauses etc
8. Business Economic losses viz. contract disputes trademark and patent infringements, losses arising from breach of non-compete clauses etc.
9. Cases involving medical insurance claims, medical malpractices resulting in economic losses.
10. Mediation arbitration in alternative dispute resolution mechanisms due to familiarity of forensic accountants with legal issues and procedures, helping individuals and businesses resolve disputes with minimum disruption and loss of time.

## ☞ TERMINOLOGIES USED PERTAINING TO FORENSIC ACCOUNTING:

1. **Forensic investigation:** This refers to using specialized investigative skills to undertake inquiry in such a manner that outcome shall have application in court of law. Forensic investigation may be grounded in areas like accounting, medicine or engineering.

2. **Forensic Audit:** This refers to investigation of a fraud or presumptive fraud with a view to gathering evidence that could be presented in courts of law. It is essentially a blend of propriety, investigative, regularity and financial audits. The Objective is to ascertain whether true business value has been reflected in the financial statement and during the course of examination to find whether any fraud has taken place.

## ☞ WHAT DOES A FORENSIC ACCOUNTANT DO?:



A Forensic Accountant is often retained to analyze, interpret, summarize and present complex financial and business related issues in a manner which is both understandable and properly supported.

Forensic Accountants can be engaged in public practice or employed by insurance companies, banks, police forces, government agencies and other organizations.

A Forensic Accountant is often involved in the following:

- Investigating and analyzing financial evidence;
- Developing computerized applications to assist in the analysis and presentation of financial evidence;
- Communicating their findings in the form of reports, exhibits and collections of documents; and
- Assisting in legal proceedings, including testifying in court as an expert witness and preparing visual aids to support trial evidence.

In order to properly perform these services a Forensic Accountant must be familiar with legal concepts and procedures. In addition, a Forensic Accountant must be able to identify substance over form when dealing with an issue.

## ☞ DETECTION TECHNIQUES USED IN FORENSIC ACCOUNTING:

**A. Critical Point Auditing (CPA):** In CPA, symptoms of fraud are filtered out from regular transactions where they may be concealed. Scrutiny for CPA purpose may involve use of:

1. Trend analysis
2. Checking unusual debits/credits in the accounts
3. Discrepancies in receivable /payable / inventory balances evidenced from financial records corresponding subsidiary records.
4. False credits to boost sales with corresponding debits to non-existent/dummy personal accounts.

## ☞ CRITICAL ASPECTS TO BE FOLLOWED WHILE CONDUCTING FORENSIC ACCOUNTING:

1. The objective of forensic accounting is to determine correctness of accounts and whether any fraud has taken place.
2. Some of the techniques used could be analysis of past trends or 'substantive' or in depth checking of selected transactions.
3. There is no limitation of time period unlike statutory audits and thus accounts may be examined in details from very beginning.
4. In case of, verification of stock, realizable value of current assets and provisions or liability estimation etc. Independent verification of selected / suspected items may be carried out.
5. In case of off-balance sheet items like contracts, regularity and propriety of these transactions are examined.
6. In case of adverse findings, legal determination of fraud and naming persons behind the fraud is contemplated.

## ☞ FORENSIC ACCOUNTANT'S ROLE:

Forensic accountants utilize an understanding of business information, financial reporting systems, accounting and auditing standards, evidence gathering and investigate techniques, Litigation procedures and processes to perform their work. They also play a pro-active role in risk reduction by designing and performing extended procedures as part of statutory audit, acting advisor to audit committee, fraud deterrence engagements and assisting in investment analysis research.

They may play a coherent role against money laundering activities which may involve recovering proceeds of crime. In UK, the relevant legislation for the same is contained in proceeds of Crime Act, 2002.

### B. Propriety Audit (PA):


1. PA is conducting by supreme audit government accounts prepared are in order , in terms of approvals and sanctions of expenditures incurred, whether the expenditure incurred was need-based and that the revenues have been realized in time and properly credited to government accounts.
2. The analogy of "value for money audit" is applied to forensic audits whereby financials frauds are unearthed saving wasteful and unwarranted expenditures.

## ☞ CHARACTERISTICS A FORENSIC ACCOUNTANT SHOULD POSSESS:

1. Forensic accounting requires specialized knowledge about techniques of finding out the frauds: the forensic accountants must have patience and an analytical mindset.
2. Ability to think where he questions seemingly benign documents, looks for inconsistencies, searches for evidence of criminal conduct, looks beyond the number and grasps the substance of the situation.
3. Some other characteristics which could aid a forensic accountant could be:
   a. Curiosity
   b. Persistence
   c. Creativity
   d. Confidence
   e. Sound Professional judgement.

4. Good Communication skills including effective listening, considering various alternatives open and ability to see the large picture are other attributes that could be useful to the forensic accountant.

☞ **How can a Forensic Accountant be of assistance:**

A Forensic Accountant can be of assistance in various ways, including:

~ ***Investigative Accounting***

- Review of the factual situation and provision of suggestions regarding possible courses of action.
- Assistance with the protection and recovery of assets.
- Co-ordination of other experts, including:
  - o Private investigators;
  - o Forensic document examiners;
  - o Consulting engineers.
- Assistance with the recovery of assets by way of civil action or criminal prosecution.

~ ***Litigation Support***

- Assistance in obtaining documentation necessary to support or refute a claim.
- Review of the relevant documentation to form an initial assessment of the case and identify areas of loss.
- Assistance with Examination for Discovery including the formulation of questions to be asked regarding the financial evidence.
- Attendance at the Examination for Discovery to review the testimony, assist with understanding the financial issues and to formulate additional questions to be asked.
- Review of the opposing expert's damages report and reporting on both the strengths and weaknesses of the positions taken.
- Assistance with settlement discussions and negotiations.
- Attendance at trial to hear the testimony of the opposing expert and to provide assistance with cross-examination.

☞ **FORENSIC ACCOUNTING OPPORTUNITIES:**


Forensic accounting as such is centuries old since KAUTILYA the famous economist, recognized the need for forensic accountants, when he mentioned forty different ways of embezzlement. SHERLOCK HOLMES was perhaps the most famous practicing forensic chemist.

Growing Cyber Crimes, Failure of Regulatory agencies to track security scams, busting of many co-operative banks and collapse of Giant Corporation like Enron emphasize the need of using forensic accounting or chartered Accountants in India, forensic accounting provides an exciting opportunity to foray into this field. Growing regulatory and compliance procedures shall demand greater services in the nature of forensic accounting practice. According to 'Accounting Today' nearly 40% of top 100 American accounting firms are expanding their forensic and fraud service. With Indian corporate now turning global, with higher volume of cross-border transactions, use of hi-tech technology leaving little audit trail, use of forensic accounting in India is likely to catch pace.

☞ **Conclusion:**

Forensic accounting though a new field in Indian accounting world has tremendous potential as a new practice area for Indian CAs given the increasing use of e-commerce application, cyber frauds and increasingly complex transaction in both domestic as well as cross-border businesses. Indian CAs with their extensive theoretical education and practical experience can create forensic accounting and auditing as their niche area.

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# ARTICLE...

**Accounts of a company which has been audited and have been adopted by the members are sacrosanct i.e. binding on the Assessing Officer?**

**CA. Kaushik D. Shah**
*The author is the past President of CAA, practising since 1976. He can be reached at dshahco@gmail.com.*

Let me first refer to the provisions regarding Tax on Book Profit

***SECTION 115JB : MINIMUM ALTERNATE TAX***

| Section | Applicability for which assessment year | When these provisions are applicable | Consequences |
|---|---|---|---|
| 115JA | 1997-98 to 2000-01 | If income of a company under normal provisions is lower than 30% of "Book Profit" | 30% of "Book Profit" shall be deemed as total income of the company. |
| 115JB | 2001-02 onwards | If tax liability of a company under normal provisions is lower than 18% of "Book Profit" | "Book Profit" shall be deemed as total income and 18% of the book profit should be deemed as tax liability |

How will the Book Profit be determined: The net profit as per the profit and loss account (***after 15 adjustments)*** is the book profit.

The 15 adjustments in brief are as follows:

***Amount to be added back if debited to profit and loss account:***

1. Income-tax paid or payable and the provisions therefor.
2. Amounts carried to any reserves, by whatever name called.
3. Amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities.
4. Amount by way of provision for losses of subsidiary companies.
5. Amount or amounts of dividends paid or proposed.
6. Amount of expenditure relatable to any exempt income (if such income is not subject to MAT).
7. Amount of Depreciation**.
8. Amount of deferred tax and the provisions therefor and the amount or amounts set aside as provision of diminution in the value of any asset.

***Amount to be deducted from net profit:***

9. Amount withdrawn from reserves or provisions, if any such amount is credited to the profit and loss account.
10. Income exempt from tax.
11. Depreciation debited to profit and loss account.**
12. Amount withdrawn from revaluation reserve credited to profit and loss account to the extent

it does not exceed the amount of depreciation on account of revaluation of assets.

13. Amount of loss brought forward or unabsorbed depreciation, whichever is less, as per books of account.

14. Profit of sick industrial unit.

15. The amount of deferred tax, if any such amount is credited to the profit and loss account.

****Depreciation** debited to profit and loss account shall be added back. However, depreciation (not being depreciation which arises because of revaluation of assets) shall be deducted as given in point no (11) above.

Every assessee, being a company, shall for the purposes of this section prepare its Profit and Loss Account for the relevant previous year in accordance with the provisions of Parts II and III of Schedule VI to the Companies Act, 1956 (1 of 1956)

**Provided** that while preparing the annual accounts including profit and loss account

(i) The accounting policies;

(ii) The accounting standards adopted for preparing such accounts including profit and loss account;

(iii) The method and rates adopted for calculating the depreciation

shall be the same as have been adopted for the purpose of preparing such accounts including profit and loss account and laid before the company at its annual general meeting in accordance with the provisions of section 210 of the Companies Act 1956.

**Provided Further** that where the company has adopted or adopts the financial year under the Companies Act 1956 (1 of 1956), which is different from the previous year under this act:-

(i) The accounting policies;

(ii) The accounting standards adopted for preparing such accounts including profit and loss account;

(iii) The method and rates adopted for calculating the depreciation,

shall correspond to the accounting policies, accounting standards and the method and rates for calculating the depreciation which have been adopted for preparing such accounts including profit and loss account for such financial year or part of financial year falling within the relevant previous year.

The question arises whether the accounts of a company which has been audited and have been adopted by the members are sacrosanct i.e. binding on the A.O.

**Only in the following 2 cases, the A.O. can rewrite the profit and loss account –**

- ***If the profit and loss account is not prepared according to the Companies Act :*** If it is discovered that the profit and loss account is not drawn up in accordance with the provisions of Parts II and III of the VIth schedule to the Companies Act.

- ***If accounting policies, accounting standards or rates or method of depreciation are different:***

  According to the first proviso to section 115JB(2), the accounting policies, accounting standards adopted for preparing such accounts, the method and rates of depreciation which have been adopted for preparation of the profit and loss account laid before the annual general meeting should be followed while preparing profit and loss account for the purpose of computing book profit under section 115JB

  Now, many companies prepare two sets of accounts one first under the Companies Act and

the second under the Income Tax Act. Due to such practice, different accounting policies/ standards and method or rate of depreciation are adopted and therefore higher profits are reported to the shareholders while lower profits are disclosed to tax authorities.

Due to the above reason i.e if the accounting policies/standards and the rate or method of depreciation are not the same then it is kept open for the A.O to recalculate net profit as is reported to the shareholders.

Let me refer to the case of **Dynamic Orthopedics P. LTD v. Commissioner of Income Tax 321 ITR 300 (SC)**

The appellant assessee in the P&L account had provided depreciation at the rates specified in rule 5 of the Income Tax Rules 1962. While completing the assessment of income, the A.O. recomputed the book profit for the purpose of section 115J of the Income Tax Act,1961 after allowing depreciation as per schedule XIV to the Company's Act.

It was held that the whole purpose of section 115J of the Act , therefore was to take care of the phenomenon of prosperous "zero tax" companies not paying taxes though they continued to earn profits and declare dividends. Therefore a minimum alternate tax was sought to be imposed on "zero tax" companies. Section 115J of the Act imposes tax on a deemed income. Section 115J of the Act is a special provision relating only to certain companies . The said section does not make any distinction between public and private limited companies. Only Parts II and III of Schedule VI to the 1956 Act have been incorporated legislatively into section 115J of the Act. Therefore the applicability of Parts II and III of Schedule VI to the 1956 Act does not arise. If a company is a MAT company, then be it a private limited company or a public limited company, for the purpose of section 115J of the Act, the assessee company has to prepare its profit and loss account in accordance with Parts II and III of Schedule VI of 1956 Act alone.

Plain reading of the decision of Dynamic Orthopedics P. LTD cited supra is that when section 115J refers to preparation of profit and loss account in accordance with the provision of Part II and III of Schedule VI to the Companies Act 1956, the depreciation has to be provided as per Schedule XIV of the Companies Act 1956, and the depreciation cannot be provided as per the rates prescribed in Rule V of the I.T. Rules i.e. tax depreciation. And hence, the A.O. has the right to recompute the book profit even though the profit and loss account is certified by the auditor and adopted by the members in AGM.

Therefore question as to whether depreciation is to be claimed as per Income Tax Rules,1962, for purposes of computing book profit under section 115J or as per Schedule XIV to Companies Act, is to be referred to Larger Bench. Also, despite the provisions contained in section 355 of the Companies Act, the computation of depreciation in the case of private companies must also be made on the basis of Schedule VI to the Companies Act and not as per provisions of the Income Tax Act.

As held in the case of ***CIT vs. Kovai Maruthi Paper & Board (P.) Ltd [2008] 168 Taxman 299 (Mad.),*** once the profit and loss prepared by the assessee is certified by authorities under Companies Act as having being properly maintained in accordance with Companies Act, Assessing Officer has limited power of making increase and reductions as provided for in Explanation *to section 115J*

In case of ***Gearhart India Ltd v. CIT 65 TTJ 345*****,** where the court held that when the account suffers defects i.e. when the accounts do not disclose true and fair state of affairs, the A.O. can recompute the book profit.

It is submitted that while determining the book profit under section 115JB of the Act, the A.O. does not have the jurisdiction to go behind the Net Profit shown in the profit and loss account except to the extent provided in the explanation. Therefore the A.O. cannot

recompute the book profit as shown In the profit and loss account.

It was provided in the case of ***CIT vs. Avery Cycle Industries [2004] 89 ITD 497 (Chd.)*** that for the purpose of computing book profits no adjustment can be made by way of reduction of interest on borrowed capital, which is not debited in profit and loss account.

It is submitted that as per section 115JB the companies are required to pay "Minimum Alternate Tax" on the book profit subject to certain adjustments provided in the explanation to the said section.

In the case of **Apollo Tyres LTD v. Commissioner of Income Tax 255 ITR 273 and Malyalam Manorama vs. CIT [2008] 169 Taxman 471 (SC),**it was held that the use of words 'in accordance with the provisions of parts II and III of schedule VI to the Companies Act' was made for the limited purpose of empowering the assessing authority to rely upon the authentic statement of accounts of the company. While so looking into the accounts of the company, an Assessing Officer under the Income-Tax Act has to accept the authenticity of the accounts with reference to the provisions of the Companies Act which obligates the company to maintain its accounts in a manner provided by the Companies Act and the same to be scrutinized and certified by the statutory auditors and will have to be approved by the company in its general meeting and thereafter to be filed before the Registrar of Companies who has a statutory obligation also to examine and satisfy that the accounts of the company are maintained in accordance with the requirements of the Companies Act

It was held in the case of **Malyalam Manorama vs. CIT [2008] 169 Taxman 471 (SC)** that the short question that arises for consideration in this tax appeal is whether it is open to the A.O. to make adjustment to the book profits beyond what is authorized by the definition given in Explanation to section 115J of the Income Tax Act, if the accounts are prepared and certified to be in accordance with Parts II and III of Schedule VI to the Companies Act, 1956. In the case of Apollo Tyres Ltd. [2002] 255 ITR 273, the apex court held that while computing the income under section 115J of the Income Tax Act, the A.O. has only power to examine, whether the book of account were certified by authorities under the Companies Act as having been properly maintained in accordance with the Companies Act".

## ***CONCLUSION***

It is submitted that as per section 115JB the companies are required to pay Minimum Alternate Tax on the book profit subject to certain adjustments provided in the explanation to the said section. However, there is no scope for recomputation of the book profit beyond the explanation provided in the section. However, if a view is taken that the A.O. has power to adjust the book profit then the sanctity of the audit of accounts and approval and adoption of accounts become meaningless. However, if the accounts of the company are certified as not disclosing true and fair state of affairs, then it appears that the A.O. has the powers to recompute the book profit. However, when accounts are certified by the auditor, approved by the directors, adopted by the members in AGM, and no defects are pointed out and the same have been filed with the registrar of companies, such accounts are binding to the A.O. for the purpose of computing book profit u/s 115JB of the I.T Act, 1961.

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An investment in knowledge always pays the best interest.

**Benjamin Franklin**

# ARTICLE...

## NATURE OF INCOME ARISING FROM SHARE TRANSACTIONS-A TING TONG BATTLE - BUSINESS INCOME V/S CAPITAL GAIN (CONTD. FROM PAGE 464 OF DECEMBER, 2011 - JANUARY, 2012 ISSUE)

**CA. Jignesh Parikh**
*The author is practising Chartered Accountant. He can be reached at jigneshpparikh@gmail.com*

**3** ***ACIT vs. Bulls & Bears Portfolios Ltd. (2011) 137 TTJ 741***

Assessee is a broker as well as investor. It has maintained the investment portfolio separately income of which was liable to be taxed as capital gains, as intention in respect of this was to hold the investment as investment only and shown as such in the books of accounts. Income thereon was shown and treated as capital gains in successive assessments. Income to be assessed as capital gains.

**4** ***Shantilal M. Jain vs. ACIT (Mum.) (Trib.) (Unreported)***

Though in case of transaction of large volumes, magnitude, frequency, continuity, regularity, the ratio between purchase & sale of shares are treated as income from business, but in certain circumstances, income from such transactions is treated as STCG as a reason of Rule of consistency propounded by Bombay High Court in Gopal Purohit 228 CTR 582 (Bom.), which is squarely applicable

**5** ***CIT v Naishadh V. Vachharajani (Bombay High Court). (Unreported)***

The Tribunal recorded the finding that in a number of cases the assessee had held the LTCG shares for more than 10 years and that the purchase and sale of shares within a period of one year had been offered as STCG. In the preceding AY, the AO accepted this. As per Gopal Purohit 228 ITR 582 (Bom) (SLP Dismissed) it is open to an assessee to trade in the shares and also to invest in shares. When shares are held as investment, the income arising on sale of those shares is assessable as LTCG/STCG. Accordingly, the decision of the Tribunal in holding that the income arising on sale of shares held as investment were liable to be assessed as LTCG/STCG cannot be faulted

**6** ***Jayshree Pradip Shah vs. ACIT (2011) 51 DTR 344 / 131 ITD 326 (Mum.)(Trib.)***

Where the assessee had carried out about 800 transactions in shares of more than 200 listed companies with borrowed funds and the purchases and sale of shares was the only activity of the assessee with a very short holdings period, and substantial time was devoted for such activity, in a regular and systematic manner, the profit from such transactions was rightly treated as business profit as against short-term capital gains claimed by the assessee.(A. Y. 2004-05)

**7** **Spectra Shares & Scrips ( P) Ltd v Dy CIT ( 2011) 62 DTR 411 ( Hyd) (Trib).**

Assessee carried on the activity of buying and selling shares and units of mutual funds in a systematic and regular manner with high frequency and volumes and repetitive purchases and sales of the same scrip throughout the year , the Tribunal held it has to be assesses as business income and the revision order under section 263 directing the A.O. to be assess the same as business income was held to be justified

**8** ***CIT vs. Rohit Anand (2010) 46 DTR 236 (Delhi)***

Assessee carrying on jewellery business invested in shares and treated shares as investment in the books. The Tribunal on the basis of facts found that the investment is out of own fund and not borrowed fund, that investment is not rotated frequently, that the total number of transactions

are very few, that all the shares purchased are not sold and rather held for quite number of days, held that the transactions are to be treated as giving rise to the capital gain and cannot be held as trading in shares. High Court in appeal confirmed the decision of Tribunal.

**How the PMS Transactions be taxed ?**

Investment in the Portfolio Management Scheme is made with the intention of ' Wealth Maximization' and not with the intention of 'Profit Maximization' and hence income arising from the same should be taxed as Capital Gain. This view gets support from below mentioned case laws.

The Mumbai Tribunal in an occasion to decide held as follows in the case of ***ITO vs. Radha Birju Patel (Mum.)(Trib.)***

Transactions carried out via PMS are in nature of transactions meant for Wealth maximization & not encashing profits on appreciation in value of shares. In case where assessee is engaged in systematic activity of holding of portfolio through PMS manager, it cannot be said that main object of holding the portfolio is to make profit by sale of shares. The high number of transactions are misleading as these are computer split transactions and not independent transactions. Hence, gains arising out of PMS transaction has to be assessed as Capital Gain and not business income

Even the Pune Tribunal in the case of **ARA Trading & Investment Pvt. Ltd. vs DCIT (2011) 47 SOT 172(Pune)** held that

(i) Given the definitions of the term "business" and "capital asset" in s. 2(13) & 2(14), shares, if held for more than 12 months, will be a long-term capital asset, inspite of continued and systematic dealings; (ii) On facts, as the assessee had engaged a portfolio manager to look after its' investments and all decisions to buy and sell were taken by the portfolio manager and not by the asessee, the assessee cannot be called a "dealer"; (iii) The object of the PMS was to maximize the value of the portfolio. It was "wealth maximization" and not "profit maximization"; (iv) In the balance sheet, the shares were valued at cost and not at lower of cost or market value;

**Whether Share / PMS Fees paid to Portfolio is allowable as Deduction in computing PMS Capital Gain?**

In the recent judgment, the above issue was positively answered by **KRA Holding & Trading P. Ltd. v DCIT (2011) 46 SOT 19 Mumbai** Tribunal following the judgment of its jurisdictional High Court in case of CIT v Shakuntala Kantilal (1991) In this case the tribunal held that

In computing capital gains u/s 48, payments are deductible in two ways, one by taking full value of consideration net of such payments and the other by deducting the same as "expenditure incurred wholly and exclusively in connection with the transfer". The expression "full value of consideration" contemplates additions and deductions from the apparent value. It means the "real and effective consideration", which can be arrived at only after allowing the deductible expenditure. The PMS fee, on profit sharing basis, was for the twin purposes of acquisition and sale of the securities. The fact that bifurcation between the two is not possible is not relevant. Accounting Standard 13 (Accounting for Investments) issued by ICAI provides that brokerage, fees and duties have to be added to the cost of investments

**Can gain on sale of Shares held for a period of less than 30 Days be treated as Business Income?**

Our own Ahmedabad Tribunal in the case of **Sugamchand C Shah vs ACIT (2010) 37 DTR (Ahd)(Trib) 345** has held that

In respect of gain on sale of shares held for more than 365 days, when in the past the department has accepted the sale of shares holdings of more than a year as investment and profits thereon has been assessed under the head "capital gains" the gain should be assessed as long term capital gains. In respect of other shares with frequent transactions where shares are held for more than a month they should be treated as investment and assessable as short term capital gains. Where the shares are held less than a month the same may be treated as profit from business.

Even the Honourable **Jaipur Tribunal in the case of Asst CIT v Kavita Devi Agarwal ( 2011) 48 SOT 191 (Jaipur) (Trib)** has taken the same view.

With due respect to Honourable Ahmedabad and Jaipur Tribunal this judgment is not appropriate on below mentioned grounds

1. Once it is established that the intention of the assessee is not to trade in the shares but to invest in the shares, shares become the capital asset and income arising on transfer of the same should be taxed as in the chapter of Capital Gain only. Subdivision of Capital Gain in to Business Income is not justified.
2. A true investor will always keep a close watch on the market and take a decision to switch over or otherwise as soon as he discovers an opportunity in order to maximize the gains.
3. When the law itself provides that gain arising on sale of share held for a period of less than 12 months to be a Short Term Capital Gain as against 36 Months in other cases, the intention as to what will be considered as Short Term and Long term is quite clear and no court or tribunal has any authority to disturb or challenge the same.

The above referred arguments are also supported by below mentioned case laws.

| Sr No | Case Law | Conclusion |
|---|---|---|
| 1 | Hitesh Satishchandra Doshi vs JCIT (ITAT Mumbai) | On facts, even the gains on shares held for 30 days and less had to be assessed as STCG and not business profits because:<br>(a) There cannot be a sub-division of transaction relating to STCG. The transactions cannot be bifurcated on the basis of holding period of 30 days so as to classify a part of the gain as STCG and a part as business profit;<br>(b) The assessee had separate portfolios for investment and trading and in the books, the shares giving rise to the STCG had been treated as an "investment" and not as "stock-in-trade". The shares were valued at cost and not at lesser of market value;<br>(c) In view of the consistent treatment of the assessee, it is established that the intention of the assessee at the time of acquiring the shares was for investment and not for trading;<br>(d) The assessee had used own funds and not borrowed funds to acquire the shares;<br>(e) As regards the frequency of purchase and sale of shares, transactions through the electronic system of Stock Exchange split a single order into numerous transactions. This gives an unrealistic figure of the number of transactions;<br>(f) The fact that the gains from shares held for less than 30 days was Rs. 15.19 lakhs as compared to the gains of Rs. 37.76 lakhs on shares held for more than 30 days shows the assessee's intention to hold the shares for a longer period and to earn income of appreciation of the value of the |

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|---|---|---|
| | | shares and not earn the profit in the short period change in the price of the shares;<br>(g) The assessee was regularly earning dividend income;<br>(h) It is acceptable for an investor to reshuffle his portfolio in a short period in order to reduce the risk of loss of capital or income; |
| 2 | Dy. CIT vs. SMK Shares & Stock Broking (ITAT Mumbai) | While volume of transactions is an important indicator of the intention of the assessee whether to deal in shares as trading asset or to hold the shares as investor, it is certainly not the sole criterion. The Assessing Officer's conclusion that since sale and purchase had been determined by the volatility in the market, the same is against the basic feature of investor is not based on sound rational reasoning. A prudent investor always keeps a watch on the market trends and, therefore, is not barred under law from liquidating his investments in shares. The law itself has recognized this fact by taxing these transactions under the head "Short Term Capital Gains". If the Assessing Officer's reasoning is accepted, then it would be against the legislative intent itself; Some part of the STCG had arisen out the earlier investment which had been accepted as being on investment account. As the modus operandi of the assessee remained the same in regard to other shares purchased during the year, the assessee's claim could not be negated only on the basis of frequency of the transaction |

## CONCLUSION

The above referred rulings, though not conclusive but give clear hint that judgment is given by the tribunals and high courts by paying importance to INTENTION OF ASSESSEE which is judged based on the ACCOUNTING TREATMENT IN THE FINANCIAL STATEMENTS. Though some concrete tests are required to be installed either by amendment or otherwise but meanwhile one must take care of following points to take advantage of above referred judgments.

Steps to be applied to take the benefit of above referred judgment

1. So far as possible there should be two demat accounts.
2. In one demat account the assesse can carry out the transactions income of which will be offered as Capital Gain and the income of Second Demat Account should be offered as Business Income. This Demat account will be used to carry our intra day , future and options etc.
3. Books of Account must be Maintained.
4. Shares held in Demat Account, should be classified as Investment in Financial Statement.
5. In view of Contrary decisions as regards nature of income of shares held for less than 30 days, one should take a practical call keeping in mind litigation cost and other relevant factors.

**Source of Information Information available from Internet.**

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# GLIMPSES OF SUPREME COURT RULINGS

**Advocate Samir N. Divatia**
*The author is practising advocate since 1974. He can be reached at sndivatia@yahoo.com.*

## 22 TORT LAW-NEGLIGENCE :

A person may be responsible for an act, yet he may not be negligent. The negligence is a factual issue and can only be established through cogent evidence. Illustratively, a child who suddenly runs on to a road may be responsible for an accident, but was the child negligent? The answer to this question would emerge by unraveling the factual position. The person in whose care the child was, at the relevant juncture would be negligent in such eventuality.

It has to be decided whether a claim made u/s 163A of Motor Vehicles Act, is a claim under the "fault" liability principle or under the "no-fault" liability principle. The claimant in order to establish his right to claim compensation under a particular provision has to establish that the same does not arise out of "wrongful act" or "negligence" or "default", the said provision will be deemed to fall under the "fault" liability.

***[National Insurance Co. Ltd v. Sinitha (2012) 2 SCC 356 ]***

## 23 CENTRAL EXCISE- MANUFACTURE :

The test to determine whether a thing comes within ambit of "manufacture" : the process of manufacture has to be: (a) statutorily recognized or (b) result in transformation of raw materials into a new and different article or thing having a different identity, characteristics and use. The mere improvement in quality does not amount to manufacture. It is only when change or a series of changes take commodity to a point where commercially it can no longer be regarded as the original commodity but is instead recognized as a new and distinct article that manufacture can be said to have taken place.

***[CCE v. Osnar Chemical Pvt. Ltd (2012) (2 ECC 282) ]***

## 24 PENALTY UNDER R. 173Q OF CENTRAL EXCISE RULES :

The issue involved interpretational nature and Commr. himself found it difficult to hold that assessee knowingly cleared excisable goods without payment of duty. No penalty can be levied.

***Uniflex Cables Ltd v. CCE ( 2011) (271 ELT 161)***

## 25 TAX AVOIDANCE- TAX PLANNING – SEC.9(1)(i) :

If one scans through the various case laws of the House of Lords in England, one thing is clear that it has been a cornerstone of law that a taxpayer is enabled to arrange the affairs so as to reduce the liability of tax and the fact that the motive for a transaction is to avoid tax does not invalidate it unless a particular enactment so provides. If the arrangement is to be effective, it is essential that the transaction has some economic or commercial substance. Revenue cannot tax a subject without a statute to support and every taxpayer is entitled to arrange the affairs so that taxes shall be as low as possible.

Provision of 'look through' is to be expressly provided for in the statute or in the treaty – This clause cannot be read into the section by interpretation – Sec.9(1)(i) is not a 'look through' provision.

A legal fiction has a limited scope. A legal fiction cannot be expanded by giving purposive interpretation particularly if the result of such interpretation is to transform the concept of chargeability.

In the application of a judicial anti-avoidance rule, the Revenue may invoke the 'substance over form' principle or 'piercing the corporate veil' test only after it is able to establish on the basis of the facts and circumstances surrounding the transaction that the impugned transaction is a sham or tax avoidant; while ascertaining the legal nature of the transaction, the

Revenue / Court has to look at the entire transaction as a whole and not to adopt a dissecting approach .

***[Vodafone International Holdings B. V. Vs. Union of India & Anr. (66 DTR 265) ]***

## 26 ELECTRICITY – UNAUTHORISED USE – RULES OF PRACTICAL INTERPRETATION

Section 135 of the Electricity Act, 2003 deals with an offenceoftheftofelectricityandthepenaltythatcan be imposed for such theft. This squarely falls within the dimension of criminal jurisprudence and mens rea is one of the relevant factors for finding a case of theft. On the contrary, Section 126 of 2003 Act does not speak of any criminal intendment and is primarily an action and remedy available under the Civil Law. It does not have features or elements which are traceable to the criminal concept of mens rea. Thus, it is clear that the expression "unauthorized use of electricity" under sec. 126 deals with cases of unauthorized use even in the absence of intention which would be different from cases where there is dishonesty, abstraction of electricity by any of the methods enlisted under sec. 135.

The expression "means" would not always be opened to such a strict construction that the terms mentioned in the definition clause under such expression would have to be inevitably treated as being exhaustive. There can be a large number of cases and examples where even the expression "means' can be construed liberally and treated to be inclusive but not completely exhaustive of the scope of the definition, of course, depending upon the facts of a given case and the provisions governing that law.

As regards the interpretation of contractual documents, the common sense view relating to the implication and impact of provisions is the relevant consideration so as to achieve temporal proximity of the end result. Another similar rule is the rule of practical interpretation. It must be understood that an interpretation which upon application of the provisions at the ground realities would frustrate the very law should not be accepted against the common sense view which further such application.

***(Southern Electricty Supply Co. of Orissa Ltd Vs. Sri Seetaram Rice Mills ) [2012] 2 SCC 108)***

## 27 VOID/NULL JUDGEMENT OR ORDER

It is the settled proposition of law that a judgement or decree obtained by playing fraud on the Court is a nullity and non est in the eye of law. Such judgement/decree has to be treated as a nullity by every Court whether superior or inferior. It can be challenged in any Court even in collateral proceedings. Even non-disclosure ofallthenecessaryfactstantamounttoplayingfraud on the Courts. If the party withholds a vital document in order to gain advantage on the other side then he would be guilty of playing fraud on the Court as well as on the opposite party.

***(UOI Vs. Ramesh Gandhi) [2012] { 1SCC 476 })***

## 28 TRANSFER OF IMMOVABLE PROPERTY – GENERAL POWER OF ATTORNEY

The immovable property can be legally and lawfully transferred or conveyed only by a registered deed of conveyance. Transactions of the nature of general power of attorney sales or sale agreement/will transfers do not convey title and do not amount to transfer nor can they be recognized as valid modes of transfer of immovable property. Such transactions cannot be relied upon or made the basis for mutations in municipal or revenue records. A lease can be validly transferred only under a registered assignment of lease.

***(Suraj Lamp & Inds. P. Ltd Vs. State of Haryana) [ 340 ITR 1]***

***ED Note : This general proposition of law should be read subject to the extended law under Income-tax Act, 1961 by Sec. 2(47)(v) /(vi).***

## 29 ADMINISTRATIVE OR EXECUTIVE ACTION- ARBITRARY

An action can be said to be arbitrary and capricious, where a person, in particular, a person in authority does any action based on individual discretion by ignoring prescribed rules, procedures or law and the action or decision is founded on prejudice or preference rather than reason or fact.To be termed as arbitrary and capricious, the action must be illogical and whimsical, something without any reasonable explanation.

**(Sanchit Bansal v. Jt. Admission Board) { (2012) (1 SCC 157)}**

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# FROM THE COURTS

## 71 SEC. 40A(2)(b) : TRADE DISCOUNT IS NOT EXPENDITURE AND HENCE NOT APPLICABLE :

**UNITED EXPORTS V/S. CIT**
**(2010) 330 ITR 549 (DEL)**

**Issue :-**

Whether provisions of Sec 40A(2)(b) are applicable to trade discount ?

**Held :**

Provisions of Sec. 40A(2)(b) in the Act pertains to disallowance of an expenditure which is made by the assessee, i.e. an amount spent by the assessee as an expenditure. The expression used in this provisions is "incurs any expenditure in respect of which payment has been or is to be made to any person" (Emphasis Supplied). The emphasised words clearly show that actual payment must be made and there has to be an expenditure incurred before the provision can be said to be applicable. A trade discount, and admittedly it is not in dispute the subject matter of the claim is a trade discount, is not an expenditure, clearly therefore there does not arise the question of applicability of Sec. 40A(2)(b).

## 72 EVIDENTIAL VALUE OF STATEMENT DURING SURVEY :

**CIT V/S. DHINGRA METAL WORKS**
**(2011) 196 TAXMAN 488 (DEL)**

**Issue :**

Can addition be made to income, solely on the basis of statement made during survey proceedings ?

**Held :**

From a reading of section 133-A, it is apparent that it does not mandate that any statement recorded under section 133-A would have an evidentiary value. For a statement to have a evidentiary value, the survey officer should have been authorized to administer oath and to record sworn statement. This would also be apparent from section 132(4).

**CA. C. R. Sharedalal**
*The author is the past President of CAA, practising since 1953. He can be reached at jcs@crsharedalalco.com.*

**CA. Jayesh C. Sharedalal**
*The author is the past President of CAA, practising since 1981. He can be reached at jcs@crsharedalalco.com.*

It is apparent that Sec. 132(4) specifically authorizes an officer to examine a person on oath, section 133-A does not permit the same.

Moreover, the word "may" used in Section 133A(iii), clarifies beyond doubt that the material collected and the statement recorded during the survey are not conclusive piece of evidence by themselves.

In any event, it is a settled law that though an admission is extremely important piece of evidence, it cannot be said to be conclusive and it is open to the person, who has made the admission, to show that it is incorrect.

Since in the instant case the assessee had been able to explain the discrepancy in the stock found during the course of survey by production of relevant record including the excise register of its associate company, the A.O. could not have made aforesaid addition solely on the basis of the statement made on behalf of the assessee during the course of survey.

## 73 WAIVER OF CAPITAL AMOUNT OF LOAN : SEC. 28(I), 28(IV), AND SEC. 2(24), SEC. 36(I)(III) AND SEC. 41(1) NOT APPLICABLE.

**ISKRAEMECO REGENT LTD. V/S. CIT**
**(2011) 196 TAXMAN 103 (MAD)**

**Issue :**

Whether waiver of principal amount of loan can be treated as income u/s 28(iv) read with Sec. 2(24), or Sec. 36(i)(iii) or Sec. 41(1) ?

**Held :**

Sec. 28(iv) speaks about the benefit or perquisite received in kind. Such a benefit or perquisite received in kind other than in cash would be an income as defined u/s 2(24). In other words, to any transaction which involves money, section 28(iv) has got no application.

Therefore, the transaction in the instant case being a loan transaction having no application with respect to Sec. 28(iv), the same could not be termed as an income within the purview of Sec. 2(24). In other words, inasmuch as section 28(iv) was not applicable to the transaction on hand, it could not be termed as income which could be made taxable as receipt. Hence such a receipt which do not have any character of an income being that of a loan could not be made exigible to tax.

Similarly, Section 41(1) also could not have any application inasmuch as the said provision would be applicable to a trading liability. Accordingly, a loan received for the purpose of capital asset would not constitute a trading liability and, hence, Sec. 41(1) had no application.

The revenue submitted that the facts involved in the instant case would come under the purview of Sec, 28(i). The said contention could not be accepted for the simple reason that it was not the case of the A.O. as well as the other authorities that the instant case would come under purview of Sec. 28(i). The authorities proceeded only on the footing that Sec. 28(iv) would be applicable. Further, Sec. 2(24) defines 'income'. While defining 'profits and gains', it refer to transactions involved under Sec. 28(iv). Therefore, in as much as the previsions contained under Sec. 28(i) having been not defined as income under Sec. 2(24) the same would not partake the character of the income and, therefore it is not assessable to tax. In other words, only an income as defined u/s 2(24) can be made assessable to tax. It is a well established principle of law that all receipts are not income and, therefore, liable to be taxed.

In so far as the reference made u/s 36(1)(iii) was concerned, said section speaks about other deductions. The said provision deals with the amount of interest paid in respect of capital borrowed for purpose of business. Therefore it had no relevance to the instant case.

## 74 SEC. 54 : CAPITAL GAIN : INVESTMENT IN FOUR RESIDENTIAL FLATS : EXEMPTION AVAILABLE.

**CIT V/S. SMT. K.G. RUKMINIAMMA**
**(2011) 196 TAXMAN 87 (KAR)**
**(2011) 331 ITR 211 (KAR)**

**Issue :-**

When capital gain from sale of a residential house arises, whether investment of the same can be exempt when invested in four residential flats ?

**Held :-**

The context in which the expression "a residential house' is used in section 54 makes it clear that it was not the intention of the legislation to convey the meaning that it refers to a single residential house. If that was the intention, they would have used the word "one". As in the earlier part the word used are buildings and lands which are plural in number and that is referred to as " a residential house", the original asset, an asset newly acquired after the sale of the original asset also can be buildings or lands appurtenant thereto, which also should be "a residential house". Therefore, in letter "a" in context it is used should not be construed as meaning "Singular". But , being an indefinite article, the said expression should be read in consonance with the other words "buildings and lands" and, therefore, the singular "a residential house" also permits use of plural by virtue of section 13(2) of General clauses Act.

In the instant case, the consideration for selling property was invested in four flats. All the four flats were situated in a residential building. Those four residential flats "constituted "a residential house for the purpose of sec. 54. Profit on sale of property was used for residence. The four residential flats could not be construed as four residential houses for the purpose of section 54. They had to be construed only as "a residential house" and the assessee was entitled to the benefit accordingly.

## 75 CHARITABLE TRUST AND CARRY FORWARD OF DEFICIT :

**DIT V/S. RAGHUVANSHI CHARITABLE TRUST**
**(2011) 197 TAXMAN 170 (DELHI)**

**Issue :**

Whether deficit can be carried forward in the case of a charitable trust ?

**Held :**

High Court made a mention of decision in the case of CIT v/s. Institute of Banking Personnel (2003) 263 ITR 110 (Bom) ( and referred decision of various High Courts) as under :-

On the argument of revenue that there is no provision in the case of a charitable trust of carry forward of the excess of expenditure of earlier years to be adjusted against income of the subsequent years, High Court has stated :-

We do not find any merit in this argument of the Department. Income derived from trust property has also got to be computed on commercial principles and if commercial principles are applied then adjustment of expenses incurred by the trust for charitable and religious purposes in earlier years against the income earned by the trust in the subsequent year will have to be regarded as application of income of the trust for charitable and religious purposes in the subsequent year in which adjustment has been made having regard to the benevolent provisions contained in Sec. 11 of the Act and that such adjustment will have to be excluded from the income of the trust u/s 11(1)(a) of the Act.

It is clear from the above that as many as five High Courts have interpreted the provisions in identical and similar manner. Learned counsel for the revenue could not show any judgment where any other High court has taken contrary views.

## 76 FOR REFERENCE TO VALUATION OFFICER, PRIOR REQUIREMENT IS REJECTION OF BOOKS :

**SARGAM CINEMA V/S. CIT**
**(2011) 197 TAXMAN 203 (SC)**

**Issue :**

Whether A.O. can refer the matter to Valuation Officer before rejection of books of account ?

**Held :**

In the present case we find that Tribunal had decided the matter rightly in favour of the assessee inasmuch as the Tribunal came to the conclusion that the assessing authority could not have referred the matter to the Departmental Valuation Officer (DVO) without the books of account being rejected. In the present case, a categorical finding is recorded by the Tribunal that the books were never rejected. This aspect has not been considered by the High Court. In the circumstances reliance placed on the report of the DVO was misconceived.

For the above reasons, the impugned judgment of the High Court is set aside and the order passed by the Tribunal stands restored to the file. Accordingly, the assessee succeeds.

## 77 VIEWPOINT OF PRUDENT BUSINESSMAN : NO ROVING INQUIRY :

**CIT V/S. ROCKMAN CYCLE INDUSTRIES PVT. LTD.**
**(2011) 331 ITR 401 (P & H) (FB)**

**Issue :**

Transactions are to be looked into from mere tax effect and whether roving inquiries are permitted while considering the claim of interest paid at a higher rate than realization ?

**Held :**

On the facts that assessee borrowed funds at 18% rate of interest and invested in shares of sister concern which declared dividend at 4%, department sought to disallow the difference. High Court has held as under:-

While deciding the issue High Court has referred the decisions of Supreme Court right from A. Raman and Co. (1968) 67 ITR 11, B. M. Kharwar (1969) 72 ITR 603 and S.A. Builders (2007) 288 ITR 1.

Ultimately High court has held that :-

The Assessing Officer or the Appellate authorities and even the courts determine the true legal relation resulting from a transaction. If some device has been used by the assessee to conceal true nature of the transaction, it is the duty of the taxing authority to unravel the device and determine the true character. However, the legal effect of the transaction can not be displaced by probing into the "substance of transaction". The taxing authority must not look at the matter from their own view point but that of a prudent businessman. Each case will depend on its own facts. The exercise of jurisdiction cannot be stretched to hold a roving inquiry or deep probe.

High Court has also observed as under :-

"We may proceed on the basis that tax planning is permissible even if it results in avoidance of tax as observed in Azadi Andolan (2003) 263 ITR 706 (SC)".

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# TRIBUNAL NEWS

## 51 ACIT, LARGE TAXPAYER UNIT Vs. TUBE INVESTMENTS OF INDIA LTD 133 ITD 79 (CHENNAI)

**Assessment Year 1999-2000, Order Dated: August 10, 2011**

### BASIC FACTS

Assessing Officer initiated reassessment proceedings against the assessee for the year under consideration on the issue of excess claim of deduction under section 35D. On appeal made to tribunal, Accountant Member held that reassessment proceedings were not valid because addition made by the assessing officer has been deleted by the CIT(A) in earlier years based on the working submitted by the assessee. However Judicial Member held that as the assessment was completed in the present case u/s 143(1) of the Act, assessing officer was having complete jurisdiction to reopen the case provided he has reasons to believe that income has escaped assessment. Judicial Member also held that as in the present case, requirements of law has been fulfilled, reopening was justified. In view of the difference in opinion, the matter was referred to the Third Member.

### ISSUE

**Whether reopening of case for excess claim of deduction u/s 35D was justified in view of the fact that addition made by the assessing officer was deleted by CIT(A) in earlier years? Whether where assessment was completed u/s 143(1), assessing officer was justified in reopening the case for the assessment year in question?**

### HELD

In the instant case, assessment was completed u/s 143(1) and the assessing officer has recorder reasons for reopening the assessment. The said reasons were communicated to the assessee. The claim of the assessee u/s 35D was not correct according to the assessing officer and in view of the same, assessing officer initiated the reassessment proceedings. Reasons recorder by the assessing officer fits into the term of "reasons to believe". Merely because the Commissioner (Appeal) has deleted the same addition made in the earlier year cannot take away the jurisdiction of the assessing officer. The matter decided by the Commissioner (Appeals) is not the final one. Assessing officer has considered appeal before the tribunal against the order of Commissioner (Appeals). The matter would be assumed to have reached finality if at all the assessing officer does not contest an appeal against the Commissioner's order. Also the fact that the ITAT gave decision in favor of the assessee in appeal filed by the assessing officer against the order of Commissioner in earlier year would not restrict the assessing officer in reopening the case because the order of the ITAT was passed after the reassessment proceedings were initiated for the year under consideration. While reopening an assessment, what are important are prima facie reasons and not the final verdict. In the present case, assessing officer recorded proper reasons for the reopening and hence it was held that assessing officer was right in initiating reassessment proceedings.

**CA. Yogesh G. Shah**
*The author is practising since 1986. He can be reached at yshah@deloitte.com*

## 52 DREDGING CORPORATION OF INDIA LTD. Vs. ACIT 142 TTJ 252 (VISAKHA)

**Assessment Year 2006-07 to 2008-09, Order Dated: July 25, 2011**

### BASIC FACTS

For the year under consideration, assessee was granted a refund u/s 143(1) which got increased while passing regular assessment order. The case of the assessee got reopened and while passing the reassessment order, refund got reduced due to certain

additions made. Hence the assessing officer levied interest u/s 234D of the Act on the amount that became collectible from the assessee. Assessee challenged levy of interest before the CIT(A) who held the matter in favor of the assessee. Department went into appeal before the ITAT.

**ISSUE**

**Whether where assessment has been completed u/s 143(3) by determining a refund and which got reduced while passing order u/s 147 of the Act, Assessing Officer was justified in levying interest u/s 234D on the amount that became collectible from the assessee?**

**HELD**

After considering the facts placed on record, ITAT held that plain reading of Section 234D says that in case refund has been granted to the assessee while passing intimation u/s 143(1) and the same becomes collectible from the assessee at the time of regular assessment, then an interest has to be levied as per provisions of Section 234D. The word used in the section is "regular assessment" and as per Section 2(40), regular assessment means assessment made under sub section (3) of section 143 or section 144. Hence a reassessment proceeding under section 147 after completion of the regular assessment u/s 143(3) was to be excluded from the purview of "regular assessment". Explanation to section 234D was not applicable in the instant case because of the fact that assessment was not carried for the first time u/s 147. Hence order of the CIT(A) was upheld with the decision that interest u/s 234D would not be applicable in the appellant's case.

## 53 FOUR SOFT LIMITED Vs. DCIT 142 TTJ 358 (HYD)

**Assessment Year 2006-07, Order Dated: September 09, 2011**

**BASIC FACTS**

During the year under consideration, assessee gave corporate guarantee to ICICI Bank UK and DCS Group. TPO held that the guarantee is an obligation and if the principal debtor fails to discharge its liability, then guarantor is liable for the same and hence TPO determined a commission at 3.75% as ALP under CUP method on the basis of the commission charged by ICICI Bank as benchmark. Assessee contended that the said transaction does not amount to international transaction and hence no adjustment should be made. Hon'ble DRP confirmed the action of the TPO. Against the same, assessee went into appeal before ITAT.

**ISSUE**

**Whether corporate guarantee provided by the assessee for loan obtained by its subsidiary outside India falls within the definition of international transaction? Whether TPO was justified in determining arm's length price of the same?**

**HELD**

TP legislation provides that income has to be calculated for international transactions as per section 92B of the Act. Neither corporate guarantee falls within the definition of international transaction nor any guidelines are provided by the TP legislation for corporate guarantee. Therefore in the absence of charging provisions, lower authorities were not justified in bringing the said transaction in the TP study and thereby within the definition of international transaction. Finally it was held that TP adjustment is not required in respect of corporate guarantee provided by assessee.

## 54 ACIT vs. NATIONAL STOCK EXCHANGE OF INDIA LTD. 142 TTJ 189 (Mumbai)

**Assessment Year 1997-98, 1998-99 & 2001-02 Order Dated: 27th May, 2011**

**BASIC FACTS**

In the instant case, the assessee company was incorporated by nationalized banks to start screen based trading to replace the existing floor based trading in stocks and shares. For this screen based trading, the assessee company was required to install VSAT network, the hub was installed in the premises of the assessee company, whereas VSAT antenna and monitors were installed in the premises of member brokers. The network mainly consisted of hub equipment, which is located in the members' premises. The Assessing Officer by invoking provisions of

section 38(2) estimated that 40 percent of such network could be said to have used for the assessee's business and disallowed 60 percent of depreciation on this equipment. The CIT(A) held the Assessing officer's order is not justified by telling that in the absence of installation of VSAT antenna and monitor in the premises of the members, member brokers could not have executed various transactions in the stock exchange. Revenue challenged the order of CIT(A).

**ISSUE**

**Whether the mere fact that part of the equipments were installed at the premises of the members, but owned by the assessee sufficient enough to disallow part of depreciation?**

**Held**

After considering the facts placed on record, the ITAT held that there was no doubt that part of the system had been used by the brokers also but the business of the assessee was not possible without the installation of VSAT antenna and monitor in the premises of the members. In the absence of installation of VSAT antenna and monitor in the premises of the members, member brokers could not have executed various transactions in the stock exchange. Therefore the system was meant for the purpose of business of the assessee. Further the member brokers could not have possibly used the system for any other purpose than to execute the share transactions with the assessee.Even if it is assumed that brokers also got some benefit out of this system, it cannot be said that the same has not been used for the purpose of business of the assessee. Therefore it was entitled to full depreciation on such equipments. Hence the CIT(A) decision was upheld and mere fact that part of the equipments were installed at the premises of members, but owned by the assessee, was not sufficient to disallow part depreciation.

## 55 DRILBITS INTERNATIONAL (P) LTD vs. DCIT142 TTJ 86 (PUNE)

**Assessment Year 2006-07, Order Dated: 23rd August, 2011**

**BASIC FACTS**

In the instant case, the assessee company acquired the unit of G on slump sale basis consisting of all its assets which included intellectual property rights such as designs, drawing, manufacturing process and technical know-how for a consideration of 17.01 crores. The registered valuer valued the acquired know-how at Rs.2.41 crore and the royalty payable for the use of brand name, trademark, logo, etc. at Rs.2.67 crores. The AO disallowed the depreciation claimed on the same contending that the assesse had not purchased any know-how from G and the assesse is entitled to use the trademark, logo, brand name of G free of cost for three years. This was not justified as the assesse had paid for the unit in its entirety, i.e. Unit consisting of trademark, logo, manufacturing process, know-how, etc. Simply because it is mentioned in the agreement that the user of all the items like logo, trademark, brand name allowed to the assesse for three years by G free of cost, does not mean that it is of no value to the user of these items. The agreement between the seller and the purchaser cannot restrict the right of the purchaser to record the asset at its fair book value.

**ISSUE**

**Whether the assessee can claim depreciation on an amount of expense valued by the valuer as capital expense, being purchase of user of brand name, logo, trademark, know-how in respect of products manufactured by the unit which was acquired by the assesee at slump price?**

**Held**

Contents of the sale purchase agreement between assesse and G should be read in its totality for clear understanding of terms and conditions agreed upon therein. It also cannot be disputed that the assesse has paid Rs.17.01 crores in lump sum for the unit in its entirety which logically infers that consisting of trademark, logo, brand name, designs, drawings, etc. Simply because it is mentioned in the agreement that the user of all the items like logo, trademark, brand name allowed to the assesse for three years by G free of cost, does not mean that it is of no value to the user of these items. Likewise, simply because there is no specific value done to the acquisition right over the intangible assets being transferred to the assesse company in the balance sheet of the transferor, does

not mean there was no intangible assets in the form of technical know-how, designs, drawings, etc. The assessee's lump sum payment of Rs.17.01 crores for all these rights and assets is very clear and hence apportionment thereof amongst the various assets and rights has to be made and which has been done in the present case as per the valuer's report. The registered valuer valued the acquired know-how at Rs.2.41 crores and the royalty payable for the use of brand name, trademark, logo, etc. at Rs.2.67 crores. The authorities below have not disputed the above values determined by the approved valuer. Since the assesse had purchased the user of trademark, logo, brand name for three years and similarly intellectual property rights like design, drawings, know-how in respect of products manufactured by the unit was acquired, the expense incurred in this regard is valued as capital expense and hence the claim of depreciation on this expense was allowable. Accordingly, the AO is direct to allow the claimed depreciation on the above assets.

## 56 KANTILAL C SHAH vs. ACIT 133 ITD 57(AHD)

**Block Period 1-4-1985 to 31-3-1995 & 1-4-1995 to 12-12-1995, order dated- 24/06/2011**

### BASIC FACTS

A search operation was carried out on 12/12/1995 & during search operation cash, jewellery, books of account & certain documents pertaining to the assessee were found & seized. The assessee was a director in a company & partner in new firms. The statement of the assessee u/s 132(4) was recorded on same day whereunder admission with regard to unaccounted income of Rs. 6.20 lakhs were made. Said unaccounted income consisted of (i) marriage expenditure (ii) household expenditure (iii) unexplained investment in NSC & shares, (iv) payment of on money on purchase of flats. The assessing officer, thereafter, made additions in respect of unaccounted income admitted u/s 132(4). The assessee strongly contended that no addition should have been made merely on the basis of a statement recorded u/s 132(4) when there was no evidence or incriminating material discovered at the time of search. The assessee further alleged that impugned disclosure of Rs. 6.20 lakh was obtained forcefully; hence the said statement was not binding on him.

The assesse had gone in appeal before the tribunal and at that time contested that proper opportunity of hearing was not granted. In view of these facts the co-ordinate Bench had considered the said request of providing a re-hearing and restored the matter back to the AO with the direction to grant adequate opportunity and to decide accordingly. The assessment order under appeal has been passed following the direction of the Tribunal.

### ISSUE

**Whether statement recorded u/s 132(4) is an evidence by itself & any retraction contrary to that should be supported by strong evidence for demonstrating that earlier evidence recorded was under coercion?**

### HELD

When an assessee had made a statement of facts, he can have no grievance if he is taxed in accordance with that statement. The AO has not made any enhancement or substitution in the amounts as offered/ disclosed in the statement. The assessee was in knowledge relating to the facts contained in the statement. The facts were such that there was no scope of existence of other evidence & department accepted the facts disclosed by the assessee in the statement.

The assessee was not able to produce any evidence which would direct towards deleting the additions & also no evidences relating to the contention that the statement u/s 132(4) was obtained forcefully & under coercion. The allegation of the assessee was submitted nearly after nine months through an affidavit which showed that the assessee was not confident about filing of the retraction. In the light of above deliberations, it was held that the statement recorded on the date of search has evidentiary value & the retraction being general & vague was to be ignored. The tribunal dismissed the appeal.

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# UNREPORTED JUDGMENTS

In this issue we are giving full text of two decisions OF Ahmedabad Income Tax Appellate Tribunal. The first one in the case of M/s Parry Engineering & Electronic P. Ltd. deals with the issue regarding claim of depreciation and additional depreciation in respect of Windmill and whether such depreciation should be available on the entire Renewable Energy device which also includes Windmill.

The Second decision in the case of M/s Neo Structo Constructions Ltd. deals with the issue of allowability of losses incurred pursuant to invocation of bank guarantee given for performance of the contract. The Tribunal in the decision finds that the view of the department that the loss incurred by the assessee due to non-performance of the contract is capital expenditure is not correct as such contract was not a new business, but since assessee was already in business, such contract was a part of the existing business and hence such loss was allowable as business loss.

We hope the readers would find both the decisions helpful.

**CA. Sanjay R. Shah**
*The author is the past President of CAA, practising since 1981. He can be reached at sarshah@deloitte.com*

**13** *IN THE INCOME TAX APPELLATE TRIBUNAL AHMEDABAD BENCH "**C**" AHMEDABAD*

Before **Shri Mukul Kumar Shrawat, Judicial Member** and **Shri A Mohon Alankamony, Accountant Member**
**ITA No.3026/Ahd/2009**
Assessment Year:-2006-07

Neo Structo Construction Ltd. **V/ s**. Addl . CI T Range1,
A/ 1, A/ 4, Nayan Park, Surat
Ichhapore,
P. O. Surat – 394 5120

**PAN No. AAACN7717N**

| Appellant . . | Respondent |
|---|---|
| By Appellant | Shri K.P. Shah, AR |
| By Respondent | Shri Vinod Tanwani, SR-DR |
| Date of Hearing | 21-02-2012 |
| Date of Pronouncement | **24**-02-2012 |

**O R D E R**

**PER Mukul Kumar Shrawat, Judicial Member:-**

This appeal has been filed by the assessee arising from the order of Ld. Commissioner of Income-tax (Appeals)-I, Surat dated 23-09-2009 for the assessment year 2006-07.

2. The number of grounds have been raised, however, the issue is in respect of a disallowance of Rs.70,95,392/- representing the performance bank guarantee which was encashed by ONGC. The issue is whether it was a capital expenditure or if business loss then to be held as revenue expenditure incidental to the business of the assessee.

3. Facts in brief as emerged from the corresponding assessment order passed u/s. 143(3) of I.T. Act dated 12-11-2008 was that assessee-company is engaged in the business of construction and erection of plant mainly in respect of public sector units like ONGC, HPCL, KRIBHCO, CRL etc. The assessee has also undertaken the said work for private sector like Reliance, ESSAR, ISPAT etc for the year under consideration. Total turnover was at Rs.68,56,71,539/- and the gross profit (GP for short) at Rs.20,51,25,204/-. The GP for the year under consideration was stated to be 29.91% as against the GP rate of the past year at 24.13%. It was noted by the Assessing Officer that a sum of Rs.70,75,392/- was debited to profit and loss account in respect of encashment of bank guarantee. It was explained that the assessee had accepted an off-shore job work of ONGC, A "performance bank guarantee" was given to ONGC. Due to certain technical reasons, the assessee was not able to perform or even to start the job. Due to non-performance, the said amount being 7.5% of the annualized contract value was encashed by the ONGC. The relevant portion of the explanation is reproduced below:-

*"On award of the contract the company's team of engineers visited various offshore platforms of ONGC to evaluate & access the work and to plan execution of the various jobs. However, on detailed check-up the conditions and various other details involved with the job were very different from the scope of work depicted in the tender documents and it transpired that the lack of physical inspection in the pretender-stage had created this anomaly. It is also transpired that the existing conditions made the tendered rates totally unviable because of the various hidden factors and costs. Therefore, the company took-up the matter with ONGC vide letter dated 26th April, 05 that, it was not possible to go ahead with the execution of the job, due to difference in the scope of work award and specified in the tender documents and requested ONGC to terminate the contract and return the bank guarantee.*

*ONGC did not terminate the bank guarantee but en-cashed the bank guarantee stating the non performance of the contract by the company. Even though, it was possible to have proceeded legally, it is extremely difficult to fight a legal battle with an organization like ONGC which is mammoth and have bottomless cash reserves, while it would have broken-up the organization like assessee-company. Hence, the assessee company took the loss of Rs.70.75 Lacs which otherwise would have resulted in crores of rupees of loss if the contract was performed. This was considered as a prudent business decision and the business loss was accepted by the assessee company.*

*The assessee company went forward by deploying its engineers in other sectors which had borne fruit since then. The necessary Xerox copy of correspondence is enclosed herewith for your ready reference."*

3.1) The Assessing Officer was not convinced and he has held that the bank guarantee was not a business expenditure to be allowed u/s.37(1) of IT Act and that it was in respect of a non-performance of the contract, hence, pertained to the work, which was not executed, therefore capital in nature. The said amount was disallowed and the matter was carried before the First Appellate Authority.

4. The Ld. CIT(A) has held that admittedly the assessee had not begun the work. The contract was awarded on 04-02-2005 as per the bidding made by the assessee. On visit of technical team, the assessee came to know that the work could not be started, so the assessee has accordingly informed the ONGC. As per the terms of the contract the assessee was required to mobilize the man power within 45 days. Since the assessee had not even started the work therefore the nature of the expenditure was nothing but a capital expenditure. Ld. CIT(A) has referred the case law of Hon'ble Supreme Court in the case of *Swadeshi Cotton Mills Co. Ltd. V. CIT* (1967) 63 ITR 65 (SC) and confirmed with the disallowance.

5. With this factual background we have heard both the sides. As per the Notification of the award of contract dated 04-02-2005 the assessee was required to furnish a "performance bank guarantee" for an amount of Rs.70,75,392/- i.e. @ 7.5% of the annualized contract value. The assessee, in-turn, as per terms of the award of the contract had been requested "to issue a bank guarantee" . Accordingly, the bank vide an undertaking dated 07-02-2005 furnished "performance guarantee" to ONGC. Thereafter vide letter dated 03-05-2005 ONGC has informed the termination of the contract award and invoked the said guarantee in terms of one of the clauses of the award. Rather, the ONGC has informed the assessee to reserve its right to lodge the claim for damages arising due to termination of the contract by the assessee. With this factual background, we are of the view that it was wrong on the part of the **Revenue Department to consider each contract as a start of new business. This contract was part of the business activity of the assessee. The term 'contract' has altogether a different meaning than the term ' business'. A 'contract' can be a part of the 'business' , rather in a 'business' there can be existence of several 'contracts'.** Undoubtedly a huge turnover was

made during the year under consideration pertaining to the civil and electric works carried on by the assessee during the year under consideration. The Revenue Authorities have wrongly applied the law pronounced in the case of *Swadeshi Cotton Mills Co. Ltd.* (supra) because in that case the expenditure was incurred to avoid unnecessary investment in the capital asset. In that precedent the expenditure was held as an outside the account of the profits and gains of the assessee. Contrary to this, in the present case, the impugned expenditure did not represent an investment in any capital asset. Rather, in the case of ***Jamna Auto Industries v. CIT*** **(2008) 214 CTR 649 (P&H) (FB), the Hon'ble court has held that damages for breach of contract is allowable as business expenditure if not incurred for contravention of any law. Likewise, in the case of *CIT v. Rajaram Bandekar* (1994) 121 CTR 233 (Bom), the Hon'ble court has held that the payment made by firm to terminate an inconvenient contractual obligation in terms of a settlement is wholly and exclusively for the purpose of its business.** We therefore hold that during the continuity of the business if in a particular contract the assessee had to compensate for his own default by offering performance guarantee which was contractual obligation and that the said business continued later on, then a disallowance for a particular contract be not considered separately, that too, to treat the same as a capital expenditure. It was altogether a wrong notion on the part of the A.O., hence we hereby reverse the findings of the Revenue Authorities and direct to allow the claim.

6. **In the result, grounds raised by assessee are hereby allowed.**

This Order pronounced in Open Court on 24.2.012.

(A. Mohan Alankamony) (Mukul Kumar Shrawat)
(Accountant Member) (Judicial Member)

24/02/2012

**14 IN THE INCOME TAX APPELLATE TRIBUNAL AT AHMEDABAD,**

**"A" BENCH**

**BEFORE S/SHRI G.C. GUPTA, VICE-PRESIDENT AND TEJ RAM MEENA, ACCOUNTANT MEMBER**

ITA No.3317/Ahd/2011

With CO No.44/Ahd/2012

[Asstt.Year : 2007-2008]

| | | |
|---|---|---|
| ACIT (OSD) Ahmedabad 380 015. | Vs. | Parry Engineering & Electronics P. Ltd. Harkuver Haveli Opp: Jain Temple Gandhi Road Ahmedabad. **PAN : AAACP 6747 J** |
| **Appellant)** | | **Respondent)** |
| Revenue by | | Shri Rahul Kumar, Sr.DR |
| Assessee by | | Shri G.C.Pipara. |
| Date of Hearing | | 29th February, 2012 |
| Date of Pronouncement | | 02-03-2012 |

**O R D E R**

**PER G.C. GUPTA, VICE-PRESIDENT:** This is Revenue's appeal and the assessee's CO directed against the order of the Commissioner of Income Tax (Appeals)-XI, Ahmedabad dated 31.10.2011 for the assessment year 2007-2008.

**ITA No.3317/Ahd/2011 (Revenue's appeal)**

2. The only ground raised in this appeal of the Revenue reads as under:

*"1. The ld.CIT(A) has erred in law and on facts in deleting the disallowance of excess claim of depreciation of Rs.56,85,621/- and additional depreciation of Rs.35,66,299/- on windmill."*

3. The learned DR submitted that the assessee has claimed depreciation on civil work undertaken by it on the installation of windmill at the rate of 80%. He submitted that the disallowance of depreciation on civil and electrical works, payment to GEDA and capitalized interest was rightly made by the AO. He submitted that as per the provisions of Income Tax Rules, depreciation at the rate of 80%

was allowably only on the device of windmill and not on the entire cost including civil works, electrical installation, development expenses and other machinery etc. He submitted that it is not clear that whether the interest capitalized represents certain loan amount invested in the purchase of land also. This part needs verification by the AO. The learned counsel for the assessee has opposed the submissions of the learned DR. He submitted that as per the provisions of the Act, depreciation at the rate of 80% is allowable on the entire device which is capable of generating electricity using the wind energy. He submitted that the civil and electrical works are necessary for the installment of the windmill and therefore the depreciation and additional depreciation on the same was rightly allowed by the learned CIT(A).

4. We have considered rival submissions and perused the orders of the AO and the CIT(A). The depreciation is allowable on renewable energy device which also includes windmill. The depreciation at the rate of 80% is allowable on the entire device which is capable of generating electricity using wind energy. There is no provision in the Act to bifurcate the device into several parts and allow depreciation thereon at different rates of depreciation. The foundation, civil and electrical works are necessary for the installation of the windmill and is clearly part and parcel of the windmill project on which depreciation at the rate of 80% is allowable. The CIT(A) has referred to the decisions of the High Courts while deciding the issue in favour of the assessee. Accordingly, the ground taken in the appeal of the Revenue with regard to the depreciation and additional depreciation on the foundation, civil & electrical works, installation, payment to GEDA is dismissed. However, with regard to depreciation on the capitalized interest, there is no finding in the orders of the AO and the CIT(A) that no part of the borrowed amount was utilised for the purchase of the land. Accordingly, this limited issue is restored to the file of the AO with the directions to verify the facts and in case the borrowed amount has been utilised for the purpose of purchase of the land, then to disallow the depreciation on the capitalized interest to that extent. We direct accordingly.

**CO No.44/Ahd/2012 (Assessee's CO)**

5. The ground of the assessee's CO reads as under:

*"1. The ld.CIT(A) has erred in confirming the disallowance of Rs.90,115/- made by the AO u/s.14A r.w.s. 8D without appreciating the fact that introduction of Rule 8D is w.e.f. AY 2008-09 and is not applicable for the year under consideration i.e. AY 2007-08 and that no interest bearing funds have been used for earning exempt income. In view of elaborate submissions filed and the legal position laid down by various courts of law including the Hon'ble Apex Court in the case of CIT Vs. Walfort Share & Stock Brokers P. Ltd. 326 ITR 1 (SC), the provisions of section 14A are not attracted in cse of the appellant in absence of any proximate cause for disallowance. Accordingly, the ld.CIT(A) ought to have deleted the impugned addition of Rs.90,115/-"*

6. We have heard both the parties. In the facts and circumstances of the case, we restore this issue to the file of the AO with directions to decide the same afresh in the light of the decision relied upon by the assessee in the ground of the CO and to allow due opportunity of being heard to the assessee.

7. In the result, the Revenue's appeal is partly allowed for statistical purpose and the CO of the assessee is allowed for statistical purpose.

*Order pronounced in Open Court on the date mentioned hereinabove.*

| | |
|---|---|
| Sd/- | Sd/- |
| **TEJ RAM MEENA** | **G.C. GUPTA)** |
| **ACCOUNTANT MEMBER** | **VICE-PRESIDENT** |

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# CONTROVERSIES

**Whether mere disallowance of claim or if the claim of assessee is rejected, amounts to concealment of income and penalty u/s 271(1)(c) is applicable ?**

**Issue:**

Whether disallowance of expenditure\claim of deduction or addition to income amounts to concealment of particulars of income or filing of inaccurate particulars of income ?

**Proposition:**

A penalty u/s.271(1) (c) of the Act ('Concealment Penalty') can be imposed in cases where the assessee has concealed the particulars of his income ('Concealed Income') or furnished inaccurate particulars of his income ('Furnishing Inaccurate Particulars of Income'). The action of imposition of penalty should clearly bring out whether the penalty is imposed on account of concealed income or for furnishing inaccurate particulars of income.

In many cases, expenditure incurred by the assessee are disallowed by the assessing officer for various reasons viz., that the expenses are in excess of statutory limits provided under the act or for want of proper verification of supporting, etc, thereafter, the assessing officer initiates penalty proceedings as the assessee had furnished inaccurate particulars of income.

It is seen that whenever any expenditure or the claim for deduction is disallowed or whenever any income has been added to the total income, though it is disputed that the Assessing Officer invariably initiates penalty proceedings u/s 271(1)(c) for concealment of particulars of income or filing of inaccurate particulars of such income. This action of Income Tax department has become as good as routine and regular practice. This issue has been raised in the open house meeting with the Chief Commissioners of Ahmedabad but without any response. Be that as it may. However, it is proposed that whenever any addition has been made to the total income, the question of penalty u/s 271(1)(c) for concealment of particulars of income or for inaccurate particulars of such income does not arise

**CA. Kaushik D. Shah**
*The author is the past President of CAA, practising since 1976. He can be reached at dshahco@gmail.com.*

**View Against the Proposition :**

The question arises that if the assessee claims excessive deductions knowing that they are incorrect, does it amount to concealment of income? *The falsehood in accounts* can take either of the two forms; (i) an item of receipt may be suppressed fraudulently; (ii) an item of expenditure may be falsely (or in an exaggerated amount) claimed, and both types attempt to reduce the taxable income and, therefore, both types amount to concealment of particulars of one's income as well as furnishing of inaccurate particulars of income.

If there is a deliberate concealment and false/ inaccurate return has been filed, which is revised after the assessee is exposed of the falsehood, it would be treated as concealment of income in the original return and would attract penalty even if revised return has been filed before the assessment has been completed.

Where claim made in the return appears to be ex facie bogus, it would be treated as case of concealment or furnishing of inaccurate particulars and penalty proceedings would be justified.-**CIT vs Escorts Finance Ltd.[2009] 183 Taxman 453 (Delhi).** In the instant case, it was to be examined as to whether the claim made under section 35D was bogus or it was a bona fide claim. The assessee pleaded bona fide, as according to it, it was based on the opinion of the chartered accountant. The high court further observed that hence this was not a 'wrong claim' but a 'false claim' preferred by the assessee.

Division Bench of the Apex Court in the case of **Union of India vs. M/s Dharmendra Textile Processors - [(2007) 295 ITR 244 (SC)]** doubted the correctness of the view expressed in case of Dilip N. Shroff (supra) and the matter was referred to a Larger Bench. The

Larger Bench in the case of **Union of India & Ors. Vs. M/s Dharmendra Textile Processors & Ors.[(2008) 306 ITR 277 (SC)]** held that the penalty u/s 271(1)(c) of the Act creates a civil liability therefore, willful concealment **is not an essential ingredient for attracting civil liability** unlike the matter of prosecution u/s 276C of the Act. Accordingly the larger bench overruled the decision of Dilip N. Shroff (supra) **only to the extent** it held that mens rea was an essential ingredient for the penalty u/s 271(1)(c) of the Act.

In the case of **K.P. Madhusudhanan vs. CIT (2001) 169 CTR (SC) 489 : (2001) 251 ITR 99 (SC)**, it was held that it cannot be laid down as a general prescription that no penalty can be levied for agreed assessment; assessee having surrendered the amount of unexplained credits for assessment clearly admitting that entries were not recorded by him on the correct dates and temporary loans obtained by him were not recorded at all, he was liable to penalty under s. 271(1)(c) of Income Tax Act

**View in favour of the Proposition:**

It goes without saying that for the applicability of section 271(1)(c), conditions stated therein i.e firstly, there has to be concealment of the particulars of the income, and secondly, the assessee must have furnished inaccurate particulars of its income must be fulfilled.

Let me now refer to the decision of **Dilip N. Shroff vs. Jt. CIT-[(2007) 291 ITR 519 (SC)**

In the above case, the brief facts were: For the A.Y. 1998-99, the assessee had computed long-term capital loss of Rs.34.12 lakhs on transfer of 1/4th interest in property at Mumbai and the same was computed by taking Fair Market Value (FMV) of the property as on 1-4-1981 as the cost of acquisition as provided in S. 55(2)(b) of the Act and, it seems, on that basis Indexed Cost was determined. The FMV was determined (based on the Registered Valuer's Report) at Rs.2.52 crores. However, for the purpose of assessment, such valuation was obtained from the District Valuation Officer (DVO), who had determined such FMV at Rs.1.44 crores. This had resulted into a long-term capital gain of Rs.3.09 crores as against long-term capital loss of Rs.34.12 lakhs computed and shown by the assessee. On these facts, Concealment Penalty of Rs.68.78 lakhs was imposed, which was confirmed by the First Appellate authority as well as the Appellate Tribunal. The appeal preferred by the assessee before the High Court u/s.260A of the Act was dismissed in *limine*. Under this circumstance, the issue relating to the levy of Concealment Penalty came up before the Apex Court in the above case

"In the above case it was held that the order imposing such penalty is quasi-criminal in nature and **'Concealment of Income' and 'Furnishing Inaccurate Particulars', both refer to deliberate act on the part of the assessee.** In substance, the Court expressed the view that *mens rea* is essential ingredient for invoking provisions relating to the Concealment Penalty. Therefore, this became one of the major defences for the assessee in the matter of levy of Concealment Penalty.

The Supreme Court in Dilip N. Shroff's case (supra) had found in the facts of the case that there was no intent to conceal income in the absence of "enough materials to show that the action on the part of the appellant may not be said to be such which would attract penal proceedings and also that only because of difference of opinion between the two valuers, the assessee cannot be charged for concealing either the particulars of income or furnishing inaccurate particulars under Sec. 271(1)(c) of the Act".

In the case of **CIT vs. Reliance Petroproducts Pvt. Ltd [(2010) 322 ITR 158 (SC)]**, the Apex Court had an occasion to deal with a situation, whether penalty could be levied in a case where merely because the disallowance of expenditure/claim of deduction or addition to income is confirmed by the Appellate authority

The assessee is a company and the relevant Assessment Year is 2001-02. The Return was filed on 31.1.2001 declaring loss of Rs.26,54,554/-. This assessment was finalized under Section 143(3) of the Act on 25.11.2003 whereby the total income was determined at Rs.2,22,688/-

In this assessment the addition in respect of interest expenditure was made. Simultaneously penalty proceedings under Section 271(1)(c) of the Act were also initiated on account of concealment of income/ furnishing of inaccurate particulars of income. The said expenditure was claimed by the assessee on the basis of expenditure made for paying the interest on the loans incurred by it by which amount the assessee purchased some IPL shares by way of its

business policies. However, admittedly, the assessee did not earn any income by way of dividend from those shares. The company in its Return claimeddisallowanceoftheamountofexpenditure forRs.28,77,242/-invokingtheprovisionsof14Aof the Act.

This disallowance was deleted by the Commissioner of Income Tax (Appeals) [CIT (A)], however the Tribunal confirmed the order of the CIT (A) by holding that, merely because the interest has been confirmed by the Tribunal that does not mean that the assessee has concealed the income or filed the inaccurate particulars thereof. The order of the Tribunal was challenged by the Revenue authorities before the High Court. The High Court considering the concurrent findings of appeal filed by the CIT (A) and the Tribunal dismissed the appeal filed by the Revenue. Under these circumstances, the issue came up before the Division bench of the Apex Court at the instance of the Revenue.

The arguments of the revenue before the Apex Court were

- As the claim made for the interest expenditure was not accepted by the assessing officer nor by the Appellate Authority and, therefore, it was obvious that the claim did not have any basis and was made with the ***mala fide intentions*** and was totally without legal basis.
- The expenditure could not have been claimed as only the interest paid in respect of capital borrowed for the purposes of the business or profession could have been claimed and it was clear that the interest in the present case was not in respect of the capital borrowed. Further, it was submitted that section 14A of the Act, also provides that no deduction could be allowed in respect of the expenditure incurred which does not form part of the total income under this Act.

The arguments made by the assessee before the Apex Court were

- That the language of section 271(1)(c) of the Act had to be strictly construed. The section being a taxable statute and more particularly a penal provision it must be strictly construed. In other words it was submitted that unless the wording directly covered the factual situation in the appeal, penalty u/s 271(1)(c) of the Act cannot be levied.
- That there was no concealment or any inaccurate particulars regarding the income submitted in the return.

SC observed that the terms "furnishing inaccurate particulars of income" is not defined in the Income-Tax Act, but reading the words in conjunction they must mean the details furnished in the returns are not accurate. The apex court further observed that Reliance Petroproducts has furnished all details of its income.

The SC ruling went in favour of Reliance Petroproducts. The apex court held that the *I-T department cannot levy penalty on a taxpayer if his claim for deduction is not acceptable to the tax authorities.* Penalty is leviable only if there is proven concealment of income.

In this case**, the I-T officials had rejected the company's claim for deduction** on its interest expenditure and levied a penalty on the ground of furnishing inaccurate particulars of income. Under the I-T Act, furnishing inaccurate particulars of income attracts a penalty. In the department's view making incorrect claims is the same as furnishing incorrect income details.

According to **the I-T department, the interest expenditure did not merit deduction** because I-T laws provide for deduction only for interest paid for capital borrowed for the purpose of business or profession. The interest payments in this case did not fall into this category and hence was not deductible. Therefore, the claim for deduction is incorrect.

Reliance Petroproducts took the stand that **the I-T laws do not provide for penalty unless there is a concealment of income or furnishing of incorrect details of income**. The company also pointed out that its interpretation of the issue had been accepted by an appellate commissioner and the Income-Tax Appellate Tribunal in the previous year.

SC observed that the terms "furnishing inaccurate particulars of income" is not defined in the Income-Tax Act, but reading the words in conjunction they must mean the details furnished in the returns are not accurate. The apex court further observed that Reliance Petroproducts has furnished all details of its income.

It was suggested that by making incorrect claim for the expenditure of interest, the assessee has furnished

inaccurate particulars of income. Dealing with this contention, after referring to the dictionary meaning of the word 'particulars', the Court stated that the same used in S. 271(1)(c), would embrace the meaning of the details of claim made. It is an admitted position that in the present case no information given in the return was found to be incorrect or inaccurate. It is not, as if, any statement made or any details supplied were found to be factually incorrect. Therefore, at least, prima facie, the assessee cannot be made guilty of furnishing inaccurate particulars of income. The court further, observed that if the contention of the Revenue is accepted by the assessing officer for any reason, the assess would be penalized u/s 271(1)(c) of the Act which cannot be the intention of the Legislature.

**Summation**

After the judgement of the Apex Court it is now finally concluded that merely making/preferring a claim of deduction or expenditure which is not sustainable in law or which is not accepted by the Revenue authorities by itself will not amount to furnishing inaccurate particulars of income within the meaning of provisions of section 271(1)(c) of the Act.

The Hon'ble Apex Court in the case of **Sree Krishna Electricals vs. Sate of Tamil Nadu & Anr. [(2009) 23VST 249 (SC)]** held that when certain items were duly incorporated in the books of account though not included in the return furnished or by claiming exemption of such turnover, there was no case for imposing a penalty.

Debit of patently disallowable items like payment of income-tax or write off of a capital asset like equipment in the books were not adjusted in the income reported in the return. Considering that the assessee was a company, which can be presumed to have professional assistance in computation of its income subject to compulsory audit, the High Court in **CIT vs. Zoom Communications P. Ltd. [2010] 327 ITR 510 (Delhi)** restored the penalty deleted by Tribunal. The High Court referred to the decision of the Supreme Court in **CIT vs. Reliance Petroproducts Pvt. Ltd [(2010) 322 ITR 158 (SC)]** and did not accept the explanation that the mere fact that the factual information was already available in the P&L A/c should spare penalty.

Let me now refer to the decision of the Lordship of **Delhi High Court in the case of CIT vs Mahanagar Telephone Nigam Ltd.**. In the said case, the honorable High Court held as under:

"The AO imposed section 271(1)(c) on the ground that the assessee had filed "inaccurate particulars" by wrongly (i) claiming deduction for contribution to a 'staff welfare fund' despite the bar in section 40(A)(9) and the qualification of the auditors and (ii) claiming depreciation on vehicles 25% though the prescribed rate was 20%. The assessee argued that despite section 40(A)(9), the payment to the fund was allowable as "business expenditure" and that the higher depreciation was claimed on the basis that the vehicles were "plant and machinery" despite the lower rate prescribed for vehicles in the Rules. The CIT(A) & Tribunal deleted the penalty. On appeal by the department, HELD dismissing the appeal:

There is no finding by the AO that the assessee furnished inaccurate particulars and that its explanation was not bonafide. Accordingly, the imposition of penalty u/s 271(1)(c) was a "complete non-starter". A mere erroneous claim made by an assessee, though under a bonafide belief that, it was a claim which was maintainable in law cannot lead to an imposition of penalty. The claim for deduction was made in a bonafide manner and the information with respect to the claims was provided in the return and documents appended thereto. Accordingly, there is no furnishing of "inaccurate particulars". Making of an incorrect claim for expenditure does not constitute furnishing of inaccurate particulars of income (Reliance Petroproducts 322 ITR 158(SC) followed"

Where the assessee had claimed a deduction knowing that they were incorrect, such a claim would be vulnerable for penalty to the extent, that the taxable income gets reduced. Concealment would therefore be either by way of under-statement of income or by a claim, which is inadmissible. Further the Apex Court while dealing with the penal provision of section 271(1)(c) of the Act held that no fault could be found with the reasoning in the judgement in Dilip N. Shroff (supra), where the Court explained the meaning of the terms "conceal" and "inaccurate" in the judgement. It was only on the point of *mens rea* that the Dilip N. Shroff (supra) was upset. The word "inaccurate particulars" in section 271(1)(c) of the Act means that the details supplied are not accurate, not exact or correct, not according to the truth or erroneous. In absence of such finding penalty u/s 271(1)(c) of the Act is not leviable.

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# JUDICIAL ANALYSIS

## INTERESTING DECISIONS UNDER S.40(A)(IA) OF THE ACT.

- **DCIT *v.* S.K. Tekriwal ([2011] 15 taxmann.com 289 (Kol.))**

**Advocate Tushar Hemani**
*The author is practising advocate. He can be reached at tusharhemani@gmail.com*

**xxx...**

**3.** We have heard rival submissions and gone through facts and circumstances of the case. The brief facts are that assessee is engaged in the business of construction of bridges, roads, dams and canals, and heavy earth moving activities in contract with government and semi-government bodies, such as, BRO, PWD, NTPC etc. Return of Income was filed on 27.10.2007 showing total income at Rs.45,49,360/-. During the course of assessment proceedings, A.O noticed that the assessee has debited total payments of Rs.3,37,37,464/- in the P&L a/c under the head 'machine hire charges'. The Assessing Officer also found that the assessee has deducted tax @ 1% on such payments, therefore, he required the assessee as to why tax u/s. 194-I of the Act was not deducted. It was explained before the Assessing Officer that payments were made to sub-contractors for completion of specific work; and therefore, tax was deducted @ 1% as per the provisions of section 194C(2) of the Act. The payments were not made for hiring of machines, but, the same have been wrongly grouped under the head 'machine hire charges'. Copies of agreements with the concerned parties were filed at the assessment stage to show that they were sub-contractors, who were assigned specific work; and that the payments do not actually relate to hiring of machines. The Assessing Officer did not accept the explanation. The Assessing Officer observed that it was clearly mentioned in the agreements that the rate are exclusively for machine and maintenance, all material will be supplied by us. The Assessing Officer concluded that the payments were made for hiring of machines, and that the provisions of section 194-I of the Act are applicable in the case of the assessee and so, tax should have been deducted @ 10%. The Assessing Officer then made proportionate disallowance under the provisions of section 40(*a*)(*ia*) of the Act in respect to 'machinery hire charges'. Aggrieved, assessee preferred appeal before CIT(A).

**4.** The CIT(A) deleted the disallowance by holding the 'machinery hire charges' expenses falling u/s. 194C(2) of the Act, by holding as under:

"7. I have considered the assessment order and the submission of the appellant. I have also perused the assessment record. The AO has relied solely on the accounting entries made in the books of account in as much as the sub-contract expenses are clubbed under the head 'machine hire charges'. The AO has confined himself only to a particular line mentioned in the agreement; but, has failed to properly analyze the agreement in its totality. The nature and particulars of work that has been assigned to each sub-contractor is clearly specified in the agreement, which includes back filling, gravel filling, morum/ sand filling and rubber soiling; excavation with transportation; PCC, RCC and Dewatering; Pile & Open foundation work; Earthworks in filling from earth-quarry to works-site with all lift in layers as

approved by the Railways, including all machineries &equipments and manpower regarding earth transportation, loading & unloading; and, providing RCC M-30 grade in well curb using concrete mixture and manual means and machinery and completing the job as per specification and direction of E/I.

In each of the agreements, the quantity of work is fixed, and, the rate is also fixed on the basis of such quantity of work. I find substance in the argument that hire charges depend on the time period for which the machines are used. But, in the present case, the time consumed by the sub-contractors, or the period for which the machines are used, is not at all a factor in deciding the payments made to the sub-contractors; it is only on the basis of the quantity of work that the payments have been made. The sub-contractors are required to complete the assigned job by utilizing their machines and equipments, and also, by employing local labour. But then, the time period for which the machines and equipments are used has no role in deciding the payments made to the sub-contractors; moreover, labour charges are paid by the sub-contractors, and, the sub-contract expenses debited in the books of account of the appellant do not include labour charges. It was contended before me that the nature of work assigned to the subcontractors is such that there was actually no requirement of any material in completion of the work, except for providing RCC M-30, where the principal employer itself has supplied the required material (iron and cement) for quality reasons. It was also argued that the payments made to the sub-contractors have been shown by them as receipts from sub-contract work. The P & L a/c, Computation of Income, etc., in respect of some sub-contractors is available in the assessment record, e.g., Archana Shah, Julie Agrawal and SwetaAgrawal. I find that they have shown the payments made by the appellant to them as receipts from sub-contract work, and, offered profit @ 8% on such receipts.

The decision of the AO is not based on proper findings. The AO has confined himself only to the accounting entries made in the books of account, and failed to properly analyze the material on record. The explanations, and also the evidences, submitted by the appellant seem to have been summarily rejected more on ground of presumption and assumption than on factual ground. This has led the AO to a state of affairs where salient evidences have been overlooked. In view of the above, I am of the opinion that the payments of Rs.3,37,37,464 were made to the sub-contractors, and, that the provisions of section 194C(2) are applicable in the case of the appellant. Since the appellant has deducted tax @ 1% on such payments, which is in conformity with the provisions of section 194C(2), the provisions of section 40(*a*)( *ia*) are not attracted. The addition is directed to be deleted. The grounds raised by the appellant are liable to be allowed."

Aggrieved, revenue is in appeal before us.

**5.** From the order of CIT(A), we find that CIT(A) has gone into the controversy of assessee falling under the head 'sub-contractor' or falling under the head 'rent', the expenses made under the head 'machinery hire charges'. It is also a fact that the assessee has deducted TDS u/s. 194C(2) of the Act and covered itself under the head 'sub-contractor'. We find that CIT(A) after verifying records and explanation submitted by assessee reached to a conclusion that payments are in the nature of contract payments made to sub-contractors. On merits, we are in agreement with the findings of CIT(A) and even revenue before us could not controvert the same. Another facet of this issue is that once the assessee has deducted TDS u/s. 194C(2) of the Act, whether disallowance can be made by invoking the provisions of section 40(*a*)( *ia*) of the Act. The relevant provision reads as under:

"40(*a*)( *ia*) any interest, commission or brokerage, rent, royalty, fees for professional services or fees

for technical services payable to a resident, or amounts payable to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work), on which tax is deductible at source under chapter XVII-B and such tax has not been deducted or after deduction has not been paid on or before the due date specified in sub-section (1) of section 139:"

In this provision it is provided that where in respect of any sum, as referred in this section, tax has not been deducted or after deduction has not been paid on or before the due date specified in sub-section (1) of section 139 of the Act, such sum shall be disallowed as a deduction while computing the income of the assessee for the previous year relevant to AY under consideration. But in the present case before us, the assessee has deducted tax, although u/s. 194C(2) of the Act and it is not a case of non-deduction of tax or no deduction of tax as is the import of section 40(*a*)(*ia* ) of the Act. Even otherwise if it is considered that this particular sum falls under section 194I of the Act, it may be considered as tax deducted at a lower rate and it cannot be considered a case of non-deduction or no deduction. Similar view is taken by **'C' Bench of Mumbai ITAT in IT Appeal No. 20 (Mum.) 2010 in the case of *Dy. CIT* v. *Chandabhoy & Jassobhoy* dated 8-7-2011**, wherein it is held that there is no dispute with reference to the deduction of tax u/s 192 of the Act with the fact that the alleged consultants, in their individual assessments declared these payments as salary payments and accepted by revenue as it is. Further, it is held that the assessee had deducted tax u/s. 192 of the Act as against the allegation of revenue that the provisions of section 194J of the Act would be attracted as these consultants are in the capacity of professionals. The Bench held that the provisions of section 40(*a*)(*ia*) of the Act will not apply as the said provision can be invoked only in the event of non-deduction of tax but not for lesser deduction of tax. In that case the assessee has deducted tax u/s. 192 of the Act as against section 194J of the Act as against the claim of revenue.

**6.** In the present case before us the assessee has deducted tax u/s. 194C(2) of the Act being payments made to sub-contractors and it is not a case of non-deduction of tax or no deduction of tax as is the import of section 40(*a*)( *ia*) of the Act. But the revenue's contention is that the payments are in the nature of machinery hire charges falling under the head 'rent' and the previous provisions of section 194-I of the Act are applicable. According to revenue, the assessee has deducted tax @ 1% u/s. 194C(2) of the Act as against the actual deduction to be made at 10% u/s. 194-I of the Act, thereby lesser deduction of tax. The revenue has made out a case of lesser deduction of tax and that also under different head and accordingly disallowed the payments proportionately by invoking the provisions of section 40(*a*)(*ia*) of the Act. The Ld. CIT, DR also argued that there is no word like failure used in section 40(*a*)( *ia*) of the Act and it referred to only non-deduction of tax and disallowance of such payments. According to him, it does not refer to genuineness of the payment or otherwise but addition u/s. 40(*a*)( *ia*) can be made even though payments are genuine but tax is not deducted as required u/s. 40(*a*)( *ia*) of the Act. We are of the view that the conditions laid down u/s. 40(*a*)( *ia*) of the Act for making addition is that tax is deductible at source and such tax has not been deducted. If both the conditions are satisfied then such payment can be disallowed u/s. 40(*a*)( *ia*) of the Act but where tax is deducted by the assessee, even under *bona fide* wrong impression, under wrong provisions of TDS, the provisions of section 40(*a*)( *ia*) of the Act cannot be invoked. Here in the present case before us, the assessee has deducted tax u/s. 194C(2) of the Act and not u/s. 194-I of the Act and there is no allegation that this TDS is not deposited with the Government account. We are of the view that the provisions of section 40(*a*)( *ia*) of the Act has two limbs, one is

where, *inter alia,* assessee has to deduct tax and the second where after deducting tax, *inter alia,* the assessee has to pay into Government Account. There is nothing in the said section to treat, *inter alia,* the assessee as defaulter where there is a shortfall in deduction. With regard to the shortfall, it cannot be assumed that there is a default as the deduction is not as required by or under the Act, but the facts is that this expression, 'on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction has not been paid on or before the due date specified in sub-section (1) of section 139'. Thus section 40(*a*)(*ia*) of the Act refers only to the duty to deduct tax and pay to government account. If there is any shortfall due to any difference of opinion as to the taxability of any item or the nature of payments falling under various TDS provisions, the assessee can be declared to be an assessee in default u/s. 201 of the Act and no disallowance can be made by invoking the provisions of section 40(*a*)(*ia*) of the Act.

Accordingly, we confirm the order of CIT(A) allowing the claim of assessee and this issue of revenue's appeal is dismissed.

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- **ITO vs Ramesh Industries (ITA No. 3148/Ahd/2008)**

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In Revenue's appeal the only issue involved is whether disallowance made under section 40(a)(ia) of the Act would be treated as business profit for the purpose of deduction under section 80IB. The AO disallowed a sum of Rs.7,25,031/- on account of non-deduction of tax. The assessee had made the payments to various parties but had not deducted the tax thereon. The payment was disallowed as per provisions of section 40(a)(ia). He also disallowed the claim of deduction under section 80IB on such addition, arguing that the addition is not business profit and, therefore, assessee is not eligible for such deduction.

9. The ld. CIT(A) allowed the claim of the assessee holding it to be a business income.

10. We have heard the parties and carefully perused the material on record. The issue is directly covered in favour of the assessee by the decision of the Tribunal in the case of **ITO vs. M/s ChiragPlast in ITA No.2415/Ahd/2009 Asst. Year 2006-07** pronounced on 23rd October, 2009 wherein was held as under :-

*"5. Regarding ground No. 2, we are of the considered view that even if addition is sustained, then assessee would be entitled to deduction under Section 80IB as it would be only the business profit. Section 40(a)(ia) falls in chapter (iv) and under "the head computation of business income." Any addition proposed by the Assessing Officer by invoking a provision falling in chapter (iv) under the "Head computation of business income, particularly between section 28 to 43D, would be made under the "Head income from business and Profession" and not under the head "Income from other sources", unless specifically so provided. Accordingly, though proposed by the Assessing Officer on the ground that TDS has not been paid to the account of the Central Government within time is in order, but assessee is entitled to deduction under Section 80IB thereon as it would be only a part of business profit. The argument of the Learned DR that assessee may claim benefit again on payment basis is premature and academic as there are enough legal recourses open to prevent such claims. As a result we do not find any force in this ground raised by the revenue. The same is dismissed."*

Since the facts and circumstances of the case are the same, following above decision we, uphold the order of ld. CIT(A) and dismiss the ground raised by the Revenue.

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# Commercial Aspects of Civil Construction

**CA. Sandesh Mundra**
*The author is practising since 2004. He can be reached at sandeshmundra@gmail.com*

**Stores Controls at the Construction Site Series on Construction was started in March, 2011 with following topics:-**

a. Accounting policies and Standard for construction industry.
b. Tendering and Budgeting
c. Direct Tax Aspects
d. Service Tax Aspects for Civil Contractors
e. Service Tax Aspects for Builders and Real Estate Developers
f. Practical Illustrations on VAT and Service Tax
g. VAT and the construction sector
h. Inter-state Works Contracts
**i. Internal Controls at Construction Site**
   1. Human Resource
   2. Stores
   **3. Engineering**
   4. Commercial Procurement
   5. Account
j. Structuring of sales invoice
k. Applicablity of Labour Laws to the sector
l. Designing MIS Systems for a civil construction company
m. Project Completion
n. Relevance of Information Technology to the construction sector
o. Banking requirement of the sector
p. Insurance needs of the sector
q. ISO Implementation and Process Documentation
r. Planning Internal Audit of a construction site

**This month's topic is –**

***Internal Controls – Role of Engineering Department***

As far as internal controls are concerned, role of Engineering Department is very crucial. The project manager usually is an Engineer and is the chief architect behind running the project. He is responsible for taking crucial decisions at the site. Many a times the decision making has to be very quick. Various points to be taken care have been bifurcated into two broad headings:-

1. Engineering on day to day basis
2. Project Completion

**1. Engineering - Day to Day basis**

1.1 Study of Tender Terms

1.2 Additional Points to be kept in mind (Mainly by sub-contractors)

1.3 Mobilization at Site

1.4 Availability of Drawing, Front for Work

1.5 Understanding the rules and prevailing norms in the Client Environment

1.6 Work Planning Daily / Weekly / Monthly

1.7 Pre planning for FIM / Own Material

1.8 Joint Measurement Report (JMR) – Work completion & Extra work

1.9 Sub Contractor Work Order

1.10 Client & Sub Contractor billing and Certification

1.11 Monthly Reconciliation – FIM & Principal Material and related issues

**1.12 Preventive action for Malfunctions**

**2. Checklist for Project Completion**

2.1. Final bill preparation and certification

2.2. FIM and Raw Material Reconciliation with bill and balance qty.

2.3. Fulfillment of Client Work Completion Procedures

2.4. Receivable & Liability Status Clearance

2.5. Statutory compliances

2.6. Delayed submission of Final bill

## 1. Engineering:

As far as engineering role is concerned, tender is the first document to be properly studied and analysed so that the project revenue is structured so as to match the cash outflows involved in executing the project.

### 1.1. Study of Tender Terms & Conditions

Following points need proper study in order to give a proper quote:-

| S. N | Details sought for | Catch |
|---|---|---|
| 1 | Work order Value – Permissible Variation / LD Clause | Variation Limits should not be more than 25%. Further LD clause should not have a upper limit of more than 10%. If LD clause exists , contractor may insist upon Incentive Clause for timely or early completion. |
| 2 | FIM - RMC / Cement / Steel? market rates | Wastage Norms as per Standard, Debit Rates as per |
| 3 | Work completion period availability of drawings and work front | Delay to be ignored if the same is due to delay in |
| 4 | Facilities from the Client - Labour colony, Land, Power & Water supply. | Whether Free / Chargeable. Availability at Single Point / Multiple Points |
| 5 | Billing period cycle, Bill certification period and advance payment percentage against bill submission and post certification | Third Party Certification should not be a necessary requirement for release of payment. Atleast 70% adhoc should be released against uncertified bills. |
| 6 | Check whether any prescribed format for client bill? | Compliance with laws – Formats permissible under VAT and service tax to be seen. |
| 7 | Whether the job is new or left over one? | Investigation required if it's a left over job where the cost is expected to be higher. |
| 8 | Safety / Quality Norms | Impact on Time and Money as different clients have different ground level disciplines. |
| 9 | What are the requirements with each RA bill? | Agencies / Department involved in Certification |
| 10 | What are the rates of principal items (like Excavation, RMC supply, Shuttering etc.) | Higher Margins may be kept in some of the initial items to take care of initial cost of set up. |
| 11 | What deductions shall be made by client from RA bill | Only those agreed as per WO. Adhoc deductions should not be entertained and clearly objected by way of written communication. |
| 12 | Service tax / VAT / WCT extra or inclusive? | Exemptions – Paper Work / State specific norms to be made clear |
| 13 | Whether running plant expansion or construction of new plant building? | Cost of doing a job in an already running plant i.e. plant expansion may be higher due to scarcity of space available for work execution. |

| | | |
|---|---|---|
| 14 | Physical visit of the work locations | This is necessary to understand Local Material Rates / Terrain for Equipments / Labour colony area / Distance from the city. |
| 15 | Internal Logistics | Location of Porta Cabin where the office set up is to be done vis-a-vis Client office / Labour Colony / Batching Plant / Store |
| 16 | Bank Gaurantee | Amt / Performance / Time Validity |
| 17 | Mobilisation Advance | Normally 5-10% advance should be released. However advance recovery should not be in equal instalments but in proportion to the monthly bills. |

**1.2. Additional Points to be kept in mind mainly by sub-contractors**

**1.2.1.** Ensure to avoid the Tendency of main contractor to pass on all the scope to the sub-contractors without proper rates.

**1.2.2.** Sometimes we may find that even fabrication is a part of the drawings and has to be done at no extra cost.

**1.2.3.** Linking the payment for the extra work with the corresponding payment to the main contractor is a pitfall.

**1.2.4.** Reduction in W.O duration without increase in rates is not acceptable.

**1.2.5.** Instead of specifications like best material or best quality, it is always advisable to specify the make or brand or give full specifications in the work order to avoid any dispute at a later stage.

**1.2.6.** If there is a clause for inspection by third party, then the third party will come at its on leisure. Payment should not be withheld for want of third party inspection and It should be routine exercise.

**1.2.7.** Unless actual inspection of the site is carried out, it should not be confirmed to have been done.

**1.2.8.** If any guarantee against any risk or damage is accepted, its better to find out if the risk is insurable. And if yes, then the cost needs to be factored into at the time of rate finalisation.

**1.2.9.** Liquidated damages should always be subject to a maximum overall cap.

**1.2.10.** Escalation clause is required if job duration is more than 9 months

**1.2.11.** If job extends beyond schedule for reasons/ delay attributable to client or the main contractor, it is advisable to demand compensation for the same.

**1.2.12.** Future changes in tax laws should be considered.

**1.3. Mobilization:**

As a Project manager, one has to jot down the resources required to execute the project. Sometimes due to shortage or non availability of resources, project can suffer despite rates being good. Following resources should be taken care of and quantity assessed both initially and also at the time of peak months :-

**1.3.1.** Skilled and unskilled labour strength required.

**1.3.2.** Staff with designation required for the site at the time of startup.

**1.3.3.** Type of machineries and equipments required (Like – JCB & Loader, Batching plant capacity, Miller, Crane, etc.).

**1.3.4.** Types of vehicles required (Like – Staff Bus, Sumo, Utility, Trailer, Tractor & Dumper, Bike etc.).

**1.3.5.** Computer or Laptop systems, Printer/Scanner/ Copier, Data card or Broad band required at the site.

**1.3.6.** Assessing which telecom service provider's network is better in the local area(Vodafone / Airtel / Tata – Docomo / BSNL) and the number of connections required.

**1.3.7.** Availability of portable cabin / readymade office at the site. Whether the company needs to build or arrange Container on its own is to be decided.

**1.3.8.** Staff Camp / Mess system and the expected cost. Further number of staff who shall be staying out of company accommodation and HRA decision to be done in their case.

**1.4. Availability of Drawing, Front for Work:**

After the site mobilization, the project manager needs to strongly follow up for drawings and work front from the client. Many a times work is started without availability of drawings as a result of which the work could be delayed affecting the work performance and profit margins adversely. For any delay client needs to be communicated accordingly.

**1.5. Understanding the rules and norms in the Client Environment:**

It is very important to understand the procedures and requirements to perform work in client locations, like

**1.5.1.** Whether work location is required to be inspected by client's safety department

**1.5.2.** Details of Personal protection equipments (PPE) required

**1.5.3.** What are the other safety norms to be taken care of? Client may have a mechanism of raising safety debit noted for safety violations. The same can be passed on to the sub-contractors accordingly.

**1.5.4.** Whether test or certified agency certificates are required to use Tools or equipments?

**1.5.5.** Cube Testing discipline, if the contractor has its own batching plant.

**1.6. Work Planning Daily / Weekly / Monthly:**

**1.6.1.** Without goals and planning, the work can never be completed within the agreed time frame i.e., "*Where there is no goal & planning, no Achievement*". Goals need to be set on Daily / Weekly and Monthly basis after discussion with the staff and then everything has to go after that need to achieve the same. If the Work is being carried out without effective goal and planning, no effective output can be achieved.

**1.6.2.** Also it is necessary to review Daily / Weekly & Monthly Plans so as to ensure work completion within time.

**1.6.3.** When we plan for work – we need to keep in mind - client priority, availability of resources, availability of drawing & front, weather, Funds etc.

**1.7. Pre planning for FIM / Own Material:**

Pre planning (system and procedure) is required for FIM and Own material so as to make it available in time at the time of opening the work front.

**1.8. Joint Measurement Report (JMR) – Work completion & Extra work:**

Joint measurement report (JMR) needs to be signed by the Client / Consultant after completion of work. This is required in monthly client bill. Daily work progress report (DPR) needs to be prepared for all site locations from all concerned engineers and supervisors of client. This needs to be prepared sub contractor wise so that monthly bills of client and sub contractor are prepared easily and within time frame.

**1.9. Sub Contractor Work Order:**

Sub Contractor work orders should be prepared with original at HO and a copy at site. Item codes and language should be as per client work order so that reconciliation becomes easy. If rate is revised, amendment paper should be prepared to avoid any dispute later on. Project Manager and Project commercial head / Project Director need to jointly approve any such amendment. Many a times it may happen that work allotted to the sub-contractors are broken down into various components. In such cases one may say that it is difficult to track the comparison between client qty and sub-contractor qty. Following example would make things clear:-

***For example:***

| Item Code | As per | Item description | UOM | Rate |
|---|---|---|---|---|
| 1234 | Client | Providing reinforcement including cutting, bending, binding, fixing in position including the cost of channels, bars (Binding Wire is in your scope). | MT | 4500 |

***FIM or Raw Material shall be provided to contractor for work by Company:***

| | | | | |
|---|---|---|---|---|
| 1234-A | Contractor | Reinforcement Cutting | MT | 700 |
| 1234-B | Contractor | Reinforcement Bending | MT | 800 |
| 1234-C | Contractor | Reinforcement Fixing | MT | 1200 |
| | **Contractor** | **Total Rate of item code-1234 is ——>** | **MT** | **2700** |

**1.10. Client & Sub Contractor billing and Certification:**

Billing period / Frequency should be same for client & the sub contractor so that quantity reconciliation can be done at periodic intervals.

Client Running Accounting (RA) bill should be prepared and submitted in time frame so that its certification is done in time and funds are released timely otherwise once the cycle is disturbed, then it shall affect fund management adversely throughout the project.

Delayed client billing in turn shall affect sub contractor billing and quantity comparison of client with sub contractor. Many a times as a result of this delay excess quantity is given to sub contractor as compared to client billing which shall adversely impact the project profitability.

**1.11. Reconciliation – FIM & Principal Material:**

Wherever running accounting bill is prepared for the client, one needs to prepare reconciliation statements to match balance quantity for FIM and own purchases (Major Raw Materials only) to avoid discrepancies and revenue loss. The issue here is assessment of physical quantities lying at the site especially in case of steel, for which an experienced supervisor is required.

If material consumption by the sub-contractor goes beyond standard norms then the same needs to be passed on to the respective sub-contractor. However for this, material issue mechanism and the controls have to be set accordingly right from the start of the project. The only challenge that remains is regarding transfer of material from one contractor to another at the site, for which an experienced stores personnel is required.

**1.12. Preventive action for Malfunctions:**

| S. N. | Particular | Malfunction | Preventive Action |
|---|---|---|---|
| 1 | Material procurement | Project Manager / Site Incharge or Commercial incharge can procure material at higher rates. | a) Watch on MIS<br>b) Monitoring the budget<br>c) Purchase Rate Audit<br>d) Major purchases to be handled centrally. |
| 2 | Misuse & Wastage of Material | Site Engineer may consume material more than the standard norms example – Plywood and Batton etc. | a) Monthly Reco of Material consumption.<br>b) Watch on Budget |
| 3 | Pmt of excess quantity | Engineer can give excess quantity to contractor than claimed from client | Client vs Contractor Quantity MIS |
| 4 | Company resources | Theft / Pilferage at site | Timely physical verification by internal auditor. |

## 2. Checklist for Project Completion

### 2.1. Final bill preparation and certification:

Final bill can be timely prepared If following issues are properly taken care of:-

- Cumulative Executed Quantity.
- All pending extra item claims should be included, if pending.
- Necessary follow up for W.O amendment if Actual Qty > WO Qty.
- Release of Qty on Hold for want of various reasons.
- Fight for the incentive clause.
- If any company asset is given on rental / hire basis to other party as per instruction from client, the same should be claimed in final bill.
- If resources like equipment / manpower have remained ideal due to non availability of front, it should be claimed in the final bill.
- NOC shall have to be obtained from various departments of the client

### 2.2. Final FIM and Raw Material Reconciliation with bill and balance qty.:

***Formula:***

- Total Material Inward
- Less: Material Returned / Transferred
- Less: Standard Consumption = Balance Quantity at Site / Store
- Less: Standard Scrap Generation
- In case this quantity is not available at site / store, there could be various possibilities:-
  - Excess consumption as compared to standard
  - Theft / Pilferage during the project
- In case of excess consumption, some portion can be recovered from the measurement contractor, if not recovered till date.
- Proper justifications are required from the project manager and appropriate action should be taken in case of abnormal difference between actual and standard balance
- Balance FIM material which shall not be used needs to be returned with sign and stamp from the client.

### 2.3. Fulfillment of client work completion procedure:

In case of project completion, client to have checklist for the same so the contractor needs to ask the same from the client and compile each point accordingly.

### 2.4. Receivable & Liability Status Clearance:

Get status of project liability with break up of nature of creditor and special remark for local creditors. It is best suited if ledger confirmations for the same are obtained.

- Follow up for payment receivable from client after bill certification
- Clear local liabilities to avoid any demobilization harassment from them.

### 2.5. Statutory compliance:

Follow up and get pending WCT & TDS receivable certificates from client.

- Give all necessary details for VAT return filing to local sales tax consultant and other details, if any required for audit.
- Get any pending forms like C & F from the department, also reconcile with the forms issued till date.
- Clear o/s local pending liabilities like Road tax, Entry Tax, Employee Professional Tax etc.

### 2.6. Possible reasons for delayed submission of Final bill:

| S. N. | Points | Corrective Action |
|---|---|---|
| 1 | Non updation of FIM data with stores. | Physical verification of FIM with stores records. |
| 2 | Reconciliation of FIM | Required with each RA Bill. |
| 3 | Work order Amendment | Some foresightedness and Strong Follow up with the client. |
| 4 | Change in Project Manager / Billing Engg. | Regular documentation<br>Proper Back up practice at HO<br>Process Checklist |
| 5 | Proper compilation of Hard and soft copies of all the Running Bills | Data Control and Regular Audit. |

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# INTERNATIONAL TAXATION

## Bangalore Tribunal rules on transfer pricing issues related to intra-group software development services

**CA. Dhinal A. Shah**
*The author is Central Council Member of ICAI. He can be reached at dhinal.shah@in.ey.com*

**CA. Nehal Sheth**
*The author is practising since 2002. He can be reached at nehal.sheth@in.ey.com*

The Bangalore Income-tax Appellate Tribunal (Tribunal), in the case of Kodiak Networks (India) Private Limited has adjudicated on certain transfer pricing (TP) issues with respect to transactions entered into by the Assessee with its associated enterprise (AE) for provision of software development services. The Assessee is an Indian company engaged in providing software development services to its AE. The Assessee's transfer pricing documentation supported an operating profit of 10.70% on operating costs as an arm's length price (ALP) for provision of services to the AE for the year under dispute (Assessment Year 2006-07). The Assessing Officer determined the arm's length margin at 19.13% during audit proceedings. The Assessing Officer rejected the economic analysis undertaken by the Assessee on various grounds and undertook a fresh comparability analysis based on data and information not available to the Assessee while preparing the documentation. Specifically, the Assessing Officer modified the screening filters used by the Assessee for selecting comparable data and introduced additional comparables after obtaining information that was not available in the public domain. In addition, the Assessing Officer denied the benefit of the 5% range applicable to the audit year.

The Tribunal upheld the use of data that was not available at the time of document preparation as well as the powers of the Assessing Officer to use information that is not in the public domain. The Tribunal however held that the Assessing Officer is required to furnish the information that is not in the public domain to the Assessee so the Assessee has an opportunity to provide objections, if any, against use of such data. The Tribunal upheld the Assessee's contention on the need to apply quantitative criteria for screening comparables based on the size/ turnover of the Assessee as the criteria could have a bearing on comparability. The Tribunal also upheld the need to provide the benefit of the 5% range to the Assessee based on the law that was applicable for the relevant year.

The Tribunal remanded the matter back to the Assessing Officer for re-determination of the ALP based on the guidance articulated above.

### Background and facts of the case

The Assessee, an Indian company, is engaged in providing software development services to its AE. Based on a TP study conducted for the relevant year, the Assessee determined that its transactions with the AE were arm's length in nature. The Assessee used the Transactional Net Margin Method (TNMM) with operating profit on operating cost as the profit level indicator (PLI) for the TP analysis. The Assessee also relied on the 5% range that was available under the provisions of the ITL for the relevant year.

During audit proceedings, the Assessing Officer conducted a fresh comparable search based on information that was not available to the Assessee while preparing the documentation as well as introduced additional comparables based on information that was not in the public domain. The Assessing Officer made an upward TP adjustment to the value of the international transactions undertaken by the Assessee without giving the benefit of the 5% range.

Being aggrieved by the Assessing Officer's order, the Assessee filed objections with the Dispute Resolution Panel (DRP), an alternate dispute resolution mechanism under the ITL. The DRP broadly upheld the TP adjustment proposed by the Assessing Officer.

The Assessee filed an appeal before the Tribunal, the second-level appellate authority, against the TP adjustment.

**Contentions of the Assessee**

The Assessee argued that the Assessing Officer arbitrarily selected comparables / companies in exercising his powers under the ITL for seeking information that is not in the public domain. The Assessing Officer did not provide the basis for selection of the companies he used. The Assessing Officer also did not provide the Assessee with information obtained with respect to all the cases, but restricted the information only to those cases from which he used data in his analysis. Hence, there was a violation of the principle of natural justice such that the Assessee has the right to review and object to information used against it by the Assessing Officer. In addition, the Assessing Officer did not establish whether the information obtained was authentic and complete. The Assessing Officer also used data/ information that was not available to the Assessee while preparing the TP documentation.

The Assessee also contended that size of an enterprise is to be examined for comparability purposes. Companies operating on a large scale benefit from economies of scale, higher risk taking capabilities and robust global delivery and business models compared to small or medium sized companies. Thus, the impact of differences in size should be removed by applying a quantitative screen based on size/ turnover. Based on reports of Dun & Bradstreet and the National Association of Software & Services Companies (NASSCOM) that categorize companies in the industry by size, the Assessee proposed a screening filter consistent with the industry standard of the small size/tier 3 category. As the Assessee is in the small size/ tier 3 category, the size/ turnover used in the standard industry analysis for this category should be used as a quantitative criteria for screening comparables.

The Assessee also contended that it should be given the benefit of the 5% range in accordance with the provisions of the ITL applicable at the time of the transactions.

**Contentions of the Assessing Officer**

With regard to information that was not in the public domain, the Assessing Officer argued the copies of notices that were issued to the companies as well as the copies of the replies received from companies were given to the Assessee on a CD for its comments. The Assessing Officer proposed to accept/reject these companies as comparable based on the response received from these companies. The decision of the Assessing Officer based on information collected was also duly communicated to the Assessee. The Assessing Officer is empowered to collect the details relevant to the TP proceedings for better comparability analysis. The Assessing Officer used the data for information that was available to him in the public domain whenever a company did not submit the information.

On the Assessee's contention that a quantitative criteria based on turnover should be used, the Assessing Officer contended there is no evidence to show a correlation between size and profit margins as even small companies in the comparable set have higher profit margins thant large/ established players in the industry.

The Assessing Officer contended the Assessee is not eligible for the benefit of the 5% range as the adjusted TP fell outside the range. The Assessing Officer further argued the subsequent amendment to the ITL by the Finance (No 2) Act, 2009 merely seeks to clarify the existing provision of law on the application of the 5% range.

**Ruling of the Tribunal**

- Use of information not available by the specified date

  The ITL requires a Assessee to maintain TP documentation and such documentation should "as far as possible" be contemporaneous and "should exist latest by the specified date" (i.e., the due date for filing the tax return for the relevant year). The Assessee is only required to maintain

the information and documents as may be necessary relating to the international transactions so that it can be made available to the Assessing Officer. By providing for a "specified date", the obligation is cast upon the Assessee to keep and maintain the documents by that date. The ITL has not provided for any cut-off date up to which only the information available in the public domain has to be taken into consideration by the Assessing Officer while arriving at the ALP. Hence, there is no restriction on the Assessing Officer in using information that is available after the "specified date" for determining the ALP.

- Use of information not available in the public domain

The Assessing Officer is entrusted with powers under the ITL to call for and gather any information required for determination of the ALP. Thus, he can issue notices to parties whom he considers as relevant to gather requisite information. The Assessing Officer need not inform the Assessee about the process used by him for issuing notices in exercise of his powers under the ITL nor is he under the obligation to share all the information. However, the principle of natural justice would require that where any information is sought to be used against the Assessee, the same has to be furnished to the Assessee and only after taking into consideration the Assessee's objections can the Assessing Officer proceed to make a decision. The Assessee should also be provided with an opportunity to cross-examine the party that provided the information to the Assessing Officer.

- Application of the turnover filter

The Tribunal accepted the contention of the Assessee to apply quantitative criteria for screening comparable companies based on size/ turnover relative to the size/ turnover of the Assessee. The Tribunal ruled that as the Assessee, based on turnover, could be categorized as a small size company, the turnover criteria for this categorization as per Dun & Bradstreet industry analysis reports should be used as the screening filter.

The Tribunal, while pronouncing the above, relied on its previous judgment in the case of M/s Genisys Integrating Systems (India) Pvt Ltd [ITA No. 1231(Bang)/2010] where the Tribunal upheld the application of the turnover filter on the basis that a big company would be in a position to bargain the price and also attract more customers. It would also have a broad base of skilled employees who are able to give better output. A small company may not have these benefits and therefore, the turnover also would come down reducing profit margin. The Bangalore Tribunal in the case of Genisys further went on to hold that where loss making companies are excluded from the comparables, then the super profit making companies should also be excluded.

- Benefit of the 5% range

Relying on various judicial precedents on the matter, the Tribunal held that the Assessee was entitled to the benefit of the 5% range based on law applicable for the relevant year.

The Tribunal thereafter remanded the matter back to the Assessing Officer to re-determine the ALP based on the above guiding principles.

**Comments**

Globalization has led many multinational enterprises to establish information technology, research and development (R&D) and back office operations in India. Generally, the Indian affiliates providing services operate as "captive service providers" getting remunerated on a cost plus basis and are insulated from key business risks. Captive service providers have been subject to significant transfer pricing adjustments in the past few years in India.

The approach adopted by the Assessing Officer in selection of comparable data has generally been a contentious issue in most TP controversies. While the ruling recognizes that a Assessing Officer may use data not available in the public domain in a TP audit, it also acknowledges the rights of Assessees to be provided access to the data that is proposed to be used as well as the opportunity to rebut the use of such data, including through cross-examination of the party supplying the data to the Assessing Officer.

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# FEMA UPDATE

## External Commercial Borrowings (ECB) Policy

Ref.: A. P. (DIR Series) Circular No. 51 dated November 23, 2011

Attention is invited to A. P. (DIR Series) Circular No. 19 dated December 9, 2009 relating to the all-in-cost ceiling of External Commercial Borrowings (ECB).

2. On a review of developments in the global financial markets and the fact that borrowers are experiencing difficulties in raising ECBs within the existing all-in-cost ceiling, it has been decided to revise the all-in-cost ceiling for ECB as under:

| Average Maturity Period | All-in-cost over 6 month LIBOR* | |
|---|---|---|
| | **Existing** | **Revised** |
| Three years and up to five years | 300 bps | 350 bps |
| More than five years | 500 bps | 500 bps ( no change) |

* for the respective currency of borrowing or applicable benchmark

3. The enhancement in all-in-cost ceiling is applicable up to March 31, 2012 and subject to review thereafter. The change in the all-in-cost ceiling will come into force immediately. All other aspects of ECB policy remain unchanged.

## External Commercial Borrowings (ECB) Policy – Parking of ECB Proceeds

Ref.: A. P. (DIR Series) Circular No. 52 dated November 23, 2011

Attention is invited to A.P. (DIR Series) Circular No. 26 dated October 22, 2008 relating to the External Commercial Borrowings (ECB).

2. At present, borrowers are permitted to either keep ECB proceeds abroad or remit these funds to India, pending utilization for permissible end-uses. ECB proceeds parked overseas can be invested in liquid assets, such as, deposits or Certificates of Deposit or other products offered by banks (rated not less than AA (-) by Standard and Poor/Fitch IBCA or Aa3 by Moody's), Treasury bills and other monetary instruments of one year maturity having minimum rating as indicated above and deposits with overseas branches / subsidiaries of Indian banks abroad. The underlying principle is that funds should be invested in such a way that the investments can be liquidated as and when funds are required by the borrower. ECB funds may also be repatriated to India for credit to the borrowers Rupee accounts with AD Category I banks in India pending utilization for the permissible end-uses.

**CA. Savan Godiawala**
*The author is practising since 1992. He can be reached at sgodiawala@deloitte.com*

3. Based on a review of the current macro-economic conditions, it has been decided that henceforth the proceeds of the ECB raised abroad meant for Rupee expenditure in India, such as, local sourcing of capital goods, on-lending to Self-Help Groups or for micro credit, payment for spectrum allocation, etc. should be brought immediately for credit to their Rupee accounts with AD Category I banks in India. In other words, ECB proceeds meant only for foreign currency expenditure can be retained abroad pending utilization. The rupee funds, however, will not be permitted to be used for investment in capital markets, real estate or for inter-corporate lending, as hitherto.

4. The amended ECB policy will come into force with immediate effect and is subject to review. All other aspects of ECB policy would remain unchanged.

## Foreign Direct Investment (FDI) in India - Issue of equity shares under the FDI scheme allowed under the Government route

Ref.: A. P. (DIR Series) Circular No. 55 dated December 9, 2011

Attention is invited to the A.P. (DIR Series) Circular

No. 74 dated June 30, 2011, allowing thereby issue of equity shares/ preference shares under the Government route by conversion of import of capital goods, / machineries / equipments (including second-hand machineries) and pre-operative / pre-incorporation expenses (including payments of rent, etc.), subject to terms and conditions stated therein.

2. It has now been decided to amend certain conditions in the aforesaid A.P. (DIR Series) Circular. The amended conditions are given below:

| c.f. A.P.(DIR Series) Circular No. 74 dated June 30, 2011 | Earlier condition | Revised condition |
|---|---|---|
| **Para 3 (I) (d)** | All such conversions of import payables for capital goods into FDI should be completed within 180 days from the date of shipment of goods. | Applications complete in all respects, for conversions of import payables for capital goods into FDI being made within 180 days from the date of shipment of goods. |
| **Para 3 (II) (d)** | The capitalization should be completed within the stipulated period of 180 days permitted for retention of advance against equity under the extant FDI policy. | The applications, complete in all respects, for capitalisation being made within the period of 180 days from the date of incorporation of the company. |

3. All the other instructions contained in the A.P. (DIR Series) Circular No. 74 dated June 30, 2011 shall remain unchanged.

**Foreign Investment in Pharmaceuticals Sector – Amendment to the Foreign Direct Investment Scheme**

**Ref.: A. P. (DIR Series) Circular No. 56 dated December 9, 2011**

Attention is invited to the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, notified vide Notification No. FEMA 20/2000-RB dated May 3, 2000, as amended from time to time. In terms of Schedule 1 of the Notification *ibid*, Foreign Direct Investment (FDI) up to 100 per cent is permitted in pharmaceuticals sector under the automatic route of the FDI Scheme.

2. The extant FDI policy for pharmaceuticals sector has since been reviewed and it has now been decided as under:

   (i) FDI, up to 100 per cent, under the automatic route, would continue to be permitted for green field investments in the pharmaceuticals sector.

   (ii) FDI, up to 100 per cent, would be permitted for brownfield investment (i.e. investments in existing companies), in the pharmaceutical sector, under the Government approval route.

3. A copy of Press Note 3 (2011Series) dated November 8, 2011 issued in this regard is enclosed to circular A. P. (DIR Series) Circular No. 56 dated December 9, 2011.

**External Commercial Borrowings (ECB) for Micro Finance Institutions (MFIs) and Non-Government Organisations (NGOs) – engaged in micro finance activities under Automatic Route**

**Ref.: A. P. (DIR Series) Circular No. 59 dated December 19, 2011**

Attention is invited to the Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000, notified vide Notification No. FEMA 3/2000-RB dated May 3, 2000, amended from time to time, A.P. (DIR Series) Circular No. 5 dated August 1, 2005, amended from time to time and A.P. (DIR Series) Circular No. 40 dated April 25, 2005 relating to the External Commercial Borrowings (ECB).

2. Considering the specific needs of the micro finance sector, the existing ECB policy has been reviewed in consultation with the Government of India and it has been decided that hence forth MFIs may be permitted to raise ECB up to USD 10 million or equivalent during a financial year for permitted end-uses, under the Automatic Route. Detailed guidelines on ECB for MFIs with necessary safeguards are set out below.

(i) Eligible Borrower:

The following MFIs engaged in micro finance activities shall be considered as eligible borrowers to avail of ECBs:-

- MFIs registered under the Societies Registration Act, 1860;
- MFIs registered under Indian Trust Act, 1882;
- MFIs registered either under the conventional state-level cooperative acts, the national level multi-state cooperative legislation or under the new state-level mutually aided cooperative acts (MACS Act) and **not** being a co-operative bank;
- Non-Banking Financial Companies (NBFCs) categorized as '**Non-Banking Financial Company-Micro Finance Institutions' (NBFC-MFIs)**andcomplying with the norms prescribed as per circular DNBS.CC.PD.No. 250/03.10.01/2011-12 dated December 02, 2011; and
- Companies registered under Section 25 of the Companies Act, 1956 and involved in micro finance activity.

(ii) Borrowing relationship and fit and proper status:

Further, the MFIs registered as societies, trusts and co-operatives and engaged in micro finance

- should have a satisfactory borrowing relationship for at least 3 years with a scheduled commercial bank authorized to deal in foreign exchange; and
- would require a certificate of due diligence on 'fit and proper' status of the Board/ Committee of Management of the borrowing entity from the designated Authorized Dealer (AD) bank.

(iii) Recognized lenders

ECB funds should be routed through normal banking channels. NBFC-MFIs will be permitted to avail of ECBs from multilateral institutions, such as IFC, ADB etc. / regional financial institutions/international banks / foreign equity holders and overseas organizations.

Companies registered under Section 25 of the Companies Act and engaged in micro finance will be permitted to avail of ECBs from international banks, multilateral financial institutions, export credit agencies, foreign equity holders, overseas organizations and individuals.

Other MFIs will be permitted to avail of ECBs from international banks, multilateral financial institutions, export credit agencies, overseas organizations and individuals.

Overseas organizations and individuals complying with following safeguards may lend ECB

**a)** **Overseas organisations** planning to extend ECB would have to furnish a certificate of due diligence from an overseas bank which in turn is subject to regulation of host-country regulator and adheres to Financial Action Task Force (FATF) guidelines to the designated AD. The certificate of due diligence should comprise the following (i) that the lender maintains an account with the bank for at least a period of two years, (ii) that the lending entity is organized as per the local law and held in good esteem by the business/local community and (iii) that there is no criminal action pending against it.

**b)** **Individual Lender** has to obtain a certificate of due diligence from an overseas bank indicating that the lender maintains an account

with the bank for at least a period of two years. Other evidence /documents, such as audited statement of account and income tax return which the overseas lender may furnish need to be certified and forwarded by the overseas bank. Individual lenders from countries wherein banks are not required to adhere to Know Your Customer (KYC) guidelines are not permitted to extend ECB.

(iv) *Permitted End-use:* The designated AD must ensure that the ECB proceeds are utilised for lending to self-help groups or for micro-credit or for bonafide micro finance activity including capacity building.

(v) *Amount of ECB*: With a view to ensure minimization of systemic risk, the maximum amount of foreign currency borrowings of a borrower is capped at USD 10 million during a financial year.

3. It has also been decided that Non-Government Organisations (NGOs) engaged in micro finance activities can avail of ECB up to USD 10 million or equivalent per financial year under the automatic route as against the present limit of USD 5 million or equivalent per financial year. All other conditions as detailed in our A.P. (DIR Series) Circular No. 40 dated April 25, 2005 remain unchanged.

4. **Other ECB Parameters:**

All other ECB parameters such as minimum average maturity, all-in-cost ceilings, restrictions on issuance of guarantee, choice of security, parking of ECB proceeds, prepayment, refinancing of ECB, reporting arrangements under the Automatic Route should be complied with by MFIs/ NGOs availing ECBs. The designated AD has to certify the status of the borrower as eligible and involved in micro finance and ensure at the time of draw down that the forex exposure of the borrower is fully hedged.

5. These amendments to ECB policy will come into force with immediate effect and the framework with respect to MFIs will be subject to review after one year.

## External Commercial Borrowings (ECB) denominated in Indian Rupees (INR) - hedging facilities for non-resident entities

**Ref.: A. P. (DIR Series) Circular No. 63 dated December 29, 2011**

Attention is invited to the Foreign Exchange Management (Foreign Exchange Derivative Contracts) Regulations, 2000 dated May 3, 2000 [Notification No. FEMA 25/RB-2000 dated May 3, 2000], as amended from time to time.

2. In terms of A.P. (Dir Series) Circular No. 27 dated September 23, 2011,

i. "eligible borrowers" have been permitted to avail of ECBs designated in INR from foreign equity holders under the automatic/ approval route, as the case may be, as per the extant ECB guidelines.

ii. NGOs engaged in microfinance activities have been permitted to avail of ECBs designated in INR, under the automatic route, from overseas organisations and individuals as per the extant ECB guidelines.

In order to facilitate the same, it has been decided to allow non-residents to hedge their currency risk in respect of ECBs denominated in Indian Rupees, with AD Category I banks in India, as per the details given in the Annexure to A. P. (DIR Series) Circular No. 63 dated December 29, 2011 as under:

**Purpose**

To hedge the currency risk arising out of ECBs designated in INR with AD Category- I banks in India.

**Products**

Forward foreign exchange contracts with rupee as one of the currencies, foreign currency-INR options and foreign currency-INR swaps.

**Operational Guidelines, Terms and Conditions**

· The foreign equity holder / overseas organisation or individual approaches the AD bank in India with a request for forward cover

in respect of underlying transaction for which he needs to furnish appropriate documentation (scanned copies would be acceptable), on a pre-deal basis to enable the AD bank in India to satisfy itself that there is an underlying ECB transaction, and details of his overseas banker, address, etc. The following undertakings also need to be taken from the customer –

- That the same underlying exposure has not been hedged with any other AD Category-I bank/s in India.
- If the underlying exposure is cancelled, the customer will cancel the hedge contract immediately.
- The amount and tenor of the hedge should not exceed that of the underlying transaction and should be in consonance with the extant regulations regarding tenor of payment / realization of the proceeds.
- On due date, settlement is to be done through the correspondent bank's Vostro or the AD bank's Nostro accounts. AD banks in India may release funds to the beneficiaries only after sighting funds in Nostro / Vostro accounts.
- The contracts, once cancelled, cannot be rebooked.
- The contracts may, however, be rolled over on or before maturity subject to maturity of the underlying exposure.
- On cancellation of the contracts, gains may be passed on to the customer subject to the customer providing a declaration that he is not going to rebook the contract or that the contract has been cancelled on account of cancellation of the underlying exposure.

3. Necessary amendments to the Notification No. FEMA.25/RB-2000 dated May 3, 2000 [Foreign Exchange Management (Foreign Exchange Derivative Contracts) Regulations, 2000] are being notified separately.

## External Commercial Borrowings (ECB)

**Ref.: A. P. (DIR Series) Circular No. 64 dated January 5, 2012**

Attention is invited to the Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000, notified vide Notification No. FEMA 3/2000-RB dated May 3, 2000, amended from time to time, issued vide Notification No.FEMA.120/RB-2004 dated July 7, 2004, as amended from time to time, A.P. (DIR Series) Circular No. 5 dated August 1, 2005, as amended from time to time, A.P. (DIR Series) Circular No.17 dated December 4, 2006, A.P. (DIR Series) Circular No. 1 dated July 04, 2011 and A.P. (DIR Series) Circular No. 27 dated September 23, 2011 relating to the External Commercial Borrowings (ECB).

2. The ECB limit for eligible borrowers under the automatic route was enhanced to USD 750 million or equivalent per financial year per borrower for permissible end-uses under the automatic route vide A.P. (DIR Series) Circular No. 27 dated September 23, 2011. Consequent to the enhancement in limits, the revised average maturity guidelines under the automatic route are as follows:-

   a) ECB up to USD 20 million or equivalent in a financial year with minimum average maturity of three years; and

   b) ECB above USD 20 million and up to USD 750 million or equivalent with minimum average maturity of five years.

3. Accordingly, the requirement of average maturity period, prepayment and call / put options specified vide A.P. (DIR Series) Circular No.17 dated December 4, 2006 (for additional amount of USD 250 million) has been dispensed with.

4. It is also clarified that the eligible borrowers under the automatic route can raise Foreign Currency Convertible Bonds (FCCBs) up to USD 750 million or equivalent per financial year for permissible end-uses. Similarly, corporates in specified service sectors, viz. hotel, hospital and software, can raise FCCBs up to USD 200 million or equivalent for

permissible end-uses during a financial year subject to the condition that the proceeds of the ECB should not be used for acquisition of land.

5. Vide para 2(viii) of A.P. (DIR Series) Circular No.01 dated July 04, 2011, ECB / FCCB availed of for the purpose of refinancing the existing outstanding FCCB were to be reckoned as part of the limit of USD 500 million available under the automatic route as per the extant norms. Consequent to the enhancement in the limits under the automatic route, it is clarified that the ECB / FCCB availed of for the purpose of refinancing the existing outstanding FCCB will be reckoned as part of the limit of USD 750 million available under the automatic route as per the extant norms.

6. All other aspects of the ECB policy, such as eligible borrower, recognised lender, all-in-cost, end-use, prepayment, refinancing of existing ECB and reporting arrangements shall remain unchanged.

7. Necessary amendments to the Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 dated May 3, 2000 and Foreign Exchange Management (Transfer or Issue of any Foreign Security) (Amendment) Regulations, 2004 dated July 7, 2004 are being issued separately wherever necessary.

**Foreign Exchange Management Act, 1999 – Export of Goods and Services - Forwarder's Cargo Receipt**

**Ref.: A. P. (DIR Series) Circular No. 65 dated January 12, 2012**

Attention is invited to the A.P. (DIR Series) Circular No. 27 dated March 2, 2001, in terms of which they may accept Forwarder's Cargo Receipts (FCR) issued by IATA approved agents, in lieu of bill of lading, for negotiation / collection of shipping documents, in respect of export transactions backed by letters of credit, only if the relative letter of credit specifically provides for negotiation of this document in lieu of bill of lading and also if the relative sale contract with the overseas buyer provides that FCR may be accepted in lieu of bill of lading as a shipping document.

2. It has now been decided that authorized dealers may accept Forwarder's Cargo Receipts (FCR) issued by IATA approved agents, in lieu of bill of lading, for negotiation/collection of shipping documents, in respect of export transactions backed by letters of credit, if the relative letter of credit specifically provides for negotiation of this document in lieu of bill of lading even if the relative sale contract with the overseas buyer does not provide for acceptance of FCR as a shipping document, in lieu of bill of lading.

3. Further, authorized dealers may, at their discretion, also accept FCR issued by Shipping companies of repute/IATA approved agents (in lieu of bill of lading), for purchase/discount/collection of shipping documents even in cases, where export transactions are not backed by letters of credit, provided their 'relative sale contract' with overseas buyer provides for acceptance of FCR as a shipping document in lieu of bill of lading. However, the acceptance of such FCR for purchase/ discount would purely be the credit decision of the bank concerned who, among others, should satisfy itself about the bona fides of the transaction and the track record of the overseas buyer and the Indian supplier since FCRs are not negotiable documents. It would be advisable for the exporters to ensure due diligence on the overseas buyer, in such cases.

**(I) Scheme for Investment by Qualified Foreign Investors in equity shares (II) Scheme for Investment by Qualified Foreign Investors in Rupee Denominated Units of Domestic Mutual Funds – Revision**

**Ref.: A. P. (DIR Series) Circular No. 66 dated January 13, 2012**

Attention is invited to A.P. (DIR Series) Circular No.8 dated August 9, 2011 and A.P. (DIR Series) Circular No. 42 dated November 3, 2011 in terms of which Qualified Foreign Investors (QFIs as defined therein to mean non-resident investors, other than SEBI registered FIIs and SEBI registered FVCIs, who meet the KYC requirements of SEBI) are allowed to invest in rupee denominated units of domestic Mutual

Funds subject to the terms and conditions mentioned therein.

(I) Scheme for Investment by Qualified Foreign Investors in equity shares

2. It has now been decided to allow QFIs to purchase on repatriation basis equity shares of Indian companies subject the following terms and conditions:

(i) Eligible instruments and eligible transactions – QFIs shall be permitted to invest through SEBI registered Depository Participants (DPs) only in equity shares of listed Indian companies through recognized brokers on recognized stock exchanges in India as well as in equity shares of Indian companies which are offered to public in India in terms of the relevant and applicable SEBI guidelines/ regulations. QFIs shall also be permitted to acquire equity shares by way of rights shares, bonus shares or equity shares on account of stock split / consolidation or equity shares on account of amalgamation, demerger or such corporate actions subject to the investment limits as prescribed in para. 2 (iv) below.

QFIs shall be allowed to sell the equity shares so acquired by way of sale

(a) Through recognized brokers on recognized stock exchanges in India; or

(b) In an open offer in accordance with the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011; or

(c) In an open offer in accordance with the SEBI (Delisting of Securities) Guidelines, 2009; or

(d) Through buyback of shares by a listed Indian company in accordance with the SEBI (Buyback) Regulations, 1998.

(ii) Mode of payment / repatriation – For QFI investments under this scheme a separate single rupee pool bank account would be maintained by the DP with an AD Category- I bank in India for QFI investments under this scheme. The DP will purchase equity at the instruction of the respective QFIs within five working days (including the date of credit of funds to the single rupee pool bank account by way of foreign inward remittances through normal banking channels) failing which the funds would be immediately repatriated back to the QFI's designated overseas bank account. The sale proceeds of the equity shares will also be received in this single rupee pool bank account of the DP and shall be repatriated to the designated overseas bank account of the QFI within five working days (including the date of credit of funds to the single rupee pool bank account by way of sale of equity shares) of having been received in the single rupee pool bank account of the DP. Within these five working days, the sale proceeds of the existing investment can be also utilized for fresh purchases of equity shares under this scheme, if so instructed by the QFI. Dividend payments on equity shares held by QFIs can either be directly remitted to the designated overseas bank accounts of the QFIs or credited to the single rupee pool bank account. In case dividend payments are credited to the single rupee pool bank account they shall be remitted to the designated overseas bank accounts of the QFIs within five working days (including the day of credit of such funds to the single rupee pool bank account). Within these five working days, the dividend payments can be also utilized for fresh purchases of equity shares under this scheme, if so instructed by the QFI.

(iii) Demat accounts - QFIs would be allowed to open a dedicated demat account with a DP in India for investment in equity shares under the scheme. The QFIs would however not be allowed to open any bank account in India.

(iv) Limits - The individual and aggregate investment limits for the QFIs shall be 5% and 10% respectively of the paid up capital of an Indian company. These limits shall be over and above the FII and NRI investment ceilings

prescribed under the Portfolio Investment Scheme for foreign investment in India. Further, wherever there are composite sectoral caps under the extant FDI policy, these limits for QFI investment in equity shares shall also be within such overall FDI sectoral caps. The onus of monitoring and compliance of these limits shall remain jointly and severally with the respective QFIs, DPs and the respective Indian companies (receiving such investment).

(v) Eligibility - Only QFIs from jurisdictions which are FATF compliant and with which SEBI has signed MOUs under the IOSCO framework will be eligible to invest in equity shares under this scheme.

(vi) KYC - DPs will ensure KYC of the QFIs as per the norms prescribed by SEBI.

(vii) Permissible currencies - QFIs will remit foreign inward remittance through normal banking channel in any permitted currency (freely convertible) directly into single rupee pool bank account of the DP maintained with AD Category-I bank.

(viii) Pricing – The pricing of all eligible transactions and investment in all eligible instruments by QFIs under this scheme shall be in accordance with the relevant and applicable SEBI guidelines only.

(ix) Reporting – In addition to the reporting to SEBI as may be prescribed by them, DPs will also ensure reporting to the Reserve Bank of India in a manner and format as prescribed by the Reserve Bank of India from time to time.

(II) Scheme for Investment by Qualified Foreign Investors in Rupee Denominated Units of Domestic Mutual Funds

3. QFI investment in rupee denominated units of Domestic Mutual Funds under the Direct Route – On a further review it has been decided to modify the time period for which funds (by way of foreign inward remittance through normal banking channels from QFIs as well as by way of credit of redemption proceeds of the units of domestic Mutual Funds by QFIs in India) can be kept in the single rupee pool bank account of the DP under the scheme for investment by QFIs in units of domestic Mutual Funds (as per the terms and conditions specified in A.P. (DIR Series) Circular No.8 dated August 9, 2011 and A.P. (DIR Series) Circular No.42 dated November 3, 2011) to five working days (including the day of credit of funds received by way of foreign inward remittance through normal banking channels from QFIs as well as by way of credit of redemption proceeds of the units of domestic Mutual Funds by QFIs in India). It has also been decided to allow credit of dividend payments to QFIs on account of units of mutual funds held by them to the single rupee pool bank account subject to the condition that in case dividend payments are credited to the single rupee pool bank account they shall be remitted to the designated overseas bank accounts of the QFIs within five working days (including the day of credit of such funds to the single rupee pool bank account). Within these five working days, the dividend payments can be also utilized for fresh purchases of units of domestic mutual funds under this scheme, if so instructed by the QFI.

## Foreign investment in Single – Brand Retail Trading Amendment to the Foreign Direct Investment (FDI) Scheme

**Ref.: A. P. (DIR Series) Circular No. 67 dated January 13, 2012 & Press Note 1 (2012 Series) dated January 10, 2012**

Attention is invited to the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, notified vide Notification No. FEMA 20/2000-RB dated May 3, 2000, as amended from time to time. In terms of Schedule 1 of the Notification, FDI up to 51 per cent is permitted in Single Brand product trading under Government route of FDI Scheme.

2. The extant FDI policy has since been reviewed and it has now been decided that FDI up to 100 per cent would be permitted in Single Brand product trading under the Government route

subject to the terms and conditions as stipulated in Press Note No. 1 (2012 Series) dated January 10, 2012 issued by Department of Industrial Policy & Promotion, Ministry of Commerce & Industry, Government of India.

3. Excerpts from Press Note No. 1 (2012 Series) dated January 10, 2012 issued in this regard are as under:

**Press Note No.1 (2012 Series)**

**Subject:** Review of the policy on Foreign Direct Investment- liberalization of the policy in Single-Brand Retail Trading.

**1.0 Present Position:**

Foreign Direct Investment (FDI), in retail trade, is prohibited except in single brand product retail trading, in which FDI, up to 51% is permitted, subject to conditions specified under paragraph 6.2.16.4 of 'Circular 2 of 2011 – Consolidated FDI Policy'.

**2.0 Revised Position:**

The Government of India has reviewed the extant policy on FDI and decided that FDI, up to 100%, under the government approval route, would be permitted in Single-Brand Product Retail Trading, subject to specified conditions, as indicated in paragraph 3.0 below.

**3.0** Accordingly, the following amendment is made in *'Circular 2 of 2011- Consolidated FDI Policy',* dated 30.09.2011, issued by the Department of Industrial Policy & Promotion:

3.1 **Paragraph 6.2.16.4 is substituted with the following:**

**6.2.16.4 Single Brand product retail trading** 100% Government

(1) Foreign Investment in Single Brand product retail trading is aimed at attracting investments in production and marketing, improving the availability of such goods for the consumer, encouraging increased sourcing of goods from India, and enhancing competitiveness of Indian enterprises through access to global designs, technologies and management practices.

(2) FDI in Single Brand product retail trading would be subject to the following conditions:

(a) Products to be sold should be of a 'Single Brand' only.

(b) Products should be sold under the same brand internationally i.e. products should be sold under the same brand in one or more countries other than India.

(c) 'Single Brand' product-retail trading would cover only products which are branded during manufacturing.

(d) The foreign investor should be the owner of the brand.

(e) In respect of proposals involving FDI beyond 51%, mandatory sourcing of at least 30% of the value of products sold would have to be done from Indian 'small industries/ village and cottage industries, artisans and craftsmen'. 'Small industries' would be defined as

**4.0** The above decision will take immediate effect.

**5.0** The above provisions will be incorporated in the next Circular on Consolidated FDI Policy to be issued on 31.3.2012.

4. AD Category - I banks may bring the contents of the circular to the notice of their customers/ constituents concerned.

5. Necessary amendments to Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000 (Notification No. FEMA 20/2000-RB dated May 3, 2000) are being notified separately.

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# FINANCIAL REPORTING STANDARDS

## Introduction:

In previous column, we discussed on Standard on Auditing 700 (Revised) issued by ICAI This column dwells on the Guidance Note on Recognition of Revenue by Real Estate Developers. We had discussed this topic in our previous to previous column. That discussion was based on the Exposure Draft. The final version contains some changes that clarify various issues raised at the time of the Exposure Draft. However, from reader's point of view, we will be discussing the major points of the Guidance Note again and not just the changes made.

IFRS, IAS, SIC and IFRIC are the copyright of IFRS Foundation. The column includes references and extracts of the IFRS as issued by IASB. The IPSASB issues International Public Sector Accounting Standards (IPSAS).

## Objective and Scope:

The objective of the guidance note is to recommend the accounting treatment by enterprises dealing in real estate as sellers or developers. The term "Real Estate" has been defined as land and building and rights in relation thereto. The scope of the Guidance Note is quite broad. It includes all forms of transactions in real estate. Para 1.2 of the Guidance Note gives the following examples of transactions covered by the Guidance Note:

1. Sale of plots of land (including long term sale type leases) without any development
2. Sale of plots of land (including long term sale type leases) with development
3. Development and sale of residential and commercial units, row houses, independent houses, with or without an undivided share in land
4. Acquisition, utilization and transfer of development rights
5. Redevelopment of existing buildings and structures
6. Joint development agreements for any of the above activities

Para 1.3 clarifies that the basic purpose of the Guidance Note is to provide guidance on application of Percentage of Completion Method as required by Accounting Standard (AS) 7, "Construction Contracts" and the application of the requirements of AS 9, "Revenue Recognition" to contracts with customers involving real estate. The Guidance Note is made applicable prospectively for all projects in real estate commencing on or after April1, 2012 and to those existing projects where no revenue was recognized till 31 March 2012. Earlier application is permitted. Hence, for existing projects, the whims and fancies of management continues.

**CA. Manish Iyer**
*The author is practising since 2003. He can be reached at cmanishiyer@gmail.com*

## Some Definitions:

The Guidance Note has introduced new terms such as Project, Project costs and Project revenues. Adding new terms in Guidance Note would only increase the complications. Also, it should be noted that unless the guidance note is incorporated into AS 7 as an explanation, the Guidance Note will be binding only on the members of the Institute of Chartered Accountants of India. Hence, looking to the status of the Guidance Note, the Institute of Chartered Accountants of India should have amended the existing standard on Construction Contracts to include the new terms and get it notified by MCA.

The term project has been defined as the smallest group of units / plots / saleable spaces which are linked with a common set of amenities in such a manner that unless the common amenities are made available and functional, these units / plots / saleable spaces cannot be put to their intended effective use. Project revenue is measured as the consideration received or receivable. This statement is quite vague. What does the word 'consideration' mean has not been clarified. IFRS requires revenue to be measured at the fair value of the consideration received or receivable. AS 9 requires revenue to be measured at the charges made to customers. However, the guidance note does not provide any guidance on the measurement of revenue, whether it is fair value or something else. Cost of land is included as project costs along with construction costs. Similarly, project revenues includes revenue

pertaining sale of land. Under IFRS, cost of land and the revenue of land is recognized separately from construction costs and revenues as the same cannot be constructed.

**Accounting for Real Estate Transactions:**

Para 3.2 of the Guidance Note states that the typical features of most construction / development of commercial and residential units have all features of a construction contract such as:

1. Land development
2. Structural engineering
3. Architectural design
4. Construction

It may be noted that the Guidance Note identifies a contract as construction contract based on legal form of the contract. The Guidance Note does not explain how the definition of "Construction Contract" contained in AS 7 is applied to contracts for real estate. It is worth to note that under IFRS, IFRIC 15 clarifies the application of the definition of "Construction Contract". The definition of 'Construction Contract' in AS 7 or IAS 11 requires the contract to be specifically negotiated contract. IFRIC 15 clarifies that an agreement for the construction of real estate is a construction contract when the buyer is able to specify the major structural elements of the design of the real estate before construction begins and / or specify major structural changes once construction is in progress. Thus, under International Financial Reporting Standards, most of the residential and commercial complex development projects would be sale contracts instead of construction contract. However, the Guidance Note in paragraph 3.3 states that in case of real estate sales, the seller usually enters into an agreement for sale with the buyer at initial stages of construction which has the effect of transferring all significant risks and rewards of ownership if the agreement is legally enforceable. Any acts performed by the entity after such a legally enforceable agreement for sale are on behalf of the buyer in the manner similar to a contractor. Accordingly, revenue in such cases is recognized by applying the percentage of completion method on the basis of the methodology explained in AS 7. However, the Guidance Note misses out in clarifying how revenue should be recorded at the time the legally enforceable agreement for sale is entered into. Paragraph 4 of the Guidance Note explains the application of principles of AS 9 to real estate project. Para 4.2 clarifies that the revenue recognition process is usually identified when the following conditions are satisfied:

1. The entity has transferred to the buyer all significant risks and rewards of ownership and the seller retains no effective control of the real estate to a degree usually associated with ownership
2. The seller has effectively handed over possession of the real estate unit to the buyer forming part of the transaction
3. No significant uncertainty exists regarding the amount of consideration that will be derived from the real estate sales; and
4. It is not unreasonable to expect ultimate collection of revenue from buyers

Thus, the statements of Paragraphs 3.3 and 4.2 are conflicting. Paragraph 3.3 states that the transfer of significant risks and rewards evidenced by legally enforceable agreement for sale is the only condition precedent for changing the nature of the contract from sales to construction contract whereas paragraph 4.2 has three more conditions for recognizing revenue from sales. This may be the reason why the Guidance Note is silent of recognition of revenue at the time the legally enforceable agreement for sale is entered into because the other three conditions specified in Paragraph 4.2 have not been satisfied. However, if this is the case, the Guidance Note should have clarified that the seller should have to disclose the amount of revenue, the recognition of which has been postponed. Also, it is difficult to understand how can the developer, who is constructing on his own behalf suddenly starts acting on behalf of the customer without any consideration being given or received. From the balance sheet perspective, till a legally enforceable agreement for sale is entered into, the real estate is an finished good ready for sale of the developer enterprise. Once the legally enforceable agreement for sale is entered into, the real estate becomes work-in-progress of the developer enterprise. It is difficult to grasp how a finished good ready for sale can become work-in-progress not ready for sale by entering into a contract. This is a major weak point of the revised Guidance Note. The Guidance Note looks from Profit and Loss Statement perspective rather that Balance Sheet perspective as required by the Framework for the Preparation and Presentation of Financial Statements issued by Institute of Chartered Accountants of India. The discussion on the Guidance Note will be continued in further columns.

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# INDIRECT TAXES CORNER

**CA. Bihari B. Shah**

*The author is the past President of CAA, practising since 1970. He can be reached at biharishah@yahoo.com.*

## [I] IMPORTANT NOTIFICATIONS/CIRCULARS:

### EASY VAT REGISTRATION:

For registration under GVAT Act as well as CST Act, new procedure is announced for immediate issue of registration numbers.

The Hon. Commissioner of Commercial Taxes, State of Gujarat, has made an amendment in the Rules vide Notification No. 41 dated 1.12.2011 for issue of registration immediately with a view to simplification in procedure and to obtain a transparency for issuing the same. The new rules will help the dealers for obtaining immediate registration and those who want to take the advantage, are requested to follow the procedure announced vide Circular No. 126 dated 1.12.2011 issued by the Department. As the procedure is lengthy, it is not reproduced IN THIS COLUMN.

## [II] IMPORTANT JUDGMENT:

### [A] Whether RTO Charges, handling charges are part of Sales Price?

Under Maharashtra VAT Act, an important judgment is pronounced by **Hon. Bombay High Court in case of Additional Commissioner of Sales Tax vs. Sehgal Autoriders Pvt. Ltd.** on dated 11.7.2011. The salient parts of the judgment are reproduced hereunder for the benefit of the readers.

The issue was taken by the Department to the Bombay High Court by way of appeal under the MVAT Act, 2002. The High Court has now decided the issue.

Before the High Court the main argument of the Department was that the delivery is to be seen in light of effective delivery. It was contended that as per Motor Vehicle Act / Rules the motor vehicle cannot be plied on road unless registered. It was argued that the customer can drive away the veh icle from the dealer's place when it is registered in his name and since the charges mentioned above are prior to the above event they are taxable.

On behalf of the dealer it was contended that the registration is the responsibility of the buyer who becomes owner of the vehicle. It is only the owner who gets it registered. The sale note is issued for the said purposes which completes sale and delivery.

The further activities of registration, etc. are on behalf of the buyer as agent and the handling charges are towards such services, a separate transaction and it is a post-sale transaction. It was also contended that the provisions of the Motor Vehicles Act are for separate purpose and cannot be brought in for interpretation of the MVAT Act. The provisions of sale of the Goods Act, 1930 were also relied upon.

The High Court referred to Rule 47 of the Motor Vehicle Rules and observed that as per the said rule the dealer has to issue a certificate of giving delivery to the buyer, so as to enable the registration of the vehicle under the Motor Vehicle Act. The High Court on the above facts observed as under.

" The contention of the Revenue, however, is that delivery cannot be granted to the owner by the holder of a trade certificate under Rule 42 unless the motor vehicle has been registered. Rule 42 however does not, as it cannot, override the obligation which section 39 imposes on the owner of obtaining registration. Moreover, Rule 42 cannot be construed in isolation from the other provisions which have been made in Chapter III of the Central Motor Vehicles Rules, 1989.

Rule 41, for instance, specifies the purposes for which the holder of a trade certificate may use a vehicle in a public place. Among the purposes is for proceeding to and from any place for the registration of the vehicle. Similarly, under clause (d) of Rule 41, the holder of a trade certificate may use a vehicle in a public place for proceeding to or returning from the premises of the dealer or of the purchase for the purposes of delivery.

Rule 42 provides that no holder of a trade certificate shall deliver a motor vehicle to a purchaser, without registration, whether temporary or permanent. It is evident that an application for registration is required to be made in accordance with Rule 47. Rule 47, as a matter of fact, stipulates that an application for registration has to be made within a period of seven days from the date of taking delivery of the vehicle. The application has to be accompanied by a sale certificate. The statutory form for the sale certificate stipulates that delivery has been handed over to the purchaser. The Tribunal, in the present case, has found, as a matter of fact, that upon receipt of the price of the goods, the respondent issues a gate pass in the name of the purchaser and issues a sale certificate in the prescribed form showing delivery of the motor cycle. The sale is complete and transfer of property in the motor cycle takes place to the purchaser coupled with the delivery thereof. The obligation to obtain registration is that of the purchaser.

When a dealer facilitates the obtaining of a registration certificate, he acts for and on behalf of the purchaser, because the obligation under the law to obtain a registration certificate is cast upon the owner of the vehicle. The application for the issuance of a registration certificate and the grant of a registration certificate are both post-sale events. The charges that are levied by the appellant and recovered as handling charges are in respect of a service rendered to the purchaser upon the completion of the sale of the motor vehicle. Handling charges cannot be regarded as forming part of ' the valuable consideration paid or payable to a dealer for any sale made'. The handling charges cannot be regarded as ' any sum charged for anything done by the seller in respect of the goods at the time of or before delivery thereof.'

Observing as above the High Court held that the holding of the Tribunal that registration / handling charges is not part of sale price was correct and did not require any interference.

[B] **Penalty for not furnishing the Audit Report under the Maharashtra VAT Act.**

Recently Hon. Bombay High Court in case of Additional Commissioner of Sales Tax vs. Ankit International, pronounced an important judgment on interpretation of sec. 62(2) of MVAT Act 2002. The said section provides for the penalty equal to 1/10th percentage of the total sales for default of furnishing the audit report within the stipulated time.

In this matter Hon. Bombay High Court held that the discretion to impose the penalty extended to the quantum of the penalty also.

The fact of the case is as under.

The appellant has furnished the audit report pertaining to the year 2006-2007 after expiry of time limit and therefore the Commissioner has imposed a penalty of Rs. 83,000/- equal to 1/10th percentage of the total sale as provided under section 61(2) for late submission of audit report.

The appellant has gone to the Tribunal and argued that the person who had conducted the audit, has taken the employment elsewhere and when these facts came to his knowledge, an audit was conducted and report was belatedly filed. In these circumstances, the Tribunal reduced the penalty to 30% i.e. Rs. 25,000/-. Being aggrieved, the department filed a further appeal before the Hon. Bombay High Court. The Hon. Bombay High Court held that the imposition of penalty under sub-sec. 61(2) is not mandatory. The commissioner had a discretion to determine as to whether a penalty should or should not be imposed.

The Legislature held that the commissioner " may impose penalty after giving the dealer a reasonable opportunity of being heard " and the Hon. Bombay High Court has confirmed the Tribunal Order. This decision is applying to Gujarat VAT Act also under the following provisions i.e. Sec. 12(7), Sec. 34(5) and Sec. 34(8).

[C] **Sale of Machinery attached to the land to the ICICI Bank for taking finance is not sale of goods and is not liable to tax.**

Appellant sold machinery attached to land to the ICICI Bank Mumbai and took back it on lease. Assessing Officer held that the sale of machinery is liable to tax. It was contended before Hon. Tribunal that the sale transaction is merely a financial management. Machinery was attached to the land. A report of the spot visit of Ld. Asst. Commissioner of Commercial Tax (Audit) Surat was produced before the Hon. Tribunal. As per the report the machinery was attached to the land. Hon. Tribunal following S. C. Judgment in the case of **M/s. Sundaram Finance Ltd. 17 STC 489)** and referring definition of goods as provided in section 2(12) held that the transaction is not sale of goods liable to tax. Hon. Tribunal set aside levy of tax and levies of interest and penalty.

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# CST LAW UPDATE

**18. DEEMING FICTION-NOT TO BE EXTENDED BEYOND PURPOSE.**

In the case of **INDIA EXPORTS V.STATE OF U.P. AND OTHERS. [2012] 47 VST 126 (All).**

**Background of the case :-**

The petitioner-dealer, an industrial unit established in a special economic zone manufacturing furniture, which was cleared for sale to domestic tariff area units under section 2(i) of the Special Economic Zones Act, 2005 mostly to hotels promoting furniture as capital goods under the Export Promotion of Capital Goods Schemes on concessional customs duty. The dealer also exported furniture outside India. For the assessment year 2006-07, the Deputy Commissioner (Administration) rejected the account books and imposed tax liability, levying Central sales tax on the sales to domestic tariff areas units, on the ground that by notification dated January 17, 2007 issued by the State Government, the exemption granted by notification dated May 5, 2006 in respect of the Central sales tax on sales from special economic zones to domestic tariff area units was withdrawn.

**Held**, that the deeming provision is not to be inferred in law. It has to be either provided by legislation validly enacted and competent to declare such deeming provision with its consequences. There can be no inference drawn from deeming provisions from the provisions of any Act. The deeming provision also cannot be inferred from the analogy drawn from different Acts. The fiction in law is to be created by law itself and not by any inference to be drawn from the law.

A fiction in law cannot be extended beyond its purpose

The arguments that since SEZ is deemed to be outside the customs territory of India, the sale from SEZ to DTA has to be treated as import, is not born out from the provisions of either the SEZ Act, 2005 or the Central Sales Tax Act, 1956.

**CA. Priyam R. Shah**
*The author is practising since 1998. He can be reached at priyamrshah@yahoo.com*

**19. CENTRAL SALES TAX- EXEMPTION-CONSIGNMENT SALE OUTSIDE STATE.**

In the case of **RAJHANS VEGETABLE OIL REFINERY P LTD. V. STATE OF GUJARAT AND OTHERS [2012] 47 VST 269(Guj)**

**Background of the case :-**

The appellant-dealer was engaged in the business of buying, selling and manufacturing of soyabean, palmolein and other edible oils. Upon notice issued by the Sales Tax Officer, the dealer produced evidence in respect of its claim made under section 6A of the Central Sales Tax Act, 1956, but the assessing officer rejected the claims and raised a demand. This was affirmed by the Deputy Commissioner (Appeals) and by the Tribunal. On appeal contending that the Tribunal had brushed aside the evidence produced by the dealer without cogent reasons and that the entire assessment had been made on the basis of material without affording any opportunity to the dealer to deal with it :

Held, allowing the appeal, that the assessment order clearly indicated that the assessing officer had proceeded on assumptions and presumptions and with a pre-determined mind placing reliance upon material gathered behind the dealer's back without furnishing it to the dealer or calling upon the dealer to explain anything in the context of the material. Such material formed the basis for the assessing officer coming to the conclusion that the sales were made directly to parties and not through consignee agents. The appellate authority without considering the submissions advanced by the dealer, more or

*Contd. on page no. 594*

# SERVICE TAX REVIEW

**In this issue, judgement on Banking & other Financial Service and Business Auxilliary Service are reproduced for the benefit of Members.**

**CA. Ashwin H. Shah**
*The author is the past President of CAA, practising since 1975. He can be reached at ashwinshah.ca@gmail.com*

## 1) HUDCO v. Commissioner of Service tax, Ahmedabad

**[2012] 17 taxmann.com 14 (Ahd. - CESTAT)**
**CESTAT, AHMEDABAD BENCH**

- **Whether reset charges and pre-payment charges can be considered as cost incurred by borrower towards value added services like restructuring of loan, pre-payment of loan and same are liable to service tax under head 'Banking and other financial service'?**

The assessee was involved in the business of providing finance for housing and urban development. For providing said service, it was paying service, tax under category of 'Banking and other financial service'. During the course of audit, the department noticed that the assessee had collected reset charges from customers for restructuring of interest rates. The assessee had also recovered pre-payment charges from customers on pre-payment of Part/Full loan during loan period. Invoking extended period of limitation, service-tax demand was confirmed on the assessee for receipt of above charges under category of 'banking and other financial service'.

The assessee being a wholly owned government company and the fact that it did not pay service tax only on pre-payment charges and reset charges and also in view of the fact that accounting treatment given to these items as additional interest has been accepted by the Income-tax department, would be sufficient for invoking provisions of section 80 of the Finance Act, 1994. Accordingly, while upholding the demand of service-tax and interest, penalties imposed under various sections of the Finance Act, 1994 are set aside.

## 2) Green Channel Travel Services (P.) Ltd. v. Commissioner of Service Tax

**[2012] 18 taxmann.com 267 (Ahd. - CESTAT)**
**CESTAT, AHMEDABAD BENCH**

- **Whether service tax is leviable on rendering the services of obtaining passport and visa?**

The issue regarding Service Tax liability on the appellant for the amount received as income/ commission charged by him for rendering the services of obtaining passport and visa.

After hearing both sides on Stay Petition, we find that the appeal itself can be disposed off after allowing Stay Petition for waiver of pre-deposit of amounts involved. Accordingly, the Stay Petition is allowed and appeal is taken up for disposal.

Ld. Counsel would produce a copy of CBE&C Circular No. 137/6/2011-S.T., dt.20.04.01, wherein the Board has clarified that the service provided by visa facilitator in the form of assistance to individuals who intend to travel abroad, directly, does not fall under any taxable service under Section 65(105) of Finance Act, 1994.

<u>Circular regarding Service tax clarification on assistance for processing of visa applications is as under:-</u>

An issue has been brought before the Board, seeking a clarification as to whether service tax liability would arise on the assistance

provided by visa facilitators, to individuals directly, for processing of visa applications.

The same has been examined. Assistance provided by a visa facilitator, for obtaining visa, to a visa applicant or for foreign employer does not fall within the scope of supply of manpower service. Visa facilitators, while providing visa assistance directly to individuals does not act on behalf of the embassies, as agents of the principal and hence service tax is not leviable within the meaning of business auxiliary service. Also where the assistance is rendered to an individual directly, by a visa facilitator, and the visa applicant pays the service charge on his own (meaning such service charge is not borne by any business entity), the same cannot be considered as support service for business or commerce.

Visa facilitators, merely facilitate the procurement of visa and directly assist individuals who intend to travel abroad, to complete the immigration formalities. Visa facilitators collect certain statutory charges like visa fee, certification fee, attestation fee, emigration fee, etc. from the visa applicant, which are remitted to the respective authorities, and in addition collect service charges for themselves as remuneration for the assistance provided by them to obtain the visa. Such a service provided by a visa facilitator, in the form of assistance to individuals directly, to obtain a visa, does not fall under any of the taxable services under section 65(105) of the Finance Act, 1994. Hence service tax is not attracted.

However, service tax is leviable on any service provided other than assistance directly to individuals for obtaining visa, falling under the description of any taxable service, as classifiable under the appropriate heading. To cite a few instances, where in addition to rendering assistance directly to individuals for obtaining visa, visa facilitators may also act as agents of recruitment or of foreign employer, in which case, service tax is leviable to the extent under the service of 'supply of manpower'. In certain other cases, for example, a visa facilitator, may be rendering visa assistance to individuals who are employed in a business entity, but the service charge may be paid by the business entity on behalf of those individuals, to the visa facilitator, in which case, service tax is leviable under 'business support service'.

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*Contd. from page no. 591*



less, had reiterated the findings recorded by the assessing officer and had in fact recorded contradictory findings. The appellate authority had nowhere dealt with the contentions raised by the dealer nor considered the evidence placed on record by it. The Tribunal had merely recorded that certain specific instances had been mentioned in the assessment order for rejecting the genuineness of transactions and that the dealer had not countered such specific instances. The Tribunal had lost sight of the fact that it was the categorical case of the dealer that material had been gathered behind its back and that it had not been afforded any opportunity to deal with it. In the circumstances, when such material was never put to the dealer, there was no question of the dealer having countered it. Thus, the findings recorded by the Tribunal clearly suffered from non-application of mind. When the dealer had raised specific contentions before the Tribunal, the Tribunal was required to apply its mind to the contentions and after appreciating the evidence on record, record its findings in respect thereof. The order of the Tribunal was to be set aside, the appeal restored to the file of the Tribunal for decision afresh after giving a reasonable opportunity of hearing to the parties. If the Tribunal deemed fit, it shall also be open to the Tribunal to further remand the matter either to appellate authority or to the assessing officer.

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# CORPORATE LAWS UPDATE

**CA. Chirag M. Shah**
*The author is practising since 1991. He can be reached at mnshahco@gmail.com*

## CIRCULARS

**(1) Sub: Filing of conflicting returns by contesting parties – clarification regarding.** (General Circular No. 1/2012 F.No.17/135/2011-CL V Dated the 10th February, 2012) issued by Government of India, Ministry of Corporate Affairs

To,
All Regional Directors,
All Registrars of Companies,

Sir,

I am directed to invite a reference to Ministry's Circular No. 19 and 20 of 2011 issued on 02.05.2011 laying down certain procedure to regulate cases wherein filing of conflicting returns with regard to appointment of Directors of change of Director / Directors was laid down. In the light of some specific cases wherein it appears that either there was lack of consent of the removed/ changed director or due process of law were not followed, it has been decided to supersede the circulars.

2. In order to avoid such eventualities wherever there is management dispute, the company is required to mandatorily file the attachment relating to cause of cessation along with Form 32 with the ROC concerned irrespective of the ground of cessation, viz. (a) retirement; (b) disqualification; (c) death; (d) resignation; (e) vacation of office u/s.283 or 313 or 260; (f) removal u/s 284; (g) withdrawal of nomination by appointing authority or (h) absence of re-appointment.

3. In case, any Director is aggrieved with his cessation in the company, he may file complaint in the Investor Complaint Form. On receipt of complaint, the ROC concerned will examine the complaint and mark the company as having 'management dispute'. Also, the ROC will issue a letter to the company and the parties to settle the matter amicably or get an order/interim order from a Court or Tribunal of competent jurisdiction. Till such dispute is settled, the documents filed by the company and by the contesting groups of Directors will not be approved/registered/recorded and will thus not be available in the registry for public viewing.

Yours faithfully,

Sd/-

(Monika Gupta),

Assistant Director.

**(2) Sub: Registration of Companies of LLPs which have one of their objects is to carry on the profession of Chartered Accountant, Cost Accountant, Architect, Company Secretary etc.** (General Circular No. 2/2012 F.No.17/165/2011-CL V Dated the 1st March, 2012).

To,
All Regional Directors,
All Registrars of Companies,
Registrar of LLPs

Sir,

I am directed to say that at the time of incorporation of Companies, where one of the objects is to carry on the business of Banking, INsurance or to paractice the profession of Charatered Accountancy, Cost Accountancy & Company Secretaries, then the concerned Registrar of

Companies shall incorporate the same only on production of in-principle approval / NOC from the concerned regulator / professional Institutes.

2. Further, in this connection, it is also stated that where one of the objects is to carry on the business / profession of Architecture, then the concerned Registrar of Companies / Registrar of LLP shall incorporate the same only on production of in-principle approval / NOC from the concerned regulator.

3. This issues with the approval of CAM.

Yours faithfully,
Sd/-
(Monika Gupta),
Assistant Director.

**(3) Sub: Allotment of Director's Identification Number (DIN) under Companies Act,1956.** General Circular No. 4/2012 F.No.2/1/2011-CL V Dated 9th March, 2012,

Sir,

In continuation of General Circular Nos. 32/2011 dated 31.05.2011, 66/2011 dated 04.10.2011 and 70/2011 dated 15.12.2011 on the subject cited above, I am directed to say that the time for filing form DIN-4 by DIN holders for furnishing PAN and to update PAN details has been extended upto 30.04.2012.

Yours faithfully,

( U.C.Nahta),

Director (Inspection & Investigation)

**NOTIFICATIONS:**

**(1) Companies (Accounting Standards-Second Amendment) Rules 2011 MCA Notification Dt 29 December 2011 - Amending AS 11 Reg Forex differences / losses accumulation**

"....Forex differences / losses can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortized over the balance period of such long term asset or liability, by recognition as income or expense in each of such periods.."

**Extracts of MCA Notification**

GSR :- In exercise of the Powers conferred by clause (a) of sub-section (1) of section 642 read with sub-section (1) of section 210A and sub-section (3C) of section 211 of the Companies Act, 1956 ( 1 of 1956), the Central Government in consultation with the National Advisory Committee on Accounting Standards, hereby makes the following amendments in the Companies (Accounting Standards) Rules, 2006, namely :-

1. (1) These rules may be called the Companies (Accounting Standards) (Second Amendment) Rules, 2011,

(2) They shall come into force on the date of their publication the Official Gazette.

2. In the Companies (Accounting Standards) Rules, 2006, (hereinafter referred to as the said rules), in the Annexure, Under the heading "B. ACCOUNTING STANDARDS", in the sub-heading "Accounting Standard (AS) 11 relating to The Effects of Changes in Foreign Exchange Rates", after paragraph 46, the following paragraph shall be inserted, namely,-

" 46A. (1) In respect of accounting periods commencing on or after the 1st April, 2011, for an enterprise which had earlier exercised the option under paragraph 46 and at the option of any other enterprise (such option to be irrevocable and to be applied to all such foreign currency monetary items), the 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 , in so far 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 amortized over the balance period of such long term asset or liability, by recognition as income or expense in each of such periods, with the exception of exchange differences dealt with in accordance with the provisions of paragraph 15 of the said rules.

(2) To exercise the option referred to in sub-paragraph (1), an asset or liability shall be designated as a long term foreign currency monetary item, if the asset or liability is expressed in a foreign currency and has a term of twelve months or more at the date of origination of the asset or the liability:

Provided that the option exercised by the enterprise shall disclose the fact of such option and of the amount remaining to be amortized in the financial statements of the period in which such option is exercised and in every subsequent period so long as any exchange difference remains unamortized."

**(2) Companies (Accounting Standards) Amendment Rules,2011: MCA Notification dated 29th December, 2011 Reg Deferment of Accumulation of Forex losses until 31 March 2020**

Extracts

GSR....:- In exercise of the powers conferred by clause (a) of sub- section (1) of Section 642 read with sub-section (1) of Section 210A and sub-section (3C) of Section 211 of the Companies Act, 1956 (1 of1956), the Central Government in consultation with the National Advisory Committee on Accounting Standards, hereby makes the following amendment in the Companies (Accounting Standards) Rules, 2006, hereinafter called the said rules, namely:-

1. (1) These rules may be called the Companies (Accounting Standards) Amendment Rules, 2011.

(2) They shall come into force on the date of their publication in the Official Gazette.

2. In the said rules, in the annexure under the heading "B. Accounting Standard", in the sub-heading "Accounting Standard (AS) 11 relating to "The Effects of Changes in Foreign Exchange Rates", in paragraph 46, for the words and figures "46. In respect of accounting periods commencing on or after 7th December, 2006 and ending on or before 31' March, 2012, the following shall be substituted, namely :-

"46. In respect of accounting periods commencing on or after 7th December, 2006 and ending on or before 31' March, 2020.

**NEWS YOU CAN USE:**

**Ind Accounting Standards – CARVE OUT for Implementation & Compliance by NACAS**

The Ind As have been prepared by NACAS and with its recommendation submitted to MCA. NACAS adopted due consultative proposed of hosting the draft Ind As insisting comments/suggestions and therefore after deliberated with industries representative in NACAS. The finally recommended Ind AS have the following carve outs. These carve out have been made to fill up the gap/differences in application of Accounting Principles Practices and economic conditions prevailing in India.

**1. <u>Ind AS 21- The Effects of Changes in Foreign Exchange Rates</u>**

It requires recognition of exchange differences arising on translation of monetary items from foreign currency to functional currency directly in profit or loss.

**Carve out**

Ind AS 21 permits an option to recognise exchange differences arising on translation of certain long-term monetary items from foreign currency to functional currency directly in equity. In this situation, Ind AS 21 requires the accumulated exchanged differences to be amortised to profit or

loss in appropriate manner.

**2. Ind AS 28 – Investment in Associates**

(i) Paragraph 25 require that difference between the reporting period of an associate and that of the investor should not be more than three months, in any case.

**Carve out**

The purchase 'unless it is impracticable' has been added in the relevant requirement i.e. paragraph 25 of In AS 28.

(ii) IAS 28 requires that for the purpose of applying equity method of accounting in the preparation of investor's financial statements, uniform accounting policies should be used. In other words, if the associate's accounting policies are different from those of the investor, the investor should change the financial statements of the associate by using same accounting policies.

**Carve out**

The phrase, 'unless impracticable to do so' has been added in the relevant requirements i.e. paragraph 26 of Ind AS 28.

**3. Ind AS 32 – Financial Instruments in Presentation Part.**

A carve out as an exception has been included to the definition of 'financial liability' in paragraph 11(b)(ii), Ind AS 32 to consider the equity conversion option embedded in a convertible bond denominated in foreign currency to acquire a fixed number of entity's own equity instruments as an equity instrument if the exercise price is fixed in any currency. This exception is not provided in ISA 32.

**4. Ind AS 39 – Financial Instruments: Recognition and Measurement**

IAS 39 requires all changes in fair values in case of financial liabilities designated at fair value through Profit and Loss at initial recognition shall be recognised in Profit or loss IFRS 9 which will replace IAS 39 requires these to be recognised in 'other comprehensive income'

**Carve out**

A proviso has been added to paragraph 48 of Ind AS 39 that in determining the fair value of the financial liabilities which upon initial recognition are designated at fair value through profit or loss, any change in fair value consequent to changes in the entity's own credit risk shall be ignored.

**5. Ind AS 103, Business Combinations**

IFRS 3 requires bargain purchase gain arising on business combination to be recognised in profit or loss.

**Carve out**

Ind AS 103 requires the same to be recognised in other comprehensive income and accumulated in equity as capital reserve, unless there is no clear evidence for the underlying reason for classification of the business combination as a bargain purchase, in which case, it shall be recognised directly in equity as capital reserve.

**6. Ind AS 101, First-time Adoption of Indian Accounting Standards**

**(i) Presentation of comparatives in the First-time Adoption of Indian Accounting Standards (Ind AS) 101 (corresponding to IFRS 1)**

IFRS 1 defines transitional date as beginning of the earliest period for which an entity presents full comparative information under IFRS. It is this date which is the starting point for IFRS and it is on this date the cumulative impact of transition is recorded based on assessment of conditions at that date by applying the standards retrospectively except to the extent specifically provided in this standard as optional exemptions and mandatory exceptions. Accordingly, the comparatives, i.e., the previous year figures are also presented in the first financial statements prepared under IFRS on the basis of IFRS.

**Carve out**

Ind AS 101, requires an entity to provide comparatives as per the existing notified Accounting Standards. It is provided that, in addition to aforesaid comparatives, an entity may also provide comparatives as per Ind AS on a memorandum basis.

**(ii) Presentation of reconciliation**

IFRS 1 requires reconciliations for opening equity, total comprehensive income, cash flow statement and closing equity for the comparative period to explain the transition to IFRS from previous GAAP.

**Carve out**

Ind AS 101 provides an option to provide a comparative period financial statements on memorandum basis. Where the entities do not exercise this option and, therefore, do not provide comparatives, they need not provide reconciliation for total comprehensive income, cash flow statement and closing equity in the first year of transition but are expected to disclose significant differences pertaining to total comprehensive income. Entities that provide comparatives would have to provide reconciliations which are similar to IFRS.

**(iii) Cost of Non-current Assets Held for Sale and Discontinued Operations on the date of transition on First-time Adoption of Indian Accounting Standards (Ind AS).**

**Carve out**

Ind AS 101 provides transitional relief that while applying Ind AS 105 – Non-current Assets Held for Sale and Discontinued Operations, an entity may use the transitional date circumstances to measure such assets or operations at the lower of carrying value and fair value less cost to sell.

**(iv) Foreign currency gains/losses on translation of long term monetary items**

**Carve out**

Ind AS 101 provides that on the date of transition, if there are long-term monetary assets or long-term monetary liabilities mentioned in paragraph 29A of Ind AS 21, an entity may exercise the option mentioned in that paragraph regarding spreading over the unrealised Gains/Losses over the life of Assets/Liabilities either retrospectively or prospectively. If this option is exercised prospectively, the accumulated exchange differences in respect of those items are deemed to be zero on the date of transition.

**(v) Financial instruments existing on transition date**

**Carve out**

Ind AS 101 provides that the financial instruments carried at amortised cost should be measured in accordance with Ind AS 39 from the date of recognition of financial instruments unless it is impracticable (as defined in Ind AS 8) for an entity to apply retrospectively the effective interest method or the impairment requirements of Ind AS 39. If it is impracticable to do so then the fair value of the financial asset at the date of transition to Ind-ASs shall be the new amortised cost of that financial asset at the date of transition to Ind ASs. Ind AS 101 provides another exemption that financial instruments measured at fair value shall be measured at fair value as on the date of transition to Ind AS.

**(vi) Definition of previous GAAP under Ind AS 101 First-time Adoption of Indian Accounting Standards.**

IFRS 1 defines previous GAAP as the basis of accounting that a first-time adopter used immediately before adopting IFRS.

**Carve out**

Ind AS 101 defines previous GAAP as the basis of accounting that a first-time adopted used immediately before adopting Ind ASs for its reporting requirements in India. For

instance, for companies preparing their financial statements in accordance with the existing Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006 shall consider those financial statements as previous GAAP financial statements.

**(vii) Cost of Property, Plant and Equipment (PPE), Intangible Assets, Investment Property, on the date of transition of First-time Adoption of Indian Accounting Standards.**

Ind AS 101 provides an entity an option to use carrying values of all assets as on the date of transition in accordance with previous GAAP as an acceptable starting point under Ind AS.

**B. Carve outs for specific industries**

**7. Ind AS 18 – Revenue**

On the basis of principles of the IAS 18, IFRIC 15 on Agreement for Construction of Real Estate, prescribes that construction of real estate should be treated as sale of goods and revenue should be recognised when the entity has transferred significant risks and rewards of ownership and has retained neither continuing managerial involvement nor effective control.

**Carve out**

IFRIC 15 has not been included in Ind AS 18, Revenue. Such agreements have been scoped out from Ind AS 18 and have been included in Ind AS 11, Construction Contracts.

**8. Ind AS 18 – Revenue**

**Carve out**

A footnote has been added in paragraph 1 to Ind AS 18, Revenue, that for rate regulated entities, this standard shall stand modified, where and to the extent the recognition and measurement of revenue of such entities is affected by recognition and measurement of regulatory assets/liabilities as per the Guidance Note on the subject being issued by the Institute of Chartered Accountants of India.

**9. Indian Accounting Standard on Agriculture (Corresponding to IAS 41)**

IAS 41, Agriculture, requires measurement of biological assets, viz. living animals and plants at fair value and recognizing gains and losses arising on such measurement in profit or loss, unless ascertainment of fair value is unreliable...

**Carve out**

It has been decided to revise the Standard and not to issue the standard as it is.

**10. Ind AS 19 – Employee Benefits vis-a-vis IFRSs/IASs restricting options.**

According to Ind AS 19 the rate to be used to discount post-employment benefit obligation shall be determined by reference to the market yields on government bonds, whereas under IAS 19, the government bonds can be used only where there is no deep market of high quality corporate bonds. To illustrate treatment of gratuity subject to ceiling under Indian Gratuity Rules, an example has been added in Ind AS 19. IAS 19 permits various options for treatment of actuarial gains and losses for post – employment defined benefit plans whereas Ind AS 19 requires recognition of the same in other comprehensive income, both for post-employment defined benefit plans and other long-term employment benefit plans. The actuarial gains recognised in other comprehensive income should be recognised immediately in retained earnings and should not be reclassified to profit or loss in a subsequent period.

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# FROM PUBLISHED ACCOUNTS

## AS 6 - Depreciation Accounting

### COAL INDIA LIMITED ANNUAL REPORT 2010-11

**A. Significant accounting Policies:**

**7.0 DEPRECIATION**

7.1 Depreciation on fixed asset is provided on straight line method at the rates and manner specified in schedule XVI of the companies Act, 1956 (as amended) except for:

| | | |
|---|---|---|
| (a) | The Earth Science Museum | 5.15% |
| (b) | High volume samplers and respiratory dust | 33.33% |
| (c) | Telecommunication Equipment | 15.83% |
| (d) | General Communication/ Instrumentation Systems | 10.55% |

Depreciation on such equipment is charged over the technically estimated life, at higher rates.

Further, depreciation on such equipments/ HEMM is charged over the technically estimated life at higher rates viz. 11.88%, 13.57%, and 15.83% as applicable. Depreciation on asset added/ disposed off during the year is provided on pro-rata basis with reference to the month of addition/disposal, except on those assets attracting 100% depreciation (SLM basis) which are fully depreciated in the year of their addition.

Value of land acquired under Coal Bearing area (acquisition & development) Act, 1957 is amortized on the basis of the balance life of the project. Value of leasehold land is amortized on the basis of lease period or balance life of the project whichever is earlier.

7.2 Prospecting, boring and development expenditure are amortized from the year when the mine is brought under revenue, in 20 years or working life of the project whichever is less.

**CA. Pamil H. Shah**
*The author is practising since 1995. He can be reached at pamil_shah@yahoo.com*

7.3 Depreciation on SDL and LHD (equipments) are charged @19% p.a. and @15.83% p.a. respectively.

7.4 Depreciation after major overhauling of Helicopter is charged @47.5% p.a., based on its expected year of life/flying hours.

### TECPRO SYSTEMS LIMITED ANNUAL REPORT 2010-11

**Schedule 14: Significant accounting Policies and Notes to the Accounts**

**(g) Depreciation**

Depreciation is provided on a pro-rata basis under the straight line method. The rates of depreciation prescribed in schedule XVI to the Companies Act, 1956 are considered as the minimum rates. If the management's estimate of the useful life of a fixed asset at the time of acquisition of the asset or of the remaining useful life on a subsequent review is shorter than that envisaged in the aforesaid schedule, depreciation is provided at a higher rate based on the management's estimate of the useful life/ remaining useful life. Rates of depreciation (where different from the rates prescribed in Schedule XVI to the companies Act, 1956) have been derived on the basis of the following estimated useful lives:

| | Estimated useful life (in years) |
|---|---|
| Office equipment | 6 |
| Furniture and fixtures | 5 |
| Vehicles | 2-10 |
| Temporary sheds at project sites (To continue with the project period)* | 1-5 |

| | |
|---|---|
| Patterns | 3 |
| Shuttering and Scaffolding** | 4 |
| Office building* | 28.44 |

*Included in Building in Schedule 5 of the financial statements

**Included in Plant and Machinery in Schedule 5 of the financial statements

Leasehold land is amortized over the period of the lease. Leasehold improvements are depreciated over the period of lease or the useful life of the underlying asset, whichever is less.

Depreciation on additions is being provided on a pro rata basis from the date of such addition. Similarly, depreciation on asset sold/ disposed off during the year is being provided up to the date on which such assets are sold/ disposed off.

Asset costing individually Rs. 5000 or less are depreciated fully in the year of purchase.

**ONGC ANNUAL REPORT 2010-11**

**Schedule-26:**

**13. Depreciation and Amortization**

13.1 Depreciation on fixed assets is provided for under the written down value method in accordance with the rates specified in Schedule XIV to the Companies Act, 1956.

13.2 Depreciation on additions/ deletions during the year is provided on pro rata basis with reference to the date of additions/ deletions except items of plant and machinery used in wells with 100% rate of depreciation and low value items not exceeding Rs. 5000/- which are fully depreciated at the time of additions.

13.3 Depreciation on subsequent expenditure on fixed assets arising on account of capital improvement or other factors is provided for prospectively.

Depreciation on refurbished/ revamped assets which are capitalized separately is provided for over the reassessed useful life at the rates which are not less than the rates specified in Schedule XIV to the Companies Act, 1956.

13.4 Depreciation on fixed assets (including support equipment and facilities) used for exploration, drilling activities and on related equipment and facilities is initially capitalized as part of exploration cost, or producing properties and expensed/ depleted as stated in policy 6 above.

13.5 Leasehold land is amortized over the lease period except perpetual leases.

13.6 Intangible assets are amortized over the useful life not exceeding five years from the date of capitalization.

**PETRONET LNG LIMITED 2010-11**

**Schedule 17: Significant accounting Policies**

**4. Depreciation/ Amortization**

Tangible Assets -

(a) Cost of lease hold land is amortized over the lease period.

(b) Depreciation on fixed assets other than those costing upto Rs.5,000 is provided on straight line method in accordance with the rates and in the manner specified in Schedule XIV of the Companies Act, 1956.

(c) Assets costing upto Rs.5,000/- are depreciated fully in the year of purchase/ capitalization.

Intangible Assets –

(d) Software/ Licenses are amortized over 3 years on straight line Method.

**ADANI POWER LIMITED 2010-11**

**SCHEDULE- 19 Significant Accounting Policies and Notes on Consolidated Accounts**

**7. Depreciation**

(i) Depreciation on fixed assets is provided on straight line method at rates and in the manner specified in schedule XIV to the companies Act, 1956.

(ii) Depreciation on Assets acquired/ disposed off during the year is provided on pro-rata basis with reference to the date of addition/disposal.

(iii) Assets costing less than Rs.5000/- are written off in the year of purchase.

(iv) Cost of lease hold land is amortized over a period of lease.

(v) Cost of Intangible assets are amortized over the period of 5 years.

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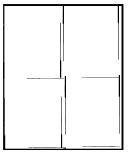
# BITS & BYTES

## Information System Audit.



**CA. B. M. Zinzuvadia**
*The author is practising since 2001. He can be reached at bmzinzuvadia@cmshah.com*

Before we discuss information system audit, we must look into the Information System and understand what Information System is? A computer is integral part of the information system, besides, the organizational structure, policies and procedures of the organization also play vital roles in development of information system in an organization.

First we need to understand computer system. Earlier computers were big in size and slower in speed. The new generation of computers are smaller and faster. The cost of computers reduced over a period as they become smaller and faster. The size of the computer has now become irrelevant, some personal computers are more powerful than old day's mini and mainframe computers. Better classification of computer would be, in term of their functions, such as a computer can be a server, or a client/workstation or a standalone computer.

A workstation is basically a client computer which is connected with the more powerful server. The term workstation is now outdated. A server is a computer system that provides services to other computers attached to it. The computers attached to the servers are called clients. It is not necessary that a client must be a computer, it can be a part of computer also, say, a printer can be a client. Some time it can be a server also for printing service. Servers mainly work on network and they process service requests from the clients. A server can offer multiple services at a time. Present day servers are almost similar to the personal computer with some modification in the hardware and internal structure.

## Components of a computer system.

Basically, computers are data processing machine and as in other machines, it obtains data (the raw material) through input devices, and processes that data in processing units and releases the processed data through different output devices.

Thus it has input devices, processing parts and output devices. Majority of the data storage device work as input devices as well as output devices. Data processing devices are unique and they perform the assigned task only.

### Input Devices

Any device that collects data for the central processing unit is input device. Thus keyboard, mouse and data storage units are input devices.

Touch screen, light pen, trackball and joystick are some advanced version of input devices.

### Processing units

The central processing unit (CPU) is the heart of the computer system. The mother board with hard disk, slots for other devices, RAM, other circuits and processers to gather makes Central Processing unit. Followings are important amongst them.

1. Processors.

   The processors are sometime itself refers as CPU. The reason is very simple, it performs the most important work of a computer. It processes the data. Basically, processor has two parts. Control unit and arithmetic logic unit. Control unit understand the commands and execute the command. Majority of the work done by control unit involve moving/copying data, say reading files

*Contd. on page no. 606*

# FROM THE GOVERNMENT

**CA. Chandrakant H. Pamnani**
*The author is the President of CAA. He can be reached at chpamnani@gmail.com*

**CA. Kunal A. Shah**
*The author is the Hon. Secretary of CAA. He can be reached at cakashah@gmail.com*

## (A) INCOME TAX

### (1) *Exemption to specified persons from requirement of furnishing a return of income u/s 139(1) for AY 12-13.*

The Central Government hereby exempts the following class of persons, subject to the conditions specified hereinafter, from the requirement of furnishing a return of income under sub-section (1) of section 139 for the assessment year 2012-13, namely:-

An individual whose total income for the relevant assessment year does not exceed five lakh rupees and consists of only income chargeable to income-tax under the following head,-

(A) Salaries ;

(B) Income from other sources , by way of interest from a saving account in a bank, not exceeding ten thousand rupees.

**(***For Full text refer NOTIFICATION NO. 9/2012 , dated 17-2-2012)*

## (B) SERVICE TAX

### (1) *Levy of service tax on toll in the nature of 'user charge' or 'access fee' paid by roads users.*

Service tax is not leviable on toll paid by the users of roads, including those roads constructed by a Special Purpose Vehicle (SPV) created under an agreement between National Highway Authority of India (NHAI) or a State Authority and the concessionaire (Public Private Partnership Model, Build-Own/Operate-Transfer arrangement). 'Tolls' is a matter enumerated (serial number 59) in List-II (State List), in the Seventh Schedule of the Constitution of India and the same is not covered by any of the taxable services at present. Tolls collected under the PPP model by the SPV is collection on own account and not on behalf of the person who has made the land available for construction of the road.

However, if the SPV engages an independent entity to collect toll from users on its behalf and a part of toll collection is retained by that independent entity as commission or is compensated in any other manner, service tax liability arises on such commission or charges, under the Business Auxiliary Service [section 65(105) (zzb) read with section 65(19) of the Finance Act, 1994].

***(Refer Circular no 152, dated 22/02/2012)***

### (2) *Clarification regarding whether value of free of cost supplies is included in the Works Contract Composition Scheme for the period prior to 07/07/2009*

The meaning of the expression 'gross amount' appearing in Rule 3(1) of the Works Contract (Composition Scheme for Payment of Service Tax) Rules, 2007, is qualified by the *Explanation* inserted in the said Rule with effect from 07/07/2009. Since the *Explanation* inserted in Rule 3(1) with effect from 07/07/2009 is clarificatory and prospective in nature, inclusion of value of free-of-cost supplies of goods and services in or in relation to the execution of Works Contract [mentioned in the *Explanation* to Rule 3(1) (a) (i) and (ii)] in the 'gross amount' for the purpose of

payment of service tax on works contract under the composition scheme, is a legal requirement, only with effect from 07/07/2009 when the *Explanation* became a part of Rule 3(1).

Where execution of works contract has commenced prior to 07/07/2009 or where any payment(except payment through credit or debit) has been made towards a works contract prior to 07/07/2009, then in those cases 'gross amount' for the purpose of payment of service tax does not include the value of free of cost supplies.

***(Refer Circular no-150, dated 08/02/2012)***

***(3) Imposition of Service Tax on Construction Services***

With respect to the levy and collection of service tax on construction services in pursuance of clauses zzq and zzzh of sec 65(105), clarification in respect of the following business models have been specified in this circular :-

a) Tripartite Business Model;

b) Redevelopment including slum rehabilitation projects;

c) Investment model;

d) Conversion model;

e) Non requirement of completion certificate;

f) Build-Operate-Transfer (BOT) projects;

g) Joint Development Agreement Model

***(For Full text refer Circular no – 151, dated 10/02/2012)***

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*Contd. from page no. 603* 

from storage devices or saving data on it. The arithmetic logic unit has two basic works to do. Arithmetic calculation such as summation, multiplication etc. and logical such as taking decisions.

2. Cache

Cache is internal temporary memories inbuilt in processors.

3. Mother board

Mother board is main circuit on which different component of the computers are mounted and it works as main channel for the data flow as well as power supply to those components. It contains different slots on it. Slots provide facility to expand the present working capacity of the computer.

4. Ports and connections.

Ports and connections let the user connect external devices such as printer, USB device etc.

5. Storage devices.

The CPU contains basic instructions stored in its inbuilt memory but it does not have any facility to store data on large scale. For such data, it needs added facility. The hard disk provides that facility. It works as input as well as output device for the processor.

6. RAM.

Random Access Memories are short term storage of large data while processing. It is primary data storage, and its presence is necessary for processor to work.

**Output Devices**

Output devices are parts that release processed data from the computer. A monitor is output device, a printer and speaker in a music system is output device.

As a system auditor, we need to understand the function of these devices, there is no need to go in technical details of these items. However, knowledge of technical information is additional qualification. Some technical knowledge is required at least to use and understand the computer jargon and to deal with technical persons. Especially in case of data storage and the method of data storage needs some technical knowledge also. We will discuss some technical part of data storage in detail next time.

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# HEALTH AND FUN

## HEALTH

### HIVES

Hives are raised, often itchy, red welts on the surface of the skin. They are usually an allergic reaction to food or medicine.

Hives usually cause itching, but may also burn or sting. They can appear anywhere on the body, including the face, lips, tongue, throat, or ears. Hives vary in size (from a pencil eraser to a dinner plate), and may join together to form larger areas known as plaques. They can last for hours, or up to one day before fading.

Angioedema is similar to hives, but the swelling occurs beneath the skin instead of on the surface. Angioedema is characterized by deep swelling around the eyes and lips and sometimes of the genitals, hands, and feet. It generally lasts longer than hives, but the swelling usually goes away in less than 24 hours.

*Causes*

When you have an allergic reaction to a substance, your body releases histamine and other chemicals into your bloodstream. This causes itching, swelling, and other symptoms. Hives are a common reaction, especially in people with other allergies such as hay fever.

Allergic reactions, chemicals in certain foods, insect stings, sunlight exposure, or medicines can all cause histamine release. Sometimes it's impossible to find out exactly why hives have formed.

*Classification*

Acute : Hives lasting less than six weeks. The most common causes are certain foods, medicines, or infections. Insect bites and internal disease may also be responsible.

The most common foods that cause hives are nuts, chocolate, fish, tomatoes, eggs, fresh berries, and milk. Fresh foods cause hives more often than cooked foods. Certain food additives and preservatives may also be to blame.

Drugs that can cause hives and angioedema include aspirin and other nonsteroidal anti-inflammatory medications, high blood pressure drugs, or painkillers.

**CA. Ganesh Nadar**
*Practising since 1996. He can be reached at ganesh@dgsm.co.in*

Chronic and angioedema: Hives lasting more than six weeks. The cause of this type of hives is usually more difficult to identify than those causing acute.

It can affect other internal organs such as the lungs, muscles, and gastrointestinal tract. Symptoms include muscle soreness, shortness of breath, vomiting, and diarrhea.

Physical: Hives caused by direct physical stimulation of the skin — for example, cold, heat, sun exposure, vibration, pressure, sweating, and exercise. The hives usually occur right where the skin was stimulated and rarely appear elsewhere. Most of the hives appear within one hour after exposure.

Dermatographism: Hives that form after firmly stroking or scratching the skin. These hives can also occur along with other forms.

*Complication*

Hives and angioedema nearly always cause:

- Itching
- Discomfort

In more-serious cases — such as when swelling occurs inside your mouth or throat — complications can include:

- Difficulty breathing.
- Loss of consciousness.
- Anaphylactic shock — a serious allergic reaction involving your heart and lungs. Your bronchial tubes narrow, it's difficult to breathe, and your blood pressure drops, causing dizziness and perhaps loss of consciousness or even death. Anaphylactic shock occurs rapidly and requires immediate medical care.

*Treatment*

The best treatment for hives and angiodema is to identify and remove the trigger, but this is not an easy task. Antihistamines are usually prescribed by your doctor or dermatologist to provide relief from symptoms.

*Management*

While waiting for hives and swelling to disappear, here are some tips:

- Apply cool compresses or wet cloths to the affected areas.
- Try to work and sleep in a cool room.
- Wear loose-fitting lightweight clothes.

**FUN**

**Every proverb has an equal and an opposite proverb.**

NEWTON'S THIRD LAW STATES: "Every Action has an equal and an opposite reaction... "

Similarly, every proverb has an equal and an opposite proverb! There always exist two sides of the same coin!

All good things come to those who wait

BUT Time and tide wait for none.

The pen is mightier than the sword.

BUT Actions speak louder than words.

Wise men think alike.

BUT Fools seldom differ.

There's no such thing as a free lunch.

BUT The best things in life are free

Slow and steady wins the race

BUT Time waits for none.

Do it well, or not at all.

BUT Half a loaf is better than none.

Birds of a feather flock together.

BUT Opposites attract.

Doubt is the beginning of wisdom.

BUT Faith will move mountains.

Great starts make great finishes.

BUT It isn't over till it's over.

Practice makes perfect.

BUT All work and no play makes Jack a dull boy.

You're never too old to learn.

BUT You can't teach an old dog new tricks

What's good for the goose is good for the gander.

BUT One man's meat is another man's poison.

Hold fast to the words of your ancestors.

BUT Wise men make proverbs and fools repeat them.

**Determination and Persistence**

In 1883, a creative engineer named John Roebling was inspired by an idea to build a spectacular bridge connecting New York with the Long Island. However bridge building experts throughout the world thought that this was an impossible feat and told Roebling to forget the idea. It just could not be done. It was not practical. It had never been done before.

Roebling could not ignore the vision he had in his mind of this bridge. He thought about it all the time and he knew deep in his heart that it could be done. He just had to share the dream with someone else. After much discussion and persuasion he managed to convince his son Washington, an up coming engineer, that the bridge in fact could be built.

Working together for the first time, the father and son developed concepts of how it could be accomplished and how the obstacles could be overcome. With great excitement and inspiration, and the headiness of a wild challenge before them, they hired their crew and began to build their dream bridge.

The project started well, but when it was only a few months underway a tragic accident on the site took the life of John Roebling. Washington was also injured and left with a certain amount of brain damage, which resulted in him not being able to talk or walk.

"We told them so." "Crazy men and their crazy dreams." "It's foolish to chase wild visions."

Everyone had a negative comment to make and felt that the project should be scrapped since the Roeblings were the only ones who knew how the bridge could be built.

In spite of his handicap Washington was never discouraged and still had a burning desire to complete the bridge and his mind was still as sharp as ever. He tried to inspire and pass on his enthusiasm to some of

his friends, but they were too daunted by the task.

As he lay on his bed in his hospital room, with the sunlight streaming through the windows, a gentle breeze blew the flimsy white curtains apart and he was able to see the sky and the tops of the trees outside for just a moment.

It seemed that there was a message for him not to give up. Suddenly an idea hit him. All he could do was move one finger and he decided to make the best use of it. By moving this, he slowly developed a code of communication with his wife.

He touched his wife's arm with that finger, indicating to her that he wanted her to call the engineers again. Then he used the same method of tapping her arm to tell the engineers what to do. It seemed foolish but the project was under way again.

For 13 years Washington tapped out his instructions with his finger on his wife's arm, until the bridge was finally completed. Today the spectacular Brooklyn Bridge stands in all its glory as a tribute to the triumph of one man's indomitable spirit and his determination not to be defeated by circumstances. It is also a tribute to the engineers and their team work, and to their faith in a man who was considered mad by half the world. It stands too as a tangible monument to the love and devotion of his wife who for 13 long years patiently decoded the messages of her husband and told the engineers what to do.

*Perhaps this is one of the best examples of a never-say-die attitude that overcomes a terrible physical handicap and achieves an impossible goal.*

Often when we face obstacles in our day-to-day life, our hurdles seem very small in comparison to what many others have to face. The Brooklyn Bridge shows us that dreams that seem impossible can be realised with determination and persistence, no matter what the odds are.

**Difference between COMPLETE & FINISHED**

People say there is no difference between COMPLETE & FINISHED.

But there is. When you marry the right one, you are COMPLETE.

And when you marry the wrong one, you are FINISHED.

And when the right one catches you with the wrong one, you are... COMPLETELY FINISHED.

**New Generation - Today's Students**

We go to school, to attend "CLASS" .

C.L.A.S.S. = Come Late And Sleep Silently.

At home, we have to "STUDY".

S.T.U.D.Y. = Sleep, TV, Unlimited-sms, Dost, Youtube.

In class, we're given "HOMEWORK."

H.O.M.E.W.O.R.K = Half Of My Energy Wasted On Random Knowledge.

While doing homework, we refer to "TEXTBOOK".

TEXTBOOK = TEXTing + faceBOOK

**Our tribute to the CWG 2010 (Common wealth games in Delhi)**

I think so there will be only one sport this year in CWG 2010... swimming.... since Delhi is flooded.

If you rearrange the letters 'Sir U Made Lakhs', you get 'Suresh Kalmadi'.

Terrorists set to skip CWG 2010 citing unlivable conditions and fear for their safety.

Who says India used to be 'sone ki chidiya'! It's still 'sone ki chidiya' ask Kalmadi!

Whats common between CWG committee and students???

Ans: both start their preparations at the 11th hour.....

With Pak Eng series more or less dusted the bookies will start betting on which roof will fall next at the CWG ...

The problem began when they decided to call it CWG village. The definition of village does vary from person to person doesn't it?

The chairman of the indian commonwealth games tried to hang himself but the ceiling collapsed...

At the 100 mts race at CWG they might fix a board near start line - GO SLOW, MEN AT WORK!

Q: How many contractors are required to change a light bulb in Delhi CWG stadium?

A: 1 Million. (1 to change bulb and rest 999,999 to hold the ceiling)

*(Information compiled from various sources from internet)*

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# ASSOCIATION NEWS

**CA. Kunal A. Shah**
*Hon. Secretary*

**CA. Ashok C. Kataria**
*Hon. Secretary*

## (A) FORTHCOMING PROGRAMMES

Details of forthcoming programme are as under:-

| Date/Day | Time | Programmes | Speaker | Venue |
|---|---|---|---|---|
| 20/03/2012 Tuesday | 5.30 PM | Technical Aspects of the Finance Bill,2012 | Saurabh N. Soparkar (Senior Advocate) | Town Hall, Ellis bridge, Ahmedabad |
| 21/03/2012 Wednesday | 4.00 PM | Technical Aspects of the Finance Bill,2012 on Service Tax and Central Excise | CA. S.S. Gupta (Mumbai) | Town Hall, Ellis bridge, Ahmedabad |
| 26/03/2012 Monday | 5.30 PM to 7.30 PM | Shri K. T. Thakore Memorial Lecture on Right to Information "RIT as a Tool to Compat Corruption" | Shri Narayan Varma, Mumbai | Shantinath Hall, ICAI Bhawan, 123, Sardar Patel Colony, Naranpura, Ahmedabad. |

## (B) IN RETROPECT

| Date/Day | Time | Programmes | Speaker | Venue |
|---|---|---|---|---|
| 08/02/2012 Wednesday | 5.30 to 7.30 PM | 4th Study Circle Meeting on "Analysis of Recent Judgment in Vodafone Case" | CA. Dhinal A Shah | Shantinath Hall, ICAI Bhawan, 123, Sardar Patel Colony, Naranpura, Ahmedabad. |
| 18/02/2012 Saturday | 5.30 to 7.30 PM | 5th Study Circle Meeting on Issues under Service Tax | CA. Hardik P Shah Surat | Shantinath Hall, ICAI Bhawan, 123, Sardar Patel Colony, Naranpura, Ahmedabad. |
| 22/02/2012 Wednesday | 5.00 PM | P. D. Prog. Lecture on "Offshore Overseas Companies - Opportunities & Challenges" | CA. Vipul Kothari, Dubai UAE | Shantinath Hall, ICAI Bhawan, 123, Sardar Patel Colony, Naranpura, Ahmedabad. |
| 03/03/2012 Saturday | | 4th Brain Trust Meeting on Issues relating to TDS and HUF (Charitable Trust If time permits) | Dr. Girish Ahuja | Shantinath Hall, ICAI Bhawan, 123, Sardar Patel Colony, Naranpura, Ahmedabad. |

GENERAL REMINDER

The members are requested to intimate changes in their email ID & mobile phone number at the Association's office, which will help the office bearers to remind you about the programmes through email and SMS.

Members who have not yet paid their contribution under the Mutual Benefit Scheme are kindly requested to pay the same at the earliest.

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