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In this issue ....

Quote of the month

"Whatever you do, make sure you do something you really like, so you don't just have your vacation to look forward to."

— Jerry Bruckheimer

We wish all our members, subscribers, readers, advertisers and well-wishers a happy and prosperous New Year.

Front cover

The confluence of pictorial feathers depicts BCAS's mission of spreading knowledge to promote excellence in ourselves and our services; and we know, sky is the limit.

Disclaimer

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Namaskaar
Namaskaar

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K. C. Narang
Chartered Accountant

Tend your garden regularly (Part II)

The question I ask myself is :

'Does my garden end with the mind-body complex ?'

The answer is **No** : It is only one part of the triangle that is 'the garden'. The other two are the 'family' and the 'society'. To have a happy life — a blooming garden — I must equally look after the other two parts. It is said : 'A happy family is the cornerstone of a happy society' — and to have a happy family it is my duty to look after their needs — both material and emotional. It is because of this that our society is 'duty-based' and not 'right-based'. We have forgotten that our rights, if at all they arise, arise only on our performing of our duty. In the present materialistic environment and in our pursuit for 'material success', the prevailing concept is that providing for material needs of the family is enough. In doing this we are overlooking a very essential ingredient — the **tending** of **emotions**. 'Emotional care' is as important if not more than material care. It has been scientifically proved that if a gardener devotes a little time and love to a plant in the garden the plant blooms better than the untended ones. Now if this is true of a plant, how true it would be of human beings. Hence it is essential to take care of the emotional needs of the family. The result would be — less old-age homes, less broken families, less of conflict and fewer divorces — a happy family. Some of us have started realising the importance of emotional care leading to the concept of spending **quality time** with the family. It is said, 'we use only ten percent of our brain'. I think we also use only ten percent of our heart. Imagine : what would life be if we were to use a little more of both, the head and the heart.

A happy family is an important constituent of a happy society. Hence the third limb of the garden is the 'Society'. We have to continually ask ourselves — as to what and how are we contributing to improve the environment in which we live. The converse of 'a happy family means a happy society' — 'a happy society ensures a happy family' is also true. Let us spend some time in serving our society either alone or through a social, professional or a religious organisation. Let us join and become an active member of a group.

This 'tending of our garden' has been beautifully summarised by Janos Selye as under :

> "A sincere balanced and kind attitude towards ourselves as well as others is the key to happiness and success in life's all avenues."

The next question is : how can we do this ? There is no short-cut. What is required is a conscious continued effort to create a balance in tending all parts of our garden.

So let us consciously tend all the parts of our triangular garden.

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ADVT.

The Move to IFRS

Editorial

The New Year heralds the end of a tax assessment season. I hope most of us have not heartily welcomed the New Year just out of relief that it signals the end of tax assessments (see poem on page 482), as well as the deadlines for compliance with CPE credit requirements.

While we sit back and relax from a hectic schedule, we also need to utilise the break and the New Year to analyse fresh opportunities and take up new initiatives, which will help us grow professionally. One such opportunity lies in the ushering in of International Financial Reporting Standard (IFRS) from 1st April 2011.

Till recently, Chartered Accountants in India had only to cope with frequent changes in tax laws, and spend substantial time educating themselves on the amended tax law provisions. Changes in accounting standards (AS) were not so frequent, and generally far less, mainly in the form of new accounting standards, and therefore did not require much study.

The recent proposal of the Institute of Chartered Accountants of India (ICAI) to move to IFRS with effect from 1st April 2011 will change that scenario for the next few years. Each one of us will need to spend a significant amount of time unlearning the old standards and relearning the new ones.

Fortunately, ICAI has restricted the applicability of IFRSs to Public Interest Entities (listed companies, banks, insurance companies, etc. or companies having turnover of more than Rs.100 crore or borrowings of more than Rs.25 crore or that holding/subsidiary companies). IFRSs in their present form would not apply to Small and Medium Entities (SMEs). This was necessary. One shudders even at the thought of ever having had to apply IFRSs to the tax audit of a proprietary concern — whether the concern would ever have understood IFRS and whether the auditor would ever have been rewarded for his additional efforts in ensuring IFRS compliance is extremely doubtful.

The move to IFRS is a welcome one, considering the extent of globalisation of the Indian economy. It is essential for our larger companies to follow IFRS, if their global ambitions are taken into account. Internationally, of course, opinion is divided as to whether IFRS in their current form are the solution to all accounting problems (see Accountant Abroad, page 445 of this issue).

The problems of implementation also are many, as highlighted by the recent Concept Paper on Convergence with IFRSs in India brought out

by ICAI. The major problem is of course the provisions of law which are contrary to various aspects of IFRS. Schedule VI of the Companies Act has not kept pace with the changing times. It has been amended, but unfortunately only for tinkering with it for purposes other than accounting, such as to disclose amounts due to micro-enterprises, etc. It takes over 4 years for a new company law to even be considered by Parliament. Will the legal changes required take place in time, or will we have to deal with a situation where the legal provisions override IFRS (as was the situation with revised AS 11) ? Would IFRS be mandatory only for auditors, or would it be made mandatory at the same time and in the same manner for companies as well, by notification under the Companies Act ?

One gets an idea of the amount of difficulties that would be faced by looking at the recent ASs issued by ICAI, which are quite similar to IFRS. Most of us would be looking at implementation of the revised AS 15, where one has now to consider all employee benefits, not just retirement benefits, customary benefits as well as contractual ones, and which requires detailed disclosures of actuarial assumptions. The new AS 30 and AS 31 require a significant relook at our accounting concepts, with redeemable preference shares having to be disclosed as debt, mark-to-market valuation of investments even if resulting in a profit, etc. The very size of the standards is daunting, even to CAs who are used to heavy reading. In fact, the Concept Paper suggests that ***50 hours of CPE credit per year only on IFRS*** *may be considered for members in practice as well as in industry till 2011. That gives us an idea of the size and significance of the change.*

The complexity of IFRS also brings home the fact that each one of us now needs to look at a greater degree of specialisation, if one is to keep pace with the developments in different fields. Having a passing knowledge of everything is becoming increasingly difficult, and dangerous. One may need to join hands with other like-minded CAs specialising in different fields to provide clients with all-round services, instead of providing the services by oneself.

CAs in India have always welcomed challenges. Learning and adapting to IFRS will provide us with the skills necessary to provide services in the field of accounting anywhere in the world. It will provide us an opportunity to take our practice to new geographical frontiers, by providing services to companies worldwide. Let us embrace this opportunity and start upgrading our skills in this New Year !

Wishing each one of you a Happy and Professionally Satisfying New Year !

Gautam Nayak

FROM THE PRESIDENT

Dear professional colleagues,

In the knowledge-driven global marketplace, intangible assets command better value than tangible assets. India has emerged as the third economy in the world barring the US and Switzerland with the highest intangible component as a percentage of the total enterprise value (TEV), value of disclosed and undisclosed tangible and intangible assets. According to Global Intangible Tracker 2007, an extensive global study on intangibles assets conducted by the London-based Brand Finance Institute, India with an estimated intangible assets component of 74% as a proportion of Total Enterprise Value (TEV) is ranked 3rd, just behind US and Switzerland.

It is certainly a matter of pride for India. The country's intellectual capital is poised for a big leap. Accounting Profession in India with its untapped potential is capable of making great value addition to this pool of intangible assets. Its ability to deliver quality service and solutions across different areas of practice will be crucial for the growth of the profession. Since the profession has the strength and vision to compete with the best brains of the world, I believe, Indian CAs will make their mark in the world economy in the days to come.

In a recently concluded 'World Accountancy Week' the International Federation of Accountants (IFAC) released the results of its first IFAC 2007 Global Leadership Survey. The worldwide leaders of the professional accountancy organisations surveyed by the IFAC believe that, a strong accountancy profession plays a key role in the country's economic growth and development. Key findings of the survey affecting the economy and the accounting profession are :

- ✓ *Desirability of convergence to a single set of international standards on auditing (ISAs) and on financial reporting (IFRSs).*
- ✓ *Adopting good practices in internal control and risk management in business.*
- ✓ *Dampening effect on an economy due to limited supply of qualified accounting professionals.*
- ✓ *Perception of accountants' integrity by the public and regulators.*
- ✓ *Reputation of the profession.*
- ✓ *Application of International Public Sector Accounting Standards to public sector bodies and Governments.*

With Indian economy aligning to the world economy, the Indian Accounting Profession needs to give a thought to these findings. Step towards adopting IFRS for listed entities in India is in the right direction. Profession must also be careful in maintaining and enhancing its reputation through quality service and ethical conduct, while attracting good young talent to the profession.

Internet has become an essential part of life including the field of education.

A study on online education supported by the Alfred P. Sloan Foundation based on responses from more than 2500 colleges and universities in U.S. reveals that nearly 3.5 million students participated in on-line learning at institutions of higher education in the United States in 2006. The participants of e-learning courses generally appear to be satisfied with their on-line classes as they are with the traditional ones.

BCAS, a forerunner in the field of professional education, is launching an e-learning course on service tax. It will be unveiled during the Residential Refresher Course soon to be held at Mahabaleshwar. This is the first professional course of its kind imparted through the internet in India. E-learning is an advanced learning technology that will transcend the geographical boundaries, eliminating the need to physically travel to the learning centre. These flexible learning programmes will make knowledge available on the subjects of interest in professional practice, at the desktops. E-learning Courses on TDS and accounting standards will also follow soon. Understanding these subjects through the medium of e-learning would be a wonderful experience for the members and others.

As North Block gets ready to present the Union Budget in less than two months from now, one aspect of the fiscal it can look at with justifiable pride is the strong flow of direct tax revenues with a growth of 45 per cent during the year. This is an appropriate time for the Government to seriously consider amending/dropping unfair and inequitable provisions in tax laws. This only will build tax payer confidence and make compliance with law easy.

On indirect tax front, estimates suggest that the entire range of domestic indirect taxes, Central and State, mark up the cost of Indian goods from computers to automotives by 25-30 per cent, in contrast to China's 15 per cent. The high levels of indirect taxes have a cascading effect on overall prices. It is hoped that the changes in the ensuing Budget will aim at leveraging the growth in indirect taxes to reduce overall costs in the economy.

BCAS has made representation to the Finance Minister on direct tax laws and service tax laws and has given various suggestions to simplify the law.

End of 2007 and beginning of 2008 are on the horizon. New Year brings new hopes, new resolutions, new vision and new opportunities. I wish each one of you a very successful, exciting and stimulating new year and end with the following :

Here's wishing you the top o' life without a single tumble.
Here's wishing you the smiles o' life and not a single grumble.
Here's wishing you the best o' life and not a claw about it.
Here's wishing you the joy in life and not a day without it.

With regards,

Rajesh Kothari

Article

Scope of clause (a) of explanation to S. 115JB — *The amount of Income-tax paid or payable, and the provision therefor*

H. Padamchand Khincha
Badrinath Simha
Chartered Accountants

Introduction :

S. 115JB(1) of the Income-tax Act, 1961 (Act in short) provides for payment of a minimum alternate tax in case the Income-tax computed on the total income falls short of 10% of the book profits of the company. For ensuring that companies do not adopt accounting practices to render the provision otiose, Ss.(2) requires the profit and loss account of companies to be prepared as per Parts II and III of Schedule VI to the Companies Act, 1956. Proviso to this sub-section further ensures that the accounting policies, accounting standards and the method and rates of depreciation adopted for the purposes of S. 210 of the Companies Act, are not varied while computing 'book profit' u/s.115JB.

Explanation to S. 115JB(2) defines 'book profits'. It is on this book profit that the minimum alternate tax has to be computed U/ss.(1). The explanation states that 'book profit' is the net profit computed U/ss.(2) and adjusted for specific additions and reductions. The adjustments specified in the explanation are exhaustive and the Income-tax authorities have no right to make other adjustments while computing the book profits. [*Apollo Tyres Ltd. v. CIT,* (2002) 255 ITR 273 (SC)]

One of the items required to be added back to the net profit is "*the amount of income-tax paid or payable, and the provision therefor*". [clause (a) of the Explanation]. In this article, an attempt has been made to examine the scope of this clause. The crucial words used in clause (a) of the explanation are 'income-tax', 'paid', 'payable' and 'provision'. Understanding of the meaning of each of these words is *sine qua non* for examining the scope of clause (a).

(a) ***Income-tax :***

Neither S. 115JB, nor any other provision of the Act defines the term 'Income-tax'. To understand the meaning of this term, one has to refer to the definition of the term 'tax' in S. 2(43) of the Act. The definition of the term 'tax', which is exclusive in nature, is pertinent for our discussion. S. 2(43) defines the term 'tax' to mean Income-tax chargeable under the provisions of the Act and fringe benefit tax payable u/s.115WA. The charging section under the Act is S. 4. It provides that Income-tax shall be charged for a particular assessment year in accordance with and subject to the provisions (including provisions for the levy of additional Income-tax) of the Act, in respect of the total income of the previous year of every person, at the rate or rates of tax enacted by any Central Act for that year.

By jointly reading S. 2(43) with S. 4, one can define 'Income-tax' as "*a tax on the total income of the previous year of every person at the rates prescribed by any Central Act. In addition to tax on total income, Income-tax also includes any additional Income-tax computed as per the provisions of the Act.*"

(b) ***Paid :***

The term 'paid' is the past tense of the term 'pay'. The Shorter Oxford English Dictionary, fifth edition, 2002, volume 2, page 2126 defines the term 'pay' to mean "*give (a thing owed, due, or deserved); discharge (an obligation, promise, etc.)*". The term 'pay' has many meanings attributable to it depending upon the context in which it is used.

When used in relation to tax under the Income-tax Act, the word 'paid' mean tax paid by or on behalf of the assessee to the Government. Apart from advance tax and self-assessment tax, it would cover tax deducted or collected at source from the assessee. For the purpose of the Income-tax Act, the deductor or collector of tax at source is the agent of the Government. Once the tax is deducted or collected at source, it is as good as paid.

In *JCIT v. Saraswati Real Estates and Investments (P) Ltd.*, ITA No. 186/Del./2000, dated 5-12-2003, the Delhi Bench of the Tribunal held that whether the Revenue gives credit for the tax deducted at source or not, the Revenue by no means can enforce the payment of the tax on the assessee. The Tribunal noted that in view of the scheme of the Act, the

entire liability rests upon the person who has deducted. It is such a person who is responsible for deposit of the same with the Central Government and it is such a person who is to be held to be an assessee in default. The assessee cannot be made to suffer on account of the default of such person who is performing the role of an agent of the Government as far as deduction of tax at source is concerned. The Tribunal observed :

> "In view of what has been discussed above, we feel that whether the Revenue gives credit for the tax deducted at source or not, but we must say that the Revenue by no means can enforce the payment of the said tax on the assessee, as in view of the scheme of the Act, the entire liability rests upon the person who has deducted it and it is such a person who is responsible for deposit of the same with the Central Government and it is such a person who is to be held to be an assessee in default and not the assessee and that the assessee cannot be made to suffer on account of the default of such person who is performing the role of an agent of the Government as far as deduction of tax at source is concerned."

S. 199 read with S. 205 supports the view that once tax is deducted at source, it as good as paid by the assessee. S. 199 provides that deduction of tax at source amounts to payment of tax on behalf of the assessee from whom the tax is deducted. However, credit towards the deducted tax will not be available to the assessee if the deductor fails to remit the amount of tax deducted from the assessee. By virtue of the protection extended to the assessee u/s.205, once tax has been deducted at source, the assessee cannot be called upon to pay the tax, whether or not the amount has been remitted to the Government.

The definition of the term 'paid' found in S. 43(2) of the Act is of no avail in the context of S. 115JB. This definition, which covers both actual and accrued payments, is applicable for the limited purposes of Chapter IV-D. Since Item (a) of the explanation to S. 115JB(2) provides separately for Income-tax payable, the word 'paid' has to be read in the context to cover actual payments only.

(c) ***Payable :***

The word 'payable' refers to amounts that have accrued but not yet paid. The Madras High Court in *Selvambal Ammal v. Venkataram,* AIR 1966 Mad. 460, has defined the term 'payable' to mean the money payable in future. The same Court in *Kothari Textiles Ltd. & Others v. CWT,* (1963) 48 ITR 816 (Mad.) has defined the term 'payable' to signify an obligation to pay at a future time, but when used without qualification, 'payable' means that the debt is payable at once as opposed to owing. In the words of the Madras High Court :

> "In the dictionary of English Law by Earl Jowitt, the meaning of the word 'payable' is thus rendered : 'A sum of money is said to be payable when a person is under an obligation to pay it. Payable may, therefore, signify an obligation to pay at a future time, but when used without qualification, payable means that the debt is payable at once as opposed to owing."

In *Premier Agro Products (P) Ltd. v. State of Kerala,* (2005) 139 STC 37 (Ker.), the High Court of Kerala, relying on several decisions, defined the term 'payable' to signify an obligation to pay at a future time as well as an obligation to pay at once. In light of these decisions, the word payable has to be understood as an obligation to pay, whether immediately or at a future time. The High Court observed :

> "A Full Bench of this Court in *M.R.F. Limited v. Assistant Commissioner, (Assmt.)-II, Sales Tax Special Circle* (1995) 98 STC 233 ; (1995) 1 KLT 809 (FB) considered the validity of the provisions of S. 29A(2B) of the Act. In that context, the Full Bench considered the meaning of the expression 'tax payable' used in the said sub-section. In paragraph 14 of the said judgment, it is observed as follows :
>
> "14. In the light of the above rival contentions, it is necessary to consider about the proper meaning to be assigned to the word 'payable' used in sub-section. According to Supreme Court, the word 'payable' is somewhat indefinite in import and its meaning must be gathered from the context in which it occurs (see *New Delhi Municipal Committee v. Kalu Ram,* AIR 1976 SC 1637). A Full Bench of the High Court of Madras has also held that the word payable has 'both a primary and a secondary meaning' or a 'basic' and 'extended meaning'. After referring to the several dictionary meanings, the Full Bench has held that the term 'payable' has two meanings (i) owing, and (ii) payable at a particular point of time, and when the term is used without any qualification, payable means 'payable at once' [See *Narayanan Chettiar v. Annamalai Chettiar,* AIR

(1961) Mad. 313]. The meaning of the word 'payable' has been given in Black's Law Dictionary as thus :

"Payable — capable of being paid; suitable to be paid; admitting or demanding payment; justly due; legally enforceable. A sum of money is said to be payable when a person is under an obligation to pay it. Payable may therefore signify an obligation to pay at a future time, but, when used without qualification, term normally means that the debt is payable at once, as opposed to 'owing'."

It is clear from the above extract that the word 'payable' may signify 'an obligation to pay at a future time' as well as 'an obligation to pay at once'."

(d) ***Provisions :***

To reiterate, the disclosure requirements of parts II and III of the VI schedule to the Companies Act are required to be complied with, in preparing the profit and loss account for S. 115JB(2). Therefore, the word 'provision' is to be understood in the sense found in Part III of the VI Schedule of the Companies Act. This part defines the word 'provision' in the following words :

"(i) The term 'provision' means any amount written off or retained by way of providing for depreciation, renewals or diminution in value of asset or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy."

Under this definition, the word 'provision' means :

(a) any amount set aside out of the profits of any year to meet any known liability, or

(b) amount set aside or written off towards depreciation, renewals or diminution in the value of assets, in either case, the amount being not quantifiable with substantial accuracy.

In light of the above, the question whether clause (a), *i.e., 'the amount of Income-tax paid or payable, and the provision therefor'* covers the following items is examined.

(A) Income-tax

(B) Surcharge

(C) Cess

(D) Interest on Income-tax

(E) Penalty and fine

(F) Fringe Benefit Tax

(G) Dividend Distribution Tax

(H) Deferred tax liability under AS-22

(I) Foreign taxes

(J) Wealth Tax and interest on Wealth Tax

(K) Credits to profit and loss account.

(A) *Income-tax :*

The term 'Income-tax', as discussed above, means the tax on total income of the previous year of every person and any additional Income-tax payable under the provisions of the Act. It is in this sense that the term 'Income-tax' has to be applied throughout the Act including in S. 115JB.

The Supreme Court in *Bhogilal Chunnilal Pandya v. State of Bombay,* AIR 1959 SC 356; *K. N. Guruswamy v. State of Mysore,* AIR 1954 SC 592 and *Shamaro Vishnu Parulekar v. District Magistrate, Thana,* AIR 1957 SC 23, has laid out the principle that when the Legislature uses the same word in different parts of the statute, subject to the context, the presumption is that the word is used in the same sense throughout that statute.

There is nothing in the context of S. 115JB to indicate that the word 'Income-tax' has to be understood in a manner different from its usage under the rest of the Act. Further, the language employed by entry (a) of the explanation is plain and simple and has to be applied as such. Income-tax paid or payable for the period or provision made for payment of income-tax for the year will have to be added to the net profits as computed u/s.115JB(2) for arriving at the book profits.

(B) *Surcharge :*

The Income-tax Act neither defines 'surcharge', nor contains any specific provisions relating to levy of surcharge. It is only in the Finance Acts that surcharge is specifically provided for. The source of the legislative power to impose surcharge on taxes is found in Article 271 of the Constitution of India which provides:

"Notwithstanding anything in Articles 269 and 270, Parliament may *at any time increase any of the duties or taxes referred to in those articles by a surcharge* for purposes of the Union and the whole proceeds of any such surcharge shall form part of the Consolidated Fund of India."

The use of the words *'at any time increase any of the duties or taxes referred to in those articles by a surcharge'* indicates that surcharge in an increase in the amount of taxes or duties covered by Articles 269 and 270 and thus form part of such tax or duties. While Article 269 covers taxes on sale and purchase of goods, Article 270 covers duties and taxes referred under the List-I (Union List) of the VII Schedule to the Constitution. Entry No. 84 of the Union list provides for taxes on incomes other than agricultural income, *i.e.,* Income-tax. Surcharge on Income-tax is an increase in the Income-tax and therefore part of Income-tax. This position is supported by the decision of the Supreme Court in *CIT v. K. Srinivasan,* (1972) 83 ITR 346 (SC). The Supreme Court observed :

> "The meaning of the word 'surcharge' as given in the Webster's New International Dictionary includes among others 'to charge; (one) too much or in addition . . .' also 'additional tax'. Thus, the meaning of surcharge is to charge in addition or to subject to an additional or extra charge. If that meaning is applied to S. 2 of the Finance Act 1963, it would lead to the result that Income-tax and Super-tax were to be charged in four different ways or at four different rates which may be described as (i) the basic charge or rate (In part I of the First Schedule); (ii) surcharge; (iii) special surcharge, and (iv) additional surcharge calculated in the manner provided in the Schedule. *Read in this way the additional charges form a part of the Income-tax and Super Tax.* It is possible to argue and that argument has been commended on behalf of the Revenue that the word 'surcharge' has been used in Article 271 for the purpose of separating it from the basic charge of a tax or duty for the purpose of distributing the proceeds of the same between the Union and the States. The proceeds of the surcharge are exclusively assigned to the Union. Even in the Finance Act itself it is expressly stated that the surcharge is meant for the purpose of the Union."

The word 'surcharge' as used in S. 2(29C) and S. 113 of the Act also indicates that surcharge is a part of Income-tax. S. 2(29C) requires surcharge to be taken as a part of Income-tax for computing the maximum marginal rate. S. 113(2) requires the tax on undisclosed income of the block period to be increased by surcharge as applicable. This establishes that Income-tax includes surcharge, additional surcharge and special surcharge computed on the income of the current year. Therefore, 'surcharge' is covered by clause (a) of Explanation to S. 115JB.

(C) ***Cess :***

Like the word 'surcharge', the word 'cess' has not been defined in the Income-tax Act. The Act does not contain any reference to the word 'cess' as levied on Income-tax, though reference to the word 'cess' in its general sense is found in S. 43B, S. 138 and S. 145A of the Act. Cess is levied u/s.2(11) and u/s.2(12) of the Finance Act, 2007. While S. 2(11) deals with 'Education Cess', S. 2(12) deals with 'Secondary and Higher Education Cess'. These two sub-sections define the respective cess as additional surcharge. These two sub-sections are extracted below :

> "(11) The amount of Income-tax as specified in Ss.(1) to Ss.(10) and as increased by a surcharge for purposes of the Union calculated in the manner provided therein, shall be further increased by an additional surcharge for purposes of the Union, to be called the 'Education Cess on Income-tax', calculated at the rate of two per cent of such Income-tax and surcharge, so as to fulfil the commitment of the Government to provide and finance universalised quality basic education."

> "(12) The amount of Income-tax as specified in Ss.(4) to Ss.(10) and as increased by a surcharge for purposes of the Union calculated in the manner provided therein, shall be also increased by an additional surcharge for purposes of the Union, to be called the 'Secondary and Higher Education Cess on Income-tax', calculated at the rate of one per cent of such Income-tax and surcharge, so as to fulfil the commitment of the Government to provide and finance secondary and higher education."

As mentioned above, since Income-tax includes additional surcharge, 'cess' forms part of Income-tax for the purposes of clause (a) of explanation to S. 115JB.

(D) ***Interest on Income-tax :***

The term 'Interest on Income-tax' is not defined under the Act. In both general and legal usage, the terms 'Income-tax' and 'interest' have different meanings. Even under the Act, these terms are used in senses distinct from each other. In *Bhor Industries Ltd. & Others v. CIT,* (1961) 42 ITR 57 (SC), the

Supreme Court held that there is nothing in the Act to show that interest on Income-tax is to be treated as tax. The Supreme Court held as under :

> "The words of the sub-section are clear to show that interest as interest is added to the tax as determined. There is nothing to show that it is to be treated as tax, and it thus retains its character of interest, but is recoverable along with the tax. Indeed, S. 29 of the IT Act makes a distinction between tax, penalty and interest. Since S. 23A speaks of deduction only of Income-tax and Super Tax, no deduction could be made in respect of this interest."

The following arguments strengthen the view that interest and Income-tax are not synonymous :

(a) The charging section for Income-tax is S. 4 while charging section for interest are various, including S. 234A to S. 234D.

(b) S. 2(43) which defines tax does not cover interest. No other provision states that interest on tax constitutes Income-tax.

(c) Several sections of the Act use the words 'tax', 'interest', 'penalty' and 'fine' simultaneously. This indicates that these terms are used distinctly from each other in the Act. S. 156, S. 171, S. 229, S. 276C and S. 277A are a few of the sections which refer to these terms together. In *Harshad Shanti Lal Mehta v. Custodian & Others*, (1998) 231 ITR 871 (SC) the Supreme Court observed that tax, penalty and interest are different concepts under the IT Act.

(d) While Income-tax is levied to fund the State activities, interest is levied to compensate the Government for denial of use of the tax it was entitled to from the assessees.

(e) Charge of Income-tax is attracted irrespective of any default on the part of the assessee, while liability to interest arises only on default of the assessee in complying with the provisions of the Act.

(f) The rates of Income-tax are prescribed in the Finance Act, except in some special cases. On the other hand, the rates of interest are prescribed in the Act itself.

(g) While the CBDT has powers u/s.119(2)(a) to relax provisions relating to interest, it does not have specific powers to reduce the levy of tax.

(h) In case two interpretations are possible, the interpretation benefiting the assessee has to be selected. The argument that Income-tax does not include interest thereon is favourable to the assessee and must be adopted. The contrary interpretation will give an artificial meaning to the word 'Income-tax' and therefore has to be avoided.

In relation to S. 115J the Kerala High Court in *CIT v. Fertilisers and Chemicals Travancore Ltd.*, (2003) 261 ITR 484 (Ker.) and the Delhi Bench of the Tribunal in *Insilco Ltd v. JCIT*, (2004) 85 TTJ (Del.) 538 have held that interest on Income-tax cannot be added back. The Panaji Bench of the Tribunal in *Salgaocar Mining Ind. (P.) Ltd. v. JCIT*, (2006) 287 ITR 197 (AT), in relation to the S. 115JA, has held that interest on Income-tax is not Income-tax. The Tribunal concluded :

> "The above discussions make it equally clear that the terms 'Income-tax', 'interest' have assumed and acquired separate meanings and are understood distinctly and differently from each other. For this reason also, it is not possible to treat 'interest' as part of 'Income-tax.' One of the well-recognised rules of interpretation is that where the statutory language is plain and clear, the task of interpretation can hardly be said to arise. The first and foremost elementary rule of construction is that it is to be assumed that words and phrases of a technical legislation like IT Act are used in their technical meaning which they have acquired. As already mentioned above, the term 'Income-tax' is understood in altogether a different sense than the term 'interest'. It means the Income-tax which has been specified in Schedule 1 to the Finance Act, 1999 and hence, its meaning cannot be artificially extended to include interest. In our humble view, interest on Income-tax clearly falls outside the scope of the term 'Income-tax' as used in Expln. (a) to Ss.(2) of S. 115JA. Wherever the intention was to include interest, the legislature has specifically provided, as in S. 156, for inclusion of interest in the phrase 'sum payable'. No provision of law has been brought to our notice to show that the term 'Income-tax' has been defined to include 'interest' within its ambit. We are, therefore, unable to artificially extend the scope of Income-tax used in Expln. (a) to Ss.(2) of S. 115JA, so as to include 'interest on income-tax' also."

S. 115JB has superseded S. 115JA and S. 115JA had superseded S. 115J. However, clause (a) of the Explanation to S. 115JB(2) has remained unchanged

and is common to all these three provisions. Therefore, decisions rendered under the other S. 115J and S. 115JA are equally applicable to S. 115JB. In light of the decisions, one can hold that interest on Income-tax does not form part of Income-tax, and should not be added back to the net profits to determine book profits.

One should however note that the Courts have interpreted 'interest on Income-tax' as forming part of Income-tax for the purposes of disallowance u/s.40(a)(ii). The authorities on the point include *Assam Forest Products (P.) Ltd v. CIT,* (1989) 180 ITR 478 (Gau.); *Parshuram Agarwal v. CIT,* (2003) 130 Taxman 774 (Gau.); *Orissa Cements Ltd v. CIT,* (1993) 200 ITR 636 (Del.) and *Mannalal Ratanlal v. CIT,* (1965) 58 ITR 84 (Ori.). These decisions were rendered on the ground that interest is an accretion to tax and it was not expended to earn the business income. Since these decisions are rendered in a different context, they should be regarded as inapplicable in the context of S. 115JB.

(E) ***Penalty and fine :***

Penalties and fines imposed under the Act are distinct in nature from Income-tax. The decisions of the Supreme Court in Harshad Mehta's case (mentioned above) and *CIT v. Hindustan Electro Graphites Ltd.,* (2000) 243 ITR 48 (SC) can be referred for the purpose. Penalty is levied by the Income-tax authorities for non-compliance with the provisions of the Act and the penalties can be waived or reduced u/s.273A. Similarly, fines are imposed by the Criminal Courts as a punishment for offences committed under the Act. In the Hindustan Electro Graphite's case, the Supreme Court observed :

> "S. 2(43) of the IT Act defined 'tax' during the relevant period as Income-tax and Super Tax chargeable under the provisions of that Act. Therefore, what is levied under the charging provision of that Act, *i.e.,* S. 4 of the IT Act, alone can be called Income-tax. Interest, penalties and fines, which are also payable under the other provisions of that Act, cannot be termed as Income-tax. They are imposed in addition to Income-tax for the purpose of enforcing the levy of Income-tax."

One can also rely on the decisions in *Salgaocar Mining Ind. (P.) Ltd. v. JCIT* (*supra*) and *CIT v. Fertilisers and Chemicals Travancore Ltd.* (*supra*), to hold that penalties and fines are not to be added back to the net profits to arrive at the book profits u/s.115JB.

(F) ***Fringe Benefit Tax :***

Income-tax includes additional Income-tax charged under any other provision of the Income-tax Act. S. 115WA, the charging section for Fringe Benefit Tax (FBT in short) employs the words 'additional Income-tax (in this Act referred to as Fringe Benefit Tax)' indicating that FBT is an additional Income-tax. If construed in this sense, FBT has to be added to the net profit to arrive at the book profits.

However, FAQ No. 103 of the CBDT Circular No. 8 of 2005, dated 29-8-2005 specifically provides that FBT need not be added back for computing book profits u/s.115JB. It states :

> "103. Whether FBT would be allowable deduction while computing 'book profit' u/s.115JB ?
>
> *Ans.* : FBT is a liability qua employer. It is an *expenditure laid out or expended wholly and exclusively for the purposes of the business or profession of the employer.* However, sub-clause (ic) of clause (a) of S. 40 of the Income-tax Act expressly prohibits the deduction of the amount of FBT paid, for the purposes of computing the income under the head 'Profits and gains of business or profession'. This prohibition does not apply to the computation of 'book profit' for the purposes of S. 115JB. Accordingly, the FBT is an allowable deduction in the computation of 'book profit' u/s.115JB of the Income-tax Act."

Circulars issued by the CBDT are binding on the authorities under the Act. This is the mandate of S. 119. The Supreme Court in *CIT v. Vasudev V. Dempo,* (1992) 196 ITR 216 (SC) and *Tanna and Modi v. CIT & others,* (2007) 292 ITR 209 (SC) has upheld the principle that executive interpretations of the Act issued by the CBDT in Circulars are binding on the authorities.

In *Ellerman Lines Ltd. v. CIT,* (1971) 82 ITR 913 (SC), *K. P. Varghese v. ITO;* [1981] 131 ITR 597 (SC) and *Navnit Lal C. Javeri v. K. K. Sen, AAC,* (1965) 56 ITR 198 (SC), the Supreme Court went ahead to hold that beneficial instructions and directions given by the Board are binding on the officers, even if they deviate from the provisions of the Act.

Therefore, an assessee can take advantage of the CBDT Circular and not add back FBT for computing book profits u/s.115JB.

(G) ***Dividend Distribution Tax :***

Dividend Distribution Tax (DDT in short) like FBT is referred to as additional Income-tax. DDT is levied under the provisions of S. 115O of the Act. S. 115O(1) provides that "any amount declared, distributed or paid by such company by way of dividends (whether interim or otherwise) on or after the 1st day of April, 2003, whether out of current or accumulated profits shall be charged to additional Income-tax (hereafter referred to as tax on distributed profits) at the rate of fifteen per cent." Since, Income-tax includes additional Income-tax, and DDT being an additional Income-tax, is required to be added back to the net profits to arrive at the book profits.

However, in *ACIT v. Balarampur Chini Mills Ltd.*, (2007) 14 SOT 372 (Kol.), the Kolkota Bench of the Tribunal has extended the benefit available to FBT under CBDT Circular No. 8 of 2005 to DDT. The Tribunal observed :

> "In our considered opinion (tax) on distribution of profit payable as per provision of S. 115-O of the Act is of similar nature as Fringe Benefit Tax payable under Chapter XII-H of the Act, since both are payable at the time of incurring certain expenditure which are in the form of fringe benefit given to employees or dividend to shareholders, which are not otherwise taxable under the other provisions of the Act. Therefore, in our considered opinion, both Fringe Benefit Tax and tax on distribution of profits are similar in nature. Since Circular No. 8, dated 29-8-2005 issued by the CBDT makes it clear that Fringe Benefit Tax is an allowable deduction in the computation of book profit u/s.115JB of the Act while dealing in question No. 103, a copy of which is also available on record, in our considered opinion, the ld. CIT(A) has rightly treated the tax on profits distributed as dividend in similar manner as Fringe Benefit Tax and has thereafter rightly directed the Assessing Officer not to add back such tax on distributed profit in the computation of book profit for the purpose of S. 115JB. We, therefore, do not see any reason to interfere with such order of the ld. CIT(A) and accordingly uphold his order and reject the grounds raised by the Revenue."

The above decision possibly does not represent a correct exposition of the law. The Tribunal has relied on FAQ No. 103 of the CBDT Circular No. 8 of 2005, in arriving at its decision. This FAQ states that Fringe Benefits Taxes are expenditure laid out wholly and exclusively for the purpose of business or profession of the employer. This is possibly because the underlying expenditure on which FBT is levied is incurred in the course of and for the purpose of earning profits from business. FBT inherently represents a tax on expenditure. The Circular states that Fringe Benefit Tax paid in relation to such expenditure, need not be added back u/s.115JB even though it attracts S. 40(a) disallowance.

Dividends are an appropriation of profits made at the sole discretion of the Board of Directors. Payment of dividends does not in anyway contribute to the profit-earning capacity of the company. It has no relation to the business of an entity. It is not an expenditure in the sense there is no obligation or liability to declare dividends. Dividends are paid out of 'post-tax profits'. DDT being a liability attached to payment of dividends, is also paid out of 'after-tax profits'. Payment of dividend and DDT thereon is not an expenditure laid out wholly and exclusively for the purposes of business or profession, nor is it a tax on expenditure. For these reasons, the benefit of the Circular in relation to FBT, should not be extended to DDT. DDT would then form part of Income-tax in clause (a) of explanation to S. 115JB.

(H) ***Deferred Taxes under Accounting Standard 22 :***

S. 211(3A) of the Companies Act, 1956 requires companies to follow the Accounting Standards in preparation of their financial statements. For this purpose, Accounting Standards means Accounting Standards prescribed u/s.211(3C). AS 22 — Accounting for Taxes on Incomes (Standard in short) issued by Institute of Chartered Accountants of India is one of the Standards now prescribed u/s.211(3C) for the purposes of S. 211(3A).

This Standard requires reconciliation between taxes computed on accounting income and taxable income as per the Income-tax Act and proper treatment and disclosure of the differences. Such differences may be either permanent or arising in one accounting year and capable of reversal in one or more subsequent periods. If they are capable of reversal in subsequent periods, a deferred tax asset or a deferred tax liability comes into existence. Where deferred tax liability arises, the Standard requires that it is properly provided for.

The Standard differentiates between deferred tax and current tax. 'Current tax' is defined in the Standard as the amount of Income-tax determined to be payable (recoverable) in respect of the income (loss) for a period, determined in accordance with the tax laws. On the other hand, 'deferred tax' is defined as the tax effect of difference between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.

Deferred tax provisions are not 'provisions for Income-tax' meant to be discharged by payment in the subsequent period, but are meant for adjustment against incomes during one or more subsequent periods. Deferred tax represents a notional adjustment to mitigate a timing mismatch. It is therefore neither tax paid, nor payable. It may not also be a provision. A provision, as noticed already, warrants the existence of a known and identifiable liability. A liability in turn presupposes a financial obligation. A deferred tax liability cannot be equated to a financial obligation of the company to pay the Government, any amount in future as Income-tax.

Hypothetically, if a company were to go into liquidation, the amount to the extent of 'deferred tax' will not constitute any liability or dues to any creditor. A credit balance in the deferred tax account should therefore not be termed as a provision. The term 'income tax' referred to in clause (a) of the explanation to S. 115JB(2) is only current tax as defined in the Standard and not the deferred tax. The Kolkota Bench of the Tribunal in *ACIT v. Balarampur Chini Mills Ltd.*, (*supra*) has also taken the view that deferred taxes are not required to be added back to the net profits to arrive at the book profits. The Tribunal held :

> "It has been submitted by the ld. DR that the above deferred tax charge is nothing but is in the nature of Income-tax, which is liable to be added in view of clause (a) to the Explanation to Ss.(2) of S. 115JB. However, in our considered opinion, such objection raised by the Department is devoid of any merit, as deferred tax means the tax effect of timing difference due to differences between taxable income and accounting income for a period that originate in one period and is capable of reversal and, therefore, such deferred tax charge is a provision for tax effect of difference between taxable income and accounting income and not provision for Income-tax paid or payable, and therefore could not be covered under Explanation (a) to Ss.(2) of S. 115JB. We have also noted down that paragraph 30 of AS-22 clearly says that deferred tax assets and liabilities should be distinguished from assets and liabilities representing current tax for the period. The Panaji Bench in case of Salgaocar Mining India (P.) Ltd. (*supra*) has also held that interest on Income-tax and Income-tax paid/payable are to be treated separately, as they are separate and distinct from each other. Likewise deferred tax charge cannot be kept at par with Income-tax paid/payable as both are quite different. Apart from the above fact, we have also noted down the objective behind enacting AS-22 by the ICAI, as deferred tax charge was meant to remove the difference between taxable income and accounting income arising due to difference between items of revenue and expenses as appearing in the statement of profit and loss A/c. and the items which are considered as revenue expenses or deductions for tax purposes or there are differences between the amount in respect of a particular item of revenue or expense as recognised in the statement of profit and loss and taxable income. Therefore, it is absolute apparent that deferred tax charge could not be termed as Income-tax paid or payable, which has to be paid out of profit earned by the assessee for the year under consideration and, therefore, in our considered opinion, the first objection raised by the Revenue does not hold any merit."

Further, clauses (i) to (vii) of the Explanation do not provide for deduction of deferred tax assets (if recognised and accounted) from the net profits. This indicates that the Legislature intended to leave deferred taxes outside the framework of S. 115JB. Therefore, provisions for deferred taxes are not provisions for income tax and the question of disallowing them u/s.115JB does not arise.

(I) ***Foreign taxes :***

Income-tax is the tax on the total income computed under the provisions of the Income-tax Act, at the rate prescribed by any Central Act. It includes additional Income-tax as per the provisions of the Act. Foreign taxes are not levied under the provision of the Income-tax Act. They are levied under the laws of the respective countries.

However, foreign taxes are paid on incomes. The same form part of total income and subjected to tax in India in case of Indian companies. In general

cases, credit for these foreign taxes is available while paying Indian taxes. Therefore, foreign taxes paid, payable or provision therefor subsumes into the Income-tax paid, payable or provision therefor. The foreign taxes can be either directly debited to the profit and loss account or adjusted along with Income-tax provision account. In either case, it has to be treated as Income-tax and added back to the net profits under Explanation to S. 115JB(2).

(J) ***Wealth Tax and interest on Wealth Tax :***

S. 3 of the Wealth Tax Act, 1957 imposes the charge of Wealth Tax on the 'net wealth' of every individual, HUF and company as on the valuation date. While Income-tax is tax on income, Wealth Tax is tax on net wealth. These two taxes are levied under different statutes to achieve different purposes. Income-tax is levied on the income earned during the previous year; Wealth Tax is levied on net wealth as on the valuation date, *i.e.*, last day of the previous year. While S. 40(a)(ii) deals with disallowance of Income-tax, S. 40(a)(iia) deals with disallowance of Wealth Tax. There is no material to treat them as synonyms. On the other hand, the Act itself differentiates between Income-tax and Wealth Tax. Therefore, Wealth Tax cannot be treated as part of Income-tax and added back to the net profit u/s.115JB.

The decision of Special Kolkata Bench of the Tribunal in *JCIT v. Usha Martin Industries Ltd.*, (2007) 288 ITR 63 (AT) rendered in the context of S. 115JA and the decision of the Bombay High Court in *CIT v. Echjay Forgings Pvt. Ltd.*, (2001) 251 ITR 15 (Bom.) support this view. The Special Bench of the Tribunal in Usha Martin's case observed :

> "In the case of M/s. Usha Martin Industries Ltd., the A.O. has also made the addition of Rs. 1,25,000 in respect of provision for Wealth Tax. The same was deleted by the C.I.T.(A). The Revenue aggrieved with the order of the C.I.T.(A) is in appeal before us. We have heard both the parties and perused the material placed before us. We have already stated above that for the purpose of S. 115JA, the addition to the book profit, which is computed as per Parts II & III of Schedule-VI to the Companies Act, can be made only if it is permissible by items No. (a) to (f) of the Explanation to S. 115JA. We find that as per clause (a) to Explanation "any amount of income-tax paid or payable and the provision therefor" is liable to be added to the book profit. However, there is no such provision for making the addition with regard to Wealth Tax. Since the provision for Wealth Tax does not fall within any of the items of Explanation to S. 115JA, we hold that the CIT(A) was justified in deleting the addition made by the AO in this regard. In view of the above, we reject the Revenue's appeal in the case of M/s. Usha Martin Industries Ltd."

Therefore, Wealth Tax paid, payable or a provision therefor cannot be treated on par with 'Income-tax paid, payable or a provision therefor'. Wealth Tax is not to be added back to the net profits in arriving at the 'book profits'.

Since 'Wealth Tax' nor 'interest on Income-tax' forms part of Income-tax for the purposes of S. 115JB, interest on Wealth Tax is also not required to be added back to the net profits while computing 'book profits'.

(K) ***Credits to profit and loss account :***

There are several items which may be credited on refund/reversal to the profit and loss account. For example, refund of Income-tax is usually credited to the profit and loss account, while Income-tax paid is debited to the profit and loss account. These items, if debited to the profit and loss account would have been added back to the book profits. Such items must be given the opposite treatment, namely, credits must be deducted from the net profits, if the debit of the same item is added back to net profits.

Conclusion :

The concept of 'Income-tax paid or payable or provision therefor' in S. 115JB has not yet received attention of the superior Courts in India. Some of the decisions referred above, rendered by the Tribunals across the country require further scrutiny at the hands of the High Courts and by the Supreme Court. The decisions of the Tribunal cannot be said to be the final word on the subject. In the absence of settled law on these points, one may follow a conservative approach while making provision or paying advance tax, but could take full advantage of the decisions while filing returns.

No folly is more costly than
the folly of intolerant idealism.

— Winston Churchill

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You can input bills & also print bills
but bills WILL NOT appear in profit/loss
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outstanding, bill register, service tax register...

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Bill printing **(your own format, size, color, font...)**
Saves standard text for different services
Clientwise bill register
Client groupwise bill register
Service tax & non service tax bill register

OUTSTANDINGS
Clientwise outstandings
Client groupwise outstandings
Datewise outstandings / Ageing
Reminder letter, ...

SERVICE TAX (with cess amendments)
Service tax billed register
Service tax collected register [various %]
Service tax liability

TDS / FBT
TDS deducted by client / FBT on various expenses
TDS deducted by you / FBT register

BOOKS OF ACCOUNTS
Bank book / Bank reconciliation
Cash book / Petty cash columnar
Ledgers / Journal book

M.I.S
Cost/Job centre profitability
Budgets vs. Actuals
Different type of fees collection
Last 3 years billing comparison
Out of pocket expenses on a client

FINAL ACCOUNTS
Profit & loss, Trial bal., Balance sheet
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TIME COSTING ON STAFF
On client
On assignment
Out of pocket
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Part A — Reported Decisions

(2007) 109 ITD 198 (Delhi)
Midland International Ltd. *v.* DCIT
A.Y. 1998-99. Dated : 12-1-2007

S. 23 r.w. S. 22 of Income-tax Act, 1961 — While taxing the rental income of property under the head 'Income from House Property', the Assessing Officer cannot consider the element of notional income by way of interest on interest-free security deposit received by the assessee for the purpose of determining annual letting value (ALV).

The assessee company had let out a commercial property on annual rent of Rs.25,30,800 and had also received Rs.25,30,800 as interest-free security. The AO was of the opinion that the assessee had received the security deposit as a result of letting out of the property. Hence, he worked out interest @ 15% on the average value of the security deposit, *i.e.*, on Rs.19,09,623 and added the same to ALV.

On appeal, the CIT(A) enhanced the ALV by adopting notional rent at 15% on sum of Rs.25,30,800 and further increased the ALV. On second appeal to ITAT, the Tribunal set aside the orders of the lower authorities and directed the AO to compute the ALV of the property in terms of C23(1)(a) and referred to the following :

(1) As per S. 23(1)(a) and S. 23(1)(b), ALV of the property is deemed to be the sum for which the property might reasonably be expected to be let from year to year, and if it is let and actual rent is in excess of such sum, then such rent received or receivable will be the ALV.

(2) The ratable value will be determined with reference :

  (i) to standard rent, if the same has been fixed, and if not fixed, then

  (ii) to municipal ratable value, in case the same is fixed, and if not, then

  (iii) as per guidelines laid down in the provisions of the Municipal Act.

(3) In any case, it cannot be done by considering any notional income representing the interest on security deposit, since a notional income was never contemplated under these Sections.

Cases referred to :

- *Godhra Electricity Co. Ltd. v. CIT*, (1997) 225 ITR 746
- *CIT v. Satya Co. Ltd.*, (1994) 75 Taxman 193
- *J. K. Investors (Bombay) Ltd. v. DCIT*, (2000) 74 ITD 274 (Mum.)

C. N. Vaze
Shailesh Kamdar
Chartered Accountants

TRIBUNAL NEWS

Part B — Unreported Decisions

(Full texts of the following Tribunal decisions are available at the Society's office on written request. For members desiring that the Society mails a copy to them, Rs.30 per decision will be charged for photocopying and postage.)

Ashok Dhere
Jagdish D. Shah
Chartered Accountants

iGate Global Solutions Ltd. *v.* ACIT
ITAT 'B' Bench, Bangalore
Before P. Mohanarajan (JM) and N. L. Kalra (AM)
ITA Nos. 248 & 249/Bang./2007
A.Ys. : 2002-03 & 2003-04. Decided on : 27-11-2007
Counsel for assessee/revenue : Padam Chand Khincha/Etwa Munda

S. 10A of the Income-tax Act, 1961 — Deduction in respect of the profit of the undertaking established in software technology park — Held, that (i) telecommunication charges reduced from export turnover are also to be reduced from total turnover (ii) loss suffered by one industrial undertaking need not be adjusted against the profit of the other industrial undertaking (iii) the amount equal to the adjustments made by the assessee to the arm's-length price, while filing the return of income, was eligible for deduction.

Per N. L. Kalra :

Facts :

The assessee was in the business of development of computer software. Its three units were located in the Software Technology Parks at Bangalore, Chennai and Pune. With reference to its claim for deduction u/s.10A in respect of the said three units, the following issues had arisen :

(i) Quantum of telecommunication charges (link cost) incurred on delivery of software, which is to be deducted from the export turnover to

arrive at the figure of the export turnover. The CIT(A) had considered 80% of the total of such cost as incurred for delivery of the software.

(ii) Whether the telecommunication charges so determined were also to be reduced from the amount of the total turnover of the undertakings to determine the amount deductible u/s. 10A.

(iii) Whether the loss suffered at its Pune unit is to be set off against the profits earned at other two units at Bangalore and Chennai before allowing deduction u/s.10A.

(iv) Whether the amount equal to the adjustments made by the assessee to the arm's-length price while filing the return of income, was eligible for deduction u/s.10A.

Held :

The Tribunal held as under :

(i) According to the Tribunal, on account of the failure of the assessee to provide details of expenses attributable to outward transmission of data, the CIT(A) was right in estimating the expense as equal to 80% of the total expenditure on telecommunication.

(ii) Relying on its own decisions in the cases of Tata Elxsi Ltd. and Infosys Ltd., it was held that telecommunication charges which were reduced for ascertaining the export turnover were also not to be considered for the purposes of total turnover, as total turnover is the sum total of export turnover and domestic turnover.

(iii) Referring to the provisions of S. 10A(4), the Tribunal noted that w.e.f. 1-4-2001, instead of 'profits of the business', the words 'profit of the business of the undertaking' have been substituted. According to it, if the Pune unit is part of the other two units and was associated with the activities done in the said two units, then it would be considered as part of the same undertaking and the loss would get adjusted. However, if it was an independent unit, then it would be treated as independent undertaking and the assessee could not be forced to have exemption in respect of such independent undertaking and the loss could be adjusted against its other income. Since the facts were not clear, the case was restored back on the file of the AO.

(iv) The Tribunal noted that it was the assessee itself who had made adjustment to the income, because arm's-length price determined was more than the consideration at which the transactions were shown in the books of account. Referring to the Memorandum explaining the provisions of the Finance Bill and the literal meaning of the word 'enhanced' in proviso to S. 92(4), the Tribunal held that the assessee was entitled to deduction u/s.10A in respect of income declared in the return of income on the basis of computation of arm's-length price.

Cases referred to :

(1) *Tata Elxsi Ltd. v. ACIT,* (ITA No. 315/Bang./2006 dated 16-10-2007)

(2) *ACIT v. Infosys Technologies Ltd.,* (ITA Nos. 653 & 969/Bang./2006 dated 17-10-2007)

Dy. CIT *v.* Delhi Financial Corporation
ITAT 'H' Bench, New Delhi
Before Vimal Gandhi (President) and R. C. Sharma (AM)
ITA No. 4566/Del./2005
A.Y. 2002-03. Decided on : 7-9-2007
Counsel for revenue/assessee : Himalini Kashyap/ Rano Jain and V. Jain

S. 36(1)(viia)(c) of the Income-tax Act, 1961 — Provision for bad and doubtful debts — Assessee following cash system of accounting — Allowability of provision so made — Held, that deduction being statutory, allowable.

Per R. C. Sharma :

Facts :

The assessee was a state financial corporation providing long-term financial assistance by way of granting loans and lease finance to industrial units. It was following the cash method of accounting. During the year under appeal, the assessee had claimed deduction to the extent of 5% of its total income by way of provision for bad and doubtful debts u/s. 36(1)(viia)(c) of the Act. The said claim was denied by the AO for the reason that the assessee was following the cash method of accounting. According to him, such deduction could be allowed only when the income which had been accrued but not received was offered for taxation, as in the mercantile system of accounting. He further observed that allowing the provisions under

the cash system of accounting defeats the very purpose of abolishing the hybrid system of accounting. On appeal, the CIT(A) allowed the deduction.

Held :

According to the Tribunal, as per the plain reading of the provisions of S. 36(1)(viia)(c), no condition of any specific system of accounting to be followed by the assessee had been provided. Therefore, the deduction being a statutory deduction, had to be allowed on the basis of the provisions made in the books of accounts, notwithstanding the fact that the assessee was following the cash system of accounting. It further noted that in the assessee's case, the debts also included the amount of loans/advances, which were not affected by the method of accounting being followed by the assessee.

Vijay Power Generators Ltd. *v.* **ITO**
ITAT 'A' Bench, New Delhi
Before R. V. Easwar (VP) and K. G. Bansal (AM)
ITA Nos. 1649/Del./2007
A.Y. : 1997-98. Decided on : 31-8-2007
Counsel for assessee/revenue : Salil Kapoor/L. M. Pandey

S. 271(1)(c) of the Income-tax Act, 1961 — Penalty for concealment of income — Non-recording of satisfaction by the AO — Penalty deleted.

Per R. V. Easwar :

Facts :

During the year under consideration, the assessee had received Rs.25.24 lacs from 15 persons as share application money. In the assessment made u/s.144, the amount was added u/s.68 on the ground that the genuineness of the transactions was not proved and the assessee did not produce any evidence in support thereof. The assessee failed in the appeal filed before the CIT(A) as well as the Tribunal.

The penalty proceedings initiated by the AO were objected to (without success) by the assessee, on the ground that the AO did not record any satisfaction in the assessment order to the effect that the assessee concealed its income or furnished inaccurate particulars thereof. On appeal, the CIT(A) confirmed the AO's order.

Before the Tribunal, it was contended by the Revenue that the reaching of satisfaction u/s.271 was an administrative action in which the form was not important and only the substance matters. If the assessment order was read as a whole without giving undue importance only to the operative part thereof, it would be clear that the AO could be said to have reached the requisite satisfaction. It was further pointed out that the addition made was also confirmed by the Tribunal.

Held :

According to the Tribunal, the AO was ambiguous when he observed that 'genuineness of the transactions is doubtful' or 'genuineness of the transactions is not proved'. He started with the premise that the monies received were fictitious, but ultimately he merely stated that the genuineness of the transactions was doubtful or was not proved. According to the Tribunal, there was a difference between the two sets of expressions *viz.*, 'fictitious' on the one hand and 'doubtful' and 'not proved' on the other hand. While concluding his reasoning and making the addition, the AO abandoned his earlier view that the monies were received from fictitious persons and seemed to have settled for less strong expressions. Relying on the Delhi High Court decisions in the cases of Ram Commercial Enterprises and Diwan Enterprises, the Tribunal allowed the appeal of the assessee.

Cases referred to :

(1) Ram Commercial Enterprises, 246 ITR 568 (Del)

(2) Diwan Enterprises, 246 ITR 571 (Del)

ITO *v.* **Navneet Kumar Malpani**
ITAT 'B' Bench, Jaipur
Before I. C. Sudhir (JM) and B. P. Jain (AM)
ITA No. 223/JP/2006
A.Y. 2001-02. Decided on : 27-8-2007
Counsel for revenue/assessee : Sanjay Kumar/Mahendra Gargieya and Shravan Gupta

S. 14 of the Income-tax Act, 1961 — Heads of income — Loss on sale of units in mutual fund — Assessee's claim to treat it as business loss and allow it to be set off against his other income rejected by AO holding the same as capital loss — On facts held that loss was business loss and can be set off against other income.

Per B. P. Jain :

Facts :

During the year under appeal, the assessee had

earned dividend of Rs.2.77 lacs and suffered a loss of Rs.2.63 lacs on sale and purchase of the mutual fund units. In his return of income filed, the dividend income was claimed as exempt and the loss was claimed as short-term capital loss. Subsequently, during the assessment proceedings, the assessee claimed that the loss be treated as business loss and be set off against his other income. The AO, relying on the Supreme Court decision in the case of McDowell and Co., observed that the assessee had adopted a dubious method to avoid tax. Accordingly, he treated the loss as capital loss and set off the same against the dividend income. Thus, the assessee's claim to treat the loss as business loss and to set it off against his other income was rejected. On appeal, the CIT(A) allowed the appeal of the assessee.

Held :

The Tribunal noted that :

- The assessee was engaged in frequent transactions of purchase and sale of shares and units in mutual funds.
- The units of mutual funds were purchased from open market and were not allotted to him on application.
- The entire holding was also sold in the open market.
- The period of holding was short.
- In accounts, the assessee had treated the same as profit from trading in shares and mutual funds.

Thus, according to it, the totality of facts and circumstances suggested that the assessee intended to do a business in shares and mutual funds. Therefore, according to it, the resultant loss or profit had to be held as loss from business. In support, it also relied on the decisions listed at Serial Nos. 1 to 3 below. Accordingly, the CIT(A)'s order was upheld and appeal of the Revenue was rejected.

Cases referred to :

1. *CIT v. Karam Chand Thapar & Sons Ltd.*, 115 ITR 250 (Cal.);
2. *CIT v. Vikram Cotton Mills Ltd.*, 169 ITR 597 (SC);
3. *Neerja Birla v. ACIT*, 66 ITD 148 (Mum.);
4. *McDowell and Co. v. Commercial Tax Officer*, 154 ITR 148 (SC).

Editor's Note : This decision was for a period prior to insertion of S. 94(7), w.e.f. A.Y. 2002-03, provisions of S. 94(7). Would also have to be considered.

Dy. CIT *v.* Spice Communication
ITAT 'B' Bench, Bangalore
Before Gopal Chowdhury (JM) and K. K. Gupta (AM)
ITA Nos. 1083 to 1085/Bang./2006
A.Ys. : 2003-04 to 2005-06. Decided on : 21-9-2007
Counsel for revenue/assessee : K. P. Rao/Padam Chand Khincha

S. 201 read with S. 194C of the Income-tax Act, 1961 — Consequence of failure to deduct tax at source — SIM card supplied as per the specification of the assessee – Whether such contract covered u/s.194C — Held, No.

Per Gopal Chowdhury :

Facts :

The assessee engaged in the business of providing communication facility had purchased SIM cards. As per the contract, the supplier was required to print the logo of the company and some instructions on the SIM cards. No TDS was made by the assessee. According to the AO, the transaction was a works contract in nature, attracting the provisions of S. 194C. Therefore, relying on the Madras High Court decision in the case of Kumudam Publications Ltd. and of the Pune Tribunal in the case of BDA Ltd., he treated the assessee as defaulter u/s.201(1) and raised the demand. On appeal, the CIT(a) held that the transaction regarding the purchase of SIM cards was not works contract in nature.

Held :

According to the Tribunal, the CIT(A) had rightly noted that the decision of the Pune Tribunal in the case of BDA Ltd. was reversed by the Bombay High Court, wherein the Court had held that where a manufacturer manufactures a product as per the specific requirement of the customer, it was a case of sale and not a contract for carrying out any work. It also agreed with the CIT(A) that in the case of Kumudam Publications Ltd., the facts were distinguishable inasmuch as in that case, the printer had printed the materials with the help of the materials supplied by its customers, whereas in the case of the assessee, no material was supplied by it and the supplier had printed the SIM card as per the specification of the assessee. Hence, no works

contract was involved. Further, relying on the decision of the Bangalore Tribunal in the case of The Bangalore District Co-operative Milk Producers' Societies' Union Ltd. and the Board Circular on the subject, the Tribunal dismissed the appeal filed by the Revenue.

References :

(1) *BDA Ltd. v. ITO*, 281 ITR 99 (Mum.)

(2) The Bangalore District Co-operative Milk Producers' Societies' Union Ltd. (ITA Nos. 350 to 354/Bang./2006 dated 19-5-2006);

(3) CBDT Circular No. 681, dated 8-3-1994

(4) *BDA Ltd. v. ITO*, 84 ITD 442 (Pune)

(5) *CIT v. Kumudam Publications Ltd.*, 188 ITR 84 (Mad.)

Part C — International Tax Decisions

9 ITO *v.* M/s. De Beers India Minerals Pvt. Ltd. [ITA Nos. 3400, 3401 & 3402/Bang./2004]

Geeta Jani
Dhishat B. Mehta
Chartered Accountants

A.Y. : 2004-05

Article 12 of India-Netherlands DTAA

Appellant by : B. Chattaraj

Respondent by : K. R. Shekar

Issue :

The amount paid to a person resident of Netherlands for geo-physical survey and obtaining report containing data of survey is not chargeable to tax in India in terms of Article 12 of the DTAA.

Facts :

The assessee, an Indian company, was given right of prospecting for minerals by certain State Governments of India. The prospecting activity (referred to as mineral reconnaissance activity) represented early stage of exploration. The activity was undertaken with a view to ascertain kimberlite area which would indicate probable patches of mineral-rich land capable of being prospected for commercial production. The activity involved collection of samples and conduct of geo-physical survey by adopting diverse technical methods.

The assessee engaged the services of M/s. Fugro of Netherlands. Fugro had a team of experts specialised in performing airborne geo-physical surveys, collecting data of survey and providing necessary report to the client, which could help in identification of mineral-rich area.

The Tribunal noted that Fugro rendered the services of conducting airborne survey by using specialised equipments. The logistics of the survey, such as schedule, positioning of equipments, etc. were decided by Fugro. Fugro deputed its own technical personnel to carry out the survey. Data collected from survey was provided to the assessee in the form of Acquisition and Processing Report in the desired format.

The AO regarded the amount as chargeable to tax in India in terms of Article 12 of India-Netherlands Treaty. In his view, the payment was payment for fees for technical services. Alternatively, the AO regarded payment to be chargeable as payment for development and transfer of a technical plan or technical design.

The CIT(A) had accepted the appellant's contention that the payment was not chargeable to tax in India. On further appeal by the Department to ITAT, the order of the CIT(A) was upheld.

Held :

The ITAT held :

- Though the service rendered by Fugro was technical in nature, it did not make available technical knowledge, experience, skill, know-how or process to the assessee.
- Relying on the following decisions and the technical explanation in protocol of India-USA Treaty, the ITAT supported its conclusion that the geo-physical survey conducted by Fugro was not included services.
  - ➢ *C.E.S.C. Ltd. v. DCIT*, (87 ITD 653) (Kol.) (TM)
  - ➢ *Raymond Limited v. DCIT*, (80 TTJ 120) (Mum.)
  - ➢ *NQA Quality System Registrar Ltd. v. DCIT*, (92 TTJ 946) (Delhi)
  - ➢ *McKinsey & Co. Inc. (Philippines) v. ACIT*, (284 ITR (AT) 227) (Mum.)

- The Tribunal concluded :

  'Fugro' has surveyed, collected and processed the data on behalf of De Beers. There is no doubt that 'Fugro' performed the services using substantial knowledge and expertise, but such technical experience, skill or knowledge has not been made available to 'De Beers'.

- It was also held that the report containing data of survey provided by Fugro did not amount to development and transfer of technical plan. The Tribunal noted that in terms of the agreement, the survey data belonged to the assessee and mere presentation thereof by Fugro in the specified format did not amount to development and transfer of technical plan or technical design within the meaning of the Treaty.

10 Sumitomo Corporation *v.* DCIT (17 SOT 197) (Del.)
A.Ys. : 1992-93 to 1995-96. Dated : 31-5-2007
Article 12 of India-Japan DTAA and S. 115A of the Act.

Issues :

- ***Fees for technical services which are not effectively connected with project PE are chargeable to tax in India under Article 12(2) of the Treaty.***
- ***Supervision project PE emerges only if number of days of supervision of each project exceeds specified threshold; aggregate duration of all projects is not to be considered.***

Facts :

The assessee, a Japanese company, had established a Liaison Office (LO) in India since 1956. LO facilitated the assessee's supplies to India by acting as communication channel between the HO and the Indian importers. In or around 1980 (much prior to signing of DTAA between India and Japan in the year 1989), the assessee and the Tax Department had entered into a settlement. The settlement provided that the LO in India would pay tax on ⅓rd of profit in respect of income from all the supplies made to India. Indian profit was agreed to be calculated, based on global formulary approach.

From 1992 onwards, the assessee expanded its activities in India and obtained certain turnkey projects. These turnkey projects admittedly gave rise to project PE in India.

One of the project PEs which the assessee had in India was in respect of paint shop of MUL. This was part of overall car project of MUL. In this project, the assessee was involved in supply, installation and supervision. In respect of MUL PE project, the assessee had paid taxes and there was no dispute on assessment thereof.

Pursuant to separate tenders floated by MUL for certain equipments for its car project, the H.O. had supplied equipments pursuant to 10 different purchase orders, for which bid was awarded to the H.O. The equipments were installed by third party contractors. In respect of these supplies, the H.O. provided supervision services, which, in respect of each of the equipments, worked out to less than 180 days.

Before the AO and the CIT(A), the assessee claimed that consideration for impugned supervision services was fees for technical services and was chargeable to tax @ 20% in terms of Article 12(2) of India-Japan Treaty.

The AO held that supervision fees were chargeable as business income under Article 12(5) read with Article 7 of the Treaty. In the view of the AO, supervision fees were effectively connected with PE of the assessee in India. The amount was accordingly held chargeable @30%. The AO supported his claim by contending that :

- LO in India constituted PE and that once the assessee had PE in India, all the income arising from business had to be charged as PE income.
- Alternatively, supervision services rendered on aggregate basis for ten supplies exceeded the period of 180 days and therefore gave rise to emergence of supervision PE.

By way of an additional ground before the ITAT, the assessee claimed that no part of supervision fees was chargeable to tax in India, as the same constituted an integral part of equipment supplies which were made on principal-to-principal basis from Japan. It was claimed that the agreement to taxation of profit in respect of supplies from Japan was contrary to legal position and was not binding on the assessee. Since supervision fees was integral and incidental to equipment supplies, the amount was not chargeable to tax in India.

The Tribunal did not admit the additional ground of the assessee. In the view of the Tribunal, the controversy all along had been limited to the

applicable rate of tax, without there being any challenge to the base taxability. In the view of the Tribunal, the facts and circumstances of the case did not persuade them to exercise discretion in favour of the assessee to permit raising the issue of non-chargeability for the first time before the Tribunal.

Held :

On the aspect of applicable rate of tax, the ITAT admitted the claim of the appellant and held that the impugned service fees was chargeable @20% in terms of Article 12(2) of the Treaty.

(1) The liaison office in India was not proved to be a permanent establishment of the assessee, as the activities of the LO were confined to functions which were auxiliary and preparatory in nature. The fact that the LO had a fixed place of business or had infrastructure was not sufficient to constitute the LO to be PE chargeable to tax. The Tribunal observed :

"So long as the LO performs functions which are preparatory and auxiliary in nature, there can be no allegation that they constitute a PE. The fact that the LO owned assets and incurred huge expenses can never be a ground to conclude that they constitute PE. The prohibition on the part of the LO to carry on activities generally done by a PE in the permission granted by RBI cannot be lost sight of. There has been no proceeding against the assessee by RBI in this regard."

(2) Presence of other project PEs can have no adverse impact on taxability of supervision fees which is not connected with such project PE.

(3) The Tribunal concluded that each equipment supply contract constituted an independent project. Accordingly, threshold of 180 days had to be applied to each project separately. Since supervision work of each of the projects lasted less than 180 days, none of the projects gave rise to emergence of supervision PE.

(4) For reckoning the length of project duration, what should be considered is the number of physical days and not the number of man days. The fact that supervision involved more than 1 employee at a time and that the aggregate man days on a given project exceeded 180 days was not relevant, so long as physical duration was of less than 180 days.

(5) For concluding that 10 different equipment supply contracts constituted 10 different projects, the Tribunal considered factors such as : separate global tenders floated by MUL, different terms and conditions of each purchase order, which were not linked with the other purchases; different performance guarantees for each contract; different third party contractors involved for installation of each machine, etc. The Tribunal noticed that the completion of work of installation of one was not dependent on the other and that different equipments were used in different segments of MUL car manufacturing plant. The Tribunal also noted that the equipments did not complement each other and it was quite probable that MUL could have selected different suppliers for different equipments. According to the Tribunal, the supply contracts did not form a coherent whole commercially, geographically and financially and the aspect of all projects being for one customer was held not decisive of the issue.

11 **Triniti Corporation USA,** *In re*
(295 ITR 258) (AAR)
Dated : 16-11-2007

Article 13 of India-USA Treaty; S. 9(1)(i), S. 163, S. 195 of Income-tax Act

Issue :

Transfer of shares of Indian company from one non-resident to another non-resident effected outside India is chargeable to tax in India.

Facts :

M/s. Triniti Corporation, USA (USCO) entered into an agreement to purchase shares of Triniti Advance Software Labs Pvt. Ltd. (ICO) from one Mr. Jeff (the transferor), a person not resident in India. The transaction was a deal for transfer of shares of ICO from one non-resident to another non-resident. The transfer was concluded in the USA.

Originally, application was filed before AAR by USCO seeking rulings on the questions (i) whether the transaction of transfer was liable to tax in India, as the transfer was between two non-residents and was concluded outside India; and (ii) whether USCO could be regarded as an agent of the transferor in terms of S. 160, 161 r.w. S. 163 of the Act.

During the course of hearing, in its written submission, the Department contended that in terms of inclusive definition of S. 163, ICO can also

be regarded as an agent of the transferor.

In the rejoinder submission filed by US co.'s counsel, it was contended that ICO cannot be regarded as an agent and that capital gain was also not chargeable to tax, as the transfer of shares had taken place outside India and the transaction is between two non-residents.

At the time of further hearing, the counsel of US co. had admitted that capital gains was chargeable to tax in India, as the transaction involved transfer of shares of ICO and that USCO was an agent of transferor in terms of S. 163 of the Act. It was clarified that the application was filed before the authority to have an authoritative pronouncement with reference to this plea of the applicant.

At the time of final hearing, the Department and the applicant had requested the authority to give ruling based on submissions and concessions on record.

In the proceedings which took place before the AAR, the authorised representative of the transferor agreed that (i) USCO can be regarded as an agent u/s.163 of the Act, for the purpose of taxation of capital gains; and (ii) the transferor is liable to pay tax in India in view of provisions of S. 9(1)(i) of the Act read with provisions of India-USA Treaty.

The ruling was thus sought on the basis of above admission and representation.

Held :

(a) In terms of S. 9(1)(i), any income accruing or arising, whether directly or indirectly, through the transfer of a capital asset situated in India was chargeable to tax in India, as income deemed to accrue or arise in India.

(b) Shares of ICO constitute an asset situated in India and gain arising on transfer of such shares can be regarded as income accruing or arising to a non-resident through transfer of such capital asset in India.

(c) S. 9(1)(i) would take care of taxation when transfer of a capital asset situated in India took place outside India pursuant to a transaction between two non-residents.

(d) Chargeability under the Domestic Act was also not relieved by the Treaty as Article 13 of India-USA treaty permits taxation of capital gains in accordance with provisions of domestic law of India.

(e) In terms of S. 163, the purchaser of capital asset from non-resident who pays sales consideration to non-resident transferor can be regarded as an agent. Accordingly, USCO [the applicant] was an agent of the transferor, which position was also admitted by the applicant.

(f) Since USCO was held to be an agent, the AAR declined to deal with the Department's contention as to whether ICO can be regarded as an agent.

(g) The AAR also observed :

"Incidentally, we would like to observe that in view of the conclusions we have reached, the applicant has to keep in view the provisions of S. 195 of the Act relating to tax deduction at source."

One fine Morning
When my half day learning
Of ESOP lessons had just ended
At the famous ghia hall.....
The powerpoint was
Fairly crisp from very
Pravin Dr shah who
Himself notoriously banked
His own by pass table treat!
A cavalcade of gurus
Floated my deep sleep
Of Saturday morning.....
SVG who tended my audits traits
NAP nurturing my very spine
YP breeding laughter in person
VHP how to embrace with
Love and care
AHD how to win slow and steady
And wear fatigue away
SP will humour and simplicity
SED with sharp legal mind but
Not sans humane bend
PNS ever to direct and guide
All these gurus flavoured my
Life with pleasure and care

— B. V. Dalal, C.A.

K. B. Bhujle
Advocate

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A. Unreported :

29 **Reassessment : S. 147 and S. 148 of Income-tax Act, 1961 : A.Y. 2001-02 : Mere change of opinion in subsequent year does not constitute 'reason to believe' for a valid notice u/s.148 : Reopening based on such change of opinion is not valid.**

[*Siemens Information System Ltd. v. ACIT (Bom.)*, W. P. No. 2386 of 2006; dated 11-10-2007]

The petitioner company was eligible for deduction u/s.10-A and u/s.10-B of the Income-tax Act, 1961 for different units situated at different places. For the A.Y. 2001-02, the assessment was completed u/s.143(3) of the Act, allowing the claims for deduction u/s.10-A and u/s.10-B by adopting the method which the Assessing Officer found to be proper. For the A.Y. 2003-04, a different Assessing Officer adopted a different methodology and negatived the similar claim. On the basis of such assessment for the A.Y. 2003-04, the Assessing Officer issued notice u/s.148, dated 13-3-2006 for the A.Y. 2001-02. The assessee's objections to the notice were rejected.

On a writ petition filed by the assessee challenging the reopening, the Bombay High Court quashed the notice u/s.148 and held as under :

"(i) The real issue is whether on the facts of the case, can it be said that this is a case of mere change of opinion ? The Assessing Officer can assume jurisdiction u/s.147 of the Act on any fresh information or change in the legal position or the like. However, can the succeeding Assessing Officer because such officer holds a view different on the interpretation of the provisions of the law, which were considered by the previous Assessing Officer, result in issuing the notice u/s.148 of the Income-tax Act ? In this context, whether on the facts of the case, there was material for the Assessing Officer for 'reason to believe' that income chargeable to tax has escaped assessment ?

(ii) When a challenge is made to a notice u/s.148 of the Act, what the Court is required to examine is whether material exists on record for the Assessing Officer to form the requisite belief. Mere change of opinion cannot form the basis of reopening a completed assessment.

(iii) In the instant case, the second Assessing Officer for A.Y. 2003-04 on the same set of facts has taken a view which is different from the view taken by the previous Assessing Officer for A.Y. 2001-02, on the interpretation of the same provisions of law. It is possible in the absence of finality to a question of law, that an Assessing Officer on the same set of facts could take a different view. Would that attract the provisions of S. 148 of the Income-tax Act because the second Assessing Officer holds a different view on the interpretation of the provisions ? The accounting system is the same. The returns have been filed in the manner prescribed by the Form. On these facts because the second Assessing Officer differs with the opinion of the earlier Assessing Officer on the interpretation of the provision without any other additional material, is he entitled to assume jurisdiction to issue a notice u/s.148 ? In our opinion, such a belief would amount to a mere change of opinion. The remedy in case like this would be to invoke or resort to the other applicable provisions of the Act. If the ITO does not possess the power of review, he cannot achieve that object by initiating proceedings for reassessment or by way of rectification of mistake. A mere change of opinion on an interpretation of a provision by itself without anything more, cannot give rise to 'reason to believe'. The power of reopening an assessment has been conferred by the Legislature not with the object of enabling the Income-tax officer to reopen the full declaration made against the revenue in respect of questions raised that arose directly for consideration in the earlier proceedings. If that were not the legal position, it would result in placing an unrestricted power of review in the hands of the assessing authorities depending on their changing moods."

B. Reported :

Assessment : Validity : A.Ys. 1994-95 and 1995-96 : Assessment order passed, relying on report from an institute without giving an opportunity to cross-examine the analyst concerned, is invalid being in violation of principles of natural justice.

[*CIT v. Dharam Pal Prem Chand Ltd.*, 212 CTR 253 (Del.)]

The assessee was manufacturing chewing tobacco (Zaffrani Patti). In the course of the assessment proceedings for the A.Ys. 1994-95 and 1995-96, the Assessing Officer drew samples of Zaffrani patti and sent them to the Shri Ram Institute for Industrial Research, New Delhi, with a request to ascertain the percentagewise presence of silver in different qualities/brands of Zaffrani patti. The said institute sent its report. On the basis of the said report the Assessing Officer estimated the total consumption of silver in the manufacture of various products of the assessee. The assessee filed objections and requested for opportunity to cross-examine the analyst. The Assessing Officer completed the assessment without giving the assessee an opportunity to cross-examine the analyst. The CIT(A) came to the conclusion that the assessee was not given permission to cross-examine the analyst and that was enough to vitiate the assessment order. Accordingly, the CIT(A) set aside the assessment order. The Tribunal upheld the decision of the CIT(A).

On appeal by the Revenue, the Delhi High Court upheld the decision of the Tribunal and held as under :

> "There can hardly be any doubt that the Assessing Officer had based his assessment order on the report obtained from an Institute and the correctness of that report was itself under challenge by the assessee who had not only filed objections thereto, but also sought permission to cross-examine the analyst. The Assessing Officer did not permit cross-examination of the analyst. There is no doubt that even if the strict rules of evidence may not apply, the basic principles of natural justice would apply to the facts of the case. The Assessing Officer placed reliance upon the report of the Institute for deciding against the assessee. The report cannot be automatically accepted, particularly since there is a challenge to it and the assessee had sought permission to cross-examine the analyst making the report. Since the Assessing Officer did not permit the correctness or otherwise of the report to be tested, there is a clear violation of principles of natural justice committed by him in relying upon it to the detriment of the assessee. No substantial question of law arises for consideration."

Business expenditure : S. 37(1) of Income-tax Act, 1961 : A.Y. 1999-00 : Interest on loan utilised for business activities is allowable business expenditure : Interest cannot be disallowed on the ground that the assessee had other funds by way of business receipts, etc. which could have been utilised for business activity.

[*CIT v. Dalmia Bros. (P) Ltd.*, 164 Taxman 63 (Del.)]

The assessee had raised certain loans and had utilised them for business activity *inter alia*, for office rent, vehicle repair, petrol expenses, etc. and had claimed the interest on that loan as business expenditure. For the A.Y. 1999-00, the Assessing Officer disallowed the claim on the ground that the assessee had professional receipts for that purpose and there was no reason for the assessee to utilise loans for its business activities, instead of utilising the receipts from business. The Tribunal allowed the claim for deduction.

On appeal by the Revenue, the Delhi High Court upheld the decision of the Tribunal and held as under :

> "(i) The Tribunal relied upon a decision of this Court in *CIT v. Dalmia Cement (Bharat) Ltd.*, (2002) 254 ITR 377, wherein it was held that the reasonableness of the expenditure could be gone into only for the purposes of determining whether, in fact, the amount was spent. Once it is established that there was a nexus between the expenditure and the purpose of the business, the Revenue cannot justifiably claim to put itself in the armchair of the businessman or in the position of the Board of Directors and decide how much is reasonable expenditure having regard to the circumstances of the case.
>
> (ii) In view of the decision of this Court to the effect that the Assessing Officer cannot claim to run the affairs of the assessee in a manner that he thinks appropriate, which is what has happened in the present case, we find that no substantial question of law arises."

Business expenditure : S. 37 of Income-tax Act, 1961 : A.Y. 1995-96 : Assessee sugar industry : Bakshish paid to labourers employed by contractors is business expenditure : Allowable as deduction u/s.37.

[*CIT v. Samarth Sahakari Sakhar Karkhana Ltd.*, 294 ITR 540 (Bom.)]

The assessee was a co-operative society engaged in manufacture and sale of sugar. The assessee had claimed deduction of the amount paid by way of bakshish to the labourers employed by the contractors. The Assessing Officer disallowed the claim. The Tribunal allowed the claim.

On appeal by the Revenue, the Bombay High Court upheld the decision of the Tribunal and held as under :

> "Giving bakshish to the workers employed by the harvesting and transport contractors had been the practice prevailing in the State of Maharashtra for decades and such expenditure had been consistently allowed in the past, not only in the case of the assessee, but also in the case of several other sugar factories. The Tribunal had noted that it was only the skilled labourers who could do the job of harvesting and transporting the sugarcane and the general labourers could not do such job work. With a view to induce the labourers to continue with the work during the summer months, bakshish ranging from Rs.200 to Rs.250 was given to the labourers employed by the harvesting and transport contractors. The Tribunal was justified in holding that the payment was deductible."

Business expenditure : Capital or revenue : S. 37(1) of Income-tax Act, 1961 : A.Y. 1997-98 : Customised software is of an enduring nature : Software which is not customised requires frequent upgradation and expenditure on such software is revenue expenditure, allowable as business expenditure.

[*CIT v. G. E. Capital Services Ltd.*, 164 Taxman 46 (Del.)]

For the A.Y. 1997-98, the assessee company had claimed deduction of expenditure incurred on MS Office software which was not customised software, as revenue expenditure. The Assessing Officer disallowed the claim holding that it is capital expenditure. The Tribunal allowed the claim.

On appeal by the Revenue, the Delhi High Court upheld the decision of the Tribunal and held as under :

> "(i) The Tribunal was of the view that due to the technological changes and the need to upgrade the software on regular basis, it cannot be said that the software was of an enduring nature. The software for which the expenditure was incurred was MS Office, which is not a custom-built software for the assessee and it is common knowledge that this software requires regular upgradation.
>
> (ii) Where customised software is prepared, then it could be of an enduring nature, but in this case, MS Office is not customised software and it cannot be said that the software does not require frequent upgradation. There is no error committed by the Tribunal in taking the view that it did."

Business expenditure : Capital or revenue : A.Y. 1992-93 : Advance to suppliers of tools and dies is revenue expenditure : Deduction allowable as business expenditure.

[*CIT v. Honda Siel Power Products Ltd.*, 212 CTR 314 (Del.)]

The assessee company was manufacturing portable generator sets. Prior to the A.Y. 1992-93, the assessee was amortising the advances made by it to the manufacturer of tools and dies, on the basis of the actual quantity of components used in the production of generator sets. A.Y. 1992-93 onwards, the assessee claimed the advances as revenue expenditure. The case of the assessee was that the payment made as advance was non-recoverable and the ownership of the tools and dies remained with the manufacturer. The Assessing Officer rejected the change in the method and disallowed the claim for deduction. The Tribunal held that the tooling advance was for facilitating the trading operations of the assessee and further that tools and dies continued to remain the property of the manufacturer. The Tribunal allowed the claim for deduction.

In appeal filed by the Revenue, the Delhi High Court upheld the decision of the Tribunal and held as under :

> "In order to treat an item of expenditure as capital expenditure, it will have to be shown that the asset in question, for which the advance has

been paid is actually in the ownership of the assessee. At no point of time was such expenditure claimed as capital expenditure by the assessee. That being the position, there was no justification for the AO to disallow the deduction of the tooling advance on the ground that the assessee, though not owning the asset in question, was deriving an enduring benefit from it. The fact that the moulds and dies continue to remain the property of the manufacturer is decisive in determining the nature of the expenditure. The tooling advance paid to the vendors is also non-refundable. Not only is there an assurance of continued supply of components, but as a result of this arrangement there is a price advantage. Earlier these components were imported and now there would be an indigenised source of supply. In these circumstances, the finding of the Tribunal that the enduring advantage obtained by the assessee is only in the revenue field and not in the capital field, cannot be faulted."

Business income : Deemed income u/s. 41(1) of Income-tax Act, 1961 : A.Y. 1996-97 : Unilateral write-off of liability is not sufficient for addition of income u/s.41(1) : Insertion of Explanation 1 to S. 41(1) by Finance (No. 2) Act, 1996 applicable only from A.Y. 1997-98.

[*CIT v. EID Mohd. Nizamuddin*, 212 CTR 13 (Raj.)]

For the A.Y. 1996-97, the AO made an addition of Rs.11,80,973 on account of writing back of the said amount by the assessee in the P&L a/c by relying on Explanation 1 to S. 41(1) of the Income-tax Act, 1961. The Tribunal deleted the addition.

On appeal by the Revenue, the Rajasthan High Court upheld the decision of the Tribunal and held as under :

"(i) The fact that clarification was introduced by introducing Explanation 1 u/s.41(1) clearly shows that doubt was prevailing in respect of applicability of S. 41(1) in case of unilateral write-off. Benefit of doubt must go to the assessee.

(ii) S. 16 of Finance (No. 2) Act, 1996 clarifies that Explanation 1 is effective from 1st April 1997, and is applicable in relation to A.Y. 1997-98 and subsequent years. Therefore, the liability written back unilaterally by the assessee in the A.Y. 1996-97 is not chargeable to tax."

Cash credit : S. 68 of Income-tax Act, 1961 : A.Ys. 1998-99 and 1999-00 : Share application money : Even if subscribers to increased capital not genuine, share capital cannot be regarded as undisclosed income of assessee.

[*CIT v. Electro Polychem Ltd.*, 294 ITR 661 (Mad.)]

For the A.Ys. 1998-99 and 1999-00, the Assessing Officer made additions u/s.68 of the Income-tax Act, 1961 in respect of the share application money on the finding that the assessee had brought undisclosed income by way of share applications in fictitious names. The Tribunal deleted the additions.

The Madras High Court dismissed the appeal filed by the Revenue, applying the judgments in the case of *CIT v. Stellar Investment Ltd.*, (1991) 192 ITR 287 (Del.) and *CIT v. Stellar Investment Ltd.*, (2001) 251 ITR 263 (SC) and held as under :

"Even if it was assumed that the subscribers to the increased share capital were not genuine, under no circumstances could the amount of share capital be regarded as undisclosed income of the company."

Income : Accrual of : Interest on irrecoverable loans : A.Y. 1998-99 : Principal amount written off as bad debt and the claim of assessee allowed in subsequent years : There was no real accrual of interest income.

[*CIT v. Goyal M. G. Gases (P) Ltd.*, 212 CTR 305 (Del.)]

For the A.Y. 1998-99, the Assessing Officer had made addition of notional interest on the advances given by the assessee to seven parties, on the ground that the assessee was following mercantile system of accounting and interest had accrued to the assessee as its income. The assessee contended that in the subsequent year, the assessee had written off the loans given to the seven parties as bad debts and the Assessing Officer had also accepted the writing off of the principal amount. The Tribunal deleted the addition.

On appeal, the Revenue submitted that the Tribunal was in error in taking note of subsequent events and should have strictly gone by the principles of the mercantile system of accounting and on that basis it should have been held that the Assessing Officer was correct in taking the interest on those advances as income having accrued to the assessee.

The Delhi High Court upheld the decision of the Tribunal and held as under :

> "Both the CIT(A) and the Tribunal came to the conclusion that there was no real accrual of interest. It has been noted that the interest had not even been recorded in the assessee's books of account. The assessee had also issued a notice to the parties u/s.138 of the Negotiable Instruments Act for dishonour of cheques issued by all (except one of the debtors) followed by initiation of appropriate proceedings. The debts were written off as bad debts and were also allowed by the AO in the subsequent years. These facts lead to the inescapable conclusion that realisation of even the principal amount was in jeopardy and, therefore, there cannot be said to be any real accrual of income by way of interest. There is no fault in this view taken by the Tribunal and no substantial question of law arises for consideration."

Revision : S. 41(1) and S. 263 of Income-tax Act, 1961 : A.Y. 1989-90 : Assessee surrendered Group Gratuity Scheme with LIC and received sum in the relevant year : Assessee continued to show amount payable under scheme as liability in balance sheet : CIT not justified in directing to assess the amount so received u/s.41(1).

[*CIT v. Tamil Nadu Warehousing Corporation*, 212 CTR 228 (Mad.)]

The assessee had surrendered the Group Gratuity Scheme with LIC and had received a sum of Rs.8,22,925 in the A.Y. 1989-90. The amount was continued to be shown as payable under the scheme as liability in the balance sheet. The AO had not assessed the said amount in the assessment order passed u/s.143(3) of the Income-tax Act, 1961. The CIT passed a revision order u/s.263 of the Act and directed the AO to assess the said amount u/s.41(1) of the Act. The Tribunal allowed the appeal filed by the assessee and set aside the order of the CIT.

On appeal by the Revenue, the Madras High Court upheld the decision of the Tribunal and held :

> "Assessee having continued to show the amount payable under the Group Gratuity Scheme as liability in the balance sheet even after surrendering the scheme, the same is not assessable u/s.41(1) and, therefore, CIT was not correct in passing order u/s.263 on the ground that the Assessing Officer had not made proper enquiry."

Special audit : S. 142(2A) of Income-tax Act, 1961 : Audit is for the purpose of satisfying one about the authenticity and credibility of accounts prepared by the assessee : AO cannot direct u/s.142(2A) the preparation of fresh books.

[*CIT v. Bajrang Textiles*, 294 ITR 561 (Raj.)]

Pursuant to search u/s.132 of the Income-tax Act, 1961 on 20-11-1997, block assessment proceedings were commenced by a notice u/s.158BC, dated 7-9-1998. Only one day before the period for completing the block assessment was expiring, the Assessing Officer issued directions u/s.142(2A) of the Act for special audit and the block assessment order was passed on 24-5-2000. The Tribunal noticed that the Assessing Officer had not merely referred the accounts to be audited under special audit by an auditor named by him, but he had directed the special auditor to prepare the books of account in the form of cash book, ledger, on the basis of the documents/papers seized during the course of search as per his directions. The auditor was also required to prepare trading, profit and loss account, which were recorded in the regular books of account and further to determine the undisclosed income of the block period. The Tribunal came to the conclusion that the reference to the special audit u/s.142(2A) of the Act was not for the purpose for which the provision was enacted, but merely for getting an extended period for completing the assessment, which is not permissible under the law. The Tribunal held that the reference to the special audit was illegal and consequently the assessment order was barred by time.

On appeal by the Revenue, the Rajasthan High Court upheld the decision of the Tribunal and held :

> "Apparently, the order was for preparing fresh books rather than to conduct a special audit. This was on the face of it, beyond the scope of provisions of S. 142(2A) of the Income-tax Act. No authority has been given to the Assessing Officer to direct the preparation of fresh books by referring a matter to an auditor under special audit. Audit is for the purpose of satisfying one about authenticity and credibility of accounts prepared by the assessee, but not for preparing new account books as per directions of the AO. Apparently, the Tribunal found that it was abuse of process by the Assessing Officer. The findings given by the Tribunal are findings of fact based upon the relevant material."

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Interest and project-completion method

1. Issue for consideration :

1.1 S. 36 of the Income-tax Act permits a deduction for an amount of interest paid in respect of capital borrowed for the purposes of business or profession. The deduction under the Section, is allowed in computing the total income, independent of the method of accounting followed by the an assessee and is permitted even where the borrowing is for purchase of a capital asset, subject to the restrictions contained in the proviso to the said Section.

1.2 An assessee accordingly is eligible for deduction for interest paid, once he establishes that the borrowings were the purposes of business.

1.3 A developer or a builder engaged in the business of construction may, like any other businessman, borrow funds for the purposes of his construction business and pay interest thereon. Ordinarily, this interest qualifies for deduction u/s. 36(1)(iii) of the Act.

1.4 A developer follows the work-in-progress or the percentage-of-completion method of accounting for determining his profits or losses of the business of construction. Alternatively, he follows the project completion method or the completed-contract method of accounting. In the first method, the interest paid is debited to the Profit & Loss Account, while in the alternative method, the interest may or may not be debited to the Profit & Loss Account.

1.5 An issue has arisen about the eligibility for the claim of deduction for payment of interest in the case of a developer following the project-completion method of accounting pending the completion of the project. The issue gets more pronounced where the developer has included such interest as part of the work-in-progress and has claimed such interest u/s.36 in computing his total income without debiting the same in the Profit & Loss Account.

1.6 Just when it was believed that the issue under consideration has been settled by a recent decision of the Bombay High Court, the issue is kicked alive by the recent decision of the Special Bench of the Income-tax Appellate Tribunal, wherein a view has been taken against the claim of such a deduction in the year of payment by distinguishing the said decision of the Bombay High Court.

2. Lokhandwala Construction's case :

2.1 The issue had arisen in the case of *CIT v. Lokhandwala Construction Inds. Ltd.*, 260 ITR 579 (Bom.). In that case, the assessee-company was engaged in the business of construction of buildings. The assessee followed mercantile system of accounting and project-completion method for computing its profits. It had secured development rights in respect of a plot of land situated at Kandivali from a trust for an agreed consideration. A sum of Rs.1.10 crores was paid by the assessee to the transferor of the said plot of land out of loans amounting to Rs.1.15 crores. The assessee claimed deduction of Rs.14,09,942 paid as interest on the said money borrowed u/s.36(1)(iii) of the IT Act. By an assessment order dated 30th Sept. 1986, the claim for deduction was allowed. However, the CIT, exercising his authority u/s.263 of the IT Act, came to the conclusion that the loan of Rs.1.15 crores was utilised by the assessee for acquiring an asset and, therefore, the claim for deduction u/s.36(1)(iii) could not have been allowed; that it was not a revenue expenditure because it was a loan raised for acquiring a capital asset. Accordingly, the CIT cancelled the assessment order disallowing the interest of Rs.14,09,942.

2.2 In the second appeal to the Tribunal, following its earlier decision, the Tribunal held that the interest paid by the assessee could not be treated as a capital expenditure. Being aggrieved, the Department filed an appeal to the Bombay High Court u/s.260A of the IT Act.

2.3 The following question of law was referred to the Court :

> "Whether, on the facts and in the circumstances of the case, the Tribunal was correct in law in holding that the interest claimed as revenue expenditure amounting to Rs.14,09,942 cannot be treated as capital expenditure and added to

work-in-progress in spite of the fact that other expenses on project were being capitalised by the assesee itself and holding that the CIT was wrong in directing the AO to disallow the said interest and treat the same as capital expenditure as a part of work-in-progress, thereby quashing the order u/s.263 of the Act of the CIT ?"

2.4 The Court noted the factual position; that the assessee undertook two-fold activities of buying and selling flats and construction of buildings, and the profits from both the activities were assessed u/s.28 of the IT Act, but the Court was concerned with the second activity, namely, the Kandivali project; that according to the CIT, the loan was raised for securing land/development rights, which, according to the CIT, constituted a capital asset and since the loan was raised for securing a capital asset, the interest incurred thereon constituted part of capital expenditure; that this finding of the CIT was erroneous; that in the case of *India Cements Ltd. v. CIT*, 60 ITR 52 (SC), it was held by the Supreme Court that in cases where the act of borrowing was incidental to carrying on of business, the loan obtained was not an asset; that for the purposes of deciding the claim of deduction, it was irrelevant to consider the purpose for which the loan was obtained; that the Court in the case was concerned with deduction u/s.36(1)(iii).

2.5 Having noted the factual position and the position in law, the Court observed that in the present case, the assessee was a builder who had undertaken the project of construction of flats under the Kandivali project by use of loans for obtaining stock-in-trade and the said Kandivali project constituted the stock-in-trade of the assessee, which project did not constitute a fixed asset of the assessee.

2.6 The Court, in pursuance of the above observations, held that since the assessee had received loan for obtaining stock-in-trade, the assessee was entitled to deduction u/s.36(1)(iii) of the Act. It observed that while adjudicating the claim for deduction u/s.36(1)(iii) of the Act, the nature of the expense, whether the expense was on capital account or revenue account, was irrelevant as the Section itself provided that interest paid by the assessee on the capital borrowed by the assessee was an item of deduction. It also held that the utilisation of the capital was irrelevant for the purposes of adjudicating the claim for deduction u/s.36(1)(iii) of the Act by applying the judgment of the Bombay High Court in the case of *Calico Dyeing & Printing Works v. CIT*, 34 ITR 265 (Bom.), wherein it was held that all that the assessee had to show was that the capital which was borrowed was used for business purpose in the relevant year of account and it did not matter whether the capital was borrowed in order to acquire a revenue asset or a capital asset.

3. **Wall Street Construction's case :**

3.1 The issue again came for consideration in the case of *Wall Street Construction Ltd. & Anr. v. JCIT*, 102 TTJ 505 (Mum.) (SB). In that case, both the assessees were engaged in the business of construction and were following project-completion method of accounting, which according to the Tribunal meant that the profits arising from a particular project were offered for taxation in the year in which that project was complete or substantially complete. The assessees were simultaneously constructing multiple projects, and accounts were separately maintained for each project. The assessees had borrowed on interest substantial funds which were used as working capital for execution of the various construction projects. Such interest was not in the nature of direct cost of the project and the expenditure was treated as a 'period cost' and was claimed as a deduction in the year of accrual.

3.2 It was claimed that this procedure for claiming deduction in respect of interest for each year u/s. 36(1)(iii), instead of adding it to the cost of the project, was being consistently followed by the assessees. The AO rejected this claim and held that interest expenditure had to be added to the value of work-in-progress, as the assessees were following the project-completion method of accounting. The AO's view was upheld by the CIT(A), with the result that the issue came to be agitated before the Tribunal.

3.3 In the appeal, the following issue was referred for consideration of the Special Bench :

"Whether, where an assessee is following project-completion method of accounting, the interest identifiable with that project should be allowed as deduction in the year when the project is completed and income is offered from the project or it should be allowed on year-to-year basis ?"

3.4 It was contended before the Tribunal by the assessees that the relevant issue stands covered in the case of one of the assessees Wall Street Construction Ltd. for A.Y. 1994-95, vide order dated 17th Aug. 2003 (ITA No. 3477/Mum./1998), and also in the case of Natasha Construction Ltd. for A.Ys. 1996-97 and 1997-98 (ITA Nos. 4527 and 4528/Mum./2001). Reliance was also placed on the Bombay High Court decision in the case of *CIT v. Lokhandwala Construction Industries Ltd.*, 260 ITR 579 (Bom.).

3.5 On the other hand, on behalf of the Department, it was submitted that the method of accounting was changed by the assessees and that it was incorrect to say that the method of claiming deduction for interest from year to year was consistently followed by the assessee and was accepted by the Department in earlier years. The Department also relied on the decision in the case of *S. K. Estates (P) Ltd. v. ACIT*, 60 ITD 621 (Mum.), wherein it was held that interest cost must be added to the value of work-in-progress, where the assessee was following the project-completion method of accounting.

3.6 On behalf of the assessees, the following six relevant questions were posed :

(i) In a case of a builder following the project-completion method, engaged in simultaneous construction of multiple projects, whether interest cost was a period cost or it had to be added to the value of work-in-progress ?

(ii) Whether interest on such borrowings which could not be directly linked to a particular project, was to be allowed from year to year or was to be added to the value of work-in-progress ?

(iii) What was the impact of AS-7 issued by the Institute of Chartered Accountants ?

(iv) Whether the Bombay High Court decision in the case of Lokhandwala Construction Industries Ltd. (*supra*) concluded the controversy ?

(v) Whether in the case of a builder following the project-completion method, the work-in-progress was to be considered as stock-in-trade or capital asset ?

(vi) Whether a system of accounting consistently followed by the assessee and accepted by the Department in earlier years could be discarded by the Department having regard to the ratio of the Bombay High Court in the case of *CIT v. Goodlas Nerolac Paints Ltd.*, 188 ITR 1 (Bom.) ?

3.7 It was further contended that if the interest cost was not deducted u/s.36(1)(iii) on the basis of accrual from year to year, it would result into distortion in the profits shown in a case where no borrowed funds had been raised *vis-à-vis* a case where the construction activity had been carried out with the help of interest-bearing borrowed funds. It is pointed out that eventually, when the projects were complete and the constructed premises were sold, the cost, being value of work-in-progress, would substantially vary in the two cases, whereas the market value would be the same if the projects were otherwise identical and similarly located.

3.8 It was reiterated that the issue was concluded by the Bombay High Court decision in the case of Lokhandwala Construction Inds. (*supra*) and further was covered in assessee's own case by the orders of the Tribunal for preceding assessment years, and accordingly on merits the interest had to be allowed from year to year.

3.9 On behalf of the Department, it was submitted that :

(i) in the books of account, the interest expenditure had been consistently segregated between different projects and was added to the value of the work-in-progress as reflected in the books of account; that in one of the cases, up to the A.Y. 1991-92, the assessee did not even claim deduction in respect of interest u/s. 36(1)(iii); that the assessees started claiming deduction only while computing the total income for the purpose of filing returns of income, in spite of the fact that in the books of account, the interest expenditure was uniformly and consistently added to the value of work-in-progress; that the assessees were actually following a consistent method of accounting where interest expenditure was added to the value of work-in-progress.

(ii) the provisions of S. 36(1)(iii) prescribe the deduction only when the interest was 'paid', which payment should be determined according to the method of accounting followed, on the basis of which the profits or gains were computed.

(iii) claiming interest from year to year u/s. 36(1)(iii) actually distorted the profits earned

by the assessee of a particular project, because the interest cost which pertained to one project had been claimed by the assessee against the income of another project.

(iv) the only issue considered by the Court in the decision in the case of Lokhandwala Construction Industries Ltd. (*supra*) was whether the interest on borrowed capital utilised for obtaining development rights in respect of loan was a capital expenditure or revenue expenditure allowable u/s.36(1)(iii) in the case of an assessee engaged in the business of construction of buildings and that the relevant question as to whether the interest cost should be added to the value of work-in-progress in the case of an assessee following the project-completion method, was never addressed by the Court.

(v) that under the matching concept of income and expenditure, an expenditure which was relevant to the earning of income only should be deducted from such income, so that a correct picture of the real income chargeable to tax could emerge. For this proposition, he relied on the decision in the case of *Taparia Tools Ltd. v. JCIT*, 260 ITR 102 (Bom.).

(vi) to determine the question of taxability, principles of accountancy have to be taken into account and the ordinary principles of commercial accounting should be applied.

(vii) in the case of *J.C.T. Ltd. v. ACIT*, 61 TTJ (Cal.) 206, it was held that the deduction u/s. 36(1)(iii) was not available if a different treatment had been given in the books of account.

(viii) AS-7, para 8.8, made it clear that if finance costs were specifically attributable to a particular contract, the same had to be included as part of accumulated contract costs and that this accounting mandate was further fortified by AS-16.

3.10 In deciding the case, the Tribunal noted that there was no dispute about the fact that in the books of account, the interest expenditure was allocated to different projects and the interest expenditure referable to a particular project was added to the value of work-in-progress in respect of that project and that the assesses had changed the method of accounting. It further noted that the case of Lokhandwala Construction Industries Ltd. (*supra*) arose in entirely different facts where the Court was concerned with the question as to whether the interest expenditure was a capital expenditure or revenue expenditure, where the Court held that it was immaterial as to whether the borrowed funds were utilised for acquiring a capital asset or revenue asset for allowing a deduction u/s.36.

3.11 The controversy, the Tribunal noted was totally different in the appeal before it, where it was concerned with the question as to whether interest expenditure identifiable with a particular project, in the case of an assessee following project-completion method of accounting, was to be deducted as period cost from year to year or the same was to be added to the cost of that particular project, so as to allow deduction eventually in the year of completion of the project.

3.12 In the view of the Tribunal, the true profits in such a case could be determined only when entire cost of the project, direct or indirect, including finance cost was added to the value of work-in-progress. For this proposition, the Tribunal relied on the matching concept, as propounded in the case of Taparia Tools Ltd. (*supra*). It further observed that claiming deduction in respect of interest against the income of some other projects, which were completed during the relevant years, resulted into distortion of the correct profits which must be determined as per the project-completion method followed by the assessees. Accordingly, the Tribunal held that where an assessee was following the project-completion method of accounting, the interest identifiable with that project should be allowed only in the year when the project was completed and the income from that project was offered for taxation.

4. Observations :

4.1 The facts of the Wall Street Construction's case seem to have largely decided the issue against the assessee. In that case, the assessee had included the interest paid in valuing the work-in-progress for the year and had not debited the same to the Profit & Loss Account. In spite of the contrary accounting treatment, the assessee had claimed the said interest as a deduction in computing the total income by invoking the provisions of S. 36(1)(iii). The claim of the assessee had resulted into a claim of huge loss for the year. On these facts, the Tribunal distinguished the facts in Lokhandwala Construction's case and decided that the ratio of the said decision of the High Court had no application to the facts of the case. It appears to us that the claim of the

assessee for deduction might have had a greater force and might have been considered favourably by the Tribunal, had the said interest been debited to the Profit & Loss Account.

4.2 The Tribunal also took a strong notice of the fact that the assessee in the preceding previous years had debited the interest to the Profit & Loss Account, and such interest was allowed as deduction by the authorities as also by the Tribunal in the assessee's own case for those years on the prevailing facts. The assessee, in the later years, had changed the method of accounting whereunder the interest paid was debited to the value of work-in-progress. It appears to us again that the decision of the Tribunal could have been different, had there been no change in the method of accounting.

4.3 The Tribunal invoked the matching concept of accountancy for deferring the allowance of deduction of an expenditure. It held that an expenditure under the matching concept of accountancy should be allowed in the year in which the income was recognised. With utmost respect to the Tribunal, it is noted that the matching concept of accountancy is invoked for an allowance of an expenditure, like it was done in the case of Calcutta Co. by the Supreme Court, 37 ITR 1, where the income was advanced for taxation and the Supreme Court held that in such circumstances, the probable or estimated expenditure yet to incur for earning such income, should be allowed as a deduction. In fact, the decisions relied upon by the Tribunal for invoking the matching concept were delivered in the above context by following the ratio of the said decision in Calcutta Co.'s case.

4.4 Yet again, it is relevant to notice that Accounting Standard 7, in its revised form, is not applicable to an enterprise engaged on its own account in development and construction of real estate and sales thereof. Further, under the revised Accounting Standard, the projects commencing on or after 1-4-2003 are permitted to follow only percentage-of-completion of method of accounting. Under the new position, a builder or a developer is required to follow AS-9 which provides for recognition of revenue and costs and expenses. This standard requires that the cost and the expenditure should be accounted for as and when they are incurred.

4.5 It is by now an accepted position in law that the tax laws need not follow in the footsteps of accountancy and that an accounting treatment should not determine the allowance of a claim for deduction or treatment of a receipt as an income under the taxation laws. It is also beyond debate that a specific provision in law, like S. 36(1), shall override and prevail over the accounting treatment. S. 36(1)(iii) is one such specific provision which in clear and certain language, permits the deduction for interest on compliance of the requirements of that Section. Once the said requirements are found to be satisfied, the assessee qualifies for the deduction and nothing else should prevent the claim of the assessee for a deduction. This precisely is what the ratio of the decision of the Bombay High Court in the Lokhandwala Construction's case is. This part of the decision remains uncontroverted and, in our respectful opinion, remained to be distinguished, and was required to be respected and followed.

4.6 It is to be noted that the same Mumbai Tribunal in a decision delivered in the case of *JCIT v. K. Raheja (P) Ltd.*, 102 ITD 414 and in a few other cases, following the said decision in the Lokahandwala Construction's case, had held that the interest paid by a builder following the project completion method of accounting was allowable in the year of payment, in accordance with the provisions of S. 36(1)(iii) of the Act.

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ADVT.

Mayur B. Nayak
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Chartered Accountants

India-UAE Tax Treaty — A New Look

India-UAE Tax Treaty has been a matter of controversy ever since the decision of the Advance Ruling Authority in case of Cyril Eugene Pereira. There were conflicting decisions by AARs and Tribunals about the applicability of the UAE Treaty. On 26th March 2007, a protocol was signed between India and the UAE for amendment of various provisions of the original Tax Treaty signed on 29th April 1992. This article highlights the amendments, their possible rationales and probable impact on the cross-border investments and business between India and the UAE.

1.0 Historical perspective[1]

The original Tax Treaty with the UAE was signed on 29th April 1992. In the UAE, no taxes are levied on individuals. Even on corporates there is very limited taxation. The original Treaty contained the usual provisions as contained in treaties with other countries of the world, which have full-fledged taxation systems in place. Moreover, CBDT Circular No. 734[2], dated January 24, 1996 specifically mentioned that NRIs in the UAE would be eligible for reduced rate of taxes in terms of the India-UAE Tax Treaty. This resulted in double non-taxation *vis-à-vis* certain income (especially capital gains) from India arising to individuals resident in the UAE.

Judicially different interpretations were given to the purpose of signing the India-UAE Tax Treaty and its applicability. In M. A. Rafik's case,[3] which related to the India-UAE Tax Treaty, the Authority for Advance Ruling (AAR) observed that, 'India is also in the process of looking out for foreign countries interested in investing in India and must have considered the DTAA as providing an opportunity to improve the economic relations between the two countries and encourage the flow of funds from Dubai'.

Interpreting differently the purpose of the India-UAE Tax Treaty, the AAR in case of Cyril Eugene Pereira[4] observed that 'Double Taxation Agreements are agreements to avoid tax being levied twice by the two countries on the same income in the same year. It is not a device for evasion of the only tax imposed by a country on the income of a person resident in another country'. In Abdul Razak A. Meman's case,[5] the AAR upheld partial applicability of the Treaty to individuals resident in the UAE. Some of the other decisions rendered by the AAR or the Tribunal in respect of the UAE Treaty are as follows :

Sr. No.	Case	Citation
AARs		
01	Al Nisr Publishing	239 ITR 879 (1999)
	(Benefit of India-UAE Tax Treaty was granted to partnership firm in the UAE in respect of business income from India)	
02	UAE Exchange Centre LLC	268 ITR 9 (2004)
	(Provisions of India-UAE Tax Treaty were made applicable to the Indian liaison office to hold that it constituted PE on peculiar facts of the case)	
03	Emirates Fertilizer Trading Co. WLL	142 Taxmann 127 (2005)
	(Benefit of India-UAE Tax Treaty was granted to the partnership firm in UAE in respect of capital gains in India)	
04	Gutal Trading Establishment	278 ITR 643 (2005)
	(Benefit of India-UAE Tax Treaty was denied to a proprietary concern based on the decision in Abdul Razak's case)	

[1] For further insight of the subject, readers are well advised to refer the detailed article titled "Applicability of the India-UAE Treaty to Residents of UAE" in March 2006 issue of the BCAJ published in this Column.

[2] [1996] 217 ITR (St.) 0074

[3] 213 ITR 317, Also see — Dr. Rajnikant Bhat's case (1996) 222 ITR 562

[4] [1999] 239 ITR 650 (AAR)

[5] [2005] 276 ITR 306

Sr. No.	Case	Citation
Tribunal		
04	ADIT *v.* Green Emirates Shipping and Travels	99 TTJ 988 (Mum.) (2006)
	(While granting the benefits of India-UAE Treaty, the Tribunal upheld double non-taxation, relying on the Supreme Court's decision in case of Azadi Bachao Andolan[6])	

The Mumbai Tribunal in case of Green Emirates, as well as the AAR in case of Abdul Razak, urged the Central Government to resolve the confusion over the applicability of the India-UAE Treaty to individuals residing in the UAE. It is in this background the recent amendments to the India-UAE Tax Treaty may be read and appreciated.

2.0 Amendments to the India-UAE Tax Treaty and their implications :

2.1 *Effective date :*

The amendments carried by the protocol signed on 26-3-2007 would be effective in India w.e.f. 1st April 2008[7], *i.e.*, A.Y. 2009-10.

2.2 *Article 4 : Residence :*

Paragraph 1 of Article 4 has been replaced by two paragraphs providing objective criteria for determining the residential status of individuals and other entities.

(i) *Individuals :*

Hitherto, there was ambiguity about the applicability of the treaty to individuals in the UAE, as in absence of tax laws therein, it was difficult to determine the residential status of an individual. Now the amendment provides that if an individual is present in the UAE for a period or periods totalling in the aggregate at least 183 days in the calendar year concerned, he would be regarded as individual resident in the UAE. In case of India, the residential status would be determined depending upon the liability to tax, based on the established residential tests. However, it is specifically provided that a person who is liable to tax in India in respect only of income from sources in India, then such a person would not be regarded as person resident of India under the Treaty provisions.

The impact of this amendment is that a person who is non-resident of India, who may be liable to tax in India only in respect of income sourced from India, would not be eligible to take advantage of the India-UAE Tax Treaty. The AAR in cases of Dr. Rajnikant Bhat and M. A. Rafiq[8] had taken a view that both of them were resident of India under the original Treaty provisions in absence of specific bar as provided in the amended treaty.

(ii) *Companies :*

A company which is incorporated in the UAE and which is managed and controlled wholly in the UAE would be regarded as resident in the UAE.

The fallout of this amendment is that besides incorporation of a company in the UAE, the total control and management of the company should lie in the UAE, in order to qualify as resident of the UAE.

(iii) *Government entities :*

Amended Paragraph 2 provides that the Republic of India, its political subdivisions or local authority thereof including Government institutions of India would be regarded as residents of India. Similarly in case of the UAE, the Government and its political subdivisions or local Government including Government institutions of the UAE are deemed to be resident of the UAE. Abu Dhabi Investments Authority is specifically recognised as a resident of the UAE.

2.3 *Article 7 : Business profits :*

Paragraph 3 of Article 7 is amended to provide that in determining the profits of a PE, deduction of expenses including executive and general administrative expenses will be in accordance with the provisions of and subject to the limitations of the tax laws of the concerned State.

The implication of this amendment is that the deductibility of expenses of an Indian PE of a company resident in the UAE would be subject to provisions of the Income-tax Act, 1961. Therefore, head office expenses of such a PE would be restricted to an amount equal to five per cent of its adjusted total income.

6 [2003] 263 ITR 706.

7 Vide notification No. 282/2007, dated 28th November 2007 reported in 295 ITR (St.) 40 [2007].

8 Both Dr. Rajnikant Bhat and M.A. Rafiq were otherwise non-residents of India, taxed in India only in respect of Indian sourced income.

2.4 *Article 10 : Dividend :*

The rate of tax on dividends in the source country (*i.e.*, where the company paying the dividend is resident) is rationalised to 10% from the existing 5 and 15%.

This amendment has hardly any practical utility, as dividend income is exempt in the hands of the recipient in India where dividend distribution tax is paid, and there is no tax on receipt of dividend in the UAE.

2.5 *Article 13 : Capital Gains :*

Paragraph 3 of Article 13 has been replaced by three paragraphs. Hitherto, capital gains were taxed only in the country of which the alienator (transferor of the capital asset) was resident.

The amendment provides for source-based taxation, especially in respect of alienation of shares of a company. Accordingly, gains from the alienation of shares of a company, the property of which consists directly or principally of immovable property situated in a particular State is taxed in that State. Similarly, gains from the alienation of shares of companies other than mentioned above will be taxed in the State wherein the company whose shares are sold is resident.

The impact of this change is that short-term capital gains (whether STT paid or not) as well as the long-term capital gains (LTCG) on which Security Transaction Tax (STT) is not paid arising to a UAE resident will now be taxable in India. LTCG on sale of shares on which STT is paid are in any case exempt from tax in India.

2.6 *Article 24 : Income of Government and Institutions :*

Paragraph 1 of Article 24 is replaced to provide that income of the Government including capital gains tax is exempt in the source State. While the residents are taxed on capital gains in the source State, the Governments have ensured that their income continues to be exempt in the source State.

2.7 *Article 26 : Non discrimination :*

The amendment provides that difference in the rate of tax charged to a PE (of a non-resident company) in comparison to that of a domestic company would not amount to discrimination.

2.8 *Article 29 : Limitation of benefits :*

A new Article 29 has been added, which reads as under :

> "An entity which is a resident of a Contracting State shall not be entitled to the benefits of this Agreement if the main purpose or one of the main purposes of the creation of such entity was to obtain the benefits of this Agreement that would not be otherwise available. The cases of legal entities not having *bona fide* business activities shall be covered by this Article".

This Article is included to discourage Treaty shopping. The entity intending to avail Treaty benefits will have to comply with business purpose tests *i.e.*, the genuineness or commercial justification of the structure, rather than merely availing Treaty benefits. India's Treaties with USA and Singapore[9] contain similar anti-avoidance provisions.

3.0 **Conclusion :**

Amendments carried out to the India-UAE Tax Treaty would provide much warranted certainty to the tax implications on investments by residents of the UAE in India. Provisions of anti-avoidance measures in the UAE Tax Treaty like 'Limitation of Benefits', requirement of total control and management in the UAE/India to qualify for Treaty benefits reveal India's recent stand on tax treaties.

9 Refer the recent protocol signed by India on 29th June 2005, effective from 1st August 2005.

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ADVT.

This series of articles introducing securities laws for listed companies to the lay reader continues . . .

SECURITIES LAWS

Jayant Thakur
Chartered Accountant

Some Consent Orders

Consent Orders :

Members will recollect that the Guidelines for giving consent and compounding orders — plea bargaining — released earlier this year by SEBI were discussed in detail in this column. Several consent orders have been issued thereafter and it appears that the scheme has had a good start.

Members will also recollect that under these Guidelines, persons who have any proceedings against them pending before SEBI, SAT, etc., can approach the High Powered Advisory Committee ('HPAC') formed for this purpose to settle the matter. If the requirements of the Guidelines are complied with, the proceedings may be brought to an end in a mutually agreed manner. The objective appears to be to ensure justice, while at the same time, relieving SEBI and the parties concerned from the costs, delay and efforts of long drawn proceedings.

Consent orders passed recently are for proceedings pending before SEBI and the Securities Appellate Tribunal. It may be recollected that even if the matter is before SAT, the matter can still be referred for a Consent Order under the Guidelines and the mutually agreed consent terms can be affirmed by SAT.

Some illustrative orders are being briefly reviewed here to highlight the variety of circumstances under investigation and the manner in which they have been settled through these Guidelines.

Chugh Securities Private Limited :

Pursuant to the investigation conducted by SEBI in respect of the dealings in the scrip of Munjal Showa Limited during the year 2004, it was alleged that the stock-broker Chugh Securities Private Limited (hereinafter referred to as the 'noticee') executed structured trades in the scrip for some of its clients and thereby violated the relevant provisions of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices) Regulations, 2003 and of the Code of Conduct for Stock-brokers specified in Schedule II read with Regulation 7 of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992. Adjudication proceedings were initiated by issue of a 'show-cause' notice to the noticee to inquire into the alleged violations under the SEBI (Procedure for Holding Inquiry and imposing Penalties by Adjudicating Officer) Rules, 1995.

The broker offered to pay Rs. 1 lakh pursuant to proposed consent terms. These were accepted by the HPAC and accordingly the pending proceedings were disposed of.

Other examples are summarised here :

Name of party	Allegation	Offer accepted
M/s. First Custodian Fund (India) Ltd.	Irregularities in trading of the shares of Blue Information Technology Ltd. and consequent violations of relevant provisions of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995 and of the Code of Conduct for stock-brokers.	Rs. 5 lakhs
ADD Investments	Price manipulation in the shares of Granules India Ltd. and alleged violations of the relevant provisions of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995.	Rs. 3 lakhs
Jyotish Bhogilal Stock Brokers Pvt. Ltd.	Alleged irregularities in the scrip of Manna Glass Tech Limited and consequently enforcement proceedings have been initiated and alleged that the applicant has not exercised due care and diligence in terms of the Code of Conduct prescribed for stock-brokers.	Rs. 1 lakh
P. N. Vijay Financial Services Pvt. Ltd.	Violations of the relevant provisions of SEBI (Portfolio Manager) Rules, 1993 read with relevant provisions of the SEBI (Portfolio Managers) Regulations 1993, the Code of Conduct of Portfolio Managers and other provisions.	Rs. 5 lakhs

Name of party	Allegation	Offer accepted
Ratnakar Finstock Pvt. Ltd.	That the applicant was involved in structured deals in the form of cross-deals and self-trades and consequent violation of the relevant provisions of the Code of Conduct specified for stock-brokers.	Rs. 5 lakhs

There were other orders on similar lines too. Now let us consider orders for matters pending before the Securities Appellate Tribunal.

Settlement before SAT :

Name of party	Matter	Offer accepted
Ramanlal D. Shah	Appeal against order of SEBI suspending certificate of registration of broker for six months.	Rs. 5 lakhs
Reliance Share and Stock Brokers Private Limited	Appeal against order of SEBI suspending certificate of registration of broker for four months.	Rs. 50 lakhs

Conclusion :

It has been stated that numerous other applications are pending before the HPAC and some further orders have also been passed. Watch this column for further reports on interesting cases out of those reported.

Much of the present difficulty in industrial relations arises from the fact that too many employers as well as too many legislators take the Labour Leader more seriously than he deserves to be taken, while taking the ordinary, everyday, middle-of-the-road wage-earner less seriously than he deserves to be taken.

— Whiting Williams

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Part A
Exemption for services relating to exports

Puloma Dalal
Bakul B. Mody
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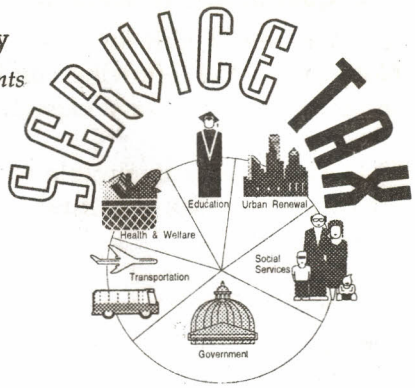

1. Introduction :

Continuing appreciation of the rupee against the US dollar compelled exporters of goods from India to either raise their prices of exports or suffer a dent on profit margins or lose export orders to other global competitors. The exporters therefore strongly pleaded for exemption from Service Tax liability on input services used by them in their exports. Much-awaited and delayed exemption was cautiously or half-heartedly declared by issuing Notification No. 40/2007-ST on 17-9-2007. Within a short-while, Notification No. 41/2007-ST was issued on 6-10-2007, superseding Notification No. 40/2007-ST. Apprehensions of possible misuse of the exemption has resulted in imposition of restrictions and conditions in the Notification and limited application. Expectation of exporting fraternity of zero tax rate still appears a distant reality. Further, under the guise of exemption, what is notified is a remission mechanism for filing a refund claim in respect of a few specified services. A further addition to this list was made vide Notification No. 42/2007-ST, dated 29-11-2007. Manufacturer-exporters manufacturing dutiable goods can avail the benefit of refund provisions under Rule 5 of the CENVAT Credit Rules, 2004. However, Manufacturer-exporters of exempted goods and merchant-exporters can avail benefit to the extent available under the Notification. The scope, procedure and limiting features of this Notification are discussed below.

2. Scope and coverage :

Notification Nos. 41/2007 and 42/2007-ST have been issued under Ss.(1) of S. 93 of the Finance Act, 1994 — (The Act) which grants exemption to certain specified taxable services used by an exporter for goods exported. Service Tax paid on the following specified services is eligible for refund.

Sr. No.	Taxable service	Date of eligibility from	Classification under sub-clause of S. 65(105) of the Act
(a)	Services provided by ports or persons authorised by ports for export of goods.	17-9-2007	(zn)
(b)	Services provided by other ports or persons authorised by other ports for export of goods.	17-9-2007	(zzl)
(c)	Services provided by goods transport agency for transport of goods from Inland Container Depot — (ICD) to port/dock by road.	17-9-2007	(zzp)
(d)	Services provided for transport of goods by rail from Inland Container Depot — (ICD) to port/dock by rail.	17-9-1007	(zzzp)
(e)	Services of insurance including reinsurance for export of goods.	6-10-2007	(d)
(f)	Services provided by a technical inspection and certification agency for export of goods.	6-10-2007	(zzi)
(g)	Services provided by technical testing and analysis agency for export of goods.	6-10-2007	(zzh)
*(h)	Specialised cleaning services, namely, disinfecting, exterminating, sterilising or fumigating of containers used for export of goods.	29-11-2007	(zzzd)
*(i)	Services of storage and warehousing for export goods.	29-11-2007	(zza)

*(The two services were added by making amendment in Notification No. 41/2007-ST, vide Notification No. 42/2007-ST))

3. **Conditions for claiming refund :**

In order to be eligible for claiming refund under this Notification, the following conditions are required to be fulfilled by every exporter.

3.1 An exporter is eligible to claim refund only when Service Tax is actually paid on specified services.

3.2 Service Tax paid on :

- Technical inspection and certification service, or
- Technical testing and analysis service, or
- Specified specialised cleaning service

is eligible for refund claim when exporter furnishes a copy of the written agreement between exporter and buyer of goods, wherein requirement of undertaking such certification, testing or specialised cleaning service is mentioned.

3.3 In case of specified specialised cleaning service and storage warehousing service, the service provider should be accredited/approved by the competent statutory authority to provide such services.

3.4 The storage place or warehouse should be exclusively used for storing of export goods.

3.5 No CENVAT Credit of Service Tax paid on the services should be availed, for which refund is claimed.

3.6 Export should be made without availing drawback of Service Tax paid on the above specified services under Customs, Central Excise Duties and Service Tax Drawback Rules, 1995.

3.7 Refund of Service Tax paid on the above specified services should not be made in any manner otherwise than under this Notification.

4. **Exemption to exporter when he is also a person liable for payment of Service Tax under reverse-charge mechanism :**

When an exporter is liable to pay Service Tax being an availer/user of any of the above specified services, he is exempt from payment of Service Tax on such services. For instance, if an exporter has used goods transport agency's service for movement of goods from ICD to port, and thereby he is liable to pay Service Tax under the reverse-charge mechanism, he is eligible to claim exemption from Service Tax under this Notification, as he is otherwise also eligible for the refund of the Service Tax paid on such services used for the exported goods.

5. **Procedure for claiming refund :**

5.1 Where to submit the application of refund ?

- A manufacturer-exporter is required to submit the application with the Assistant/Deputy Commissioner of Central Excise having jurisdiction over the factory where the goods are manufactured.
- A merchant-exporter is required to submit the application with the Assistant Deputy Commissioner who has jurisdiction over the registered office of the merchant-exporter.

5.2 What procedure is prescribed to be followed when an exporter is not registered ?

- The exporter, whether a merchant or a manufacturer who is not registered under Central Excise or Service Tax Authority is required to file a declaration in the prescribed form (provided in the Notification) with the respective jurisdictional Assistant/Deputy Commissioner prior to filing a claim for refund of Service Tax under this Notification and obtain a Service Tax Code (STC) number which would be granted within seven days from the date of submission of the said Declaration Form.

5.3 When does an exporter file a claim of refund ?

- The refund claim is required to be filed on quarterly basis within 60 days from the end of the relevant calendar quarter, during which the goods are exported.

  (*Note* : Although the Notification does not clarify or provide definition of 'quarter', the Service Tax Rules,1994 provide for quarter as a calendar quarter like January to March, July to September, etc.)

- The export will be regarded to have been made on the date on which the Customs Appraising Officer has permitted clearance and loading of the goods in accordance with S. 51 of the Customs Act,1962. The Officer issues an order known as 'let export order'.

  (*Note* : One should not consider the actual date of export or the date of sailing of vessel as the 'date of export'. The date of 'let export order' is the date of export. Therefore, while claiming refund, the relevant quarter may be decided considering the date of the 'let export order'.)

6. Which documents are required to be enclosed with the claim of refund ?

6.1 Documents substantiating export of goods and other relevant details :

- Documents such as ARE-1 duly endorsed by the customs authorities, copy of shipping bill, non-negotiable copy of bill of lading along with the copy of the export invoice, invoice of the provider of service, etc. should be submitted.
- In case of technical testing and technical inspection and certification services, the invoice of the service providers should be issued in the name of the exporter and should only relate to exported goods, thereby establishing direct nexus between service received and goods exported. It is recommended therefore to have shipping bill number written on the invoices of these service providers for cross-reference.

6.2 Documents evidencing payment of Service Tax to input service providers.

- Invoice copies of service providers of specified services, along with proof of payment of the amount mentioned in invoices, such as copies of bank statements or copy of challan in GAR-7 and/or receipt of the service provider, etc. should be enclosed with the claim of the refund.
- In practice, it is observed that exports are effected through availing the services of custom house agents or freight forwarders — intermediaries. Therefore, the specified service providers are paid by these agents or intermediaries. CHAs/intermediaries should be instructed to provide certificate of payment to specified service providers. Further, it should be ensured to follow the practice of providing reference of shipping bill number on the invoice issued by service providers. In case of port services & transportation services of rail and road, the Notification does not provide the requirement of bills to be in the name of exporters. However, the proof of specified service used for export goods would have to be provided. Therefore, photocopies of invoices of specified service providers bearing shipping bill reference should be obtained to the extent possible in order to avoid rejection of the claim for want of proof.

6.3 Copy of agreement entered into by the exporter with the buyer wherever applicable *i.e.*, in cases where refund is conditional upon mention of requirement of the specified service in the written agreement.

6.4 Since refund is eligible only in case of specified services, exporter may ensure to obtain invoice with category of service written on it or obtain proof of payment like copy of GAR-7 challan or copy of registration certificate of the provider of service.

6.5 In case of insurance service, copy of the policy and premium receipt in the name of exporter, and the policy should relate specifically to exported goods only.

6.6 In case of specialised cleaning services and storage/warehousing services, accreditation/approval of the agency or warehouse, respectively being a precondition, the proof of such accreditation or approval *viz.* either copy of such certificate or mention of accreditation number or the fact of approval on their invoice can fulfil the said condition. Further, in case of warehousing service, unless a certificate to the effect that the warehouse is used exclusively for storing export goods is obtained, the condition of the Notification will not be satisfied.

7. Recoverability of refund :

If the exporter has not been able to realise sales proceeds for exported goods within stipulated period under FEMA 1999 including any extention of the period, Service Tax refunded shall be recoverable, treating the recovery as Service Tax erroneously refunded. Under FEMA (Export of Goods and Services) Regulations 2000, export sales proceeds have to be realised within six months from the date of exports. However, in case of certified status holder exporters, 100% EOUs, and units under STPs BTP schemes, etc., realisation and repatriation is permissible up to twelve months. Under certain circumstances, this limit is further extended by RBI. Therefore, if proceeds are not realised within this time limit, then only recovery provisions would be invoked.

8. Limitations and difficulties in the mechanism :

- The exemption or remission is available only in case of Service Tax paid on a few specified

services. The services such as those of custom house agents, business auxiliary service covering commission paid to agents abroad and services of other intermediaries used for exports, courier services, transportation from factory or registered place of the merchant-exporter to port/dock (in cases when goods are not exported through ICD), banking and financial services, in addition to general services like telephone, Internet, etc. are not covered by the Notification.

- A number of services like port services, goods transporters' services, transport by rail, etc. are usually obtained by custom house agents or freight forwarders for the exporters. Payment towards these services is often made by shipping companies, steamer agents or freight forwarders and thereafter the same is recovered from the exporters under the popular nomenclature of 'Terminal Handling Charge' (THC). Service Tax on the said THC is paid by steamer agents/shipping companies/freight forwarders, as the case may be, under the head 'business support services'. Claiming refund on such service, tax payment appears difficult under the prescribed mechanism, as providing evidence of invoices/copies of the invoices of specified service providers is found difficult in actual practice.
- In view of the stringent documentation requirement, the benefit would be available to a few exporters. In many cases, invoices issued may not contain necessary details to prove that the service was utilised for the goods exported only. Thus benefit may accrue to only a small number of exporters who can undergo the rigours of lengthy and cumbersome paper work.
- No specific format is prescribed in the Notification for making claim of refund on the lines of Form R and Form A, respectively, which are prescribed in the case of refund u/s.11-B of the Central Excise Act, 1994 or refund under Rule 5 of the CENVAT Credit Rules, 2004. Form A under the CENVAT Credit Rules being more relevant here, it appears that submission of details in the same format may suffice for the purpose of this Notification No. 41/2007-ST also.

Part B
Some Recent Judgments

1. **Banking and other financial services :**

- Equipment leasing and hire-purchase. Appellant manufactured industrial boilers and in some cases, supplied the goods on lease basis on account of financial constraints of such customers — Appellant only collected interest on unpaid amount of credit, and charged no amount on account of lease management fee, processing fee or documentation charges — Activity confined to own products, and appellant not professional in leasing business for any other product — 'Interest on loan' not to form part of value of taxable service in view of Explanation 1 to S. 67 of Finance Act, 1994 (Act) inserted w.e.f. 10-9-2004 and Circular No. 80/10/2004-ST, dated 17-9-2004 — Demand not sustainable.
- Sale and service — Equipment leasing. Appellants paid Sales Tax on goods supplied to various customers on lease basis, as the same involved transfer of right to use goods — Service Tax not leviable when Sales Tax paid — S. 65(12), S. 66 and S. 73 of the Act [BSNL 2 STR 161 (SC) and BPL Mobile 7 STR 440 (Tri) relied.]
- Interest — Provisions of Explanation 1 to S. 67 of the Act added w.e.f. 10-9-2004, providing 'interest of loan' not to form part of value of taxable service, to be treated clarificatory in nature *i.e.*, effective from 16-8-2002.

[*Thermax Limited v. CCE*, (2007) 8 STR 487 (Tri — Mumbai)]

2. **Business Auxiliary Service :**

(a) Sale of lottery tickets — Lottery tickets whether goods — Petitioner engaged in purchase of lottery tickets from State Government and subsequent sale — Lottery tickets held to be actionable claims by Supreme Court and not goods as per Sale of Goods Act, 1930 — Petitioner not rendering service in relation to promotion of client's goods — Service Tax liability does not arise — Notice demanding Service Tax quashed — Article 226 of the Constitution of India — S. 65(19) and S. 73 of the Act — [Sunrise Associates (2006) 5 SCC 603 relied.]

[*Martin Lottery Agencies Ltd. v. UOI*, (2007) 8 STR 561 (Sikkim)]

(b) Sourcing customers — Loans given by financial institutions. Appellant was engaged in sourcing customers for loans — Promotion of services rendered by clients — Impugned activity covered under Business Auxiliary Services — S. 65(19) of the Act.

[*Bridgestone Financial Services v. CST*, (2007) 8 STR 505 (Tri — Bang.)]

3. **Commercial concern :**

➠ Assessee engaged in activity of conducting examinations for recruitment of clerks, officers and specialist officers in banks, financial institutions and other organisations — Object of appellant-institute is to plan, promote and provide for competent, well-qualified and efficient cadres of personnel at various levels to banks and financial institutions in the country — Mere charging of fees will not alter the position that the appellant-institute is not a commercial concern — Appellants are not a commercial concern, hence not liable to Service Tax under manpower recruitment agency services.

➠ Charitable organisation — An organisation that does not declare dividend or distribute surplus/profits to its shareholders, trustees and/or members, but ploughs back the surplus for the purpose of an object of the organisation would be a charitable organisation, if the object thereof is of charitable nature. [*Addl. CIT v. Surat Art Silk Cloth Manufacturers' Association*, 121 ITR 1 (SC), *Trustees of Tribune Trust*, (1939) 7 ITR 415 (PC) and *BCCI v. CST*, 7 STR 384 (Tri) relied.]

[*Institute of Banking Personnel Selection v. CST*, (2007) 8 STR 579 (Tri — Mumbai)]

4. **Commercial Coaching and Training :**

Exemption as Vocational Training Institute under Notification No. 9/2003-ST, denied on the ground that registration with AICTE absent — Coverage of appellant under impugned category not in dispute — Held : Notification does not envisage registration of institute with AICTE — Benefit denied by reading things not present in Notification. Trainees of appellant receive skills to enable them to seek employment or undertake self-employment. Hence Exemption admissible — Impugned order set aside — S. 65(26), S. 65(27) and S. 93 of the Act.

[*Wigan & Leigh College (India) Ltd. v. JCST*, (2007) 8 STR 475 (Tri — Bang.)

5. **CENVAT credit :**

(a) Validity of Duty-paying documents — Credits in respect of Service Tax paid on goods transport agency services availed on the basis of TR-6 challan — Objection that TR-6 challan is not a valid duty-paying document does not stand as Revenue failed to mention as to what was specified document for availing credit during relevant time — When it is not the case of Revenue that Service Tax not paid by respondents, or not otherwise entitled to credit of same, TR-6 challan has to be considered a proper document reflecting payment of tax — Credit admissible — Rule 9 of Cenvat Credit Rules, 2004 (CCR).

[*CCE v. Essel Pro-Pack Ltd.*, (2007) 8 STR 609 (Tri — Mumbai)]

(b) Credit of Service Tax paid on erection, commissioning and installation of windmills for generation of electricity away from factory premises — Electricity is not excisable — Electricity generated surrendered to the grid and equivalent quantum is withdrawn in the factory from the grid — Services used at site of windmills cannot be held as input services by the unit located far away — As electricity is not excisable, Cenvat credit not available even at premises of windmills — Cenvat credit of Service Tax held as not admissible — Penalty not imposable as issue involving interpretation — Rules 2(1) and 3 of CCR.

[*Rajhans Metals (P) Ltd. v. CCE*, (2007) 8 STR 498 (Tri — Ahmd.)]

(c) Commission agent services were availed for promoting sale of goods manufactured by appellant — Commission agents *prima facie* promote sale and once definition of input service includes services used for advertisement or sales promotion or market research, the same is an input service, more so when it forms part of assessable value for which no deduction is permissible — Balance amount relates to advertisement services for which no evidence cited to show that advertisement was done both for manufactured goods as well as traded goods — *Prima facie* case in favour of applicant — Predeposit already made sufficient — Pre-deposit of balance Service Tax, penalty and interest waived — S. 35F of Central Excise Act, 1944 (CEA) Rule 2(1) of CCR.

[*Metro Shoes Pvt. Ltd. v. CCE*, (2007) 8 STR 502 (Tri — Mumbai)]

6. **Cargo handling service :**

➠ Cargo handling service covers packing of cargo for all modes of transport — Packing undertaken to facilitate subsequent transport of cargo — Activity completed by appellant and nothing more requires to be done before transportation — Expression 'packing of cargo' wide enough to cover activities undertaken, such as unitising, strapping, packeting or packing of goods into cargo for subsequent movement by trucks and/or rail — Impugned activities undertaken amounted to Cargo Handling Service during material period — Matter remanded to original authority for excluding services provided to export cargo and re-determination of liability — Levy being new, penalty set aside — S. 65(23), S. 73 and S. 76 of the Act.

➠ Classification of Services — Unitisation, strapping and packing of goods. Appellant contended coverage under 'Packaging Service' — Revenue argued classification under Cargo Handling Service — Expression 'packing of cargo' appearing in definition of 'Cargo Handling Service' covers unitising, strapping, packeting or packing of goods for subsequent transportation — Impugned activities held as covered under Cargo Handling Service during material period — S. 65(23), 65(76b) and 65A of the Act.

[*ITW India Ltd. v. CCE*, (2007) 8 STR 490 (Tri — Kolkata)]

7. **Export exemption :**

(a) Repatriation of Receipt in foreign exchange – Exemption from Service Tax under Notification Nos. 6/99-ST and 21/2003-ST, denied holding payment received in convertible foreign exchange repatriated — Dividend in foreign exchange paid to shareholders outside India from income — Proviso to Exemption Notification indicating inadmissibility of exemption if entire payment for taxable services repatriated — Appellant not hit by proviso and having strong *prima facie* case — Pre-deposit of Service Tax, interest and penalties waived and recovery thereof stayed — S. 35F of CEA.

[*Maersk India Pvt. Ltd. v. CST*, (2007) 8 STR 627 (Tri — Mumbai)]

(b) In this case Service Tax was paid on cargo handling services provided for export cargo. Since export cargo is excluded from Service Tax and refund sought — Refund was denied in first adjudication order, holding that services rendered fall under Port Services. Refund was sanctioned in *de novo* adjudication order, but the same denied by Commissioner through revision order — Appellant holding stevedoring licence from Port Trust — Document from Port Trust indicating rendering of services directly and not on behalf of port. Held : Services rendered covered under Cargo Handling Services and not under Port Services. Export cargo handled and liability to Service tax does not arise — Impugned order set aside — S. 65(23) and S. 65(82) of the Act, — S. 11B of CEA.

Classification of services — Export cargo handling. Stevedoring licence-holder providing services in relation to export cargo in port area — S. 42 of Major Port Trust Act, 1963 providing that major port to carry out number of activities and port empowered to authorise any other person to render such services on approval from Government — Impugned licence is only a permission to provide services within port premises — Services not provided on behalf of port, but directly to clients, in relation to export cargo covered under 'Cargo handling services' and not under 'Port services' — S. 65(23), and S. 65A of the Act,.

[*Konkan Marine Agencies v. CCE*, (2007) 8 STR 472 (Tri — Bang.)]

(c) Insurance Auxiliary Service — Reinsurance brokerage received from overseas companies — C.B.E.C. Circular in the light of relevant Export of Services Rules, 2005 and Notification Nos. 6/99-ST, 2/03-ST and 21/03-ST provide that there shall be no Service Tax on export of services, irrespective of fact that consideration received in Indian currency. Since recipients of service reside abroad and have no office in India, the said service comes under export of service and non-taxable — *Prima facie* case made out to waive pre-deposit and recovery thereof stayed — S. 65(55) of the Act — S. 35F of CEA.

[*Suprasesh General Insur. Serv. & Brokers Pvt. Ltd.*, (2007) 8 STR 513 (Tri — Chennai)]

8. **Import of services :**

(a) Service provided by overseas agent outside India before introduction of S. 66A to the Act. In view of Tribunal's decision in Dimensional Stone's case, and on fact that liability in respect of service in dispute is created by introduction

of S. 66A *ibid* with effect from 18-4-2006, pre-deposit waived and recovery thereof stayed — S. 35F of CEA S. 66A of the Act [*Dimensional Stones v. Commissioner* — Stay Order dated 26-7-2007 relied.]

[*Active International v. CCE*, (2007) 8 STR (Tri — Del.)]

(b) Liability of service recipient — Date of effect — Appellant contended that taxable services received from foreign services provider became taxable by Notification No. 36/2004-ST with effect from 1-1-2005 and Service Tax not leviable on receiver prior to 1-1-2005 — Impugned services liable to Service Tax by virtue of Rule 2(1)(d)(iv) of Service Tax Rules, 1994 inserted by Notification No. 12/2002-ST — Notification No. 36/2004-ST only repetition of said Rule 2(1)(d)(iv) *ibid* — Pre-deposit of Rs.25,000 ordered and balance waived — S. 66 and S. 68 of the Act S. 35F of CEA. [Aditya Cement, 7 STR 153 (Tri) & Ispat Industries Ltd., 8 STR 282 (T) relied.]

[*Samcor Glass Ltd. v. CCE*, (2007) 8 STR 633 (Tri. Del.)]

9. **Management, maintenance or repair :**

Maintenance and repairs of share areas and common facilities in the building complex for which assessee receiving charges separately from their tenants — Lessee is bound to pay lease rent at a specified rate per sq. ft. per month and a separate fee called 'operator and maintenance fee' at a specified rate per sq ft. per month to 'lessor' — Thus 'operation and maintenance' also pertains to immovable property — Tax payable on such fee collected by assessee during period in dispute — No plea of financial hardship — In a lenient approach, assessee directed to deposit only 50% of Service Tax amount — S. 65(64) of the Act — S. 35F of CEA.

[*Tidel Park Ltd. v. CST*, (2007) 8 STR 543 (Tri — Chennai)]

10. **Penalty :**

(a) Non-payment of tax — Security agency service. Appellants canvassing that they were not guided properly by the consultant and they were under impression that Service Tax liability for earlier period has to be paid as and when payment for services rendered is received — Appellants did not approach the Revenue for any clarification — *Misguidance by consultant on provisions of law, may be the cause of non-payment of tax liability, which can be condoned* — Penalty imposed on appellants u/s.78 of the Act set aside by invoking S. 80 of the Act.

[*Rakesh Enterprises Services v. CCE*, (2007) 8 STR 577 (Tri — Mumbai)]

(b) Quantum — Real Estate Agent Service — Non-payment of Service Tax and failure to file ST-3 returns on due date — S. 76 of the Act provides for penalty of Rs.100 per day in case failure to pay tax for every day after the due date — Delay in payment of Service Tax in appellant's case ranges from 3 months to 58 months, hence enhanced penalty not exceeding Rs.100 for every day after due date — Penalty not in excess of statutory limit — Impugned revision order enhancing penalty upheld — S. 76 *ibid.* [174 ELT 19 (Tri — L.B.) relied on.]

[*Khan Estate Agency v. CCE*, (2007) 8 STR 596 (Tri — Mumbai)]

11. **Storage and warehousing :**

Appellant Corporation has been established for distribution of liquor, purchased liquor from manufacturers, stored in hired storage bases/godowns, and thereafter sold the same to various wholesalers holding appropriate licences — Demurrage fee @ Rs.2 per day charged by appellant from manufacturers in case stock of liquor not lifted within 90 days not a charge for storage of goods as ownership of goods vested in appellants themselves — Appellants not providing storage and warehousing service, hence, not liable for Service Tax — Imposition of exorbitant penalty on State Government Corporation not justified – Impugned order set aside — S. 65(102), S. 73 and S. 76 of the Act.

[*Karnataka State Beverages Corpn. Ltd. v. CST*, (2007) 8 STR 481 (Tri — Bang.)]

12. **Turnkey contract :**

Setting up of sinter plant on turnkey basis — Foreign principal contractor having Indian partner as sub-contractor for execution of part of a composite contract — Performance guarantee given by the foreign contractor. Held : Rendering of service of engineering consultancy was secondary to principal object of setting up of the plant — Department view that Indian contractor executed independent contract which was not on turnkey

basis, and was liable to tax as engineering consultants, rejected — S. 65(31) of the Act [Daelim Case relied — 3 STR 124 (Tri)].

[*Orissa Sponge Iron Ltd. v. CCE*, (2007) 8 STR 553 (Tri — Kolkata)]

13. **Valuation :**

(a) Management, maintenance or repair services — Abatement of cost of certain components/parts of elevators from gross amount received from customers under Annual Maintenance Contract (AMC) — Notification No. 12/2003-ST — Replacement of unspecified components/parts of elevators under AMC are free of charge — Components/parts supplied by assessee under AMC were Sales Tax paid — Service Tax not leviable on goods on which Sales Tax was paid, two taxes being mutually exclusive — Arguable issue — Waiver of pre-deposit and stay of recovery granted — S. 35F of CEA and S. 65(64) and S. 67 of the Act.

[*Kone Elevators India Pvt. Ltd. v. CST*, (2007) 8 STR 525 (Tri — Chennai)]

(b) Telephone service – Sale of prepaid SIM cards to dealers/distributors against payment of price below MRP, which in turn sold by latter to subscribers at MRP — Amount charged by assessee (service-provider) is amount received by them from dealers/distributors and nothing extra was charged by them — Where law prescribes value of taxable service to be the gross amount charged by service provider, Service Tax can be levied on that amount only — S. 65(109a) and S. 67 of the Act.

[*BPL Mobile Cellular Ltd. v. CCE*, (2007) 8 STR 546 (Tri — Chennai)]

Seven national crimes :

1. I don't think.
2. I don't know.
3. I don't care.
4. I am too busy.
5. I live well enough alone.
6. I have no time to read and find out.
7. I am not interested.

— William J. H. Boetcker

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Important Amendments

G. G. Goyal
Chartered Accountant
C. B. Thakar
Advocate

A note on Input Tax Credit (set-off) as on 1-11-2007 under Maharashtra VAT

S. 48 of the MVAT Act, 2002 provides for grant of input tax credit to any registered dealer in respect of tax paid on his purchases, subject to certain conditions provided in the Rules made in this behalf by the State Government. The provisions for grant of set-off are contained in Rules 52 to 55 of the MVAT Rules, 2005. There have been certain changes in the Rules from time to time. The updated position of the set-off Rules as on 1-11-2007 can be summarised as under.

Rule 52 provides for set-off on purchases affected on or after 1-4-2005.

Important conditions :

(i) To be eligible for set-off, a dealer must be registered under the MVAT Act at the time of purchase of goods, except as provided in Rule 55(1).

(ii) As per Rule 52 set off is available on purchases, from registered dealers only, of goods being capital assets and goods the purchases of which are debited to profit and loss account or trading account.

(iii) Following sums are eligible for set off :

Tax paid separately on purchases effected within the State and supported by 'Tax Invoice'. Entry tax paid under Maharashtra Entry Tax on Goods Act as well as Maharashtra Entry Tax on Motor Vehicles Act.

CST paid on interstate purchase is not eligible for set off.

(iv) Set off is allowable as and when purchase is made, irrespective of its disposal. However, it is subject to the restrictions specified in Rule 53 and negative list contained in Rule 54.

Retention in set-off

Rule 53 provides for certain circumstances in which the amount of set-off is restricted :

Circumstance	Reduction from set-off amount
(1) Purchase of fuel	@ 3% of purchase price (PP) of taxable goods used as fuel (prior to 1-4-2007, the reduction rate was 4%).
(2)(a) Manufacture of tax-free goods (other than fabrics and sugar exported as per S. 5 of CST Act, 1956)	@ 3% of PP of taxable goods (other than capital assets and fuel) (prior to 1-4-2007, the reduction rate was 4%).
(b) Resale of tax-free goods	@ 3% of PP of corresponding packing material used in packing of tax-free goods. (prior to 1-4-2007, the reduction rate was 4%).
(3) Transfer of taxable goods to branch in other State or to agent in other State	@ 3% of corresponding PP (other than capital assets and fuel) (Deduction not to apply if goods are brought back in the State within six months. In case, purchases eligible to set-off are covered by Schedule B, the reduction shall be 1%, instead of 3%). (The above reduction rate was 4% prior to 1-4-2007).
(4) If opted for Composition Scheme for Works Contract.	(a) In case of notified construction contracts : 4% of PP. (b) Other contracts : 9/25 of tax amount (thus only 16/25 or to say 64% of tax is eligible as set-off.
(5) Business discontinued or not continued by successor	No set-off on closing stock (other than capital assets) on the date of such event.

Circumstance	Reduction from set off amount
(6) If the receipts from sale of goods are less than 50% of the gross receipts of the business	Set-off is available only on plant and machinery and those goods which are sold or consigned or used in packing of the goods sold or consigned, within six months of date of purchase. This position applies from 8-9-2006.
(7) If retailer of liquor holding specific liquor licence effects sale of liquor at a price lower than MRP	Set-off available = set-off allowable on purchase x selling price ÷ MRP value of the liquor sold.
(7) (a) Office equipments and furniture and fixtures treated as capital assets	(a) From 1-4-2007 onwards : 3% of corresponding PP (Not to apply in case of leasing business). (b) From 8-9-2006 to 31-3-2007, the rate of reduction was 4%. (c) From 1-4-2005 till 7-9-2006 : No set-off
(7) (b) Electricity transmission or distribution companies	4% of purchases till 31-3-2007 and 3% from 1-4-2007.

Non admissibility of set-off — Negative List (Rule 54) :

The following purchases of goods are not eligible for set-off :

(a) Passenger vehicles, if treated as capital assets and their parts, components and accessories. However, a dealer dealing in sale of motor vehicles or leasing of motor vehicles is entitled to set-off.

(b) Motor spirits, as notified u/s.41(4) unless they are resold or transferred to branch or agent outside the State.

(c) Crude oil described in S. 14 of the C.S.T Act, if it is used by refinery for refining.

(d) If a dealer is engaged in pure job work or labour work and where only waste/scrap is sold, then no set-off will be granted on consumables and capital assets.

(e) Unit covered by the Package Scheme of Incentive under the Exemption Scheme or Deferment Scheme is not entitled for set-off of tax paid on 'raw materials' as defined in Rule 80. However, it can claim refund of tax paid on such purchases, which will be equal to set-off.

(f) Incorporeal or intangible goods, other than import licences, export permits licence/quota, DEPB, SIM cards and DFRC, are not eligible for set-off. However, software packages are eligible for set-off in the hands of software trader. Also copyrights are eligible to set-off if sold within 12 months of date of purchase. Other incorporeal and intangible goods, like trade marks : not eligible to set-off.

(g) Purchases effected by way of works contract where the contract results in immovable property other than plant and machinery.

(h) Purchases used in erection of immovable property other than plant and machinery.

(i) Purchases of IMFL in the hands of dealer opting for the Composition Scheme u/s.42(2).

(j) Purchase of various items of mandap decoration/tarpaulin, etc., after 20th June, 2006, in the hands of dealer who has opted for the Composition Scheme u/s.42(4).

(k) Purchases, in the hands of hotelier, which are treated as capital assets and which do not pertain to supply and sale of food/drinks.

(l) Purchase of office equipments, furniture, fixtures and electricity installations till 7-9-2006 (not applicable if dealer is engaged in the business of leasing).

When the king retires at night his crown rests on a nail fastened to the wall. Why, on a nail, which is nothing but a common object ? Why not on a minister's head ? Because the minister might take himself seriously and believe he is the king. No such danger with a nail.

— Elie Wiesel

Accounting Standards

Dolphy D'Souza
Chartered Accountant

Gaps in GAAP — Accounting of BOT Contracts

Governments the world over have introduced contractual service arrangements to attract private-sector participation in the development, financing, operation and maintenance of public infrastructure. In India too, these arrangements are frequently used in roads and bridge infrastructure. The arrangement typically involves a private-sector entity (an operator) constructing the infrastructure used to provide public service or upgrading it (for example, by increasing its capacity) and operating and maintaining that infrastructure for a specified period of time. The arrangement is executed with the Government, corporation or a public-sector company, often referred to as grantor.

Accounting for such arrangements under IFRS is done in accordance with IFRIC Interpretation 12, Service Concession Arrangements. Infrastructure within the scope of this Interpretation is not recognised as property, plant and equipment of the operator, because the contractual service arrangement does not convey the right to control the use of the public-service infrastructure to the operator. The operator has access to operate the infrastructure to provide public service on behalf of the grantor, in accordance with the terms specified in the contract.

The question is that the operator has constructed the asset, so if it does not recognise the construction as fixed asset, then how is the amount spent on the construction recognised ? Under IFRIC 12, if the operator provides construction or upgrade services, the consideration received or receivable by the operator shall be recognised at its fair value. The consideration may be rights to : (a) a financial asset, or (b) an intangible asset.

The operator shall recognise a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services; the grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law. The operator has an unconditional right to receive cash if the grantor contractually guarantees to pay the operator (a) specified or determinable amounts or (b) the shortfall, if any, between amounts received from users of the public service and specified or determinable amounts, even if payment is contingent on the operator ensuring that the infrastructure meets specified quality or efficiency requirements.

The operator shall recognise an intangible asset to the extent that it receives a right (a licence) to charge users of the public service. A right to charge users of the public service is not an unconditional right to receive cash, because the amounts are contingent on the extent that the public uses the service.

Under Indian GAAP, it is possible to arrive at the conclusion contained in IFRIC 12 that the operator should not recognise the construction as fixed assets. This is because of the following provision contained in Indian GAAP :

Para 34 of AS-26 :

An intangible asset may be acquired in exchange or part exchange for another asset. In such a case, the cost of the asset acquired is determined in accordance with the principles laid down in this regard in AS-10, Accounting for Fixed Assets.

Para 22 of AS-10 :

When a fixed asset is acquired in exchange or in part exchange for another asset, the cost of the asset acquired should be recorded either at fair market value or at the net book value of the asset given up, adjusted for any balancing payment or receipt of cash or other consideration. For these purposes, fair market value may be determined by reference either to the asset given up or to the asset acquired, whichever is more clearly evident. Fixed asset acquired in exchange for shares or other securities in the enterprise should be recorded at its fair market value, or the fair market value of the securities issued, whichever is more clearly evident.

However, many companies executing BOT type contracts have treated the infrastructure as fixed

(Continued on page 448)

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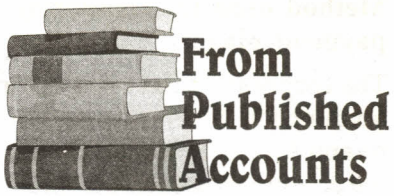
Section A : Disclosures regarding ESOPs



Himanshu V. Kishnadwala
Abhay R. Mehta
Ravikant Kamath
Chartered Accountants

Compilers' Note :

Accounting treatment and disclosures for ESOPs in financial statements in India is mandated by Guidance Note on Accounting for Employee Share-based Payments, issued by ICAI and the Employee Stock Option Scheme and Employee Stock Purchase Scheme Guidelines, issued by SEBI (for listed companies). As per the SEBI guidelines, some disclosures are also required in the Directors' Report.

🕮 Reliance Industries Ltd. — (31-3-2007)

From Directors' Report :

Grant of Stock Options to employees is a time-tested and well-established mechanism to align the interests of employees with those of the company, to provide them with an opportunity to share the growth of the company as also to foster long-term commitment. Towards achieving this goal, approval of the members of the company was obtained at the Annual General Meeting held on June 27, 2006 for introduction of Employee Stock Option Scheme.

The Employee Stock Compensation Committee, constituted in accordance with the Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999 administers and monitors the scheme.

The applicable disclosures under the Guidelines are as under :

Total options granted	2,87,28,000
Pricing formula	Rs.1,284 being the closing market price on NSE on 15-3-2007, as rounded off to Rs.1,284 plus taxes as may be levied on the company in this regard.
Options vested	Nil
Number of options granted to senior Managerial personnel	Nikhil R. Meswani — 7,00,000 Hital R. Meswani — 7,00,000 Hardev Singh Kohli — 50,000

Neither any employee has been granted options equal to or exceeding 1% of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant, nor has any employee been granted options amounting to 5% or more of the total options granted during the year.

The company has received a certificate from the auditors of the company that the scheme has been implemented in accordance with the guidelines and the resolution of the company passed at the last Annual General Meeting.

From Notes to Accounts :

Employee benefits :

(i) ...

(ii) ...

(iii) In respect of employee stock options, the excess of fair price on the date of grant over the exercise price is recognised as deferred compensation cost amortised over the vesting period.

🕮 HDFC Ltd. — (31-3-2007)

From Notes to Accounts :

Under the Employee Stock Option Scheme – 2005 (ESOS – 05), the corporation had on 25-10-2005, granted 74,73,621 stock options at an exercise price of Rs.912.90 per option, representing 74,73,621 equity shares of Rs.10 each to the employees and directors of the corporation. The said price was determined in accordance with the pricing formula approved by the shareholders *i.e.*, at the latest available closing price on the stock exchange having higher trading volume.

In terms of the scheme, the options would vest over a period of 2-3 years from the date of grant, but not later than 24-10-2008, depending upon the option grantee completing continuous service of three years with the corporation. Accordingly, during the year 35,35,432, options (previous year Nil) were vested [including 970 options (previous year Nil) vested and lapsed]. The options can be over a period of 5 years from the date of respective vesting.

Method used for accounting for share-based payment plan :

The corporation has used intrinsic value method to account for the compensation cost of stock option to employees of the corporation. Intrinsic value is the amount by which the quoted market price of the underlying share exceeds the exercise price of the option. Since options under ESOS – 05 were granted at the market price, the intrinsic value of the option is Rs. Nil. Consequently, the accounting value of the option (compensation cost) is also nil.

Movement in the options under ESOS – 05 :

	Options current year	Options previous year
Options outstanding at the beginning of the year	74,34,326	Nil
Granted during the year	Nil	74,73,621
Exercised during the year	30,83,344	Nil
Lapsed during the year	1,10,608	39,395
Options outstanding at the end of the year	42,40,374	74,34,326
Options unvested at the end of the year	37,89,256	74,34,326
Options exercisable at the end of the year	4,51,118	Nil

Since all the options were granted at an exercise price of Rs.912.90 per option, weighted average exercise price per option is the same.

Fair-Value Methodology :

The fair value of options used to compute proforma net income and earnings per equity share have been estimated on the date of grant using Black-Scholes Model.

The key assumptions in Black-Scholes Model for calculating fair value as on that date of grant *viz.* October 25, 2005, are :

1. risk-free interest rate : 6.38% p.a.
2. expected life : 2-3 years
3. expected volatility of share price : 30% and
4. expected growth in dividend : 20% p.a.

The weighted average fair value of the option, as on the date of grant, works out to be Rs.105.50 per stock option.

Had the compensation cost for the stock options granted under ESOS – 05 been determined, based on fair-value approach, the corporation's net profit and earning per share would have been as per the proforma amounts indicated below :

Rs. in crores

	Current year	Previous year
Net profit (as reported)	1,570.38	1,257.30
Add : Stock-based employee compensation expense included in the net income	—	—
Less : Stock-based compensation expense determined under fair-value base method : (Gross Rs.40.88 crores) (proforma)	27.12	15.44
Net profit (proforma)	1,543.26	1,241.86
Less : Amounts utilised out of Shelter Assistance Reserve	4.68	4.77
Net profit considered for computing EPS (proforma)	1,538.58	1,237.09
Basic earnings per share (as reported)	62.65	50.25
Basic earnings per share (proforma)	61.57	49.63
Diluted earnings per share (as reported)	58.25	48.44
Diluted earnings per share (proforma)	57.24	47.84

From Directors' Report :

During the year the corporation has not granted any stock options. The stock options granted to the employees operate under 3 schemes, namely, ESOS-1999, ESOS-2002 and ESOS-2005. The options were granted as per the pricing formula approved by you. *i.e.*, at the average of the closing price of the share during the period of 1 month preceding the date of grant under ESOS-1999 and ESOS-2002 and at the latest available closing price on the stock exchange having the higher trading volume under ESOS-2005.

During the year, 35,35,432 options were vested under ESOS-2005. The options exercised during the year aggregated to 34,42,674 of which 9,105 was under ESOS-1999, 3,50,225 under ESOS-02, and 30,83,344 under ESOS-05. The total amount realised due to exercise of options as aforesaid was Rs. 292.17 crores. As a result, 34,42,674 shares of Rs.10 each have been allotted.

During the year, 1,34,893 options lapsed. Options in force as on 31-3-2007 stood at Nil under ESOS-1999, 29,106 under ESOS-2002, and 42,40,374 under ESOS-2005. There have been no variations made during the year in the terms of options granted earlier.

Listed below are disclosure requirements in accordance with SEBI (Employee Stock Option Scheme and Employee Stock Purchases Scheme), Guidelines, 1999 in respect of options granted after June 30, 2003.

Options under ESOS-2005 were granted on 25-10-2005. The options were granted at the market price and hence the intrinsic value of the option is nil. Consequently, the accounting value of the option (compensation cost) was also nil. However, if the fair value of the options using the Black-Scholes Model was used, considering the assumptions as of the date of grant, the compensation cost, net of taxes, would have been Rs.27.12 crores (gross Rs.40.88 crores), the profit after tax would have been lesser by Rs.27.12 crores and the basic and diluted EPS would have been Rs.61.57 and Rs.57.24, respectively.

All the options were granted at an exercise price of Rs.912.90 per option. The weighted average fair value of the option (using the Black-Scholes Model) works out to Rs.105.05.

🕮 Infosys Technologies Ltd. — (31-3-2007)

From Directors' Report :

We had introduced various stock option plans for our employees. The details of options granted under the 1998 Stock Option Plan (the 1998 plan) and the 1999 Stock Option Plan (the 1999 plan) are given in the table.

The SEBI has issued the (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999. This is effective for all stock option schemes established after 19-6-1999. In accordance with these guidelines, the excess of the market price of the underlying equity shares as of the date of the grant over the exercise price of the option, including up-front payments, if any, is to be recognised and amortised on a straight-line basis over the vesting period. Our 1994 option plan came to an end in fiscal 2000.

We have the 1998 stock option plan and 1999 stock option plan, where the options are issued to the employees at an exercise price not less than the fair-market value. If the compensation cost on account of stock option granted after 30-6-2003 under the 1998 and 1999 plans was computed using the fair-value method, our compensation cost would have been higher by Rs.1 crore and Rs.2 crore and our profit would hence be less by Rs.1 crore and Rs.2 crore for fiscal 2007 and 2006, respectively. The impact on EPS of fiscal 2007 and 2006 would be Rs.0.02 and Rs.0.04, respectively.

During the fiscal 2007 and 2006, there have not been any grant of stock options under the 1998 plan, hence the weighted average fair values of grant during these years are Nil.

During the fiscal 2007, we granted 638,761 options under the 1999 plan with a weighted average fair value of Rs.582 per option. During fiscal 2006, there have not been any grant of stock options under the 1999 plan and hence the weighted average fair values of grant during fiscal 2006 is Nil.

	**1998 plan	**1999 plan
Total grants authorised by the plan (Nos.)	1,17,60,000 ADS	5,28,00,000 shares
Pricing formula on date of grant	Not less than 90% of fair-market value	Fair-market value
Variation in terms	N.A.	N.A.
Ratio of ADS to equity shares	1 ADS = 1 Equity share	N.A.
Options granted during the year* (Nos.)	—	6,38,761
Weighted average price per option granted (Rs.)	N.A.	2,120.95
Option vested as of March 31, 2007 (Nos.)	20,84,124	12,59,079
Options exercised during the year (Nos.)	22,91,213	1,78,08,689

	**1998 plan	**1999 plan
Money raised on exercise of options (Rs. crores)	197	1,019
Options forfeited and lapsed during the year (Nos.)	1,71,143	1,11,306
Total number of options in force at the end of the year (Nos.)	20,84,124	18,97,840
Grant to senior management***	—	1,27,400
Employees receiving 5% + of the total number of options granted during the year***	—	1,27,400
Employees granted options equal to or exceeding 1% of the issued capital	—	—
Diluted EPS on issue of shares on exercise calculated in accordance with AS-20	Rs.66.44	Rs.66.44

* Granted to employees of Infosys BPO Limited (majority-owned subsidiary of the company).

** Adjusted for 1 : 1 bonus issued in July 2006.

*** Granted to Mr. Amitabh Chaudhry, CEO and Managing Director, Infosys BPO Limited.

Significant assumptions used to estimate fair value of options granted during the year.

	Year ended March, 31	
	2007	2006
Risk-free interest rate (%)	7.0-7.3	N.A.
Expected life	2-6 years	N.A.
Expected volatility (%)	34-54	N.A.
Dividend yield (%)	0.2	N.A.
Market price on grant date	2,120.95	N.A.

From Management Discussions and Analysis :

1998 Employee Stock Option Plan (1998 plan) :

Pursuant to the resolutions approved by the shareholders in the Extraordinary General Meeting held on January 6, 1999, we put in place an ADS – linked stock option plan termed as the '1998 Stock Option Plan'. The Compensation Committee of the Board administers the 1998 plan. The Government of India has approved the 1998 plan, subject to a limit of 1,17,60,000 equity shares of par value of Rs.5 each, representing 1,17,60,000 ADSs to be issued under the plan. The plan is effective for a period of 10 years from the date of its adoption by the Board.

The details of the grants made and options forfeited & expired (adjusted for stock-split, as applicable)

	2007		2006	
	No. of options	Weighted-average exercise price	No. of options	Weighted-average exercise price
1998 Plan				
Outstanding at the beginning of the year	45,46,480	908	61,08,580	873
Forfeited and expired	(1,71,143)	1,845	(1,90,696)	1,131
Exercised	*(22,91,213)	860	(13,71,404)	793
Outstanding at the end of the year	**20,84,124**	**900**	**45,46,480**	**908**
Vested at the end of the year	20,84,124	900	38,10,724	961
1999 Plan				
Outstanding at the beginning of the year	1,91,79,074	575	2,81,09,874	563
Granted	6,38,761	2,121	—	—
Forfeited and expired	(1,11,306)	552	(3,33,342)	557
Exercised	**(1,78,08,689)	572	(85,97,458)	536
Outstanding at the end of the year	**18,97,840**	**1,121**	**1,91,79,074**	**575**
Vested at the end of the year	12,59,079	613	1,69,54,352	593

* Includes 90,275 options/shares exercised prior to issue of bonus shares.

** Includes 11,97,921 options/shares exercised prior to issue of bonus shares.

under the 1998 plan are provided below :

Month of grant	Options granted		Options forfeited & expired		
	Employees (Nos.)	Options (Nos.)	Grant price at market per ADS	Employees (Nos.)	ADSs (Nos.)
Apr 2006	—	—	—	—	—
May	—	—	—	20	75,000
June	—	—	—	5	41,320
July	—	—	—	7	19,160
Aug	—	—	—	—	—
Sep	—	—	—	2	1,880
Oct	—	—	—	4	17,446
Nov	—	—	—	3	7,200
Dec	—	—	—	1	800
Jan 2007	—	—	—	1	848
Feb	—	—	—	45	6,929
Mar	—	—	—	1	560
	—	—	—	**89**	**1,71,143**

During the year, 22,91,213 options issued under the plan 1998 were exercised, and the remaining ADS options unexercised and o/s as at March 31, 2007 were 20,84,124 (equivalent to 20,84,124 equity shares). Vested ADSs as of March 31, 2007 were 20,84,124 (equivalent to 20,84,124 equity shares).

Details of the number of ADS options granted and exercised are given below :

Fiscal	Granted		Exercised	
	Employees (Nos.)	Options (Nos.)	Employees (Nos.)	Options (Nos.)
1999	29	17,04,000	32	—
2000	58	11,77,200	5	95,200
2001	705	38,59,360	—	49,736
2002	476	36,34,000	—	2,23,864
2003	223	23,20,800	120	3,58,160
2004	39	3,83,600	309	10,35,480
2005	—	—	562	11,71,600
2006	—	—	531	13,71,404
2007	—	—	1,263	22,91,213
	1,530	**1,30,78,960**	**2,822**	**65,96,657**

1999 Employee Stock Option Plan (1999 plan) :

The shareholders approved the 1999 Plan in June 1999, which provides for the issue of 5,28,00,000 equity shares to employees. The 1999 plan is administered by the compensation committee of the Board. Under the 1999 plan, options were issued to employees at an exercise price not less than the fair market value, *i.e.*, the closing price of the company's shares on the stock exchange, where there is the highest trading volume on the date of grant and if the shares are not traded on that day, the closing price on the next trading day. Options under this plan may be granted to employees at less than the fair market value only if specifically approved by the members of the company in a general meeting.

The details of the grants made and forfeited and expired (adj for stock-split, as applicable) under the 1999 plan are provided in Table 1 :

TABLE 1

Month of Grant	Options granted		Options forfeited & expired		
	Employees (Nos.)	Options (Nos.)	Grant price (Rs.)	Employees (Nos.)	Options (Nos.)
Apr 2006	—	—	—	22	10,720
May	—	—	—	48	11,444
June	—	—	—	15	8,280
July	—	—	—	15	10,260
Aug	—	—	—	29	5,960
Sep	—	—	—	31	6,601
Oct	—	—	—	8	4,890
Nov	—	—	—	16	10,664
Dec	—	—	—	31	8,321
Jan 2007	—	—	—	12	5,480
Feb	—	—	—	22	6,384
Mar	288	6,38,761	2,120.95	3	22,302
	288	**6,38,761**	**2,120.95**	**252**	**1,11,306**

During the year, 1,78,08,689 options issued under the 1999 plan were exercised, and the remaining options unexercised and o/s as at March 31, 2007 were 18,97,840. Vested options as at March 31, 2007 were 12,59,079 (includes 7,602 options granted to external directors).

Details of number of options issued under the 1999 plan are given below :

Fiscal	Granted		Exercised	
	Employees (Nos.)	Options (Nos.)	Employees (Nos.)	Options (Nos.)
2000	1,124	81,16,000	22	—
2001	8,206	1,56,62,640	—	9,600
2002	5,862	1,64,04,000	—	240
2003	3,008	49,34,800	296	97,424
2004	595	15,42,400	2,651	21,48,344
2005	—	—	10,581	68,41,050
2006	—	—	16,269	85,97,458
2007	288	6,38,761	30,795	1,78,08,689
	419,083	**4,72,98,601**	**60,614**	**3,55,02,805**

The options movements under both 1998 and 1999 Stock Option Plans as of March 31, 2007 are as follows :

	Options (Nos.)
Granted	6,38,761
Exercised	2,00,99,902
Forfeited	2,82,449
Outstanding	39,81,964
Vested	33,43,203

Employee Stock Compensation under SFAS 123 :

Statement of Financial Accounting Standards 123, Accounting for stock-based compensation under U.S. GAAP, requires the pro forma disclosure of the impact of the fair-value method of accounting for employee stock valuation in the financial statements. The fair value of a stock option is determined using an option-pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option, the volatility of the underlying stock and the expected dividends on it, and the risk-free interest rate over the expected life of the option. Applying the fair value based method defined in SFAS 123, the impact on the reported net profit and basic earnings per share would be as follows :

Year ended March 31,	2007	2006
Net profit before exceptional item		
As reported	3,777	2,421
Adjusted pro forma	3,765	2,381
Basic EPS		
As reported	67.82	44.34
Adjusted pro forma	67.61	43.60

🕮 Hindustan Oil Exploration Company Ltd. — (31-3-2007)

From Notes to Accounts :

Long-Term Incentive Plan, 2005 :

The company has instituted a Long-Term Incentive Plan ('LTIP Scheme') for the benefit of the employees of the company. Under the plan, the company is authorised to distribute 5% of company's profit on ordinary activities to eligible employees in the form of cash and deferred bonus. After meeting the cash bonus component as per the LTIP scheme, the surplus is distributed as deferred bonus (stock options).

The number of shares to be issued under the LTIP scheme is determined by dividing the deferred bonus for the scheme year by the average market price of the company's shares (as quoted at the NSE) 30 days prior to the date on which the Board of Directors approve the audited accounts in relation to the scheme year or such other date as may be approved by the Board.

A trust has been formed to purchase the shares from the market. The Company funds the trust to buy the requisite number of shares, granted under ESOP. The total bonus including cash and deferred bonus is expensed during the scheme year to which it pertains.

The Remuneration and Compensation Committee of the Board of Directors of the company administer the LTIP scheme. On May 23, 2006 the company approved grant of 15,069 options, pertaining to financial year 2005-2006, at NIL exercise price. These options vest with the eligible employees after a period of three years from April 01, 2006. For financial year 2006-2007, the company has not distributed any cash or deferred bonus.

Particulars	2006-2007	
	Shares arising out of options	Exercise Price Rs.
Outstanding at the beginning of the year	15,069	Nil
Vested during the year	0	Nil
Forfeited during the year	0	Nil
Exercised during the year	0	Nil
Outstanding at the end of the year	15,069	Nil
Exercisable at the end of the year	0	Nil

🕮 Entertainment Network (India) Ltd. — (31-3-2007)

From Notes to Accounts :

Pursuant to the resolution passed by the Board of Directors and the members of the company at the meeting of Board of Directors and Extra Ordinary General Meeting of the members of the company, respectively, held on Nov. 5, 2005 the company had introduced Employee Stock Option Scheme (the scheme) for its existing and future permanent employees and directors of its subsidiary company and holding company.

The scheme provides that the total number of options granted thereunder will be 109,360. Pursuant to a resolution passed by the remuneration/compensation committee at its meeting held on Nov. 5, 2005, all 109,360 options that are exercisable for equity shares have been granted at an exercise price of Rs.90.

In accordance with the Guidance Note on Accounting for 'Employee Share-based Payments' issued by the ICAI and Employee Stock Option and Employee Stock Purchase Guidelines, 1999, issued by the SEBI of India, fair value of these options, on the grant date, is amortised over the vesting period.

Fair value of the options granted during the year, based on the report received from an independent firm of Chartered Accountants, as per Black-Scholes method of valuation, was as in Table 2 :

Particulars	2006-2007	2005-2006
Options o/s at the beginning of the year	109,360	—
Add : Options granted during the year	—	109,360
Less : Options forfeited during the year	2,610	—
Options exercised during the year	20,910	—
Options expired during the year	—	—
Options o/s at the end of the year	**85,840**	**109,360**
Exercise price for options o/s at the end of the year (Rs.)	90	90
Fair value of options amortised during the year (Rs.)	6,449,856	3,160,836

TABLE 2

Vesting date	Number of options	Fair value of options
Nov 15, 2006	34,975	95.25
Apr 1, 2007	42,775	98.40
July 1, 2007	17,255	10.36
Apr 1, 2008	8,700	105.67
July 1, 2008	5,655	107.30
Weighted average		**98.74**

Further amortisation of fair value of the options granted to the employees of Times Innovative Media Limited (formerly known as Times Innovative Media Pvt. Ltd.), the subsidiary company and Times Infotainment Media Limited, the holding company aggregating Rs.6,24,923 (previous year : Rs.282,441) and Rs.1,049,376 (previous year : Rs.439,786), respectively, have been charged to the respective companies.

From Directors' Report :

As stated in the last Annual report for the year 2005-2006, Entertainment Network (India) Limited — Employee Stock Option Scheme (hereinafter referred to as ENIL ESOS – 2005) was implemented for the benefit of the present employees of the company, its holding company and its subsidiary (including Directors) in accordance with the SEBI Guidelines.

Disclosure pursuant to clause 12 of SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme), Guidelines, 1999.

Details of the ENIL – ESOS – 2005 :

(1) Options granted : 109,360

(2) The pricing formula : at an exercise price of Rs.90 each

(3) Options vested as on the date of this report : 75,140 (net of lapse of 2,610 options)

(4) Options exercised as on the date of this report 56,870

(5) The total number of equity share arising as a result of exercise of option : maximum number of equity shares that can arise, if all options are vested and exercised, are 106,750 (total options granted 109,360 less number of options lapsed 2,610).

(6) Options lapsed : 2,610

(7) Variation of terms of options : None

(8) Money realised by exercise of options : Rs.51,18,300 (56,870 options exercised @ Rs.90 per option exercised)

(9) Total number of options in force : 49,880 (total options granted 109,360 less number of options lapsed 2,610 less number of options exercised 56,870)

(10) Employee-wise details of options granted to : (List not reproduced)

(ii) Senior managerial personnel : All the above options grantees are senior managerial personnel of the company, its holding company and its subsidiary.

(iii) Any other employee who receives a grant in any 1 year of option amounting to 5% or more of option granted during that year. The list of employees receiving a grant in 1 year of option amounting to 5% or more of option granted during that year is as below : (List not reproduced)

(iv) Identified employees who were granted options, during any 1 year, equal to or exceeding 1% of the issued capital (excluding o/s warrants and conversions) of the company at the time of grant : None of the employees were granted option, during any 1 year equal to or exceeding 1% of the issued capital under ENIL – ESOS – 2005.

(12) Where the company has calculated the employee compensation cost using the intrinsic value of the stock options, the difference between the employee compensation cost so computed and the employee compensation cost that shall have been recognised if it had used the fair value of the options, shall be disclosed. The impact of this difference on profits and on EPS of the company shall also be disclosed.

The company has calculated the employee compensation cost using the fair value of the stock options. Kindly refer to the point No. 5 of the Schedule 18 to the Financial Accounts.

(13) Weighted-average exercise prices and weighted-average fair values of options shall be disclosed separately for options whose exercise price either equals or exceeds or is less than the market price of the stock.

The options are exercisable at Rs.90 per equity share including a premium of Rs.80 per share.

Tranches of stock/options	Fair valuation of the options	No. of options
Tranche I	Rs. 95.25	34975
Tranche II	Rs. 98.40	42775
Tranche III	Rs. 100.36	17255
Tranche IV	Rs. 105.67	8700
Tranche V	Rs. 107.3	5655
Total		**109360**

(14) A description of the method and significant assumptions used during the year to estimate the fair values of options, including the following weighted-average information :

The company has used Black-Scholes theory of valuation for arriving at an indicative valuation of

the stock option.

The factors affecting the value of an option were :

- The underline value of the assets
- The exercise price
- The expected life
- The time to expiration
- The expected volatility of the underlying assets
- The risk-free interest rate
- The dividend expected during the life of the option (if any).

Ambuja Cements Ltd.
— (18 months ended 31 December 2006)

From Directors' Report :

The company has granted stock options to eligible whole-time Directors and employees for the seventh year in succession. The particulars required to be disclosed pursuant to Clause 12 of SEBI (Employees Stock Option Scheme) Guidelines, 1999 are given in subsequent paragraphs.

(a) *ESOS 2005-06 :*

During the year 2005-06, the company granted 8,73,075 stock options on 7th November, 2005 (each option carrying entitlement for five shares of the face value of Rs.2 each) to eligible whole-time Directors and employees including some employees of subsidiary companies, at an exercise price of Rs.69.60 per share. The market price of the shares on the date of grant was Rs.73.05 per share. These stock options have vested on expiry of one year from the date of grant and can be exercised during a period of four years from the date of vesting. The exercise price was determined by averaging the daily closing price of the company's equity shares during 15 days on the National Stock Exchange immediately preceding the grant. The company has adopted intrinsic-value method for valuation and accounting of the aforesaid stock options as per SEBI guidelines, and accordingly has accounted Rs.1.47 crore as employee compensation cost for the year ended 31st December, 2006.

The fair value of the options as per the 'Black-Scholes' Model comes to Rs.19.21 per option. Had the company valued and accounted the aforesaid options as per the 'Black-Scholes' Model, the net profit for the year would have been lower by Rs.11.74 crore and the diluted earning per share (with face value of Rs.2 each) would have been Rs.10.01, instead of Rs.10.09 per share.

The 'Black-Scholes' Model captures all the variables with their respective appropriateness which influences the fair value of stock options. The significant assumptions to estimate the fair value of options as per 'Black-Scholes' Model are :

1. Risk-free interest rate — 6.44%.
2. Expected life of the option — 3 years.
3. Expected volatility — 32.22%.
4. Expected dividend yield — 2.71%.

All the options granted during the year have been vested. No employee or Director has been granted options in excess of 1% of the issued equity share capital of the company. Mr. Anil Singhvi, Mr. P. B. Kulkarni and Mr. A. L. Kapur have been granted options of more than 5% of the total options granted during the year. The options granted to the eligible whole-time Directors being the senior management personnel are as follows : (*list not reproduced*)

The other employees have been granted 6,63,075 options. The details of options granted to other employees are :

Total number of employees	2,366
Total number of options granted	6,63,075
Max. number of options granted	6,000
Min. number of options granted	25
Avg. number of options granted	280

(b) *Cumulative disclosures :*

The particulars with regard to the stock options as on 31st December, 2006 as required to be disclosed under the SEBI Guidelines are as given in Table on the next page.

From Notes to Accounts :

Employee Stock Option Schemes :

The company has granted 52,82,250 (30-6-2005 — 44,09,175) stock options to its employees (including certain employees of the subsidiary companies) and whole-time Directors (other than those excluded under the SEBI Guidelines on Stock Options). Out of the above stock options, 3,75,575 (30-6-2005 — 3,50,600) have been surrendered/lapsed and 36,06,750 (30-6-2005 — 20,70,080) have been exercised. 12,99,925 (30-6-2005 — 19,88,495) stock

options are outstanding as on 31st December, 2006, which if fully exercised will result in issue of 82,16,938 shares of Rs.2 each (30-6-2005 — 1,49,13,713) equity shares. The amount of Rs.1.09 crores (30-6-2005 — Rs.0.03 crore) represents the discount on the above-said options outstanding.

Cumulative position as on 31st December, 2006 :

Nature of disclosure	*Particulars*
(a) Options granted	52,82,250
(b) The pricing formula	2004-05 and 2005-06 : The exercise price was determined by averaging the daily closing price of the company's equity shares during 15 (fifteen) days on the National Stock Exchange, immediately preceding the grant. 2003-04 : The exercise price was determined by averaging two weeks' high and low price of the company's equity shares on the National Stock Exchange, immediately preceding the grant. 1999-2000 to 2002-03 : The exercise price was the average of the daily closing price of equity shares of the company on the Stock Exchange, Mumbai during the period of 30 (thirty) days, immediately preceding the date on which the options were granted.
(c) Options vested	49,06,675
(d) Options exercised	36,06,750
(e) The total number of shares arising as a result of exercise of options	Total number of shares arising as a result of exercise of options shall be 2,65,09,836 shares of Rs.2 each.
(f) Options lapsed/surrendered	3,75,575
(g) Variation of terms of option	Nil
(h) Money realised by exercise of options	Rs.79.90 crore
(i) Total number of options in force	12,99,925
(j) (a) Details of options granted to/Exercised by the whole-time Directors	11,45,000/6,69,700 (list not reproduced)
(b) Any other employee who received a grant in any one year of option amounting to 5% or more of options granted during that year	Nil
(k) Employees who were granted options, during any one year, equal to or exceeding 1% of the issued capital of the company at the time of grant	Nil
(l) Diluted Earnings Per Share (EPS) pursuant to issue of shares on exercise of option calculated in accordance with Acounting Standard AS-20	10.09
(m) Weighted-average exercise price of options/ Weighted-average fair value of options (for grants made after June 30, 2003)	2003-04: 310 * / 67.44 ** 2004-05: 443 * / 96.73 ** 2005-06: 69.60 * / 19.21 **

* Options related to equity shares of F.V. of Rs.10. ** Options related to equity shares of F.V. of Rs.2.

INTERNAL AUDIT

Internal Audit of an SME (Engineering Unit) — *Assurance and Consulting Role*

Deepjee Singhal
Manish Pipalia
Chartered Accountants

Background :

The Managing Director of an engineering unit based in Greater Noida (UP) has been in touch with a partner of a Chartered Accountant firm since they first met a few months back at a conference organised by a Chamber of Commerce in Mumbai. As the Managing Director (MD) was progressive in his views, the CA suggested the institution of 'internal audit' at the manufacturing unit. The Managing Director felt that since the turnover is only Rs.80 crores and he, along with his family members (brothers and uncles), controls most of the operations like procurement, finance, manufacturing, etc., the internal audit would not yield any significant benefit.

The CA suggested a plan of internal audit to be a half-yearly feature with a fortnight being spent by a Chartered Accountant and a semi-qualified staff member, and he himself would be available for four days each quarter. The internal audit would cover 'process review' and suggest improvements.

In addition, it was proposed that each area like procurement, production, marketing, etc. (areas to be decided after discussing and studying the functions at the unit during the first review) be rated on a scale of 1 to 10 and scores given on basis of audit findings. This would signify areas of risk and poor management. As these scales are subjective, it would be arrived at after discussing with the auditee in each area. Cumulatively score would be given for the unit every half year. Hence, the internal audit every half year would be akin to the annual health check-up of a person. This idea and approach appealed to the Managing Director and he accepted the proposal to carry out the first internal audit on trial basis.

Methodology :

Based on the above background, the partner-in-charge of the firm had a meeting with his audit manager to chalk out a plan to achieve the above objectives and ensure that the internal audit service is really beneficial to the SME. The success of the first half-yearly internal audit would *demonstrate the value-added role of internal audit* to the MD of the engineering unit.

In the first half year it was decided that the team would focus on all major areas like Procurement, Stores including Inventory, Production, Despatches, Production, Marketing, Human Resources, and Finance & Accounts.

Throughout the internal audit, it was agreed amongst the internal audit team members, that education and awareness for institutionalised systems and procedures including importance of decisions to be taken on scientific basis rather than 'rule of thumb' would be emphasised. This is particularly relevant in SME where the decisions are mainly taken on 'rule-of-thumb' basis.

Based on the internal audit carried out, given below are a few of the observations :

1.0 ***Procurement and Stores :***

- Raw materials which formed 45% of the cost of sales were purchased personally by the MD. It was observed that he had strict control over cost. However, since the unit was cash surplus and the interest rate on cash credit was only 9%, it was pointed out that the unit should make payment to raw material creditors immediately on receipt and avail of cash discount of 2% per month — that is — 4% for two months, the period of credit availed of by the unit. This amounted to savings of 1% to 1.5% over the cost of purchases, which was a substantial saving in cost.
- There was lax control over consumables, as the family members neglected this area assuming it to be of little value compared to other activities. This had led to weak control over this area. It was noticed that bills for small consumables were booked twice and paid out twice. Items which were to be got as free supply along with bigger equipment/s were paid out, as it was not marked out properly in stores.
- In case of 'Open Orders', the rate was confirmed at some point of time; however, there was no periodical review of the rates stated in the Orders. Total purchases under such orders

amounted to Rs.8 lacs for the six months ended September 30th, 2007.

The rates currently stated in the Open Orders appeared to have been negotiated some time back and there were no comparative quotations to validate the rates mentioned in these Orders.

All such Open Orders needed to be preceded by rate confirmation after considering quotations from a specific minimum number of suppliers. The suggestion to implement a plan for purchase and recording was made.

- High-value consumable like diesel was being purchased from a dealer rather than directly from oil company. Purchase of diesel directly from the oil company was suggested and implemented, resulting in some savings in cost. This also reduced the chances of buying adulterated diesel.

2.0 ***Marketing :***

Marketing was being handled by two uncles and two brothers of the MD. They had divided the clients and interacted with the allocated clients without any co-ordination amongst themselves. This led to some confusion over supplies to customers, as there was no single person responsible for marketing.

- Almost all orders procured were supplied late and this led to levy of liquidated damages costing lacs of rupees every year. There was total absence of planning for avoiding late deliveries. More than the levy of liquidated damages, this was affecting the reputation of the unit.
- Further, since the economy was passing through a upswing, there was no dearth of orders, but due to absence of proper analysis, the unit did not concentrate on high-contribution orders. They felt that they were doing a great job, but a three-month analysis proved otherwise. The unit's market share of high-contribution items was low when compared to other competitors. The high contribution orders went to their competitors. The internal auditor recommended corrective action, which when implemented, resulted in better co-ordination and the compensation for late deliveries was substantially reduced. This step improved both profitability and client relationship.

3.0 ***Finance & Accounts :***

- There were idle funds in bank accounts and at the same time there was cash credit limit being utilised at 9%. Idle funds needed to be transferred to cash credit account. Further as a result of review of bank accounts undertaken, dormant bank accounts were identified and closed.
- Credit rating by Crisil was undertaken and a triple-A rating ensured that the bank interest on cash credit was reduced by half a percent by the bank. The credit rating was also used to assure the vendors and customers about the excellent financial position of the unit.

There were numerous observations in various areas and each area was rated from 1 to 10 rating scale. Overall, the unit got 5 and it was agreed that all observations would be acted upon for improvement. It was also agreed that with improvements and another cycle of internal audit after six months, the unit would try to get better rating.

Also, the observations were divided into measurable cost savings and process improvements, and responsibility being given to heads of departments for the same.

The observations would also be reviewed internally in the unit's monthly management meeting of the heads of departments).

Conclusion :

The Managing Director appreciated the efforts of the internal audit team and desired that the internal audit be carried out on a quarterly basis. He specially appreciated the *'understanding of the business'* by the partner of the C.A. firm and his suggestions for 'process improvements' and 'cost savings'. The Managing Director also arranged for the partner to speak at the local industry forum for SMEs, where his company's case study was presented to other SMEs. This led the internal auditing function to be elevated to providing 'business solutions'.

I never worry about action, but only about inaction. — Winston Churchill

Uday Chitale
Chartered Accountant

IFRS — Will they live up to their promise ?

At a time when many barriers to global trade have fallen and the world's economies have become increasingly linked, countries all over the world are taking steps to harmonise their accounting standards and develop a truly global language of business. Under the lead of the International Accounting Standards Board (IASB), already more than 100 countries, most notably the European Union and many Asian economies, have either implemented International Financial Reporting Standards (IFRS) or plan to do so. So far, the United States has been a holdout. But the winds are changing. On 15-11-2007, the U.S. Securities and Exchange Commission (SEC) — which up to then was requiring foreign companies to either report using Generally Accepted Accounting Principles (GAAP) or to reconcile to them — announced that it would promote international compatibility by allowing foreign companies to access U.S. capital markets while reporting under IFRS. At the same time, the SEC is contemplating changes that would grant domestic firms the choice between reporting under GAAP or IFRS. Proponents of accounting harmonisation say that IFRS will enhance the comparability of financial statements, improve corporate transparency, increase the quality of financial reporting and, therefore, ultimately benefit companies and investors.

But Wharton accounting professor Luzi Hail says that from an economic perspective, there are reasons to be skeptical about these high hopes. In particular, he questions the premise that mandating the adoption of accounting standards, even if they are of high quality, actually makes corporate reporting more informative or more comparable. In a new study titled, **'Mandatory IFRS Reporting Around the World : Early Evidence on the Economic Consequences'**, Hail and his co-authors are among the first to shed light on the alleged benefits of the ongoing international accounting convergence.

Quest for a global accounting language :

The issue of convergence represents a kind of revolution. Just a few years ago, most observers would have said there was no chance of converging U.S. accounting rules and IFRS into a single, globally accepted standard. But now it looks like it may actually happen.

Hail says the primary driver behind the increased acceptance of IFRS is a hoped-for reduction in the cost of capital together with the avoidance of costs that occur when publicly listed companies follow different reporting standards.

Until the recent move by the SEC allowing IFRS reports, if, for instance, a European company wanted to list on the NYSE or another U.S. exchange, it had to engage in a costly reconciliation between its IFRS-compliant financial records and the results under U.S. GAAP. In principle, this would not be an issue if all countries followed a single set of accounting standards. Also, if the new accounting regime forces firms to be more forthcoming in what and how they report, investors would be better off, and achieve a clearer picture of what the future holds. That is exactly what the organisations that set the standards on both sides of the ocean argue in their quest for a global accounting language.

Prof. Hail's paper notes that on average, market liquidity and firm value do increase by about 2% to 6% for firms that adopt IFRS reporting when it becomes mandatory, at least when compared to the level prior to IFRS adoption or to firms that have not yet switched. Further, total trading costs and the gap between bid and ask prices both generally decline.

An unequal sharing of IFRS benefits :

Overall, based on the favourable market reactions, it would appear that IFRS delivers what standard setters, firms and investors hoped for. A closer look, however, reveals a subtler picture. "Why is it that some publicly listed companies choose to voluntarily adopt International Financial Reporting Standards early on, while others wait until it is mandated ?" Hail asks. "Our results show that the greatest positive effects on firm value and liquidity appear to accrue to these early adopters. This makes

perfect sense, because for them the benefits of switching to IFRS should outweigh the costs; otherwise they would not have done it."

The same reasoning helps explain why some firms hold off on implementing IFRS until they are forced to adopt the standards. "If there were no gains for these firms to adopt IFRS beforehand," he says, "why should the cost-benefit trade-off all of a sudden change when they are left without choice? Obviously, there must exist some other benefits in the form of increased comparability, better risk-sharing among investors or the like that would not have occurred in the absence of the mandate."

Hail adds that the unequal sharing of benefits points to the importance of reporting incentives when evaluating the consequences of IFRS adoption. Indeed, a look at how the liquidity benefits vary across the countries that have adopted IFRS further confirms this view. "We find that not every country obtains benefits by simply adopting IFRS," says Hail. "Instead, we note that the improvements in liquidity, valuation and cost of capital are present only in countries with relatively strict enforcement regimes and in countries where the institutional environment provides incentives for more transparent earnings." In countries with weak enforcements and poor reporting incentives, the introduction of IFRS has no effect.

Such differences raise another important issue, according to Hail. It is not clear whether the beneficial effects are attributable to the adoption of IFRS alone, or to some other changes in the environment of the firms that switch. In fact, the paper suggests that the use of IFRS alone may not be enough to make corporate reporting more informative or more comparable. Hail and his co-authors note that several recent studies point to the 'limited role' of accounting standards and instead highlight the importance of firms' reporting incentives in determining observed accounting quality.

IFRS, like U.S. GAAP and other sets of accounting standards, gives firms substantial discretion. On the one hand this is a good thing, since reporting involves considerable judgment and should allow managers to convey their superior information to outside investors or, alternatively, to keep information private for competitive reasons.

But the way that firms use this discretion is likely to depend on their reporting incentives, which are shaped by such factors as a country's legal institutions, various market forces, firms' operating characteristics and managers' own personal goals. Consequently, even when standards mandate superior accounting practices and require more disclosures, it is not clear that firms implement these standards in a way that the reported numbers will indeed be more informative. This is not just a question of proper enforcement, even with perfect enforcement, observed reporting behavior is expected to differ across firms as long as accounting standards — for good reason — offer some discretion and firms have different reporting incentives."

Consequences of IFRS reporting for U.S. firms :

The study also raises questions about the anticipated benefits of allowing U.S. firms to use IFRS in their domestic reporting. "Our findings indicate that the liquidity effects for first-time mandatory adopters are smaller in countries that have fewer differences between local GAAP and IFRS or for countries that, over several years, have been gradually converging towards IFRS reporting," says Hail. "This is consistent with the notion that, in these cases, the regulatory change is likely to be of smaller magnitude."

Regarding the U.S., with its already strong enforcement institutions and lively capital markets, one expects that allowing a switch to IFRS will likely cause little capital-market benefits. "The infrastructure is already in place, and combined with the strong reporting incentives due to constant pressure from investors, we may not see much of an impact on how U.S. firms report. But perhaps U.S. firms will gain from comparability benefits, which should be more pronounced when you are late in the game and everybody else has already switched to IFRS."

Overall, the report concludes that the consequences of adopting a global accounting language should not be considered a done deal yet. "Our findings indicate that the adoption of IFRS has stirred up the process of financial reporting on a worldwide basis," says Hail. "But the lessons and merits of a convergence to global accounting standards and how this affects firms' reporting behavior on a daily basis are still being debated and will remain a major policy issue for years to come.

(*Source* : University of Pennsylvania — Knowledge @ Wharton, 28-11-2007)

THE 'WORD'

N. C. Jain
Advocate

Obiter Dicta

The law declared by the Supreme Court through its decisions is, under the Constitution, binding force on all the Courts within the territory of India. The same is the case with decisions of the High Courts which bind the lower Courts within their jurisdiction as to the law expounded by them. Principle of *stare decisis* generally expects the Courts to stand by the decided cases. For this purpose what binds is not all that is said, but only the abstract principle of law that emerges from the decision. As observed by the Supreme Court in *Union of India v. Dhanwanti Devi,* (1996) 6 SCC 44, every decision contains three basic postulates — (i) finding of material facts, direct and inferential. An inferential finding of facts is the inference which the Judge draws from the direct or perceptible facts; (ii) statements of the principles of law applicable to the legal problems disclosed by the facts, and (iii) judgment based on the combined effect of the above. The second postulate *viz.* the statement of the abstract principles of law on which a question before the Court has been decided termed ***'ratio decidendi'*** alone has the force of law and forms a binding precedent to be followed throughout the country. A decision is not confined to exposition of such principle only. In the course of a suit, many incidental questions arise which are indirectly connected with the main question for consideration. The observations on such questions, whether casual or of collateral relevance, are known as ***'obiter dicta'*** or simply *dicta* (*Maria Silva v. Piedode Cardozo,* AIR 1969 Goa 94)

2. The generality of the expressions which may be found in a judgment are not exposition of the whole law. "A decision is only an authority for what it actually decides, what is the essence in a decision is its *ratio* and not other observations found therein, nor what logically follows from the various observations made in it" [*State of Orissa v. Sudhansu Sekhar Misra,* (AIR 1968 SC 647)]. Therefore, "In considering the observation of high judicial authority, like this Court, the greatest possible care must be taken to relate the observations of a Judge to the precise issue before him and to confine such observations, even though expressed in broad terms, in the general compass of the questions before him, unless he makes it clear that he intended his remarks to have wider ambit" [*ADM Jabalpur v. Shivakant Shukla,* (1976) 2 SCC 521].

3. An ***'obiter dictum'*** may not have a binding precedent, but it cannot be denied that it is of considerable weight [*Director of Settlement A.P. v. M. R. Apparao,* 4 SCC (2000) 641]. Identification of ratio and separation of the two, entails careful reading of the decision as a whole to relate the observations to the precise issue before the Court. An interesting instance is found in the decision of the Apex Court in *CIT v. Kanji Shivji & Co.,* (242 ITR 124), where the Court was to decide about the applicability of the Explanation to S. 40(b) in the context of its own two decisions in *Brij Mohan Das Laxman Das v. CIT,* (223 ITR 225) and *Suwalal Anandilal Jain v. CIT,* (224 ITR 753) holding the Explanation to be declaratory and a later contrary decision in *Rashik Lal and Co. v. CIT,* (229 ITR 458) holding the same as prospective only. The Court upheld its earlier decisions and declared it as retrospective in application by terming its observation in Rashik Lal case (*supra*) as *obiter dicta.* The reason stated for such a view was that in Rashik Lal case the Court was dealing with allowability of commission to the partner representing HUF, whereas in the earlier two cases, the issue was allowability of interest to such a partner. Further, it was held that the said Explanation was not really an issue in Rashik Lal case. It is of relevance to point out that even though the explanation was not an issue in that case, the observation made by the Court was a reasoned and categorical one and was in response to the reference of the two cases made before them. The Court held :

> "It was further held that the Explanation was only clarificatory. It is difficult to agree with the proposition, because the Explanation was added to the Taxation Laws (Amendment) Act, 1984 with effect from April 1, 1985. By adding the Explanation, the Legislature altered the law prospectively on and from April 1, 1985. If what was contained in the Explanation was already the law in force, then giving effect to the Explanation from April 1, 1985 does not make any sense."

In *Kherawala (LB) v. ITO,* (147 ITR 67), the Gujarat High Court considered even the ***obiter opinion*** of the Supreme Court, as binding if such opinion is

given deliberately and advisedly. With this view, even the aforesaid observation would have had a binding force, if the Court did not have to choose between the two conflicting decisions.

4. Even observations related to the issue under consideration can be construed as of the nature of obiter if the same were made without consideration of all relevant aspects of the matter. In *Dhrangadhra Municipality v. Dhrangadhra Chemical Works Ltd.*, [174 ITR 77 (Guj.)], the issue concerned maintainability of suit u/s.72 of the Contract Act to claim refund of octroi paid under mistake. Reliance was placed on the earlier decisions of the Supreme Court in *Sales Tax Officer v. Kanhaiya Lal*, AIR 1959 SC and D. Cawasji's case AIR 1975 SC 813 holding that the word 'mistake' covers mistake of law and suit u/s.72 of the Contract Act, is maintainable. The Gujarat High Court did not accept the decision as precedent, for the reason that in those cases, the Court's attention was never invited on the further question as to whether the suit is maintainable, even though the claimant had not suffered any prejudice or legal injury. It can never be assumed that the Court had spoken on it, though it was never canvassed before it. Precedents *sub silentio* and without argument are of no moment [*Divisional Controller, KSRTC v. Mahadeva Shetty*, 7 SCC (2003) 199]. Considering the observation in those cases as obiter and relying on the contrary decision of the Supreme Court in *State of MP v. Vyankatlal*, AIR 1985 SC 901, the Court held that in a situation of conflict between the obiter observations and the direct ratio of the decision of the Bench of equal strength, the ratio had to prevail and would remain binding. As between the law expressed by Benches of different strength of the same Court, the Madras High Court in *Ghansham Singh v. Commissioner of Income-tax*, (141 ITR 601), observed that "normally the rule is that where the law is laid down differently in two different decisions of the Supreme Court by Benches of different strengths, the decision of the larger Bench should be followed as binding on the High Courts. However, the doctrine that a larger Bench of the Supreme Court has more authoritative force than a smaller Bench is only as between cases which yield different *ratios decidendi* and not where one judgment hands down a decision while the other lays down a dictum.

5. Observation made in respect of part of a Section having material bearing on the Section as whole may be a precedent for other part. In *Kherawala (LB) v. Income-tax Officer (supra)*, the Gujarat High Court was to consider the applicability of S. 52(1). Reliance was placed on the ratio of the Supreme Court decision in the case of *K. P. Verghese v. ITO*, 131 ITR 597, which was opposed on the ground that as the decision was in respect of S. 52(2), the observation made in respect of Ss.(1) therein cannot work as precedent. The Court observed that the observations of the Supreme Court on the true interpretation of Ss.(1) cannot be regarded as mere passing observation. At the highest, they may be treated as *obiter dicta*. The Court held that even if the opinion of the Supreme Court on a point is regarded as *obiter dictum*, it is settled that if an opinion is expressed by the Supreme Court on the interpretation of a Section after careful consideration and such opinion is deliberately and advisedly given, the opinion would be binding on the High Courts.

6. There is a thin line between *ratio decidendi* and *obiter dicta*. The relevance and the weight of observations of higher Courts in matters before the same or lower Courts is often a contentious issue. While a clear relationship of the abstract principles of law with the issues involved provides a sure basis, even the remarks in passing, though technically obiter in nature, have determinative relevance, depending upon the context, purpose and the manner in which such remarks are made.

(Continued from page 431)

ACCOUNTING STANDARDS

asset, rather than as intangible asset (or financial asset), though most banks that finance such projects are quite clear that the asset in question is an intangible asset and not a tangible asset of the operator. The practice of questionable accounting for BOT contracts under Indian GAAP, treating the construction as a fixed asset, was a consequence of the inadequate guidance in Indian GAAP (discussed above) which is not as comprehensive as the guidance contained in IFRIC 12. Nevertheless, once IFRIC 12 interpretation is issued (in India), it would not only dramatically change the accounting of BOT contracts, but also have significant tax consequences for operators.

CIC's decisions :

r2i

Right to Information

Narayan Varma
Chartered Accountant

- **Provisions of S. 6(3) of the RTI Act :**

Very often the information sought by an applicant is not in the possession of the PIO or the subject matter is not within the jurisdiction of that public authority. In such cases, S. 6(3) has made very important and interesting provision. The same reads as under :

6(3) Where an application is made to a public authority requesting for an information, :

(i) which is held by another public authority; or

(ii) the subject matter of which is more closely connected with the functions of another public authority,

the public authority, to which such application is made, shall transfer the application or such part of it as may be appropriate to that other public authority and inform the applicant immediately about such transfer :

Provided that the transfer of an application pursuant to this sub-section shall be made as soon as practicable, but in no case later than 5 days from the date of receipt of the application.

An interesting issue came in appeal before the Central Information Commission. The information was sought as under by one Mr. Jagdish Rana from the Ministry of Personnel, Public Grievances & Pensions, Department of Personnel & Training (DoPT) :

1. "Copy of the 'Noting' and Copy of the compliance Report is requested under the RTI Act, 2005 made and issued by the Ministry of Finance, etc. as per directions of the Jt. Secy., Govt. of India in Para No. 6 of the Office Memorandum No. 28034/7/86-Estt/T, dated 3-4-1985 or 3-4-1986, issued by the Ministry of Personnel, Public Grievances (Dept. of Personnel & Training), New Delhi, regarding "Posting of Husband and Wife at the same Station".
2. "Any other corrigendum, if any, issued/circulated in regard to the reference mentioned above, may also be clarified and supplied, whether the joint posting is applicable in our case when my wife Smt. Sushma Kumari is employee of Rajasthan State Govt. since July 1974 and I am employee in the Delhi Police (Essential Services) and in service as handicapped, wife is also facing long illness ?"

In response, the DoPT forwarded photo copy of the Department's OM in question, for which he had not asked and no other information. The first appeal also failed.

At the appeal hearing before the CIC, the Appellate Authority was asked why, where the question did not pertain to his Ministry, they did not transfer the request u/s.6 (3). To that, he responded by stating that the OM in question applies only to the Government of India and not to the State Governments and the issue on which information was sought pertains to the State Governments (Rajasthan & Delhi).

Based on the above, the CIC decided as under :

It was not clarified in the response of either the CPIO or the first Appellate Authority that the OM in question applied only to the Government of India and was, therefore, not applicable to the State Governments. This now stands clarified in the CPIO's response to the appeal notice. This was, no doubt, the ground for the plea that the DoPT 'had no role', but this could have been clarified in the first instance for the convenience of the applicant.

On the other hand the CIC found that the Delhi Police does come under the authority of the Ministry of Home Affairs, decidedly a Central Government organisation. Hence this matter could have been transferred to the Ministry of Home Affairs. The appeal was therefore allowed and the case was transferred to the CPIO Shri N. M. Krishnan, Director (Police), Ministry of Home Affairs, for disposal u/s.7(1) of the RTI Act, 2005.

From the above, it appears that provisions of S. 6(3) would not apply when the application is to the public authority of the Central Government, but the subject matter pertains to the public authority of a State Government and *vice-versa*.

(*Shri Jagdish Rana v. DoPT*, Appeal No. CIC/WB/A/2007/00106, decided on 10-12-2007)

• **Information on Income-tax return :**

One Shri Anil Khare of Nagpur made an RTI application to the Income-tax Department, seeking copies of Income-tax returns, assessment orders, taxes paid and so on of the Vidarbha Cricket Association, Nagpur (VCA). Both the CPIO and AA declined to disclose the information, on the ground that this pertained to confidential information of a third party.

The appellant, before the CIC, argued extensively the justification for providing such information which according to him was in public interest. VCA on the other hand argued that most of the information sought is already in public domain and in the published annual reports; it further said that VCA was a public body, deeply conscious of its reputation and would not like anybody to impeach its reputation on the basis of contested Income-tax assessments, etc.

Before the CIC, the points of decisions were :

(a) whether the Income-tax Returns filed by VCA could be said to be exempt from disclosure u/s.8(1)(d) and u/s.8(1)(j) of the RTI Act.

(b) whether the public interest override proviso u/s.8(1)(j) and u/s.8(2) applies in this case.

The CIC decided vide the order dated 10th December 2007 as under :

"It has been the decision of this Commission in the cases *Mrs. Shobha R. Arora v. Income-tax, Mumbai,* (Appeal No. CIC/MA/A/2006/00220; Decision No. 119/IC(A)/2006; date of decision : 14-7-2006) and *Ms. Neeru Bajaj v. Income-tax,* (Appeal Nos. CIC/AT/A/2006/00644 & CIC/AT/A/2006/00646; date of decision 21-2-2007) that Income-tax returns are not liable to be disclosed under the exemption S. 8(1)(d) and S. 8(1)(j) of the RTI Act. The same applies in the present case as well."

"The question now is whether those exemptions could be superseded by the public interest override u/s.8(1)(j) and u/s.8(2) provisos. As has been pointed out by the third-party's representative, all information which forms the basis of the Income-tax return filed by VCA already figures in the Annual Reports of the Association. These are audited documents and are publicly available. All the information which the appellant needs — for that reason any other person — can be had from the Annual Reports of the VCA. It doesn't seem necessary that he should be allowed access to the Income-tax returns of the VCA to obtain the same information which is otherwise available to him. The Commission is also in agreement with the third party that extreme caution has to be exercised before an Income-tax return of an assessee and the corresponding assessments be allowed to be made public."

"A mere allegation of wrongdoing on part of an assessee by an interested person cannot provide the rationale for invoking the public-interest override of S. 8(2). Nothing which the appellant has stated before the Commission would qualify to be sufficient justification to invoke the public interest clause to supersede the exemption and allow disclosure of the Income-tax returns of the VCA. The Commission cannot also be oblivious of the concern of the VCA that given the history of dispute between the appellant and the VCA, it is quite possible that by allowing access to the appellant to the VCA's Income-tax returns, an opportunity would be provided to him to besmirch the reputation of the VCA through propaganda and allusion. The VCA is understandably not willing to be drawn into controversies where it would be required to give explanations to unsubstantiated and motivated charges. The VCA also rightly stated that no return is complete till its final adjudication is over. Any premature disclosure would be liable to be misinterpreted and used as a tool to impeach the reputation of the VCA."

Based on the above, the appeal was rejected.

[*Shri Anil Khare v. CIT-I, CCIT and others,* Appeal No. CIC/AT/A/2007/00921, decided on 10-12-2007]

The RTI Act

Reporting on the judgment of the High Court of Gujarat (the Court) — continuing from November and December, 2007 issues.

The third issue decided by the Court is regarding the provisions and proceedings u/s.18 and u/s.19 of the RTI Act.

The Court ruled that the State Information Commissioner has no power or jurisdiction to pass an order u/s.18 as he did, under which he

remanded the matter to the first AA. According to the Court there is no provision in the Act remanding such application to AA, because it was a complaint u/s.18 and it violates the principle of natural justice as it was so remanded without calling the third party. The Court ruled as under :

"(i) The Information Commission has no authority or jurisdiction to pass an order directing the Appellate Authority to part with information u/s.18 of the Act.

(ii) The order clearly indicates that the Appellate Authority is left with no discretion except to issue suitable directions and to arrange to provide information.

(iii) No scope has been left for the Assistant Public Information Officer or the Public Information Officer to decide the matter considering the provisions of S. 11.

(iv) Direction is given that the lower authorities should not only provide information, but also furnish to the Commission the information so provided.

(v) The power u/s.18 is limited to hold an inquiry into a complaint and if necessary, impose penalties u/s.20. It is not an appellate power, for the appellate power is found in S. 19.

(vi) The effect of the order dated 31-1-2007 is that the petitioner has been completely deprived of statutory right of appeal. This would be evident from the fact that the Labour Commissioner has been directed to furnish information and further the Labour Commissioner has directed in turn the Assistant Labour Commissioner vide order dated 9-3-2007 to disclose the information. All appeals in the circumstances have become nugatory. Alternative remedy, which would be generally available, is completely lost in view of the order passed by the Information Commissioner."

The Court did not much analyse the scope of S. 18 read with S. 19 and the point was kept open whether S. 18 and S. 19 are working independently or not. A thing which cannot be done directly can never be done indirectly. A right vested in the third party directly u/s.11(1) read with S. 7(7) of the Act, 2005 cannot be taken away by the respondent No. 1, treating the application preferred by the original applicant dated 7th September 2006 as the complaint u/s.18 of the Act, 2005. In other words, information, which cannot be given u/s.7, can never be given u/s.18. Because S. 7 is to be read with S. 11(1), without hearing third party, no information can be supplied if it is relating to or supplied by the third party and has been treated as confidential by the third party. Thus, a grave error has been committed by the respondent No. 1 in passing the order dated 31st January 2007, which is apparent on the face of the record.

Other News

- **Governor of Maharashtra's travels :**

One Pune-based teacher sought the information about the travels of the Governor of Maharashtra who had been making frequent trips to his home state Karnataka at the expense of the State Government. In reply to the application under the RTI Act, it is revealed that Rs.35 lakhs had been spent on these 31 trips in the last 2 years. The Governor had been out of Maharashtra for more than 200 days during this period.

As a result of such disclosure under the RTI Act, it is interesting to note that stung by criticism, the Governor now has said that he will foot the bill himself including for official visits.

- **Stock exchanges :**

As reported in earlier issues whether BSE and NSE are covered under the RTI Act, the matter is to be decided by the Bombay and Delhi High Courts, respectively.

A Bench headed by the Chief CIC Mr. Habibullah had termed the Government's control over the functioning of stock exchanges as pervasive and said that bourses cannot be exempted from sharing information under the provisions of the Act.

The Chief CIC now wants the Supreme Court to resolve whether bourses can be brought under the purview of the RTI Act. The Commission is moving to get both the cases transferred to the Supreme Court.

- **Information on stolen mobiles from Delhi police :**

Delhi-based social activist Subodh Jain got a rude shock when he received a letter from Deputy Commissioner of Police (West) Robin Hibu, asking him to deposit Rs.13,949 as advance for information he sought on the number of cases of mobile thefts in the city, under the RTI Act.

"If I want information from each of the 10 police districts and I pay the said amount for each police district, then I may have to shell out Rs.1.5 lakh," Jain said, quoting the letter.

Hibu, in his letter, said the pointwise information sought by Jain was "lengthy and time-consuming" to compile. "In addition, a considerable strength of manpower of (Hibu's) office as well as all police stations will be utilised to compile this information," he said.

According to Hibu, a sub-Inspector from his office would have to be deputed for the job for two days, the cost of which was calculated at Rs.1,546. Apart from it, Jain would also have to pay Rs.1,353 for deputing a head constable for three days while another Rs.11,050 for 13 constables for their services for two days in this connection.

The dates for RTI Clinic in January are Saturdays, 5th, 12th and 19th : 11.00 a.m. to 1.00 p.m. at BCAS Premises.

Thoughts of the business of life

Edited by Lydia Forbes

Most people show more persistency in their first twelve months on earth than they show later in twelve years.

— B. C. Forbes (Founder, Forbes Magazine, 1917)

Children always take the line of most persistence.

— Marcelene Cox

Don't forget that compared to a grownup, every baby is a genius. Think of the capacity to learn ! The freshness, the temperament, the will of a baby a few months old !

— May Sarton

A child is fed with milk and praise.

— Mary Lamb

Children's talent to endure stems from their ignorance of alternatives.

— Maya Angelou

The universal line of distinction between the strong and the weak is that one persists; the other hesitates, falters, trifles, and at last collapses or 'caves in.'

— Ewin Percy Whipple

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ADVT.

Dr. K. Shivaram
Ajay R. Singh
Advocates

Allied Laws

16 ***Ex parte* Order : set aside.**

The advocate for the petitioner company had sought two weeks adjournment before the Settlement Commission. The Settlement Commission however granted only one week adjournment. On the date of hearing, the advocate could not remain present before the Settlement Commission, however, the director of the petitioner company was present. The Settlement Commission proceeded to pass the *ex parte* order.

The High Court held that in view of the complexity involved in the matter, in the larger interest of justice, the impugned *ex parte* order be quashed and the matter set aside for fresh hearing with a condition that the petitioner shall pay cost of Rs. 25,000 to the respondent.

[*Vishwa Traders P. Ltd v. UOI*, (2007) (217) ELT 191 (Bom.)]

17 **Hindu Succession Act; Prior to Amendment 1994 — Ancestral property.**

Father having 7 sons, 3 daughters and his wife (widow). His ancestral property prior to his death would be divided in eight equal parts *i.e.*, 1/8th for himself and 1/8th each for the seven sons. Each son will get 1/8th share in the total property. As married daughter could not get equal shares with sons prior to 1994 amendment.

On demise of father, his 1/8th share will go to his widow. It would be only on the demise of his widow the 7 sons and 3 daughters will get equal share in the share held by her.

On her death, the 7 sons and 3 daughters thus will each get 1/10th share from the 1/8th share of the total property.

[*Ramchandra Nathu Ghadage & Ors., v. Rajaram Nathu*, AIR (2007) NOC 2622 (Bom.)]

18 **Nominee : Insurance Act.**

On death of policy holder, all his legal heirs are entitled to the amount due under insurance policy in accordance with the Hindu Succession Act. Nominee alone is not entitled to the benefit. Nominee is only entitled to receive the amount.

The claim of other heirs cannot be frustrated only on ground that amount has already been released by insurance company in favour of nominee.

[*Smt. Somwati & Ors. v. Mahjpal & Ors.*, AIR (2007) (NOC) 2538 (UTR)]

19 **Right to Information Act — Public Information officer should give notice to third party if he intends to disclose information relating to third party.**

The important issue for consideration that arose in the matter is "Whether the third party is entitled to get written notice of request of applicant (who is seeking information) and get an opportunity of personal hearing before disclosure of information from the Public Information Officer ?"

The Gujarat High Court observed that it is a duty vested in the Public Information Officer to give an opportunity of personal hearing to the third party to get his submissions, whether he treats the information as confidential and whether information should be disclosed, if the information is relating to or is supplied by the third party.

When public body collects the information relating to or given by third party, it might not have been treated as confidential, but third party can make a submission that it is treating the said information as confidential. More so, when the information is relating to third party and is not even known to that third party, when and what information relating to third party, was collected by public body. Therefore, S. 11(1) of the Act, 2005, gives mandate to Public Information Officer to give written notice to third party if he intends to disclose information relating to third party.

[*Reliance Inds. Ltd. v. Gujarat State Information Commission & Ors.*, AIR 2007 Gujarat 203]

20 **Valuation of shares : Experts in the field of accountancy can consider the same — Cannot be challenged in Court.**

The shares of the target company had been valued by three firms of chartered accountants, namely, M/s. Deloitte Haskin and Sells who valued the

shares of the target company at Rs. 43.02 per share, M/s. Patni and Company who valued each share of the target company at Rs.64.17 and M/s. Chandha and Company who valued each share of the target company at Rs.60.04.

The Board accepted the valuation report of M/s. Patni and Company and by its order of August 19, 2005, approved the draft letter of offer incorporating the revised offer including interest.

The grievance of the appellants before the Securities Appellate Tribunal was that the Securities and Exchange Board (hereinafter referred to as the 'Board') as well as the merchant banker had not properly valued the shares of the target company in accordance with the parameters laid down in Regulation 20(5) of the Securities and Exchange Board of India (substantial Acquisition of shares and Takeovers) Regulations, 1997.

It was the case of the appellants that the valuation report of Patni & Co. did not take into account the return of net worth, the book value of the shares, or the earning per share. If these factors were considered, the value of each share would have been more than Rs.200 each.

The Appellate Tribunal dismissed the appeals preferred before it, observing that the valuation of shares could be impeached on the ground of fraud, mistake or miscarriage of justice. It could also be interfered with, if there was an apparent or arithmetical error or the valuers took into account something which ought not to have been taken into account or interpreted the regulations wrongly, or proceeded on some erroneous principles.

The Court observed that valuation of shares is a technical and complex issue which may be appropriately left to the wisdom of the experts, having regard to the many imponderables which enter the process of valuation of shares. If the valuer adopts the method of valuation prescribed, or in the absence of any prescribed method, adopts any recognised method of valuation, his valuation cannot be assailed, unless it is shown that the valuation was made on a fundamentally erroneous basis, or that a patent mistake had been committed, or the valuer adopted a demonstrably wrong approach or a fundamental error going to the root of the matter. Regulation 20(5) applies to infrequently-traded shares of a company. It lays down the parameters that must be taken note of and considered in arriving at the valuation. However, the parameters laid down are by no means exhaustive. The Regulation itself does not prescribe the weightage to be assigned to different enumerated parameters.

The weightage to be given to the different factors that go into the process of valuation, must be left to the wisdom, experience and knowledge of the experts in the field of share valuation. Such being the method of share valuation which involves subjective and objective considerations, there is considerable scope for difference of opinion even amongst experts. Even if correct principles are applied, different valuers may arrive at different valuations. Each one of them may be right, yet the valuations may differ. Mathematical precision and exactitude are not the attributes of share valuation, for at best the valuation arrived at by an expert is only his opinion as to what the value of the share should be. No doubt the variation may not be very wide between two valuations prepared honestly by two valuers applying the correct approach and the correct principles, but some variation is unavoidable.

Unless it is shown that some well-accepted principle of valuation has been departed from without any reason, or that the approach adopted is patently erroneous or that relevant factors have not been considered by the valuer or that the valuation was made on a fundamentally erroneous basis or that the valuer adopted a demonstrably wrong approach or a fundamental error going to the root of the matter, the Court would not interfere with the valuation of an expert. Valuation of shares is a technical and complex problem which can be appropriately left to the consideration of experts in the field of accountancy.

Therefore, the Court held that the board committed no error in accepting the report of Patni & Co.

[*G. L. Sultania & Anr v. SEBI & Ors.*, AIR 2007 SC 2172]

Salesmanship starts when the customer says no.

— George O. Boule, Jr.

P. N. Shah
H. N. Motiwalla
Chartered Accountants

ICAI and its MEMBERS

1. **Disciplinary case :**

In the case of *ICAI v. H.Mohanlal Giriya*, (December 2007, C.A. Journal, page 948), the Karnataka High Court has held that the Council of ICAI was justified in removing the name of the member from the Register of Members for a period of one year. In this case, the member was engaged in full time practice. He filed his Income-tax returns in the name of 'H. Mohanlal Giriya' and declared his professional income. He had also taken LIC agency in the name of 'H. M. Jain' and he filed a separate return of income in the name of H. M. Jain and declared income from agency commission in this return. This method was adopted during the years 1967-68 to 1986-87. In the first return, the name of father was shown as 'Heerachandji' and in the second return it was shown as 'F. H. Chandji'.

The Chief Commissioner of Income-tax filed a complaint before ICAI. It was reported that in the prosecution proceedings under the Income-tax Act, the member had compounded the offences. The contention of the member was that no action under the C.A. Act can be taken when offences under the Income-tax Act were compounded.

In a well-reasoned order the High Court has held that in the facts and circumstances of the case, ICAI can proceed against the member under the C.A. Act and the penalty for removal of the name of the member for one year was confirmed.

2. **Accounting for acquisition of shared manufacturing facility :**

Expert Advisory Committee (EAC) of ICAI has given an opinion on this matter as under (C.A. Journal December, 2007, page 922) :

(i) A company has three business units engaged in the business of manufacture and sale of paints, speciality chemicals and adhesives. The manufacturing facilities, *viz.*, effluent treatment plant, electrical substations, roads, fire-fighting facilities, weighbridge, canteen, etc. which are shared by all the three business units, are situated at a common site taken on lease by the company.

(ii) During the year, the company has divested its speciality chemicals business on going-concern basis for an agreed composite consideration. As per the terms of the sale agreement, a portion of the undivided land on which the manufacturing facilities of the divested business is situated, is being bifurcated for transfer to the purchaser. Certain shared facilities located on the portion of land so bifurcated, will also have to be transferred to the purchaser as a part of the aforesaid divestment. Due to the above divestment, the company will have to acquire/construct similar shared facilities at the site for its continuing business. Management estimates that such cost of acquisition/construction will be significant.

(iii) The company wants to record the sale of existing shared facilities as sale in the profit & loss account and record the acquisition/construction of new shared facilities as fixed assets. The EAC has given an opinion, relying on para 25-26 of AS-10 (Accounting for Fixed Asset), that this method of accounting is proper in the case of the company. The EAC is of the view that the alternate method of adjusting the sale proceeds of divested business against the cost of acquisition/construction of new shared facilities suggested to the company is not proper.

3. **Prospects for Members in Industry :**

ICAI had organised a Campus Placement Programme for members during August-October 2007 at 19 centres in India. Out of members who qualified in May 2007 examination, 1823 candidates participated in this programme. 252 Interview Boards representing 101 organisations interviewed the candidates and more than 60% of the candidates were selected for jobs in various industries. Highest salary offered to candidates for international posting in the above placement programme is Rs.12 lacs P.A., whereas for Indian posting it is Rs.11 lacs P.A. The following are the figures for salary range (C.A. Journal December, 2007 page 986) :

Salary range offered (per annum)	Number of candidates
Rs.9 lacs and above	32
Rs.7.5 lacs to 9 lacs	158
Rs.5 lacs to 7.5 lacs	606
Rs.3.5 lacs to 5 lacs	344
Rs.2.5 lacs to 3.5 lacs	13
Below Rs.2.5 lacs	Nil
Total	1153

4. **Exposure Draft — Proposed Accounting Standard (AS) 32 — Financial Instruments : Disclosures :**

(i) The objective of this Standard is to require entities to provide disclosures in their financial statements that enable users to evaluate :

(a) the significance of financial instruments for entity's financial position and performance; and

(b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the reporting date, and how the entity manages those risks.

The principles in this Accounting Standard complement the principles for recognising, measuring and presenting financial assets and financial liability as provided in Accounting Standard (AS) 30, Financial Instruments : Recognition and Measurement and Accounting Standard (AS) 31, Financial Instruments : Presentation.

This Accounting Standard shall be applicable to all entities for all types of financial instruments except those mentioned in the Standard. It will be recommendatory for 2 years for accounting periods commencing from 1-4-2009 and will become mandatory from 1-4-2011. This Standard does not apply to an SME.

The entity is required to disclose information that enables users of its financial statements to evaluate the significance of financial instruments as explained in detail in the Standard.

The Institute has invited comments on the exposure draft on or before 15-1-2008.

[Refer pages 1009 to 1024 of C.A. Journal, December, 2007]

(ii) The Institute has also issued Exposure Draft : Guidance on Implementing AS-32, Financial Instruments : Disclosures.

[Refer pages 1025 to 1032 of C.A. Journal of December, 2007]

5. **ICAI News :**

(*Note* : Page Nos. given below are from C.A. Journal for December, 2007)

(i) ***Auditing Standards :***

(a) *Standard on Auditing (SA) 240 (Revised)* — The Auditors' Responsibilities Relating to Fraud in Audit of Financial Statements — Released by ICAI (page 1037 — 1068).

(b) *Standard on Auditing (SA) 300* — Planning an Audit of Financial Statements — Released by ICAI (page 1069 -1076).

(ii) ***Accounting Standards :***

(a) *AS-22 — 'Accounting for Taxes on Income'*. This Standard has been held to be *intra vires* the Companies Act, 1956, by the Supreme Court. (page 910).

(b) *Proposed Limited Revision of Accounting Standards*

- AS-17 — Segment Reporting
- AS-19 — Leases

This revision is proposed in view of proposed AS-32 on Financial Instruments — Disclosures. (page 1033).

(c) *Limited Revision of AS-15 — Employee Benefits*

Text of the limited revision of AS-15, including revised Transitional Provisions, is published by ICAI (pages 992 and 1034-1036).

(iii) ***Empanelment with C&AG :***

Chartered Accountant Firms who had applied for empanelment for audit of public sector undertakings during Jan-Feb 2007 have to update their data (online) for the year 2008-09, even if there is no change in the constitution of the firm. Last date for this purpose is 29-2-2008 (page 992).

(iv) ***For students :***

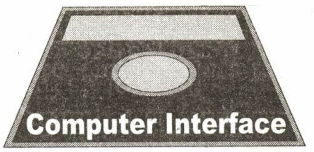
Board of Studies have withdrawn accreditation of all private computer training institutes which were imparting 100 hours' Information Technology training to C.A. Students w.e.f. 1-12-2007. Students are, therefore, advised to undergo 100 hours' I.T. training from accredited ICAI Branch Computer Centres.

10

The difference between getting somewhere and nowhere is the courage to make an early start. The fellow who sits still and does just what he is told will never be told to do big things.

— Charles M. Schwab

Samir Kapadia
Chartered Accountant



Tech update

It's been some time since my last write-up on what's hot and what's not. I have gathered a few tips and tools.

Gmail :

This word has become synonymous with email. Once upon a time, Hotmail was 'hot', today the so-called also rans have surpassed the pioneer. Though it possesses many excellent qualities, Gmail is far from perfect. Fortunately, there are some strategies that will give any user of Gmail a good chance of yielding a 'happily ever after'. I am sure that most of the readers may have a Gmail account and they would be using the same extensively, but I wanted to share my experience about a few of the features that can make the experience worth the trouble.

Gmail is catching up with times and is now offering up to 5 GB of space (rediff gives unlimited). Given the space available, a user can actually retain all the mails he receives. There are archiving features which one can use to archive all the mails that have been read and may not be required in the near future. Instead of deleting the mails, one can simply 'archive' the older/read mails. That way you may retrieve it in future. Gmail also has a host of other features like labels, filters. These can be customised and used for sorting and retrieving mails. It's one feature that I have started depending on. Apart from this, Gmails spam filter is quite good, combine it with filters and you could cut down the clutter substantially.

To tell you the truth, I have made it a habit of marking all my mails to my Gmail account. It's become my offsite back-up and also doubles up as my remote access mail box. No matter where I go, all I need is Internet access, all my mails (old and new) are available. If you really want to take advantage of Gmail on the fly, you must get a GPRS connection on your cellphone (works with PDA phones, Iphone as well as Blackberry). With the added convenience of Google Talk, Google Docs and spreadsheets, I can virtually telecommute. I am yet to experiment with the calendar option, but am confident that it will not let me down.

Open Office 2.0 The online version :

In my earlier write-ups, I have written about online desktops where a user needs only a basic PC cutting the cost per user. In my write-up on Mobility, I shared with you that you don't even need a laptop, all you need is a smart pendrive with OpenOffice loaded on it. On a similar lines, we now have Open-Office 2.0 which does not need any installation. Interested in trying out the free OpenOffice.org 2.0 office suite without having to install it on your computer ? Now's your chance. That option became possible this week when OpenOffice.org and online application vendor Ulteo launched a beta project that hosts OpenOffice.org 2.0 on Ulteo's Online Desktop infrastructure, giving users online access to the applications and up to 1GB of related data storage. In an announcement, the two groups said the project will be open to 15,000 beta users who will be able to access the applications using a Web browser on Windows, Linux or Mac OS X. Beta users will also have access to the project's instant collaboration features, which will allow participants to invite other users to join them online in working on a document together in real time. Users can send invitations to others via e-mail, allowing access to documents in either read-only or full-edit mode through a clickable link in the message.

Live Workspace file storage service from Microsoft :

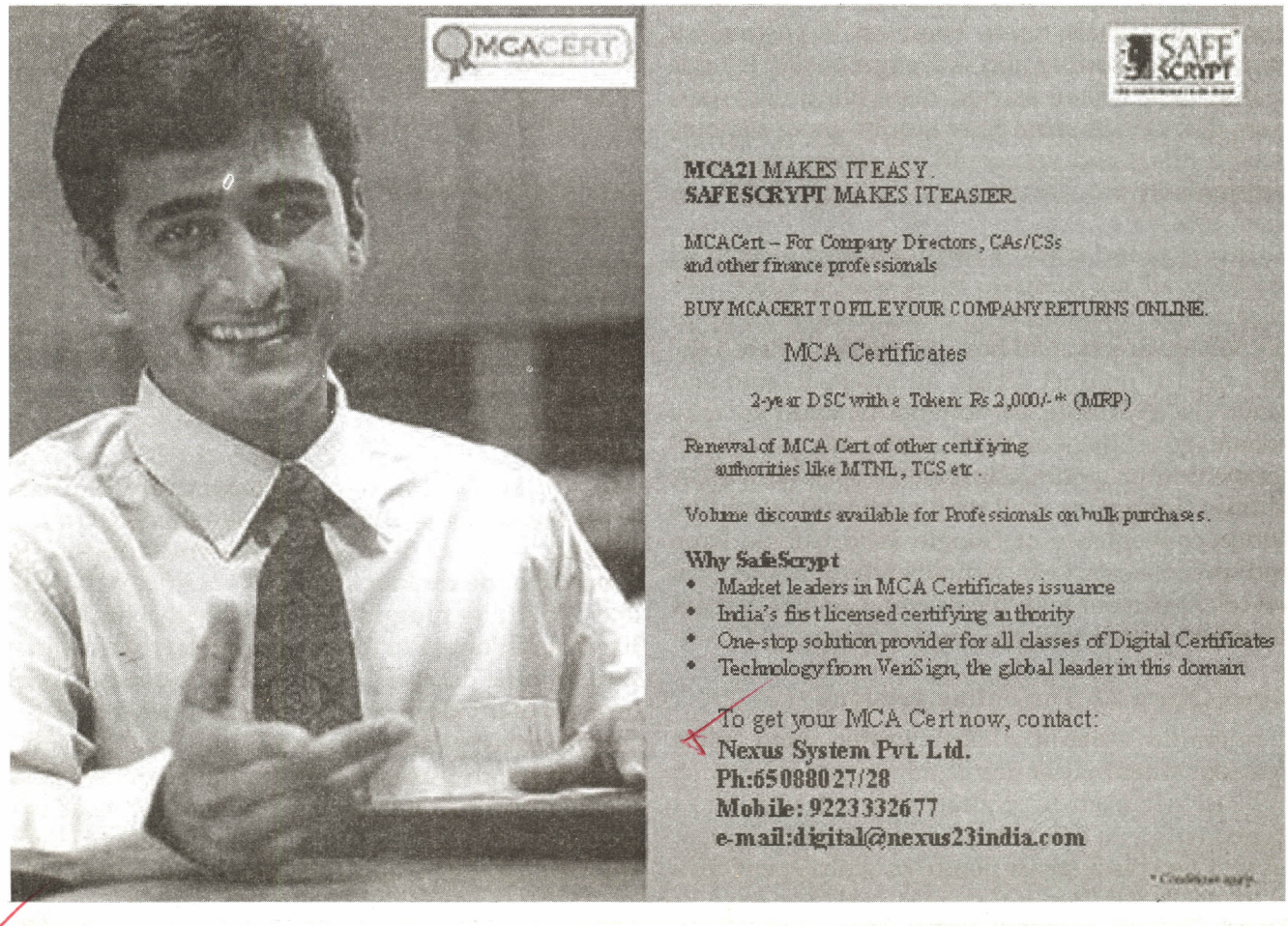
If you use Microsoft Office, you'll want to sign up for **Office Live Workspace**. Currently in beta, the free service offers online file-storage, document-sharing, and desktop-presentation features. It is likely to pose a challenge to *Google Docs and spreadsheets* & to *Zoho.*

But unlike those two productivity suites, **Workspace** *doesn't offer Web-based applications;* instead, it uses a free, **downloadable plug-in** to connect to the desktop versions of Office XP, 2003, and 2007. The plug-in installs a toolbar in Word, Excel, and PowerPoint that allows you to save new files to the Workspace site, add files already saved on your hard drive to the site, or open and edit documents previously stored online. The site supports both Internet Explorer and Firefox, (but the Firefox version lacks a useful ActiveX-enabled button that opens a stored document in the appropriate Office app with one click).

The tie-in to online storage (500 MB for the beta) contains a handy back-up and anywhere-access advantages. You can use the service to store your work documents and then access them from your home PC, for example. You also can share either individual documents or collections of documents called workspaces with anyone (*users will have to be logged in to the service to edit files*), and you can create online event or task lists that you can then synchronise with Outlook. If you're on a computer without Office, you can still preview files on the site or create simple, rich-text notes. Because you create and edit *Workspace-stored files in Office locally*, you need an Internet connection only to open a file from Workspace and save the file back there. Your changes will save the online copy when you're connected, but changes you make to the online version do not automatically synchronise with any locally-stored version (if you have one). This means you could end up with two — or more — versions of a document with the same name. *Google Docs and Zoho permit you to edit and save files online, which eliminates this potential problem.*

Workspace also throws in a bonus feature called **SharedView**, which is informally called the '**LiveMeeting Lite**.' Through it a user can invite another Workspace user to view your desktop or even take control. Office Live Workspace greatly extends the usability and convenience of Microsoft Office, but it's clearly still a beta. Most of the site wouldn't display on one of my test computers, and on the same machine, SharedView didn't work. Microsoft was unable to figure out the cause of the problems.

In the next write, I will share with you some tips on how to deal with issues like improving the speed, better network connectivity and trouble-shooting. Till then, Merry Christmas and a Happy New Year.



LAWS and Business

Cross-border acquisitions

Anup P. Shah
Chartered Accountant

1. Introduction :

1.1 In the last few Articles, we have examined whether an Indian company can merge into a Foreign company and whether a Foreign company can merge into an Indian company. Another more popular and faster method of cross-border restructuring is for a Foreign company to acquire an Indian company or an Indian company to acquire a Foreign company.

1.2 In this Article, let us study whether and if yes, **how a Foreign company can acquire an Indian company ?** This is a situation wherein a Foreign company buys out the shares of an Indian company from the shareholders of the Indian company. Thus, ultimately if the Foreign company is successful in acquiring majority of shares of the Indian company, then the Indian company would become a subsidiary of the Foreign company. Examples include the acquisition of 51.5% stake in Matrix Laboratories Ltd. by Mylan Laboratories, Inc., USA. Subsequently, Mylan made an open offer under the 'Takeover Regulations' and today has a 71% stake in the company. The relevant legal provisions in this situation are examined below.

2. Companies Act, 1956 :

2.1 There is no restriction under the Companies Act on Indian shareholders selling their shares to a Foreign company, nor is there any bar on an Indian company being held entirely by a Foreign company.

2.2 Prior permission of the Competition Commission under the Competition Act, 2002 should be obtained in cases where the said Act is applicable.

3. FEMA, 1999 :

3.1 Under the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, a Foreign company is permitted to purchase shares of an Indian company from its resident shareholders under the Automatic Route of the FIPB and the RBI. The conditions to be satisfied in this respect are as follows :

(a) The Indian company must be a company eligible for foreign direct investment under the Automatic Route.

(b) The SEBI Takeover Regulations must not be attracted. This effectively means that the sale must be for a stake which is equal to 14.99% or lower. In case the Acquirer (with persons acting in concert with it) already owns more than 15% but less than 55% in the 'Target company', then the Takeover Code is triggered if more than 5% is acquired in any financial year.

(c) The Sectoral Caps (if any) must not be breached.

(d) Financial Services Sector companies (*e.g.*, banks, insurance companies, NBFCs) are not covered under the Automatic Route. Hence, acquisition in this sector would require prior approval of the RBI. However, such acquisitions do not require the prior permission of the Foreign Investment Promotion Board ('**FIPB**').

(e) The pricing in case of listed companies must be according to the market value and in case of unlisted companies as per the fair value determined as per the CCI Guidelines.

(f) Form FC-TRS must be filed in quadruplicate along with relevant consent letters and other documents with the Authorised Dealer.

3.2 Acquisition not satisfying the above conditions would fall under Regulation 10A(b), which prescribes that transfer of shares/convertible debentures by a person resident in India to a person resident outside India requires prior FIPB/RBI approval.

3.3 At times a Foreign company sets up a wholly-owned Indian subsidiary which would make the acquisitions. In such a scenario, the FIPB permission would be required for setting up a holding company. Further, it needs to be borne in mind that the investment company cannot leverage Indian debt to fund the acquisition. If it wants to borrow, then it must do so from foreign sources.

3.4 Practical experience has shown that the RBI does not assent to transfer of shares from an Indian resident to a Foreign company in tranches. Hence, this is an aspect which should be borne in mind while structuring a transaction.

3.5 In several cases, the Foreign company desires to discharge the consideration not by way of cash, but by issuing its own shares. In such a scenario, the Indian shareholders would become shareholders of the Foreign company. This type of structure would require prior permission of the RBI.

4. SEBI Guidelines :

4.1 In case the Indian company is listed in India, and a Foreign company acquires a stake equal to 15% or more in the Indian listed company, the Foreign company would have to make a public (open) offer of up to 20% of the shares held by the public under the SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 1997. Continuing with the above example of Matrix Laboratories, Mylan had to make an open offer for 20% of the shares held by the public. The offer price must be **higher** of the following two prices :

(a) Negotiated price between acquirer and shareholders of target company

(b) Acquisition price paid by acquirer in 26 weeks prior to PA

(c) Higher of the average of :

- weekly high/low of closing prices during 26 weeks; or
- average of daily high/low of closing prices during 2 weeks

prior to the date of the public announcement. The public announcement is to be published in newspapers **within four working** days of entering into **Agreement** or **deciding** to acquire shares in a listed company.

4.2 Sometimes the Foreign company may acquire an Indian listed company and it may desire to delist the company. In such a case, it would have to follow the Delisting Guidelines issued by SEBI. If as a result of the acquisition, the non-public holding falls below the minimum level specified under the Listing Agreement (*e.g.*, 25%), then the Foreign company has to buy out the balance public holding in accordance with the reverse book-building process, wherein the acquirer quotes a floor price and the shareholders tender their bids for prices at which they want the acquirer to buy out their shares. The acquirer is free to accept or reject the bids. If he accepts the bids, then he must offer the same price to all shareholder for a period of six months from the date of delisting. If he rejects the bids, then he must ensure that the non-promoter holding is restored to the minimum level specified in the Listing Agreement.

For example, in the case of **'eServe International Ltd.'**, once it was acquired by Citibank Overseas Investment Corp., Citibank delisted its shares by following the reverse book building guidelines. The reason for delisting cited in this case was that Citibank wanted to keep several sensitive data confidential and away from the public domain.

5. Tax consequences :

5.1 The shareholders of the Indian company would have to pay Capital Gains Tax on the sale of shares by them to Foreign company, unless the shareholders are located in tax havens such as Mauritius, etc. The tax rate would depend upon whether the gain is 'long-term' or 'short-term' in nature and whether the shares are listed or unlisted. It may be noted that normally the listed shares would also be sold on an off-market basis and hence, the benefit of claiming the long-term gains as exempt would not be allowed to the shareholders of the Indian company as no STT has been paid. However, if these shares are sold through the stock exchange, *e.g.*, by way of a block deal, etc., then this exemption would be available as STT is leviable on 'block deals'.

5.2 The provisions of S. 79 are also relevant in this respect in case the Indian company is an unlisted company. S. 79 of the Act provides that in case of an unlisted company, any carry-forward and set-off of business losses and capital losses would not be allowed unless 51% of the voting power is beneficially held by the same persons on the last day of the year in which the loss is incurred and the last day of the year in which the set-off is claimed. Hence, in case the Indian company is an unlisted company and it has carry-forward business and capital losses and if more than 51% of its equity shares are acquired by a foreign company, then carry forward and set-off of losses would not be available. However, this section only applies in case of acquisition of equity shares and not to acquisition of preference shares. Further, as laid down by the Supreme Court in the case of *CIT v. Concorde*

(Continued on page 477)

miscellanea

Raman Jokhakar
Tarunkumar Singhal
Chartered Accountants

29 Mobile banking A bank in every pocket ?

Leonard Waverman of the London Business School has estimated that an extra ten mobile phones per 100 people in a typical developing country leads to an extra half a percentage point of growth in GDP per person. To realise the economic benefits of mobile phones, governments in such countries need to do away with state monopolies, issue new licences to allow rival operators to enter the market and slash taxes on handsets. With few exceptions (hallo, Ethiopia), they have done so, and mobile phones are now spreading fast, even in the poorest parts of the world.

As mobile phones have spread, a new economic benefit is coming into view : using them for banking, and so improving access to financial services, not just telecom networks, pioneering m-banking projects in the Philippines, Kenya and South Africa show the way. These 'branchless' schemes typically allow customers to deposit and withdraw cash through a mobile operator's airtime-resale agents, and send money to other people via text messages that can be exchanged for cash by visiting an agent. Workers can then be paid by phone; taxi-drivers and delivery-drivers can accept payments without carrying cash around; money can be easily sent to friends and family. A popular use is to deposit money before making a long journey and then withdraw it at the other end, which is safer than carrying lots of cash.

There is no need to set up a national network of branches or cash machines. M-banking schemes can be combined with microfinance loans, extending access to credit and enabling users to establish a credit history. Some schemes issue customers with debit cards linked to their m-banking accounts. All this has the potential to give the 'unbanked' masses access to financial services, and bring them into the formal economy.

(*Source* : The Economist, 17-11-2007)

30 71% tax trauma for India Inc : Study

Indian corporates face a total tax burden as high as 70.6%, according to a World Bank IFC-PwC study, Paying Taxes, 2008.

India ranked 165 in the overall paying taxes ranking, however, has got an overall better ranking for ease of paying taxes than China, which is at 168. It scores ahead of its eastern neighbour on two key parameters, lower total tax rate, India (70.60%) to China (73.90%).

The total tax burden includes not just corporate taxes, but also various state taxes such as VAT, municipal charges, pollution tax and social security contributions borne by a company.

The report includes a special coverage on a like-to-like comparison of the Bric economies (Brazil, Russia, India & China). 'At 165, India has an overall better ease of paying taxes ranking than China (168), and scores ahead of its eastern neighbour on two key parameters; a lower total tax rate India (70.60%) to China's (73.90%), and time to comply index where it scores ahead of Russia and Brazil also,' it highlighted.

(*Source* : The Economic Times, 20-11-2007)

31 PCAOB Fines Deloitte $1 Million

The Public Company Accounting Oversight Board has censured and penalised Deloitte & Touche $ 1 million for not following the PCAOB's auditing standards during a 2003 audit. Deloitte had knowingly allowed one of its partners who was apparently not having enough competence to lead an audit of a drug maker's financials for almost four years, according to the PCAOB.

"Deloitte failed to exercise due professional care in the performance of the audit and failed to obtain sufficient competent evidential matter to support the opinion expressed in the audit report," the PCAOB wrote in its order announcing its settlement with the audit firm, released on Monday.

Deloitte has agreed to pay the penalty and implement procedural changes without admitting or denying the audit-firm overseer's findings.

The PCAOB concluded that the audit partner failed to comply with the auditing standards requiring him to "exercise due professional care, exercise professional skepticism, obtain sufficient competent evidential matter ... and supervise assistants."

Deloitte resigned after nearly four years as Ligand's independent auditor in August 2004. At the time, Ligand noted that the auditor's reports on the previous two fiscal years "had contained no adverse opinion or disclaimer of opinion, and were not qualified or modified as to uncertainty, audit scope, or accounting principles."

But in mid-2005, Ligand announced it would restate nearly three years' worth of financials, all of which had been audited by Deloitte. For 2003, Ligand had to make a 52% adjustment for its product sales revenues, or $ 59 million less than it had previously reported.

That restatement led to an investigation by the Securities and Exchange Commission, which is still ongoing, according to the company's most recent 10-Q.

(*Source* : CFO.com, 11-12-2007)

$ 4 trillion

The amount by which Britain is getting sued for colonising Malaysia by an ethnic Indian in the country.

(*Source* : DNA, 25-11-2007)

Government Securities Act, 2006 comes into force from December 1st, 2007

The Government of India has notified December 1, 2007 as the appointed date on which the Government Securities Act, 2006 will come into force. Government Securities Regulations, 2007 will also come into effect from the same date, *i.e.*, December 1, 2007.

It may be recalled that with a view to consolidating and amending the law relating to the Government securities and its management by the Reserve Bank of India, the Parliament had enacted the Government Securities Act, 2006 (the Act). The Act received the assent of the President of India on August 30, 2006 and was published in the Gazette of India, Extraordinary, Part II — Section I on August 31, 2006 for general information.

The Act applies to the Government securities created and issued, whether before or after the commencement of the Act, by the Central or a State Government. Accordingly, the Public Debt Act, 1944 will cease to apply to the Government securities. The Indian Securities Act, 1920 has been repealed.

(*Source* : Internet news, 3-12-2007)

CBDT plans to nab tax evaders with STT

Securities Transaction Tax (STT) is all set to become an effective tool for generating intelligence about income made from market operations. The Central Board of Direct Taxes is examining ways of using the STT data on the lines of annual information return (AIR) to nab tax evaders.

The data contained in STT returns is quite useful for verification of the genuineness of the transactions carried by investor or trader, with PAN serving as a link. With the boom in stock market attracting many more, the Income-tax Department feels that STT data could turn out to be an effective intelligence tool to track tax evaders.

However, transactions in derivatives trading attract lesser STT of around 0.017%. STT collections registered a growth of 57.61 % to Rs.3,783 crore in April-October 2007.

(*Source* : www.economictimes.com)

Company secretaries allowed to advertise services

Company secretaries are set to become the first class of professionals to be allowed to advertise their services in India. The regulatory body that governs the profession is going to allow company secretaries to advertise in print, electronic and Internet media from January 1, 2008. Other professionals like doctors, engineers, chartered accountants and lawyers do not yet have this privilege.

The Institute of Company Secretaries of India (ICSI) has come out with the draft do's and don'ts for these professionals while advertising their services. "We hope to finalise the draft guidelines at a Council meeting later this month," ICSI President Priti Malhotra told ET.

The practising company secretary or the firm will have to give a declaration stating that all facts about the services are accurate. There should also be a disclaimer that ICSI has no responsibility over the contents of the advertisement by the individual professional or firm.

The proposed advertisement format for the professionals and firms could include details about willingness and unwillingness to accept work in certain areas, fees, names of clients and services rendered, speed of service and honours received, in addition to other primary details about the individual or the firm. There are separate requirements for advertisement through the website.

(*Source*: The Economic Times, 8-12-2007)

36 On your behalf

With the share of collection from tax deducted at source (TDS) declining from above 40% of gross collection in financial year 2001-02 to 27% in 2006-07, alarm bells have rung in the Revenue Department. TDS from Government departments particularly has been very low. The Government is now switching over to a new system of accounting of TDS payment. The new system envisages that all Central and State Government DDOs should be asked to apply for TAN and they would be required to make payment of TDS in accordance with the provisions of Income-tax rules.

(*Source*: The Economic Times, 28-11-2007)

37 UP to implement VAT from Jan. 1, 2008

The Uttar Pradesh Government decided to implement value-added tax (VAT) from January 1, 2008.

A decision to this effect was taken at the State cabinet meeting presided over by Chief Minister Mayawati on Friday, an official release said.

Earlier, the Government had decided to implement VAT from December 1, 2007, but following President's late approval to Uttar Pradesh Value Added Tax Bill, 2007, delayed it, the release said.

(*Source*: The Economic Times, 7-12-2007)

Readers' Views

To,
The Editor,
BCAJ, Mumbai

Re: **Salary and Government concessions for a Member of Parliament (MP)**

Respected Sir,

With reference to 'Salary and Govt. concessions for a Member of Parliament (MP)' in 'Miscellanea' section of your journal, I would like to express my views.

They are taking democracy for a ride. Are they elected representatives or elected rulers? I wonder how our economist-turned-politician turned Finance Minister P. Chidambaram, who pesters for more and more taxes from the citizens of this country, does not bother about the huge expenditure (nearly Rs.855 crores) on his colleagues including himself. It is said that equity is alien to tax laws. The same principle is aptly and unfortunately applicable to our Finance Minister. Why? Can he ever think to bring 'services' of these elected rulers under service tax? Can he ever think to tax the value of 'fringe benefits' enjoyed (exploited?) by these elected rulers? can he ever accuse any Minister in the Cabinet or MP in the Parliament itself of corruption allegedly committed by him, even if he is aware of the fact? He will never do that, since equity is alien to him.

I think an economist with a 'demon face' is always desperate for tax collection, whereas an economist with a 'human face' bothers about the end use of the tax collected from the taxpayers for the welfare of the people.

With regards,

— Aviansh Rajopadhye,
Pune.

A dinner lubricates business.

— Baron Stowell

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LIGHT  ELEMENTS

Countrymen and politicians be aware, Bapuji is coming

Avinash Rajopadhye
Chartered Accountant

Bapuji was busy that day in the morning spinning yarn on his favorite wooden Charkha. Ba, I mean Kasturba, better half of Bapuji, was performing morning ritual, sprinkling water to plants. Bapuji's sheep was grazing nearby river Ganga just stone's throw away from the Ashram. It was a pleasant view indeed. They were together in the heaven since 1948. It is true that Bapuji joined Ba later.

Ba finished her work and sat beside Bapuji and while sorting and cleaning cotton bolls, she said,

"Bapuji, life in the heaven has become dull, what do you think ?"

"I don't think so, remember the life on the earth, we fought desperately to liberate one country. What is the name of that country Ba ?" Bapuji asked, checking the thinness of the yarn coming out of the Charkha.

"Wow ! You forgot ? It is Bharat or Hindustan in our times, now known as 'India'. You know, politicians from rank and file, particularly from the Congress party observe your birth and death anniversary with great enthusiasm and fanfare, they showcase their loyalty to your ideology by wearing Khadi clothes, replied Ba.

"Oh my God ! I remember, in 1947 we liberated that country from British Rule of 150 years." Bapuji became nostalgic.

"Ba, I recollect everything right from the day one of my political career on the earth. After qualifying as barrister, I went to South Africa to practise as a lawyer, but I fought for black labourers against white rulers. There I found the power of 'truth and non violence'. My entire life was a laboratory to experiment with truth, truth and truth. When I was finally back in India, I slogged for independence of my motherland 'Bharat Mata'. 'Satyagraha' (non resistance) and 'ahimsa' (non violence) I translated into practice with the support of millions of Indians and made the British to quit India. I struggled for bringing humanity in the world. I propagated 'religious unity', not 'secularism' in today's form, throughout my life in the country. But I failed in my pursuit miserably and the partition . . . Pakistan . . . unprecedented massacre . . . I was on my way to prayers . . . three bullets pumped into my chest . . . Hey Ram . . . (Bapuji's eyes moistened). Ba put her hand on the shoulder of Bapuji and consoled him. "Bapuji, control yourself."

When Bapuji recovered from the nostalgic frame of mind he said to Ba,

"Let us have a look at the country for which we had dedicated our lives right from 1948 till today." The moment Bapuji expressed his desire, events after events flashed in the sky;

" Ba, look at Jawahar taking oath of office of the First Prime Minister of India, 26 January 1950, . . . thereafter his daughter Indira Gandhi became Prime Minister . . . imposed emergency in the country to cling to the power . . . assassinated by bodyguards . . . look ahead, her son Rajiv Gandhi became Prime Minister . . . he too was assassinated, Oh my God, the Indian National Congress party is not dissolved till today, now it is headed by Sonia Gandhi wife of Rajiv Gandhi, all from Nehru-Gandhi Family. It is disgusting-Indian National Congress has become a family property, look at that young chap, who is he ? Rahul Gandhi ! Prime Minister in the offing, . . .

Ba, look at that anti-brahamin riots after my assassination in 1948 . . . war with China . . . wars with Pakistan . . . burning Punjab . . . Blue Star operation . . .

Ba, look at that anti-Sikh riots after the assassination of Indira 1984 , mayhems after mayhems of Harijans, backward natives, landless labourers in Uttar Pradesh, Bihar, . . . Madhya Pradesh, . . . Hindu–Muslim riots all over the country ..... farmers committing suicides . . . strikes and bandhs of trade unions, political parties and so-called torch-bearers

for any social cause ... sabot-aging and looting of public properties ... whipping up of communal hatred by leaders ... agitations for reservations ...

... Look at demolition of Babri Masjid and attacks on temples, churches and gurudwaras ... killing of religious heads ...

... Conflicts on sharing of river water, boundaries, development priorities between States, conflicts between the Centre and States ...

... Look at those elections of representatives of grampanchayats, nagar parishads, corporations, State assemblies and the Parliament, not free and fair, no ethics ... horse trading, defections, vote for note, rampant corruption, booth capturing, castism, communalism, vote banks, appeasement of minorities ... candidates with criminal records, candidates contesting elections from jail, corrupt candidates getting elected enacting laws of the land, dirty politics everywhere in nooks and corners of the country ... shame, shame, disgusting ...

... Ba, look at those elected representatives behaving like elected rulers with bodyguards around them, sitting in air-conditioned offices, living in bungalows, travelling by planes, drawing huge salary and amenities, squandering people's money in the name of development, social welfare, maintenance of law and order in the country, competition with the developed countries, on the displaced priorities everywhere ...

... Ba, look at the demon of corruption ... cash for query in the Parliament, ... Stalling of Parliament, walk-outs, manhandling, abusing each other, power-crazy politicians, ministers and bureaucrats committing scandals after scandals running in crores ..., guns and ammunitions, medicines, oil, food, water, roads, bridges, houses ... dams .... hospitals ... educational institutes .... even not sparing animal fodder ....

Ba, I can't see this any more, this is not the country of my dream." Bapuji got exhausted and put his palms on his eyes. He was literally weeping like a child.

Again Ba consoled Bapuji, "Bapuji don't be so sentimental, don't be so emotional. You did your duty assigned by the almighty, snap your earthly ties, you are a Karmayogi, it is obvious, you get upset and disgusted, having seen the plight of the country you loved. Bapuji you will never go back to the earth. Cool down Bapuji, cool down."

She took Bapuji inside the hut, Bapuji's favourite place in the heaven, so he called it Muktidham. Somehow he controlled himself. For a while he was musing over what went wrong.

Chanting "Narayan Narayan" Naradmuni entered into the Ashram. Bapuji hurriedly came out of the Muktidham with his famous toothless smile to greet Naradmuni.

"Narayan, Narayan, how are you, Bapuji ?" asked Naradmuni. Instantly, Bapuji touched the feet of Naradmuni.

"Gurudev, I am quite happy and satisfied here in the heaven" Bapuji responded.

After exchange of a few pleasantries, Naradmuni gave a breaking news to Bapuji.

"Bapu, you know, yesterday there was a long discussion among heavyweights Brahma, Vishnu and Mahesh at Kailash Parbat. They were concerned about 'Bharat Bhoomi' on the earth. After lot of deliberations Bhagwan Mahesh suggested to reincarnate you on the earth for bringing back the old glory of Bharat Bhoomi and this suggestion is endorsed by all, so I am here to take you to Kailash Parbat right away."

Bapuji was shell-shocked. He felt that he was thrown in hell. There was a long pause.

"Gurudev, before your arrival Ba and me just saw the glimpses of Bharat Bhumi. I will never go back to that country, never," Bapuji hesitated.

"Bapu it's a wish of Brahma, Vishnu and Mahesh. You will have to come with me" said Naradmuni. Bapuji and Naradmuni left the Ashram and reached Kailash Parbat. The entire galaxy of gods had assembled on the Kailash Parbat. Some of them were discussing about possible choices in hushed voices. One suggestion was Hitler the erstwhile dictator, now in hell, would be the best choice for the people of Bharat Bhoomi. Somebody suggested why not Saddam Hussein, he is quite young in hell. With the arrival of Bapuji, Bhagwan Vishnu ordered, "Silence please" hush fell on the Kailash

and Bhagwan Vishnu proceeded further.

"Bapuji, you know why we called you here. As usual, Naradmuni must have told you."

"Yes my Almighty" said Bapuji in depressed voice. His famous toothless smile was nowhere on his face.

"Bapuji, It's a great privilege for me to announce that we have decided to reincarnate you on the earth to bring back old glory of Bharat Bhoomi. Very soon you will be back on the earth" declared Bhagwan Vishnu. There was loud applause echoing in heaven. The moment the applause died down Bapuji rose with folded hands and said,

"My Lord, I am sorry, I regret to say that I don't want to go back to Bharat Bhoomi".

The whole galaxy of gods was stunned. With wide open eyes they were staring at Bapuji.

It was really unexpected of Bapuji.

"Why ?" Bhagwan Mahesh thundered.

"My Lord, I can cite several reasons for my 'no' to the reincarnation, but I will list a few of them before this august galaxy of Gods. First of all it is not the country of my dream. There is deterioration of values in all walks of life, be it social, religious, economic, education or political, right from intellectuals to illiterates. The common man on the street is being corrupted by the so-called power hungry leaders coming from the grassroot level, where grassroot itself is being poisoned systematically and relentlessly. They call my ideology 'Ghandhigiri' on the lines of 'Gundagiri or Dadagiri'. My lord it's a sheer mockery of my ideology.

My Lord, Bharat Bhoomi, once called Ram Rajya, has become a slaughter house of human beings. Every day innocent people are being killed mercilessly in the name of Ram, Rahim, Jesus . . . or for political ambitions, bomb explosions, mass killings. My idea of 'religious unity', I mean prominence of all religions but dominance of none, has been tarnished to gain political mileage in the name of 'secularism'. Human life has no value. My Lord, terrorism all over the world, a new menace to human race not known to me, it is a new threat to the very existence of human race. But who bothers ? None !"

Bapuji paused for a while and sipped 'amrut', heavenly water. He proceeded further . . .

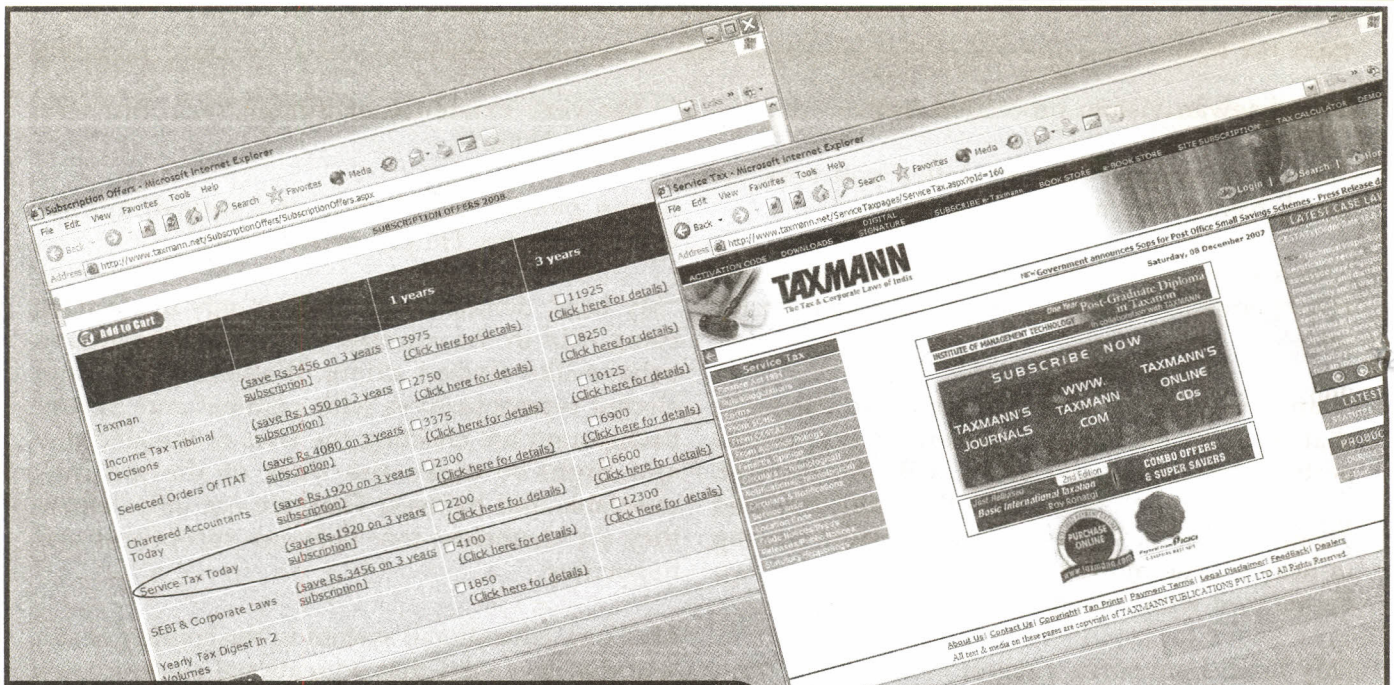
"My Lord, democracy is evident only in elections being held in the country. Elected representatives behave like elected rulers. It's hard to see that elected representatives with criminal and corrupt background are enacting the laws of the land day and night to make the lives of the millions miserable and hapless. They are not only selfish, they are shameless too. They are sycophants and hypocrites . . .

My Lord, educational system in the country is at a low ebb. It is said that educational system helps build the character of individuals and in turn the whole society. My Lord, the state of educational system in the country is so pathetic and horrible, it is churning out graduates more dangerous than school dropouts. Education has become business, a source of amassing wealth for selfish and so-called educationists and politicians.

My Lord, I would like to quote the statement made by the then Prime Minister of England Mr. Winston Churchill. He was my contemporary and I quote, "Liberty is man's birthright. However, to give the reins of Government to Congress at this juncture is to handover the destiny of hungry millions into hands of rascals, rogues and freebooters. Not a bottle of water or a loaf of bread will escape taxation; only the air will be free and the blood of these hungry millions will be on the head of Mr. Atlee. India will be lost in political squabbles. It will take a thousand years for them to enter the periphery of philosophy of politics. Today, we hand over the reins of government to men of straw of whom no trace will be found after a few years." unquote, My Lord, my all efforts have been going to selfish dogs. My Lord, Mr. Churchill was a great visionary. I salute him.

I can't rebuild this country. I can't save this country from the clutches of rascals, rogues and freebooters. I don't want to become 'father' of the ever-growing population with declining 'nationalism'. I don't see any 'unity in diversity', but I see only more and more diversity in diversity. This country has been pushed to the point of no return over a period of

(Continued on page 477)



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Full text of relevant Notifications, Circulars and Forms are available on the BCAS website : www.bcasonline.org

SPOTLIGHT

Part A : DIRECT TAXES

Pinky Shah
Sonalee Godbole
Gaurang Gandhi
Chartered Accountants

33 Extension of time limit for filing returns of income for some specific assessees : Press Release No. 402/92/2006-MC (56 of 2007), dated 14-12-2007.

Pursuant to the orders of few jurisdictional High Courts, few assessees have filed their return of income in Saral Form, instead of the new Forms which have been notified by the CBDT for A.Y. 2007-08. The Supreme Court has set aside the said orders and hence those returns filed in Saral Form would be deemed to be invalid. Accordingly, for those assessees who have filed their return of income for the A.Y. 2007-08, after 14-5-2007, in a Form other than the new Forms notified, the time limit has been extended till 29-2-2008, to file returns in the new Forms. Consequently, there would be no levy of penalty and interest.

34 Amendment to the Banking Term Deposit Scheme, 2006 : Notification No. 289/2007, dated 13-12-2007.

The Central Government has formulated the Bank Term Deposit (Amendment) Scheme, 2007 which provides that in case of jointly held accounts, in the event of death of the first holder, the term deposit can be encashed by the other holder on providing the proof of death to the bank manager.

35 Procedure for selection of cases for scrutiny for non-corporate assessees for A.Y. 2007-08.

In supersession of earlier instructions on the above subject, the Board hereby lays down the following procedure for selection of returns/cases of Non-corporate assessees for scrutiny during the current financial year *i.e.*, 2007-08.

2. The following categories of cases shall be compulsorily scrutinised :

(i) All assessments pertaining to search and seizure cases.

(ii) All assessments pertaining to surveys conducted u/s.133A of the Income-tax Act.

(iii) All returns where deduction claimed under Chapter VIA of the Income-tax Act is Rs.25 lakhs or above in stations other than the cities on computer network.

(iv) All returns, including those of non-residents, where refund claimed is Rs.5 lakhs or above in stations other than the cities on computer network.

(v) (a) All cases in which the CIT (Appeals) or ITAT has confirmed an addition/disallowance of Rs.5 lakhs or above, or if the assessee has conceded an addition in any preceding assessment year and identical issue is arising in the current year. But if the issue involves a substantial question of law, the cases may be picked up for scrutiny, irrespective of the quantum of tax involved. However, if the addition has been deleted by a superior Appellate Authority and the Department has accepted that decision, the case need not be taken up for scrutiny.

(b) All cases in which an appeal is pending before the CIT (Appeal) against an addition/disallowance of Rs.5 lakhs or above, or the Department has filed an appeal before the ITAT against the order of the CIT (Appeal) deleting such an addition/disallowance and an identical issue is arising in the current year. However, as in (a) above, the quantum ceiling may not be taken into account if a substantial question of law is involved.

(vi) All returns filed by statutory bodies, marketing committees and other authorities assessable to Income-tax.

(vii) All cases of banks and non-banking financial institutions with deposits of Rs.5 crores and above.

(viii) Cases of universities, educational institutions, hospitals, nursing homes and other institutions for rehabilitation of patients

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(other than those, which are substantially financed by the Government), the aggregate annual receipts (including donations credited to the corpus/any other fund) of which exceed Rs.10 crores in Delhi, Mumbai, Chennai, Kolkata, Pune, Hyderabad, Bangalore and Ahmedabad and Rs.5 crores in other places [Ref. S. 10(23c) & Rule 2 BC].

(ix) All cases where exemption is claimed u/s.11 of the Income-tax Act and the gross receipts (including donations credited to the corpus/any other fund) exceed Rs.5 crores in Delhi, Mumbai, Chennai, Kolkata, Pune, Hyderabad, Bangalore and Ahmedabad and Rs.1 crore in other places.

(x) (a) All cases where total value of International Transactions (as defined u/s.92B of the Income-tax Act) exceed Rs.15 crores)

(b) In all other cases where the Transfer Pricing Audit carried out in the earlier year had led to an adjustment/addition to the total income.

(xi) All cases of stockbrokers and commodity brokers as well as their sub-brokers, where brokerage received is disclosed at Rs.1 crore or above.

(xii) All cases of stockbrokers and commodity brokers as well as their sub-brokers, where there are claims of bad debts of Rs.5 lakhs or more.

(xiii) All cases of professionals with gross receipts of Rs.20 lakhs or more if total income declared is less than 20% of gross professional receipts.

(xiv) All cases of deductions u/s.10A, u/s.10 AA, u/s.10BA, u/s.10B of the Income-tax Act exceeding Rs.25 lakhs.

(xv) All cases of contractors (excluding transporters) whose gross contractual receipts exceed Rs.1 crore if total income declared from contract work is less than 5% of gross contractual receipts.

(xvi) All cases of builders following the project-completion method.

(xvii) All cases in which fresh capital introduced during the year exceeds Rs.50 lakhs in Delhi, Mumbai, Chennai, Kolkata, Pune, Hyderabad, Bangalore and Ahmedabad and Rs.10 lakhs in other cities.

(xviii) [1]All cases in which new unsecured loan introduced during the year exceeds Rs.25 lakhs.

(xix) All cases in which deduction u/s.80IA(4), u/s.80IB, u/s.80IC, u/s.80JJA, u/s.80JJAA, u/s.80LA, u/s.10(21), u/s.10(22B), u/s.10(23A), u/s.10(23B), u/s.10(23C), u/s.10(23D), u/s.10(23EA), u/s.10(23FB), u/s.10(23G), u/s.10(37), u/s.10A, u/s.10AA, u/s.10B, or u/s.10BA of the Income-tax Act is claimed for the first time.

(xx) *All cases in which loss from house property is more than Rs.2,50,000.

(xxi) *All cases in which investment in property is more than five times the gross receipts [*i.e.*, Income-tax purchase of property (008 from AIR)/(Gross Total Income (746) + Agricultural Income (762) + Income claimed exempt (125)>5)]

(xxii) *All cases in which the sum of short-term capital gains u/s.111A and long-term capital gain is more than Rs.25 lakh.

(xxiii) *All cases in which the sale of property has been shown as per AIR return but no capital gains have been declared in the return of Income.

(xxiv) *All cases in which the commission paid is more than Rs.10 lakhs.

(xxv) *All cases having business of real estate with gross turnover exceeding Rs.5 crores.

(xxvi) *All cases having business of hotels/tour operations with gross turnover exceeding Rs.5 crores if net profit shown is less than 0.05%.

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1 Selection of cases under these criteria shall not be done manually in the cities on computer network, but through Computer-Assisted Scrutiny System (CASS), for which necessary provisions have been made in the CASS software being issued by Directorate of Income-tax (Systems).

Selection of cases under these criteria in the cities on the computer network would be made through Computer-Assisted Scrutiny Systems (CASS) in respect of cases where audit report u/s.44AB has been filed. In all other cases in these cities and in all cases in cities not on the computer network, the selection would be made manually.

* Selection of cases under these criteria shall not be done manually in the cities on computer network, but through Computer-Assisted Scrutiny System (CASS), for which necessary provisions have been made in the CASS software being issued by Directorate of Income-tax (Systems).

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(xxvii) *All cases in which total depreciation claimed at the rates of 80% and 100% is more than Rs.25 lakhs.

(xxviii) All cases in which net agricultural income is more than Rs.10 lakhs.

(xxix) All cases covered by retrospective amendment in S. 80IA of the Income-tax Act, 1961 brought by the Finance Act, 2007 *i.e.*, all persons who merely execute the civil construction work or any other works contract entered into with the undertaking or enterprise referred to in S. 80IA of Income-tax Act, 1961.

Note : If a case has been assessed earlier under scrutiny for at least 2 A.Ys. but in each of the immediately preceding two years assessed u/s.143(3) of the Income-tax Act, total additions or disallowances made/sustained in appeal are less than 5 lakhs in Delhi, Mumbai, Chennai, Kolkata, Pune, Hyderabad, Bangalore and Ahmedabad and less than Rs.1 lakhs in other places, then such a case should be excluded from compulsory scrutiny under clauses (ii), (vi), (vii), (viii), (ix), (x), (xii), (xiii).

Provided that the above exclusion clause shall not apply in cases involving substantial question of law.

3. In addition to the above, where the CCIT/DGIT (International Taxation)/DGIT (Exemptions), on the matter having been brought to his notice by an authority below, is satisfied that the case needs to be taken up for scrutiny, the CCIT/DGIT (International Taxation)/DGIT (Exemptions), for reasons to be recorded in writing, may approve the selection of the case for scrutiny.

4. The CCIT/DGIF (International Taxation)/DGIT (Exemptions) may issue suitable guidelines for reducing/increasing the number of cases selected under specific clauses of para 2, for proper management of the workload as well as to avoid large-scale transfer of cases from one jurisdiction to another.

5. All returns filed in response to the notice issued u/s.148 of the Income-tax Act shall be selected for scrutiny.

6. In addition to the above, selection of cases out of returns processed on AST will be made through a Computer-Assisted Scrutiny System (CASS). Separate instructions in this regard will be issued by the DIT (Systems).

7. List of cases taken up for scrutiny during each month shall be submitted by the Assessing Officer to the CIT and the Addl. CIT, Range, by 15th of the following month and shall also be displayed on the notice board of the office.

Explanatory Circular on FBT on ESOPs : Circular No. 9/2007, dated 20-12-2007.

CBDT has issued a clarificatory circular answering some frequently asked questions in relation to FBT on ESOPs. Important clarifications provided include :

- An Indian subsidiary is liable to FBT in respect of shares allotted or transferred to its own employees whether or not there is a charge back of cost by the foreign holding company.
- An Indian subsidiary would be liable to FBT in respect of the value of the shares allotted or transferred by the foreign holding company if the employee was based in India at any time during the period beginning with the grant of the option and ending with the date of vesting of such option irrespective of the place of location of the employee at the time of allotment or transfer of such shares. In case the employee is based in India for a part of the grant period, then proportionate amount of the value of fringe benefit would be liable to tax.
- In case an employee is of a foreign company but is based in India at the time of allotment of ESOPs, then foreign company would be liable to FBT in respect of shares allotted or transferred to its employee who is based in India on a proportionate basis.
- Even if FBT is charged on a proportionate basis, there would be no effect on the cost of acquisition.
- Employer will be liable to FBT in India irrespective of whether employees have been charged to tax in different countries or not. Also no credit for tax paid elsewhere would be available.
- An employee can claim credit in a foreign country, for the FBT paid on ESOPs by the employer in India which has been recovered from him.
- An employer does not have the choice to tax ESOPs as perquisites instead of fringe benefits.
- In case of foreign companies wherein shares have been listed globally elsewhere, for FBT purposes, they would be treated as unlisted. However, while valuing the shares, the

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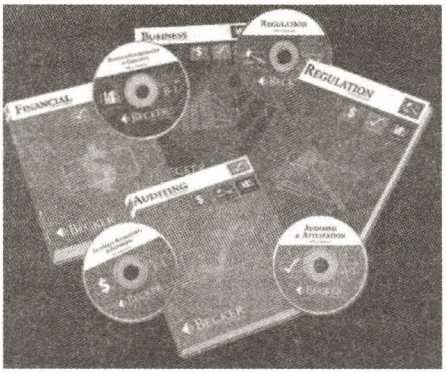

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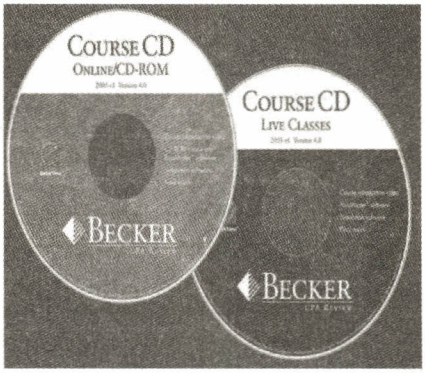

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merchant banker would take the listed price into consideration.

- The valuation needs to be done mandatorily by a Category I merchant banker listed with SEBI.
- The merchant banker should determine the FMV on the basis of alternative methods and recommend the most appropriate value.
- The valuation needs to be done on the specified date although the process of valuation can be carried out either before or after the specified date.
- In case where the employer purchases the shares and then subsequently transfers them to its employees, the fringe benefit so arising is allowable as deduction in computing the taxable income of the employer company. However, if the shares are allotted to the employees from the share capital of the company, no deduction is allowable in computing the taxable income of the company since no expenditure has been incurred by it.
- FBT would not be leviable on ESOPs allotted to non-employees.
- FIFO method needs to be followed in case there are multiple dates of vesting for different number of shares.
- It is binding upon the Assessing Officer to accept the valuation made by the Merchant Banker unless the valuation by such banker is perverse.
- Since FBT is not allowable as a deduction in the hands of employer, it would not be treated a income on the recovery of the same. Also, there is no time frame prescribed for such recovery.
- Since the specified date is the date of allotment or transfer, FBT can be recovered on ESOPs granted prior to 1-4-2007 but allotted/transferred after that date.
- The date of allotment of an Employee Stock Option shall be the date on which the underlying asset is allotted or transferred to the employee.
- The recovery of FBT from the employee by the employer will not change the cost of acquisition of the shares in the hand of the employee.
- For the purpose of this circular an Employees' Stock Option Plan shall include all schemes or plans, etc. where a specified security or sweat equity shares, being shares in a company, are allotted or transferred to an employee.

Part C : RBI/FEMA

Given below are the highlights of certain RBI circular and Notification

A.P. (DIR Series) Circular No. 20 dated December 14, 2007 — Notification No. FEMA 170/2007-RB dated 13-11-2007 — Foreign Direct Investments (FDI) — Issue of shares under FDI and refund of advance remittances.

This Circular provides that, with effect from November 29, 2007, where a company has received application money for subscription to equity shares/compulsorily convertible preference shares and compulsorily convertible debentures (equity instruments) from a non-resident investor than the company has to issue the equity instruments within 180 days from the receipt of the inward remittance or date of debit to the NRE/FCNR(B) account.

If the equity instruments have not been so issued within 180 days than the amount received has to be refunded immediately to the non-resident investor. However, in exceptional cases where refund cannot be issued within the stipulated period of 180 days, permission of RBI has to be obtained for issuing the refund beyond the stipulated period of 180 days.

Where 180 days have elapsed since the receipt of funds from the non-resident investor as on November 28, 2007 and the equity instruments have not been issued the company has to approach the Regional Office of RBI through its Bank with a definite plan for allotment of equity instruments or refund of money received.

Companies (Central Government's) General Rules and Forms (3rd Amendment) Rules, 2007 — Notification dated 16-11-2007.

Rule 4A has been substituted, which prescribes new procedure for applying and adopting a new name/change of name for companies. The important changes as compared to the old Rule include :

- The ROC may reject or ask for re-submission or further information on application ordinarily within 3 days of receipt of the application. The response time has been reduced from 7 days to 3 days.
- As per the new Rule, the maximum time allowed for adoption of name is restricted to 60 days as against 6 months. It can be further

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extended to 30 more days on payment of Rs.250 additionally. The name allowed shall lapse after expiry of 60 or 90 days, as the case may be, from the date it is allowed first.

- The re-submission is restricted to 2 (two) times after the original application is filed. After 2 times, the promoter can file a fresh application with the prescribed fee.

Amendments made to Schedule VI to the Companies Act, 1956 : Notification No. G.S.R. 719(E), dated 16-11-2007.

The important amendments include :

- Additional disclosure in the Notes to Accounts under the Micro, Small and Medium Enterprises Development Act, 2006 relating to the principal amount and interest due thereon, either paid or remaining unpaid or accrued, due and payable, but remaining unpaid at the end of each accounting year or the amount of further interest remaining due and payable even in the succeeding years, until such date when the interest dues as above are actually paid to the small enterprise;
- Under Liabilities, the break-up for creditors needs to be shown *viz.* total outstanding dues of micro enterprises and small enterprises need to be shown separately.

Payment of Bonus (Amendment) Ordinance, 2007, dated 27-10-2007.

The Govt. of India has amended the Payment of Bonus Act, 1965 by issuing the aforementioned Ordinance. This Ordinance comes into effect from 1-4-2006. The effect of this Notification would be that the basic ceiling for salary threshold has been increased from Rs.3,500 to Rs.10,000 per month. Also, the entitlement for calculation of bonus will be Rs.3,500 per month, instead of Rs.2,500. Further, those employed through contractor on building operation have now been covered under the Payment of Bonus Act.

(Continued from page 460) — **LAWS AND BUSINESS**

Industries, 116 Taxman 845 (SC) and *Shri Subhalxami Mills*, 249 ITR 795 (SC), this section does not apply to carry forward of unabsorbed depreciation.

6. **Stamp duty implications :**

6.1 In case the shares are in physical form, then stamp duty @ 0.25% of the value of shares transferred is payable. No stamp duty is payable in case of shares in dematerialised form.

7. **Directors' responsibilities :**

7.1 Although the directors of an Indian company which is being acquired by a foreign company do not have much of a substantial role to play, there are certain obligations which are cast upon them under the SEBI Takeover Regulations. Hence, in case a listed company is being acquired, the directors should become aware of the requirements. They should seek assistance of experts as to the legal and procedural requirements, so that there are no last moment surprises.

4.2 Compliance of Indian and foreign laws in such cross-border acquisitions is essential. A part of the auditor's attest function is to ensure compliance with laws. By enquiring and asking relevant questions, an auditor can add value to his services.

(Continued from page 467) — **LIGHT ELEMENTS**

60 years. My performance has been hyped. I was not alone who fought for independence of this country. I never imagined in my life that my ideology would be abused to cling to power by the Congress party. I never thought that roads, bridges, buildings, gardens, schools, colleges, hospitals would be named after me. My Lord, I never dreamed of my image on currency notes. My Lord, I remember once Churchill called me 'Naked Fakir' of India. But these selfish politicians have glorified me for their political mileage posthumously . . . So My Lord, please don't reincarnate me, I am sorry. I told you 'the satya, the truth' . . . for me truth is God."

"Bapuji, you will have to go back to earth to save Bharat Bhoomi," Bhagwan Mahesh thundered.

Bapuji kept on justifying his stand for a long time. But Bhagwan Mahesh was adamant about Bapuji's reincarnation on the earth.

Finally Bapuji declared 'Satyagraha' unto 'no reincarnation' then and there. Till today, all out efforts are being made by the galaxy of Gods to break the 'Satyagraha'. So countrymen and politicians be aware, Bapuji may come back any time . . .

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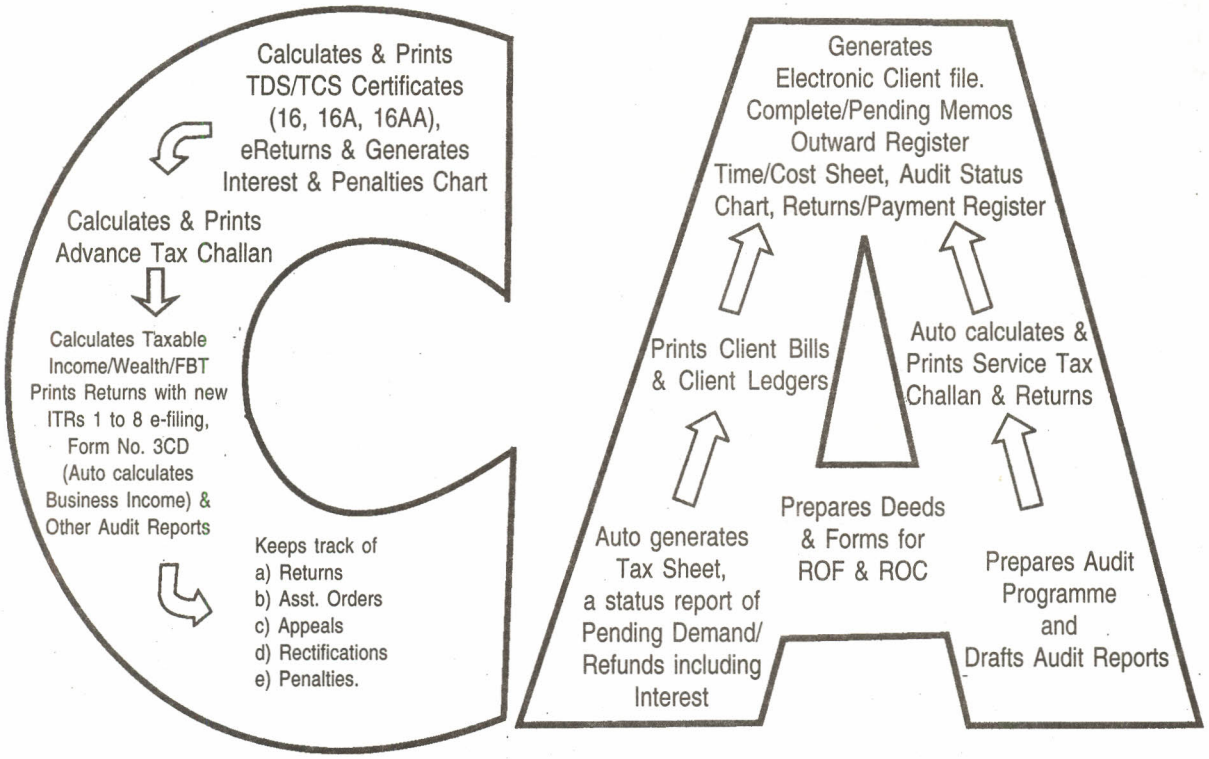

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IS IT FAIR ?

Is it fair to defeat the purpose of S. 197 by administrative hurdles ?

Chandrashekhar Vaze
Chartered Accountant

1. **Introduction :**

The menace of tedious provisions in the Income-tax Act, 1961 relating to tax deduction at source has been progressively increasing. Interest, penalty, prosecution and now the disallowance! The compliance procedures are so cumbersome that no organisation with a sizeable volume can ever claim complete compliance. Further, penalties u/s.272A for procedural defaults are disproportionately harsh. The explanation to S. 191 inserted with effect from 1-6-2003 that the deductor shall be 'in default' if the tax has not been paid by the recipient of income is hardly any solace. It is worded too mildly. The deductor is dealt with harshly for rendering service to the Government for no fee. For the recipient of income, it is equally troublesome. The situation is aggravated in the e-TDS scenario. Apart from the age-old problems that deprive an assessee of the legitimate credit of TDS such as — default of deductor in filing e-TDS, errors in deductor's returns, mismatches of PAN/TAN at NSDL, and so on.

S. 197 is intended to provide relief to those assessees to avoid higher deduction of tax. The assessee can obtain a certificate from the Assessing Officer that deduction of tax be NIL or at a rate lower than prescribed. Unfortunately in practice, this provision has become a myth. The so-called remedy is perhaps worse than the disease.

2. CBDT has so far issued two letters to the Department with good intentions — Letter No. 1(54) — 63 TPL dated 18-5-1963 specifying that the applications should be processed expeditiously. A similar letter no. 20/23/67, dated 28-7-1967 was issued specifically dealing with application received from charitable trusts.

3. However, in reality, it happens as follows :

3.1 Although S. 197(1) expressly mentions that the AO will issue the certificate, the power is exercised by ITO-TDS (a separate section). It is common sense that an officer who is assessing one's income is more suited for this task, since he is supposed to be conversant with the case; and is seized of the past records. One has to submit practically a duplicate set of past records to the TDS section.

3.2 The enquiry is nothing short of assessment — scrutiny proceedings. It involves frequent visits to I.T. Office, provide lot of documentation and answer several searching questions. It may easily take 6 to 8 weeks time obtain a certificate if the application is followed up vigorously. In effect, by the time a certificate is received, about one third of the year is already over.

3.3 Further, a certificate is usually issued only for one financial year. Thus, if one initiates the process in the month of April or May, the application is effectively taken up in June. Certificate is issued when one-third or one-fourth of the year is already over.

3.4 The problem is all the more serious in the case of charitable trusts. The trusts have to face the scrutiny at the time of obtaining certificate u/s.80-G and also for obtaining certificate u/s.197.

3.5 It is interesting to note that outside Mumbai, the Assessing Officer himself exercises this jurisdiction, which is as per the text of the Section.

4. **Suggestions :**

4.1 The jurisdiction for issuing certificate u/s.197 should be exercised by the Assessing Officer only.

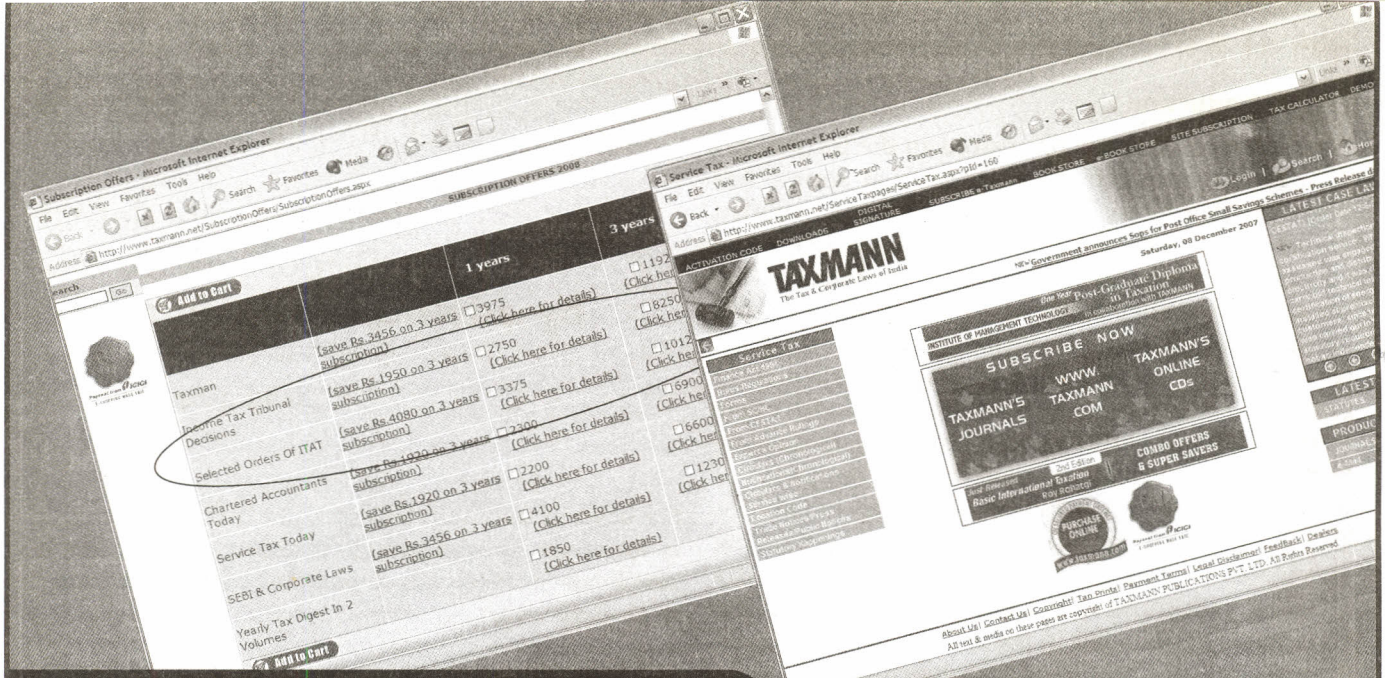
4.2 The spirit of directions issued by the CBDT should be honoured. The applications should be processed expeditiously.

4.3 Certificate should be valid for at least two financial years, especially in case of senior citizens and charitable trust.

4.4 In case of non-residents, certificate should be valid for the period of the contract.

Editor's Note :

Readers may also note the CBDT Instruction 8 of 2006, advising officers not to issue such certificates indiscriminately, which has had the effect of making officers overcautious in issuing such certificates. (*Instruction reproduced in continuation on page 491.*)



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Representation on Press Release advising taxpayers liable to TDS/TCS to furnish their correct PAN with their deductors

by **Bombay Chartered Accountants' Society**
jointly with **Indian Merchants' Chamber**

Representation

To,

November 28, 2007

Mr. P. Chidambaram
The Hon'ble Finance Minister, Government of India
North Block, Secretariat, New Delhi-110001.

Respected Sir,

Subject: **Filing of quarterly e-TDS Returns**

Recently, in Press Release No. BSC/RP/GN-421/07 (*copy attached*), dated September 25, 2007, the Government of India has announced that quarterly statements relating to tax deduction at source (TDS) would not be accepted unless 70% of the records have Permanent Account Numbers (PAN) in case of TDS/TCS statements in Form No. 26Q and 27EQ, and unless 90% of the records have Permanent Account Numbers (PAN) in case of TDS statements in Form No. 24Q.

The electronic system set up by the Government for filing of quarterly TDS returns no longer accepts the TDS return as an upload, unless the parameters set out in the Press Release are met with. The due date for the quarterly statements for the period July to September 2007 was in the middle of October. Owing to this system limitation, several persons deducting tax at source were unable to file the quarterly TDS returns in time.

It is respectfully submitted that this latest requirement which does not permit tax deductors or collectors to file their quarterly statements unless an *ad-hoc* percentage of PAN details are furnished is arbitrary and unfair on the tax deductors and collectors who are, in the ultimate analysis, doing a voluntary job of tax collection for and on behalf of the Government. As it is, the penalties, interest and disallowances meted out to tax deductors for the smallest of defaults in the matter of deduction of tax at source is very stiff and unfair. To add to this already heavy burden, now the filing of the returns itself is being hindered. It may also happen that many deductors, who are unable to file the quarterly statements for no fault of theirs, would face a penalty for non-filing.

Non-furnishing of PAN details is, in most cases, not on account of the default of the tax deductor or collector, but on account of the non-furnishing of the details by the deductee or collectee. For this, to penalise the deductor or the collector is adding insult to injury.

In view of the above, on behalf of the thousands of tax deductors and tax collectors of the country, this is an earnest request to immediately revoke the said Press Release dated 25th September with retrospective effect. If at all the Government wishes to enforce the discipline of obtaining PAN and quoting it in the necessary documents, it should consider punishing the persons who are actually at fault *i.e.*, the persons who, despite being statutorily required to obtain PAN, have not yet done so. Based on the address and other details given by tax deductors and collectors in their respective quarterly TDS statements, the Government should pursue such deductees and take necessary action against them, as permitted by the law.

Thanking you.
We remain,
Yours truly,

Rajesh Kothari	**Pinakin Desai**	**Rajesh Shah**	**Niraj Bajaj**	**Kishor Karia**
President	Chairman	Co-Chairman	President	Chairman
	Taxation Committee			Direct Taxation Committee
Bombay Chartered Accountants' Society			Indian Merchants' Chamber	

Press Information Bureau
Government of India

Tuesday, September 25, 2007

Ministry of Finance

Taxpayers liable to TDS/TCS are advised to furnish their correct PAN with their deductors

All tax deductors/collectors are required to file the TDS/TCS returns in Form No. 24Q (for tax deducted from salaries), Form No. 26Q (for tax deducted from payments other than salaries) or Form No. 27EQ (for tax collected at source).

These forms require details of all tax deductions with name and permanent account number (PAN) of parties from whom tax was deducted.

However, it has been observed that in most of the TDS/TCS returns, the PAN of the deductees is either missing or incorrect. As the requirement of filing TDS/TCS certificates has been done away with, the lack of PAN of deductees is creating difficulties in giving credit for the tax deducted and collected.

It has, therefore, been decided that TDS returns for salaries, *i.e.*, Form No. 24Q with less than 90% of PAN data and TDS returns for payments other than salaries and TCS returns, *i.e.*, Form No. 26Q and Form No. 27EQ, respectively, with less than 70% of PAN data will not be accepted for the quarter ending on 30-9-2007 and thereafter.

Tax deductors and tax collectors are, therefore, advised to obtain correct PAN details of all deductees and quote the same in the TDS/TCS returns, failing which the TDS/TCS returns will not be accepted and all penal consequences under the Income-tax Act will follow.

Taxpayers liable to TDS/TCS are also advised to furnish their correct PAN with their deductors, failing which they will also face penal proceedings under the Income-tax Act.

For and from the quarter ending 30-9-2007, in addition to Government offices and companies, filing of TDS/TCS returns in electronic form is mandatory for (i) deductor/collector required to get his accounts audited u/s.44AB of the Income-tax Act in the immediately preceding financial year, and (ii) where the number of deductees'/collectees' records in a quarterly statement for any quarter of the immediately preceding financial year is equal to more than fifty. TDS/TCS returns in paper form will no longer be accepted from such tax deductors/collectors.

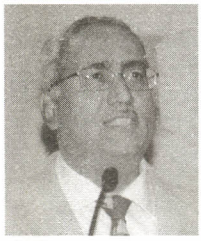
A young CA faces scrutiny

There was once a young CA with vigour,
He had not yet faced any scrutiny's rigour !
One fine day a notice came on his client,
The CA jumped with joy, here is a chance to show my talent !
The list was very long and hard he had to toil,
He believed in perfection so he burned midnight oil !
He appeared for the assessment thinking it will be just and fair,
He did not know that he was about to get a real scare !
He gave his submission and argued his case with ease,
The officer just stared at him as if he was speaking Japanese !
He thought he did well and favourable order was his surmise,
He should have asked a senior 'cause he was in for a nasty surprise !
Shocked with the huge addition, to the officer he ran,
Sir, didn't you accept whatever I said then ?
The officer smiled and said as per law I gave you a patient hearing,
Who told you that what you said, I was listening and accepting?

— Unmesh K. Mehta, C.A., Bhavnagar

Mayur Nayak
Pradip Thanawala
Chartered Accountants

Lecture Meetings :


Gautam Nayak

On 21-11-2007, Gautam Nayak, Past President of the Society, addressed the members on the subject 'Tax Deduction at Source — Recent Issues'. He discussed the various problems faced by tax-payers as well as professionals on account of erroneous interpretation of the provisions by the Tax Department. He urged the gathering to take a conservative view of the provisions, so as to avoid unnecessary litigation.

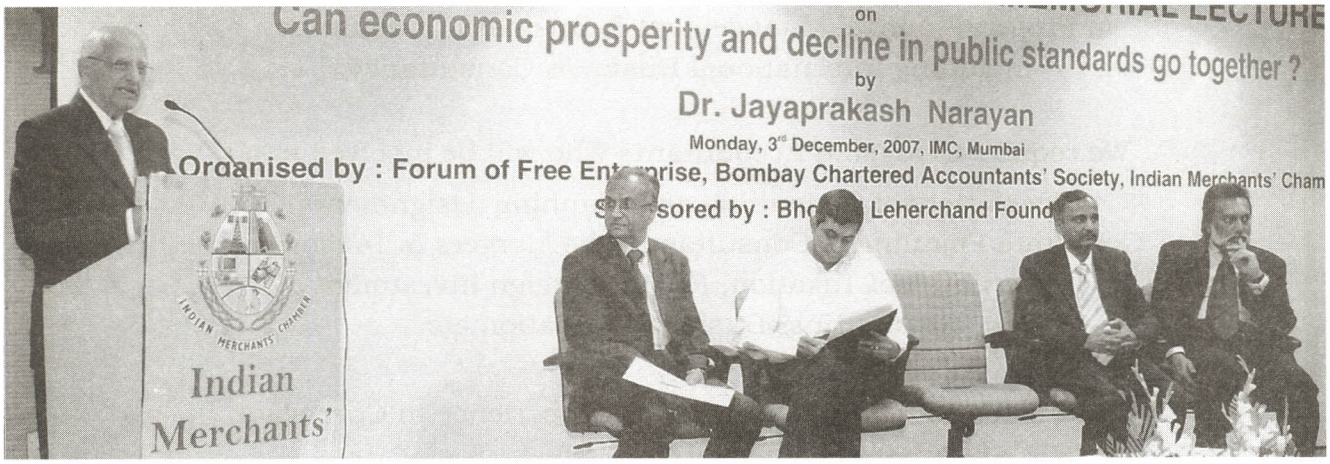
On 3-12-2007, the Society and other institutions had organised the 19th Bhogilal Leherchand Memorial Lecture. On the occasion Dr. Jayaprakash Narayan spoke on the subject 'Can economic prosperity and declining public standards go together ?' His presentation was very thought-provoking. He expressed that intellectuals should participate in public life, and such participation would substantially improve the quality of Indian politics.

Accounting & Auditing Committee :


Nandita Parekh

A half-day seminar on Internal Auditing Standards was organised on 23-11-2007. It was addressed by two eminent faculty *viz.* Bhargava Vatsaraj and Nandita Parekh. The seminar was attended by 50 participants.

Bhargava Vatsaraj dealt with 'Relevance of Internal Auditing in Present Times'. He gave information on internal auditing and the field of internal audit.



Dr. Jayaprakash Narayan, speaking at the lecture meeting. Others seen from left are : M. R. Shroff, President, Forum of Free Enterprise; S. Divakara, Secretary General, Forum of Free Enterprise; Rajesh Kothari, President, BCAS and Nirmal Bhogilal, Chairman, Bhogilal Leherchand Foundation.


Sujit Cherian

On 5-12-2007, Sujit Cherian, CA addressed the members on the subject 'Internal Audit — Emerging Tools and Techniques'. He explained to the gathering the distinction between the roles of a statutory auditor and an internal auditor. He was of the view that an internal auditor should be able to add value by making suggestions regarding existing business processes. He felt that the new entrants to the profession had tremendous scope in explained relevance of the same in context of Company Law and Clause 49 Listing requirements. He also highlighted the relevance of internal audit in context of Audit Committees. Internal Audit also serves as value addition to the client on various issues like increase in sales, profit, etc.

In the second session, Nandita Parekh dealt with the Standards SIA 1 to 3 along with the Preface to Standards on Internal Auditing and shared her experiences. She dealt with the requirements of various standards detailing their necessity. She

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explained the vital role played by various standards from the context of the clients & public at large and also discussed about privileges and responsibilities of members. She detailed the various factors involved in planning of internal audit and its documentation.

Overall, the seminar was a success, as the participants got a good insight into important aspects of internal auditing standards which need to be complied with to carry out a quality audit.

Strategic Studies Committee :

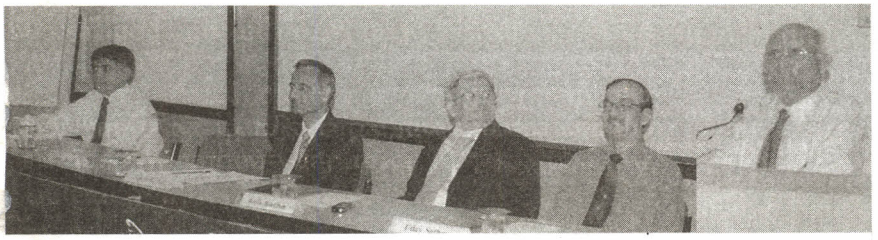
The Strategic Studies Committee of BCAS jointly with HR College successfully launched Batch V of Professional Accountant Course on 4-12-2007 at HR College. It was inaugurated by Rajesh Kothari, President. Anil Sathe, Vice-President; Kanu Chokshi, Chairman; Uday Sathaye, Vice Chairman; Prof. Parag & Manori Shah, Course Co-ordinators were present.

Duration of the course is 2½ months — 24 lectures of 3 hours each on Tuesdays, Fridays and some Saturdays.

The course will cover subjects like Income Tax, Audit, Service Tax, VAT, Excise Duty, Customs Duty, Financial Accounts, Costing, Budget, MIS, Communication & Reporting, Office Systems, Soft Skills, Tally, ERP, Personality Development, Interviews & Appraisals and Professional Ethics.

Participants are from CA firms and from industry.

Certificates will be given on the basis of written exam as well as attendance and participation.



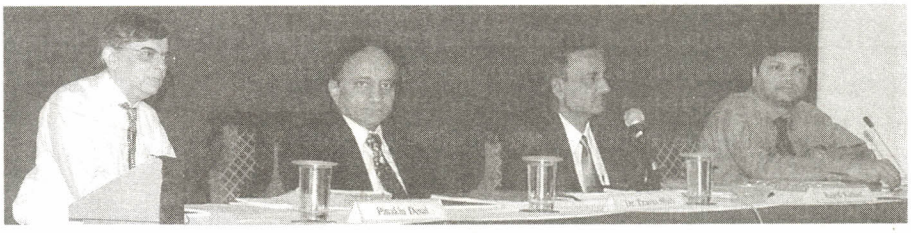
Kanu Chokshi, Chairman, Strategic Studies Committee welcoming the participants. Others seen from left are : Parag Thakkar, Professor, H. R. College; Rajesh Kothari, President, BCAS; Anil Sathe, Vice-President, BCAS and Uday Sathaye, Co-Chairman, Strategic Studies Committee.

Taxation Committee :

The Taxation Committee organised a half-day seminar on 'ESOPs — Commercial, Legal, Accounting & Tax Aspects' on 6-12-2007 at M. C. Ghia Hall. The seminar drew a packed house with several representatives of large corporate houses attending along with our members.

Dr. Pravin P. Shah made a very interesting presentation on the commercial and legal aspects of ESOPs. His insights on the various issues that one needs to take into consideration before finalising an ESOP were of great utility to the delegates. Sudhir Soni spoke about the accounting and auditing aspects. He dwelt at length on the different accounting and auditing disclosures relating to ESOPs. In the end, Yogesh Thar presented his thoughts on the tax aspects of ESOPs. He shared his views on the taxability of ESOPs under different scenarios with reference to FBT in the hands of the employer, as well as perquisites in the hands of the employees. He also referred to the various issues arising out of the valuation guidelines issued by the Govt. for computing FBT on ESOPs.

Each session had a very interactive question-answer session at the end.



Pinakin Desai, Chairman, Taxation Committee welcoming participants. Others from left are : Dr. Pravin Shah, speaker; Rajesh Kothari, President, BCAS; Saurabh Shah, BCAS member.

Indirect Taxes & Allied Laws Committee :

Enthused by the overwhelming response to the 1st Residential Study Course, the Indirect Taxes & Allied Laws Committee conducted the 2nd Residential Study Course on Service Tax on 7th, 8th & 9th September 2007 at Treasure Island Resorts, Lonavala.

80 delegates from all over the country attended this three-day course. A paper book was brought out by Indirect Taxes and Allied Laws Committee (ITALC) which contained 3 Group Discussion Papers and 2 Presentation Papers.

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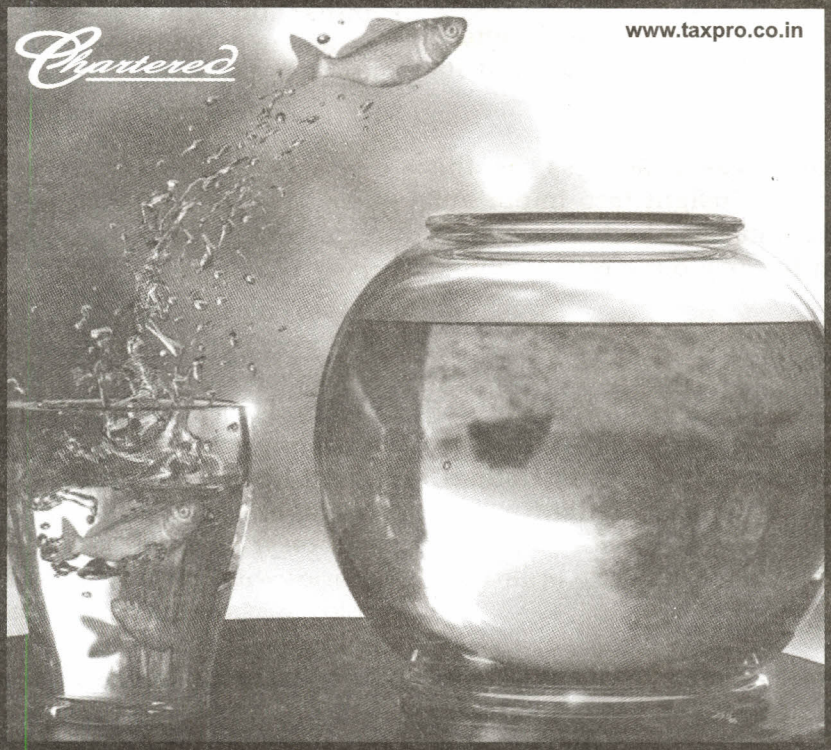

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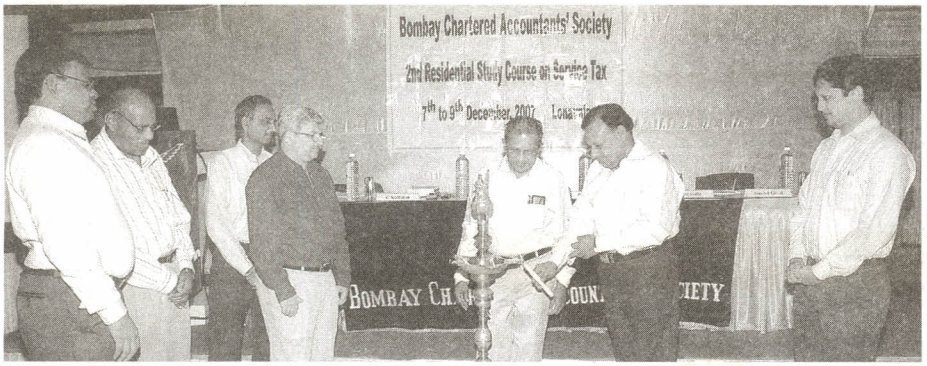


Pranay Marfatia, Chairman and Govind Goyal, Co-Chairman, Indirect Tax and Allied Laws Committee, BCAS, inaugurating the Residential Study Course by lighting the traditional lamp. Others seen from left are : Sunil Gabhawalla, Convenor; V. Sridharan, Advocate; Rajesh Kothari, President, BCAS; Anil Sathe, Vice-President, BCAS and Raman Jokhakar, Convenor, Indirect Tax & Allied Laws Committee, BCAS.

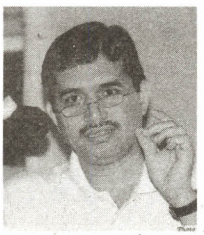
Attentive participants at the Residential Study Course.

The course was inaugurated by V. Sridharan, Advocate. In his keynote address, Sridharan touched upon some of the likely issues to arise in the arena of CENVAT Credit and drew some real-life examples from international precedents. This was followed by a presentation of P. K. Sahu, Advocate, on the topic of 'Taxation of Composite Contracts'. His clarity of thought reflected in his presentation and the speech was well appreciated by the participants.

On the second day, Rohan Shah, Advocate, presented an interesting paper on 'Import and Export of Services'. It was followed by a presentation by Sunil Kothare on 'Case Studies in Financial Services'. Both the papers were well appreciated by the participants. The afternoon was kept free for

Group discussion.

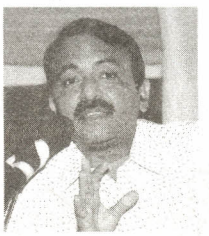
P. K. Sahu



Sunil Kothare

Rohan Shah

A. R. Krishnan



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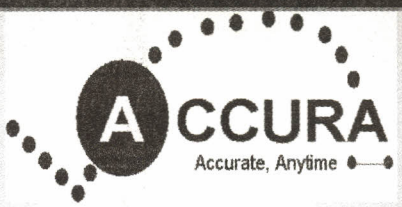

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participants to enjoy some leisure. In the evening, the hotel management organised a magic show and dance programme.

On the third day, S. S. Gupta, Chartered Accountant drew on his rich experience in the excise field and presented an interesting paper on 'Implications of Excise Propositions on Service Tax'. It was followed by an intricate presentation on 'Case Studies in Service Tax' by A. R. Krishnan, Chartered Accountant.

Human Resources Committee :

Effective Communication & Public Speaking Course for students, on December 14-16, 2007 :

"Mookam Karoti Vaachaalam" (Making the dumb speak)

The Committee had organised the above course wherein 31 students enrolled and took benefit. This is an annual event of the HR Committee and is eagerly awaited by students and members. The faculty included Vivek Patki and Vidyanand Joshi.

and to handle the situation when things are going wrong."

— Dhaiwat J. Trivedi

"I attended many programmes during my graduation, but the 'Most' interesting thing of this course is that the speaker and participants also communicate practically and not just theoretically. So this course is more practical than theoretical."

— Paresh Ramani

"I feel Confidence is all what man requires to find Courage;
Courage is all what man requires to stand;
Standing in front and standing with head held high towards your audience is all what man requires to be a Leader;
I feel like a Leader."

— Harshal Vasavada

"If you have stage fright, this for you is just right,
To shine so bright, learn and get it right."

— Dhruti Dalal

Anil Sathe, Vice-President, BCAS speaking at the Public Speaking Course. Others seen from left are : Vivek Patki, speaker; Rajesh Muni, Chairman, Human Resources Committee and Manish Sampat, Convenor, Human Resources Committee.

The following was the feed-back from a few of the participants :

"I think the programme was excellent. The faculty has been my first teacher who has made us learn something in such a light atmosphere. There were jokes, fun, but at the same time 'learning' also."

— Brinda Vithlani

"I plan to tell all my friends who are in the same or similar profession to go and attend this seminar."

— Tripti Zaware

"I have never given any speech in front of people and this programme has increased my confidence level and also taught me how to perform in front of many people

It was one of the most satisfactory efforts and rewarding experience of organising the course, as can be judged from the feedback from a few participants who benefited from the Effective Communication and Public Speaking course.

The course was made live by active participation by the students. The art of communication and effective public speaking learnt by the participants would be a stepping stone and shall go a long way in building a successful path for their public career.

In order to speak short upon any subject, think long.

— H. H. Brackenridge

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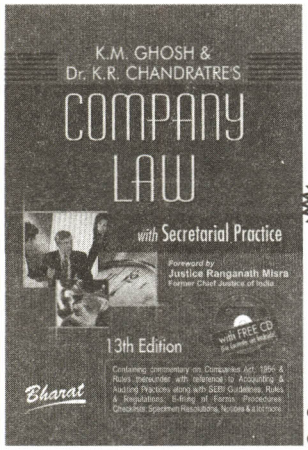

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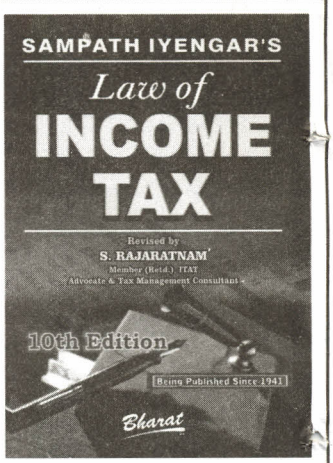

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(Continued from page 479) — **IS IT FAIR ?**

Circular details :

Indiscriminate Issuance of Certificate for Lower Deduction or Non-deduction of Tax at Source u/s.197 of Income-Tax Act — Instruction No. : 8/ 2006, dated 31-10-2006

I am directed to say that instances have been brought to the notice of the Board that assessing officers are issuing certificates for lower deduction or no-deduction of tax at source u/s.197(1) of the Income-tax Act indiscriminately and in contravention of the methodology and procedure laid down in Rules 28AA and 28AB of the Income Tax Rules. Such arbitrary issuance of certificates u/s.197(1) not only adversely affects the collection of tax at source but also seriously jeopardizes the chances of disclosure/detection at a later stage of such incomes on which no tax has been deducted or tax has been deducted at a very low rate.

2. Accordingly, all assessing officers are directed to ensure that all certificates u/s.197(1) issued by them are strictly as per the manner prescribed under Rule 28AA or Rule 28AB, as the case may be. No certificate u/s.197(1) shall be issued under circumstances, which are not covered by Rule 28AA or Rule 28AB, howsoever genuine and compelling such circumstances may be. Moreover, the assessing officer shall obtain prior administrative approval of the Range JCIT/Addl. CIT before issuing a certificate u/s.197(1). The JCIT/Addl. CIT shall satisfy himself of the fact that the certificate is being issued strictly in accordance with Rule 28AA/28AB before according his approval for issuance of the certificate. A record of such certificate issued should be maintained in the office of the assessing officer. These instructions of the Board may kindly be brought to the notice of all officers working in your charge for strict compliance.

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Reviewed by :
B. V. Dalal
Nina Kapasi
Chartered Accountants

Title : **Treatise on Special Economic Zone — Law and Practice**

Edition : Second Edition, 2008

Author : **Kanu Doshi,** *Chartered Accountant*
Yogesh Asher, *Chartered Accountant*

Pages : 1076

Price : Rs.1295 with Free CD

Publisher: Snow White

Unlike the First Edition, the Second Edition Index is user-friendly, giving adequately detailed pagewise contents and the contents are textually systematic rulewise. This makes reference easy to the otherwise complicated contents. Even index-browsing facilitates grasping the sequence of the whole text. SEZ as a subject is stretched to :

"Consideration of proposals for setting up of unit in a Special Economic Zone

Within 15 days,

Within 45 days if Board is to approve.

Reasons for approval/modification/rejection to be recorded in writing.

Approval if following criteria satisfied.

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No-No Proposals."

Chapter 1 contains elaborate definitions. Chapter 2 deals with Establishment of SEZ, detailing procedure for making proposal to the Governments — State and Central; and making application to the Board or the State Govt. for setting up SEZ, Board approval, notifying Guidelines for SEZ, development of infrastructure facilities, maintenance of sovereignty and integrity of India, security of the State and friendly relations with foreign States and so on.

Chapter 3 provides constitution of the Board of Approval and bureaucratic limbs, like Development Commissioner, his functions, setting up and operation of offshore banking unit and of International Financial Services Centre.

Chapter 4 provides for special fiscal provisions for SEZs, with provisions of the IT Act, 1961, to apply with certain modifications in relation to developers and entrepreneurs and also Chapter 5 with modifications to the IT Act, 1961, like the SEZ Act, 2005 (incl. FTZ converted into SEZ – S. 10A not to S. 10A(7B), furnish report of CA certifying correctness of the claim made, S. 80A(9) and (10), what triggers exemption u/s.54GA, choosing any 10 consecutive years out of 15, MAT not to apply to income of SEZ developer, Dividend Distribution Tax not payable by developer of SEZ and so on.

Chapters 6 to 10 likewise contain essential provisions titled — Foreign Exchange Earning — Requirements and Monitoring, Special Economic Zone Authority, Miscellaneous, Specified Officer, Exit of Units, Self Declaration and Cancellation of Exemptions, SEZ Policy — Circulars and Notifications.

Appendices 1 to 43 under Chapter 10 comprise equally essential ingredients of the SEZ Act, 2005, and the SEZ Rules, 2006.

Part 2 comprises State Governments' policies and provisions relating to SEZs, under Chapters 1 and 2 as 'Model'. Chapter 3 onwards to Chapter 17 contains Statewise policies of Andhra Pradesh, Chhattisgarh, Goa . . . to West Bengal and Chapter 18 provides Comparative Analysis of SEZ policies of State Governments.

A commendable effort is made by the authors with reference to the Second Edition which enables proper grasping of the elaborate contents of SEZ.

He who every morning plans the transactions of the day and follows out that plan carries a thread that will guide him through the labyrinth of the most busy life. The orderly arrangement of his time is like a ray of life which darts itself through all his occupations. But where no plan is laid, where the disposal of time is surrendered merely to the chance of incident, chaos will soon reign.

— Victor Hugo