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EDITORIAL

Happy New Year 2015

The Challenges and Opportunities of IFRS

CA Vinod Jain*

The Ministry of Corporate Affairs (MCA) has drawn up a revised roadmap for companies for implementation of the Indian Accounting Standards (Ind AS) converged with the International Financial Reporting Standards (IFRS) for companies other than banking companies, insurance companies and NBFCs.

The roadmap envisages a two-phase implementation. All companies, listed and unlisted, with a net worth over ₹ 500 crore together with their holding, subsidiary, joint venture or associate companies are covered in the first phase, w.e.f. April 1, 2016.

> **ROAD to Success- Responsibility, Ownership, Accountability, Discipline.**
>
> – Narendra Modi

The second phase covers all the other listed companies or those in the process of listing and all other unlisted companies with a net worth over ₹ 250 crore, w.e.f. April 1, 2017.

The time line for Banking and Insurance Companies are under consideration of RBI and IRDA.

The other companies and non-corporate businesses will continue to follow Historical Cost Based existing notified Accounting Standards.The IFRS Accounting Standards and Ind AS are based on fair value accounting of all assets and liabilities and have done away with Prudence as a basic accounting concept, permitting accounting for unrealized gains.

The Central Board of Direct Taxes has also issued final draft of Income Computation and Disclosure Standards (ICDS) for computation of income from "Profit and Gains from Business and Profession" and "Income from Other Sources".

How Fair is the Fair Value

The Fair Value Accounting base IFRS permit/require all assets and liabilities including Fixed Assets, financial instruments, investments, debentures, bonds, securities, and other liabilities to be valued at fair value. The effect of increase or decrease in value is to be adjusted in "Statement of Comprehensive Income" (extended statement of profit and loss).

The fair valuation is arrived at based on detailed Principles and a detailed international Standard on fair value determination. The existence of an active market and information in respect thereof is also crucial to ensure that fair value so calculated is not manipulated based on credit rating, market yield to maturity, risk free returns, risk estimate, estimated cash flows, alpha and beta factor and complex formulae.

There were serious allegations of manipulations of fair values by hundreds of banks and institutions including Lehmann Brothers, which collapsed during 2008 to 2011 in US and Europe.

MCA and ICAI to take on responsibility: We are quite hopeful that the Govt. of India and Institute of Chartered Accountants of India will together take responsibility of providing adequate checks and balances to undertake accounting on "Real Fair Value". It will be important to guide the Accountants, Auditors, Corporate as well as the tax department to understand complex accounting.

Fair Valuation Challenge: The Fair valuation in India is faced with many challenges

- **Shallow market:** Indian markets are very shallow in securities, commodities and various other assets.
- **Impact Cost:** The impact cost in the Indian market

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LATEST IN FINANCE

1.0 CDR Cases - RBI Analysis

CDR (Corporate Debt Restructuring) is a process where banks provide support through restructuring of genuine cases of companies in financial difficulties because of factors beyond their control. The CDR mechanism is meant to revive such cases as well as to provide safety to the money lent by the banks and financial institutions.

Out of the total number of cases referred under CDR, 49 per cent have been successfully implemented till date, according to Reserve Bank of India (RBI).

However, RBI observed that the number of cases referred to the CDR cell has come down in the recent past.

One of the reasons for this reduction could be the Reserve Bank's move to allow banks to restructure their large credits with aggregate exposure of ₹ 100 crore and above outside CDR under the Joint Lenders' Forum (JLF) constituted under the provisions of the 'Framework to Revitalize the Distressed Assets in the Economy' which became effective from April 1, 2014.

2.0 Factoring Services

What is Factoring

Factors are entities that pay SMEs (Small & Medium Enterprises) a certain upfront amount of receivables (up to 80 per cent) that SMEs expect from their buyers for selling their products. In turn, the SMEs assign their receivables to the factors, which then pursue the buyers and recover the amount. After pocketing the profit and recovering costs, factors pay back the balance to the SMEs. SMEs benefit because they get capital immediately, which in turn can be used to generate more business.

Regulatory Changes

The Reserve Bank of India, set out guidelines for setting up of and operating the Trade Receivables Discounting System (TReDS), to facilitate financing of bills of MSMEs (Micro, Small & Medium Enterprises) drawn on corporate and other buyers, including the Government Departments and PSUs. TReDS will be an electronic trade platform where the sellers will place their receivables and interested financiers will pick it up and chase the buyers.

Impediments

One of the impediments clearly is the absence of recovery tools such as Debt Recovery Tribunals (DRTs) and SARFAESI, which do not allow factoring entities to go after the buyer.

RBI relaxes Factoring Norms

According to the relaxed principal business criteria, factoring companies have to ensure that their financial assets in the factoring business constitute at least 50 per cent (against 75 per cent earlier) of their total assets and their income derived from factoring business is not less than 50 per cent (75 per cent earlier) of their gross income.

3.0 Debt Recovery Tribunal: Score Card

- **₹ 30,950 crore :** Amount recovered in 2013-14 under DRT Mechanism
- **₹ 2,36,600 crore :** Outstanding debt sought to be recovered in 2013-14
- **13 per cent :** Actual recovery for the period (2013-14)

While law indicates cases before DRTs must be disposed off in 6 months, only 25% of pending cases at the beginning of the year were disposed off during the year.

4.0 No Fresh Account needed to get benefits under Jan Dhan - Overdraft, Free Insurance

A person who is already having a bank account with any bank need not have to open a separate account under PMJDY (Prime Minister Jan Dhan Yojana). He/she will just have to get issued a RuPay card in his existing account to get benefit of accidental insurance. The overdraft facility can be extended in existing account. Accidental insurance of ₹ 1 lakh will be available to all RuPay card holders between 18-70 years. They will need to use their RuPay card once in 45 days of receipt of the card to get the benefit.

5.0 RBI eases KYC norms for NBFCs

The rules have been eased for getting KYC documents at frequent intervals.

Full KYC (Know your Customer) exercise will be required to be done at least every two years for high risk individuals and entities, at least every 10 years for low risk and at least every 8 years for medium risk individuals and entities, taking into account whether and when client due diligence measures have previously been undertaken and the adequacy of data obtained.

EDITORIAL

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IFRS Challenges and.......

range from 5% to 25% in case of most of the asset classes except Sensex/Nifty shares.

- **Information:** The information availability is very limited about actual transactions in the market, market yield, Alpha and Beta. The Arms' Length Transfer Pricing has already highlighted the absence.
- **Projections:** The valuation being made on the basis of projected cash flows are based on estimates and assumptions. The risk of motivated perception and manipulations based on false projections could risk the entire truth and fairness of financial statements

Taxation Issues: The Income tax issues will be fairly complex as the ICDS announced by CBDT as well as current tax laws are based on historical cost. How the department will deal with complex issues:

- Unrealized Income credited to Statement of Comprehensive Income or Profit and Loss Account
- Liabilities write back and write up based on fair value
- Assets write up and asset write off based on fair value
- Disclosure of sales in financial statements based on mandatory discounting factors e.g. towards staggered payments (VAT, GST issues)
- Fair valuation of derivatives and complex financial instruments
- Adjustment of various Income and Expenses heads based on complex technical accounting estimates and transactions

The Government and specially Tax Department need to confirm its stand on the above. The taxation wing may be very happy to tax unrealized gains but may be reluctant to allow deductions of impairments; write offs and write downs impacting the Profit and Loss Statement and Statement of Comprehensive Income very substantially.

Tremendous Advantages: The challenges outlined above come with great opportunities:-

Accountants: The demand for learned Chartered Accountants and their value will multiply from 2 to 4 times. The transition years will require at least 10 times more of good Chartered Accountants, Semi qualified Accounting Technicians and basic level Accountants. Even international demand of Indian CAs will go up substantially.

Banks: The Fair Falue Accounting will push up fair value of all assets of banks and insurance companies, thereby increasing their net worth from 2 to 20 times. This will result in substantial saving of additional capital requirement as estimated based on BASEL III. As per an estimate, Public Sector Bank alone will have additional Net worth of ₹ 150,000 crores to ₹ 200,000 Crores, arising out of fair valuation.

The NPA write offs and provisions will have to give way to fair value accounting and BASEL III norms.

Indian Corporate Sector: The value of Indian corporate sector will also multiply many times if all the assets are to be considered at fair value. The share market will see a new high, the borrowing power will go up and may fluctuate widely based on credit rating and market yield rates.

Gross Domestic Product(GDP): If value addition by private corporate sector is measured on fair value basis, the GDP of India will multiply to new levels. The Government may consider its own accounting on fair value based on Price Parity.

Interest Rates to be monitored and announced by RBI for Indian banking sector and Risk Free Govt securities will have a major bearing on valuations. Every reduction in interest rate will increase value of asset and decrease liability values. The net worth of business will move accordingly. Any increase in market interest rates will have a very severe negative impact on these figures.

The challenges are many and opportunities are great. A comprehensive strategic plan, preparation and cautious management will ensure sustained success.

However, it added that physical presence of clients may not be insisted at such periodic updations.

6.0 Current Coal mine owners to benefit

The phases : Govt to conduct two-phase bidding (technical & financial)

End-use : The successful bidder to meet criteria like status of end-use plant, its proximity to the mine and amount of coal needed

No loss : The end-use projects with captive mines likely to get what they had lost

Ahead in race : Earlier owners ready to jump in the race are hopeful of getting back their mines

Protecting money : Stakeholders are hopeful the govt will not let investments in end-use projects go waste

Damage control : Power-generation capacity of 28,000 MW has been affected by cancellation of coal blocks. The govt. step is highly laudable.

7.0 Stake in Coal Joint ventures

The Bill stipulates that a private sector entity cannot own more than 26 per cent in public-private joint ventures in case of coal block allocations.

However, if there is more than one private sector entity in a venture, then their total stake should not exceed 49 per cent. The Bill also prohibits government companies from alienating or transferring any interest in such joint ventures by taking loans or advances from banks or financial institutions.

8.0 PSBs can raise Capital, Government stake to stay over 52%

The Union Cabinet allowed state run banks to raise equity capital from the market subject to the condition that govt. stake should not fall below 52%, opening the way for public offers by many state run banks, including the biggest State Bank of India .

9.0 Industry-wise Position on proportion of Promoters' Pledged Shares

As of March 2014 in %

Sector	Promoters		Total Promo-ters' holding	Promoters' ownership pledged
	Indian	Foreign		
Banks	49.0	0.7	49.7	0.1
Engineering	35.8	0.5	36.3	11.2
Financial Servies	47.4	1.1	48.4	7.6
FMCG	27.9	3.2	31.1	11.7
Infrastructure	69.8	1.1	70.9	14.7
IT	43.0	4.9	47.9	11.2
Manufacturing	50.5	7.0	57.5	18.1
Media & entertainment	44.3	5.2	49.4	24.9
Petrochemicals	54.8	5.3	60.1	8.7
Pharmaceuticals	47.1	6.0	53.1	5.4
Services	46.3	9.7	56.1	25.5
Telecommunication	51.4	5.8	57.3	12.8
Miscellaneous	53.1	2.8	55.9	12.6
Total	**51.6**	**4.7**	**56.3**	**14.2**

Source: National Stock Exchange.

10.0 Indian Americans Desi Assets under USA Tax lens

The USA has enacted a law Foreign Account Tax Compliance Act (FATCA). Under the law, all financial institutions (brokerages, mutual funds, insurance companies, banks and hedge funds) in India are required to furnish information about US residents' financial accounts or investments to the US tax department - the Internal Revenue Service (IRS).

India born US resident-citizens, Green card holders and professionals with H-1B visa are required to declare details of their earnings in India and pay tax thereon to the US government according to the laws of that country. However both India and US have a treaty signed to avoid double taxation.

11.0 Cabinet nod for hiking stake in IFCI to 51%

The Government has approved raising of stake in IFCI Ltd to 51 per cent by infusing ₹ 60 crore in the country's oldest financial institution.

The current shareholding of Govt. of India in IFCI after inclusion of the preference share capital is 47.93 per cent.

12.0 Governance reform: Centre splits Chairman, MD post in state-run banks

In a bid to improve governance, the Centre has separated the posts of Chairman and Managing Director (CMD) in nationalised banks. It has also appointed Managing Directors (MD) for four banks, and they will also be designated as Chief Executive Officer (CEO).

13.0 Cabinet clears Land Acquisition Ordinance

Land Law Amendment Effect

- Faster processing of acquisition
- Fast-track process for defence and defence production
- No compromise on compensation or rehabilitation measures
- No compulsory social impact assessment for infrastructure, social infrastructure projects
- No compulsory consent from farmers for 5 project categories, such as affordable housing and industrial corridor.

14.0 Banks now borrow at Floating Rate

Banks used to source funds for their short-term needs from the RBI at a fixed repo rate, which was reviewed in every quarterly monetary policy review. But now banks are required to borrow much of their short-term requirements from the RBI, not at fixed rates, but at close to market rates.

15.0 RBI brings existing Project Loans of over ₹ 500 cr within 5/25 ambit

The Reserve Bank of India (RBI) allowed banks to refinance existing infrastructure projects under the 5/25 model, provided commercial operations have begun and the total exposure is over ₹ 500 crore. While the new norms will allow banks to refinance many loans, several projects that are stuck due to clearances will be out of the ambit of such refinancing.

Guidelines

- Only projects that have started commercial operation permitted to be refinanced
- The total exposure of the lenders should exceed ₹ 500 cr
- The requirement of 25% of the loan to be refinanced by new lenders scrapped
- Refinance may be taken up by the same lender or a set of new lenders, or combination of both
- Existing projects also allowed to be refinanced
- Accounts classified as non-performing assets could also be refinanced but will nevertheless remain NPA.

16.0 ARCs- RBI amend rules of Asset Acquisition

Asset Reconstruction Companies (ARCs) will need to focus on actual redeeming of security receipts as it is no longer possible for them to base their profit model on the basis of management fees," RBI said in its Financial Stability Report.

Now ARCs have to pay upfront 15 per cent of the bid value of non-performing loans, against five per cent earlier.

FEMA

1.0 RBI relaxes ECB norms

The Reserve Bank introduced changes in external commercial borrowings (ECB) norms under which authorized money changing banks have been allowed to create a charge on securities.

"It has been decided that banks may permit creation of charge by pledge on the shares of the JV/WOS (irrespective of the level) of an Indian party in favour of a domestic or overseas lender for securing the funded or non-funded facility under the automatic route," RBI notification said while modifying the Overseas Direct Investments norms.

In addition to joint ventures (JVs) and Wholly Owned Subsidiaries (WOSs), the RBI has announced similar concession for pledging of shares in case of step down subsidiary.

AUDIT & ACCOUNTING

1.0 Govt amends Cost Records Rules

Govt. prescribed a threshold of ₹ 35 crores for mandatory maintenance of Cost Records for following sectors:

Regulated Sectors	Unregulated Sectors
Telecommunication services, power generation, transmission, distribution and supply, petroleum-products, drugs and pharmaceuticals, fertilisers, sugar and industrial alcohol have been brought under regulated category.	33 industry/sector/ product/service have been placed under the category.
Cost Audit: Entities whose overall annual turnover is ₹ 50 crore or more and aggregate turnover of the individual products or services (where cost audit is required) is atleast is ₹ 25 crore.	***Cost Audit:*** Entities having minimum annual turnover of ₹ 100 crore would need to carry out cost audits.

CAPITAL MARKET

1.0 SEBI to Revitalise Primary Market with e-IPO

To revitalise the market, the Securities and Exchange Board of India (SEBI) will soon notify new norms to sell shares through electronic Initial Public Offers (e-IPOs). Manipulators could face stronger action in the new year, with tougher norms being finalised for insider trading.

2.0 FMC directs Commexes to pay Membership Deposits in six months

The Forward Markets Commission (FMC) has directed commodity exchanges to release interest-free deposit of members surrendering membership within six months from the date of request.

Earlier, commodity exchanges were allowed to keep interest free deposits with them for at least three years from the date of receiving request of membership surrender.

3.0 SEBI might review Delisting Framework

New Norms under review

Threshold limit	Promoter holding must cross 90%
Investor participation	25% of total public share-holders
Offer price determination	The price at which the share-holding of the promoter, after including the shareholding of the public shareholders who have tendered their shares, reaches the threshold limit of 90%
Timeline	76 days
Delisting directly pursuant to Open Offer	Allowed

CORPORATE & ECONOMIC LAWS

1.0 SC says NO to Royalty on Excavated Earth for laying foundation

The Supreme Court has held that the government is not entitled to any mining royalty if a developer excavates land for laying foundation of a building. The excavation cannot be equalled to mining.

2.0 New Bilateral Investment Treaties will help India avoid Arbitration

Bilateral Investment Treaties that the government will enter into from now on will have a provision preventing foreign investors to drag India to arbitration on any issues that have been settled by a judicial authority in India.

3.0 Arbitration Agreement needs no Signature

An arbitration agreement, even though in writing, need not be signed by the parties if the record of agreement is provided by exchange of letters, telex or other modern means of tele-communication, the Supreme Court stated.

"In such agreements, if the identity of the parties is established, and there is a record of agreement, it becomes an arbitration agreement if there is an arbitration clause showing agreement between the parties. Therefore, signature is not a formal requirement under section 7 of the Arbitration and Conciliation Act.

Govind Rubber Ltd vs Louids Dreyfus Commodities Asia Ltd.

4.0 Ex-Director not liable for Dud Cheque

The Supreme Court held that a person who was neither a director of a company nor in charge of or involved in the day to day affairs of the company at the time of issuing cheques, which bounced cannot be prosecuted under the Negotiable Instruments Act.

Pooja Ravinder vs State of Maharashtra.

INDIRECT TAXATION

1.0 States to get 1-year Grace Period for implementing GST

States will get one-year time to implement the provisions of Goods and Services Tax (GST) after introduction of the new indirect tax regime from April 2016.

With states like Tamil Nadu and West Bengal still voicing their concerns over GST implementation, the Centre has provided for this one-year extension clause in the GST Constitutional Amendment Bill which was tabled in the Lok Sabha on December 19.

2.0 GST: Biggest Tax Reform gets rolling

Creating A Single National Market

- Uniform rate in the country, but a narrow band may be allowed
- Central levies, including excise and services, to be subsumed
- State VAT, Sales Tax, Central Sales Tax, Entertainment Tax and Octroi to be replaced
- GST to be destination-based tax; consuming state to get tax
- States to be compensated fully for the first three years of rollout
- Compensation to be reduced in the fourth and fifth years
- GST council to decide on changes in GST
- Council to include Union and state finance ministers

Area-based Excise sops to continue under GST

The adoption of the Goods and Services Tax (GST) won't lead to untimely withdrawal of the excise waivers for industries in Jammu and Kashmir, North-eastern states, Uttarakhand and Himachal Pradesh. These sops would continue in some form or the other under the GST regime.

3.0 Classification of Goods

The Supreme Court of India held that where assessee sold mobile/cell phone with battery charger in same packing and it did not charge any separate amount for battery charger from customers and only amount charged was for handset, battery charger was an accessory to cell phone and was not a part of same and was liable to tax at general rate of 12.5 per cent.

State of Punjab v. Nokia India (P.) Ltd. [2014] 52 taxmann.com 410 (SC)

4.0 CENVAT Credit on Merger

The High Court of Allahabad held that where service provider had provided services to receiver during 2006-07, service recipient would be entitled to credit thereof even if, after provision of service, service provider is amalgamated into recipient retrospectively from 1.4.2006.

Commissioner of Central Excise, Kanpur v. RSPL Ltd. [2014] 51 taxmann.com 391 (Allahabad)

5.0 Group Expatriates Employment- No Service Tax Leviable

The High Court of Allahabad held that hiring expatriate employees of foreign group companies under a contract of employment on payment of salaries and related provident fund contributions, etc., does not amount to 'manpower supply services.

Commissioner of Central Excise v. Computer Sciences Corporation India (P.) Ltd.[2014] 52 taxmann.com 256

6.0 Separate contract for Goods and Services - Goods Component Taxability

The High Court of Allahabad held that where agreement between assessee and DVVNL (Dakshinanchal Vidyut Vitran Nigam Ltd.) incorporates separately value of goods or materials from value of services rendered, service tax cannot be levied on component of goods or materials.

Commissioner of Central Excise, Agra v. Goverdhan Transformer Udyog (P.) Ltd.[2014] 52 taxmann.com 377

7.0 Exemptions from Service Tax- SEZ Pre-commencement

The High Court of Gujarat held that services received by SEZ prior to commencement of authorized operations are also eligible for exemption/refund, if said service is necessary prior to actual manufacture or actual commencement of operation.

Commissioner of Service Tax v. Zydus Technologies Ltd. [2014] 52 taxmann.com 376 (Gujarat)

DIRECT TAXATION

1.0 SEBI probing listed Shell Companies' role in helping Tax evaders - False Capital Gains

The Securities & Exchange Board of India (SEBI) is probing several small companies listed on stock exchanges for their alleged role in enabling conversion of unaccounted cash into legitimate money. The regulator is probing whether these companies with no businesses or revenues are colluding with stock market operators to help tax evaders.

SEBI has found out that many of these shell companies have generated fictitious long-term capital gains for individuals. The regulator is also examining the ultimate beneficiaries of such trades, said a person familiar with the development. SEBI's preliminary investigation has shown that funds are transferred through several layers to hide the true identity of the ultimate beneficiary or owner.

INTERNATIONAL TAXATION

1.0 Section 92C- Transfer Pricing

The ITAT Hyderabad in *Brigade Global Services (P) Ltd. vs Income Tax Officer* has held that in order to determine ALP, a comparable could not be excluded only on ground that it was making loss.

[2014] 52 taxmann.com 436 (Hyderabad - Trib.)

FINANCIAL INDICATORS

	Current Rate*	Month Ago	3 Month	6 Month
3 Month LIBOR (%)	0.2541	0.2399	0.2291	0.2351
3 Month MIBOR (%)	8.63	8.55	8.88	8.97
SENSEX	27585.27	27831	26637.28	25329.14
NIFTY	8323	8355.65	7960.55	7568.55
CRR (%)	4	4	4	4
REPO (%)	8	8	8	8
REVERSE REPO (%)	7	7	7	7
Gold (per 10 gm)	26905	27220	26904	28576
Silver (per kg)	36664	38112	38130	43800
Crude (USD/bbl)	50.305	64.24	90.05	105.02
₹ vs USD	62.1605	61.95	61.1624	61.14
₹ vs Euro	73.7348	76.7499	77.6701	81.94
₹ vs 100 Yen	52.62	51.98	56.74	60.93
₹ vs RMB	10.0097	10.0319	9.9848	9.9147
₹ vs Pound	94.2788	97.1562	98.6244	102.57
MCX Aluminium (per kg)	110.55	121.95	115.7	124.2
MCX Copper (per kg)	378.9	399.35	407.75	430

As on 12th January 2015 (Sources: MoneyControl, NSE, BSE, RBI, MCX)

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2.0 Taxpayers can approach AAR for Tax Liabilities on deals above ₹ 100 Cr

In a positive move to cut tax litigation, the Central Board of Direct Taxes (CBDT) has notified that resident taxpayers who plan transactions valuing ₹ 100 crore or above can approach the Authority for Advance Rulings (AAR) for determination of their tax liabilities under such transaction.

3.0 Sales to Overseas AE not Comparable with Sales to Domestic Independent Enterprises

The Delhi ITAT has held that the Arm's Length Price (ALP) of international transactions with the Associated Enterprises (AEs) was to be determined on the basis of Transactional Net Margin Method (TNMM) and the impugned ALP adjustments on the basis of Comparable Profit Method (CPM) held vacated. It further observed that, sales to an overseas AE without any cost being incurred on marketing and sales promotion are not comparable with sales to domestic independent enterprises with full responsibilities for marketing and sales promotion.

Wrigley India (P) Ltd. vs ACIT [2015] 53 taxmann.com 16

4.0 Resale Price Method is suitable to compute ALP of goods purchased from an AE which are resold to unrelated parties

The Delhi ITAT in *Nokia india (P) Ltd vs DCIT* has held that Resale Price Method (RPM) is best suited for determining Arms Length Price (ALP) of an international transaction in nature of purchase of goods from an Associated Enterprise (AE) which are resold as such to unrelated parties and it presupposes no or insignificant value addition to goods purchased from foreign AE. *52 taxmann.com 492.*

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