KSCAA NEWS BULLETIN

English Monthly
for Private Circulation only

Vol. 3 • Issue 1 • ₹ 25/- • September 2015

Wish you happy Ganesha Chaturthi

Executive Committee Communique

Dear Professional Colleagues,

The world economy is changing trends and undergoing turbulent times. Chinese currency devalue, Greece and Euro zone crisis are not impacting Indian economy so much due to its strong fundamentals. A committee comprising top regulators and secretaries of the finance ministry has urged vigil even as it concluded there was no immediate cause for worry for India from global economic developments and financial volatility. The group, headed by Reserve Bank of India Governor Raghuram Rajan, is one of the subcommittees of the Financial Stability and Development Council (FSDC), the apex inter-regulatory body headed by the finance minister. The subcommittee felt India's strong fundamentals provided it enough protection from global developments.

In these times, the role of Chartered Accountants is critical in lending credibility to financial markets by providing high quality information in facilitating market discipline and fostering confidence of various stakeholders. This has become all the more important as the volatile nature of today's capital markets, emergence of knowledge based economy, and technological changes have posed major issues in financial reporting.

The Indian Government has enacted The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 (No. 22 of 2015). The Black Money Bill has received the assent of the President on the 26th May, 2015.The Act has been made to deal with the problem of the Black money in the form of undisclosed foreign income and assets. The Act prescribes the procedure for dealing with such income and assets and to provide for imposition of tax on any undisclosed foreign income and asset held outside India and for matters connected therewith or incidental thereto. The Finance Ministry has extended the deadline for declaring undisclosed foreign income or black money till 30th September, 2015. We urge the members to spread the awareness among the citizens to increase the compliance level which will flow back the black money in to main stream. We as Chartered Accountants have social responsibility towards such initiatives and should join hands in partnering nation building activities.

While announcing several steps for monetising gold in his Budget 2015-16, Union Finance Minister stated that stocks of gold in India were estimated to be over 20,000 tonnes but mostly this gold was neither traded, nor monetised. This September Government has notified Gold Monetisation Scheme, which would replace both the present Gold Deposit and Gold Metal Loan Schemes. The new scheme would allow the depositors of gold to earn interest in their metal accounts and the jewellers to obtain loans in their metal account. Banks/ other dealers would also be able to monetise this gold. The Finance Minister also announced the development of an alternate financial asset, a Sovereign Gold Bond, as an alternative to purchasing metal gold. The bonds would carry a fixed rate of interest, and also be redeemable in terms of the face value of the gold, at the time of redemption by the holder of the bond. This initiative will curb the import of Gold and in turn save the valuable foreign exchange.

The tax season is gearing up with release of new tax return formats by Income Tax Department with more elaborative disclosures. Department has extended the due date for filing of Income Tax Return for Assessment Year 2015-16 to 7th September 2015 from 31st August 2015 for taxpayers who were required to file their tax-return by 31st July, 2015. It has been done considering hardships faced by taxpayer in E-Filing Returns of Income on the last date i.e. 31st August, 2015 due to slowing down of certain e-services. This move is big relief for tax professionals who are under tremendous pressure to file the tax returns within time.

No Extension of Date for Filing of Returns due by 30th September for Assessment Year 2015-16 for Certain Categories of Assessees Including Companies, and Firms and, Individuals Engaged in Proprietary Business/Profession etc whose Accounts are required to be audited. Departmental release advised tax payers to file their Returns well in time to avoid last minute rush. Though the Government has received representations from various stakeholders seeking extension of date for filing of returns and tax audit reports beyond 30th September 2015, it has been decided that the last date for filing of returns due by 30th September 2015 will not be extended. The Association is filing a memorandum to the Department in this regard and communicating with other trade bodies to support the extension of due date.

Considering the inconvenience to the tax payers and hard ship faced Chartered Accountants, our Association is planning to challenge the decision of Finance Ministry not to extend the due date by filing a writ petition in the High Court of Karnataka for directing the CBDT and Government to extend the date of filing of Returns due by 30th September for Assessment Year 2015-2016 for Categories of Assesses Including Companies, and Firms and, Individuals Engaged in Proprietary Business/Profession etc., whose Accounts are required to be Audited as per Income Tax Act, 1961 from 30.09.2015. Our Association is making tremendous efforts to seek this extension which is much needed to balance our professional life.

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News Bulletin
September 2015
Vol. 3 Issue 1
No. of Pages : 20

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Executive Committee Communique

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The CBDT has notified the income computation and disclosure standards in exercise of the powers conferred by sub-section (2) of section 145 of the Income-tax Act, 1961. This notification shall come into force with effect from 1st day of April, 2015 and applicable to all taxpayers (corporate and non-corporate) following mercantile method of accounting including non-resident taxpayers. It applies to income computed under the head Profit and Gains of Business and Profession and Income from Other Sources. Our association has hosted a work shop on overview of Income Computation and Disclosure Standards for the benefit of members and fellow professionals.

Association has organised another two workshops, one on Tax Audit-Issues and Solutions and Deemed sales under KVAT Act 2003 which was well received. During printing of this edition of bulletin, another workshop on "Depreciation under the Companies Act, 2013 with special emphasis on transitional provisions" is being organised for the benefit of the professionals to bring more efficiency in their professional work.

Association intend to conduct more programmes in mofussil areas, request all members to suggest burning topics which may immensely help the members in mofussil areas from such workshops. You may send your suggestions to kscaablr@gmail.com.

Executive Committee organised a mentors meet to seek guidance and suggestions from our Past Presidents and other well wishers of the association. The discussions at the meet were really an eye opener and suggestions were worth considering. We from Executive Committee, try to adopt those suggestions to bring new dimensions to association and profession. We are grateful to our mentors for their valuable time, suggestions and guidance.

ICAI has announced Elections to its Council and Regional Councils through Notification No.54-EL(1)/2/2015 dated 3rd September 2015 and specified 24.09.2015 -6.00 PM as last date and time for receipt of nominations. Further Election Code of Conduct comes in to force from Thursday, 3rd September, 2015 and shall be in force till declaration of results of Elections. Prospective candidates shall keep in mind these code of conduct made under rule 16 of the Chartered Accountants (Election to the Council) Rules, 2006 in performing their social life and campaign. Elections are going to be held on 4th and 5th December, 2015 and our profession has seen poor turnout during voting. Members are requested not to forget this fundamental duty towards our mother Institute in electing suitable candidates who can contribute growth of our beloved profession.

Season of festivities also started with this Shravana month. We wish a happy Ganesha Chaturthi and delightful tax season for our readers. Hope we will complete all our pending audits and tax filing in time.

"Being a professional is doing the things you love to do, on the days you don't feel like doing them."

Always in service of profession,

Executive Committee
Karnataka State Chartered Accountants Association

Service Tax on Industrial Canteen Supplies

CA Mahadev.R

There is confusion with respect to levy of service tax on the services provided by outdoor caterers to industries after the amendment made in mega exemption notification no.25/2012 on 22.10.2013. Presently, few of the caterers have been charging and collecting service tax for such services unless questioned. In this article, we have tried to analyse and interpret the exemption entry which could be useful to many assessees availing the outdoor catering services.

An exemption entry 19A has been brought into the mega exemption notification in service tax from 22.10.2013 which is as follows:

*"Services provided **in relation to** serving of food or beverages **by a canteen maintained in a factory** covered under the Factories Act, 1948 (63 of 1948), having the facility of air-conditioning or central air-heating at any time during the year".*

Exemption only for A/C canteens?

With the introduction of this entry, the first confusion which got created is whether the exemption is available only in case of air-conditioned canteen maintained in factory or it covers non air-conditioned canteens as well.

In this regard, it is essential to consider exemption entry no.19 which reads as under:

"Services provided in relation to serving of food or beverages by a restaurant, eating joint or a mess, other than those having the facility of air-conditioning or central air-heating in any part of the establishment, at any time during the year".

As the canteen in a factory could also be treated as restaurant or eating joint, it could be concluded that the food served in canteen without air-conditioned facility is exempted from service tax.

Exemption to A/C canteen

The other confusion created in minds of assessee is whether the service provided by outdoor catering agency to factory is exempted or is it service provided from factory to employees exempted?

One interpretation which could be made is that the exemption is available when the canteen services are provided by factory / employer to employees and amounts are collected for it. The exemption is not available when services are provided by outdoor catering agency to factory. This is because the words used are 'services by a canteen' and not 'services provided to canteen'. Readers should also note that the Supreme Court in case of *CCE Vs. Mewar Bartan Nirman Udyog 2008 (231) ELT 0027 (SC)* has held that exemption notification has to be read strictly and the exemption has to be interpreted in terms of its language used in the notification. Similar view was held in case of *Sarabhai M Chemicals Vs CCE 2005 (179) ELT 0003 (SC)* by the Supreme Court.

The other beneficial interpretation which could be made is that exemption is available to services provided "*in relation to*" serving of food or beverages by a canteen. Even the services of outdoor catering agency are 'in relation to' serving of food by a canteen and thus eligible for exemption. The authors are of the view that this interpretation would hold good as the intention of this entry seems to be to reduce cost of food for employees. Contrary to views expressed by Supreme Court in earlier discussed case laws, the Supreme Court in case of *Comm. Of Customs Vs. M Ambalal & Co. 2010-TIOL-111-SC-CUS* had held that exemptions should generally be strictly interpreted but beneficial exemptions having their purpose as encouragement or promotion of certain activities should be liberally interpreted. In the present case, as the intention could be to reduce the service tax cost to the employees, the notification entry could be liberally interpreted.

As different views are possible, it is essential for the CBEC to clarify and remove the confusion with regard to exemption as different views are followed by the caterers. Moreover, the Cenvat credit of service tax paid on canteen service is also being disallowed to the assessee by the department stating that the services are consumed by employees. It may be noted that recently the tribunal in case of *Hindustan Coca Cola Beverages (P) Ltd. Vs. CCE* 2014-TIOL-2460 *CESTAT Mumbai* has held that the credit shall be allowed on canteen services when it is generally used for business purpose in a

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AMENDMENT IN VAT REGISTRATION CERTIFICATE

CA G.B. Srikanth Acharaya and CA Annapurna Kabra

Every dealer whose taxable turnover exceeds ten lakhs per annum is liable to get registered under KVAT law and apply electronically with the specified procedures. Now with the recent introduction of amendment procedure in KVAT registration certificate the dealer should apply for amendment in the following circumstances like:

a. Change in address

b. Addition or deletion of goods dealt by the dealers

c. Change in the name of the business

d. Change of the constitution like increase or decrease of partners

e. Additional place of business etc.

The dealer is required to logon to the departmental website using the user name and pass word provided to him. The required form can be opened by following steps.

others ⇨ Amendment based on ⇨ Self Authentication / Verification / Inspection /Check Status path way.

Under this scheme the dealer can amend under the registration fields at three levels depending on importance of the data from legal and administrative point of view. In certain fields the dealer can amend the data without any formal verification. With the deemed approval from the Registering Authority the amendments can be carried out.

1. Self Authentication: This form involves those fields that are covered under deemed approval of amendment.

By clicking on "Self Authentication" submenu consisting of Part-A, Part-B, CST/ KTEG, Bank Info, Form VAT 3, Form VAT 4 and Finish screens are appears in the left corner of the screen.

This submenu allows amendments for Fathers name, sex, Date of Birth, Registration details with other statutory authorities, contact details.

On left side of the screen existing registration details have been displayed.	On the right side of the screen field /boxes have been provided to enter new values.

Above boxes can be activated by clicking check box provided in the middle of the screen

Any amendment made in this sub menu does not require any documentary support either to be uploaded or to be handed over to the concerned jurisdictional LVO. The corrections /amendments made to the fields in this screen will be automatically saved to the system by clicking the "Submit" button in " Finish" screen.

Part A:

Click Select button – To make appropriate changes

Click Update button – To update the changes

Click Add button – To add new data

Click delete button – To delete existing data

One of the important provisions is that the dealer can enter his registration details with other statutory authorities afresh or amend the details already existing in the system.

Part B:

Click Check box – To amend the residential address which had been declared to the department at the time of obtaining registration.

Click outside Karnataka button - If business located outside the state then select your native state.

New commodity under VAT act can be added here.

CST/ KTEG: For addition of new commodity and its effective date

Click Check box - From the drop down menu select required commodity.

For dealers register under KTEG and CST Act: New commodity under VAT act can be added here and the effective date of new commodity added under, KTEG and CST Act is from Prospective date. Without first adding a new commodity under VAT in Part B, the system will not allow it to be included under CST Act.

For dealers not register under KTEG and CST Act:

Click radio button: To add new commodities. But inclusion of the commodity will not be allowed on the same day of applying for registration.

Bank info screen: To edit or delete the Bank information. If any other bank information to be added then select the other banks.

Form VAT 3 (Additional place of business): Changes can be Telephone number, Email ID or mobile number

Form VAT 4 (Partners details): Changes can be Telephone number, Email ID or mobile number

2) Verification: This form involves those fields where the amendments needs to be carried out by the LVO after duly verifying the documentary evidences filed on line by the dealer.

In Part –A number of partners in a partnership concern can be updated.

In PART- B screen, the dealer can alter the type of business If wants to include a commodity under CST Act, he has to first include the same under KVAT Act . Suppose if he is no more dealing in that commodity by clicking "Delete "button.

CST/ KTEG screen, a provision has been made to include commodities under CST Act from retrospective date subjected to condition that such commodity necessarily required to be included under KVAT Act first in the previous screen

In Form-4 screen the constitution details of partnership concern can be amended. For this purpose the dealer is required to upload the self-attested copy of reconstituted partnership deed for verification of the LVO. Once the dealer is finished with entering the details, he can click the " Submit '' button. An unique amendment application number will be generated.

3) Inspection: This form involves those fields where the amendments needs to be carried out by the LVO after duly getting a field visit report of the official of the Department

The amendments will not be automatically saved to the system unless the jurisdictional LVO approves the amendment based on the report given by the CTI.

Part-A of the screen contains the existing trade name and address of the business concern and make new entry in right side. The documents required for address proof to be uploaded in support of the amendment sought i.e change in the business address is given.

In Form VAT-3 the dealer can amend the address, contact details, date of commencement etc of the existing additional place of business. He can also add new additional place of business

Once the dealer is finished with entering the details, he can click the " Submit '' button. An unique amendment application number will be generated

4) Check Status:- In the status of the applications for amendment filed electronically by the dealer will be displayed for his information.

On reaching "Finish" screen the system will prompt the dealer to ascertain whether the details entered into the system are correct or not. Once the dealer is sure of veracity of details entered he can save the same by clicking "Submit" button. A unique amendment application number will be generated by the system for future reference by the dealer.

The above procedure has to be followed depending upon the type of amendment to be made by the dealer.

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Service Tax on Industrial Canteen Supplies

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factory where having canteen is mandatory with 250 or more workers. The issue has been discussed in detailed manner in our previous article.

It is pertinent to note that the Cenvat credit on canteen services shall be allowed to other organisation even if it is not mandatory to have canteen as per Factories Act when services are in relation to business. In this regard, we could rely on the judgment of *CST Vs. Reliance Capital Asset Mgt Ltd 2015-TIOL-447-CESTAT-MUM* wherein the tribunal held that the credit would be eligible even for small organisation. The tribunal said that even the employees of a smaller organization having less than 250 workers will also be hungry and required to be provided with canteen facility for the employees which is very logical.

Conclusion

It is very clear that the intention of the Government is to remove burden of service tax on the employees in factory. If the caterer supplying food has been charging the service tax, then the assessee shall bring the exemption entry to his notice and instruct for not charging the service tax. Such caterers could intimate the department about the view followed and claim exemption to avoid unnecessary issues from department.

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Recent Decisions of The Supreme Court and High Courts on Income Tax

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CAPITAL RECEIPT

The Andhra Pradesh High Court in CIT v. My Home Power Ltd. (2015) 276 CTR (AP) 92 has expressed the view that the amount received by the assessee-company on sale of carbon credits was a capital receipt not chargeable to tax as the carbon credits are not even directly linked with the business of power generation carried on by it.

NO DIVERSION BY OVERRIDING TITLE

In Fr. Sunny Jose & Ors. v. UOI & Ors. (2015) 276 CTR (Ker) 512 where salaries were paid by the Government of Kerala to teachers employed in various aided educational institutions who were the members of religious congregations and the precepts of Cannon Law required the teachers to entrust the amounts received by them as salaries to the religious congregations they belonged to, the Kerala High Court ruled that salaries paid to the teachers accrued to them as individuals and not to the religious congregations of which they were members, that the obligation to entrust the salaries to the religious congregations was based on personal law, that the religious congregations had no legal right to receive the salaries directly from the State Government, that the salaries were taxable in the hands of the individual teachers and that it was not a case of diversion of income by overriding title.

PRELIMINARY EXPENDITURE

Where the assessee-company incurred expenditure on issue of shares and capitalised a part of the expenditure to plant & machinery and factory equipment, such expenditure falls within the purview of section 35D which allows amortisation thereof and not under section 32 and, therefore, depreciation on the capitalised expenditure is not allowable opined the Bombay High Court in International Computers Indian Manufacture Ltd. v. CIT (2015) 276 CTR (Bom) 57.

INTEREST ON BORROWED CAPITAL

The Supreme Court in Taparia Tools Ltd. v. JCIT (2015) 276 CTR (SC) 1 where the facts were that the assessee-company following mercantile system of accounting issued debentures redeemable after five years, the debenture-holders were given two options in the matter of payment of interest, they could receive interest every half-year @ 18% per annum over the period of five years or they could receive one-time upfront payment of interest of Rs. 55 per debenture immediately and the assessee paid upfront interest of Rs. 2,72,25,000 & Rs. 55,00,000 during the years ending 31.3.1996 & 31.3.1997 respectively to two debenture-holders who exercised the option of receiving upfront interest, ruled that the entire amount of upfront interest was allowable as a deduction under section 36(1)(iii) in the respective years of payment even though the assessee had spread over the interest over a period of five years in its books of account.

ADDITION TOWARDS UNDISCLOSED PURCHASES

Where the assessee furnished copies of purchase bills, particulars of payments made by account payee cheques drawn in favour of the creditors for goods and copies of bank statements of such creditors, the Assessing Officer, for the reason that the creditors were not available at the given addresses after two to three years, could not presume that the assessee had purchased the goods by making cash payments and make an addition towards undisclosed cash purchases and introduction of bogus sundry creditors held the Calcutta High Court in CIT v. Manish Enterprises (2015) 276 CTR (Cal) 89.

REVENUE EXPENDITURE

In CIT v. Spice Distribution Ltd. (2015) 374 ITR 30 (Del) where the assessee-company trading in mobile hand sets & accessories thereof incurred an expenditure of Rs. 11,51,40,004 on advertisement, the Delhi High Court observed that advertisement expenditure is a day to day expenditure incurred for running the business and improving sales and held that the expenditure incurred by the assessee was revenue in nature.

SECTION 40(a)(ia)

Section 40(a)(ia) applies not merely to assesses following the mercantile system but also to those following the cash system and disallowance thereunder can be made when payments in respect of which tax was deductible at source had been made by the assessee to the payee by the end of the previous year without deduction of tax at source opined the Punjab & Haryana High Court in P.M.S. Diesels v. CIT (2015) 374 ITR 562 (P & H).

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Service Tax on Works Contracts

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Introduction.

On August 20, 2015, in Commissioner, Central Excise v. Larsen & Toubro Ltd., C.A. No. 6770/2004, the Supreme Court held that service tax cannot be levied on indivisible works contracts prior to June 1, 2007. The Court reasoned that sinceworks contracts were not specifically defined under the Finance Act, 1994 ("Finance Act") to be a taxable service until June 1, 2007, there was no charge or machinery to levy service tax on such contracts. This article provides a background to the levy of service tax on works contracts, discusses theSupreme Court's judgment in Larsen & Toubro, and suggests that the observations judgment may also have a bearing on the levy of VAT on construction and sales of apartments pursuant to development agreements.

Background.

Prior to June 1, 2007, a number of composite contracts that involved the transfer of property in goods as well as the rendering of services were specified to be exigible to service tax. These services included, to name a few, "consulting engineer service," "erection, commissioning, and installation service," "construction service," and "construction of complex service." In a contract providing for the rendering of each of these services, there was inevitably an element of sale of goods involved, and the Union sought to separate the transfer of property in goods involved in the execution of the contracts and levy service tax on the service element.

It was only with effect from June 1, 2007, that Section 65(105)(zzzza) was inserted into the Finance Act, providing for the levy of service tax on works contracts per se. The said provision stated that "taxable service" includes a service provided "to any person, by any other person in relation to the execution of a works contract." The Explanation appended to the provision clarified that for the purposes of the provision, works contract means a contract wherein, "transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods," and such contract is for the purpose of carrying out: (a) erection, commissioning or installation of plant, machinery, equipment or structures, etc.; (b) construction of a new building or civil structure; (c) construction of a new residential complex; (d) completion and finishing services, repair, alteration, renovation, etc.; and (e) turnkey projects including engineering, procurement, and construction or commissioning projects.

Furthermore, Rule 2-A of the Service Tax (Determination of Value) Rules, 2006, provided for the determination of the value of the service portion in the execution of a works contract. Rule2-A(i) stated that the value of the service in the execution of a works contract is the gross amount charged for the works contract less the value of property in goods transferred in the execution of the said works contract. The Explanation to Rule 2-A clarified that the "value of works contract service" includes: (a) labour charges; (b) amounts paid to subcontractors; (c) charges for planning, designing, and architect's fees; (d) charges for obtaining on hire, machinery and tools used for the execution of the works contract; (e) cost of consumables such as water, electricity, fuel, etc.; (f) cost of establishment of the contractor relatable to supply of labour and services; (g) other similar expenses relatable to labour and services; and (h) profit earned by the service provider relatable to labour and services.

The Explanation to Rule 2-A further stated that where VAT/sales tax has been paid on the actual value of goods transferred in the execution of the works contract, then such amount shall be the value of the transfer of property in goods and service tax will be payable on the balance amount. In cases where the actual value of goods transferred had not been determined, the Rule prescribed varying percentages of the value of the contract on which tax is payable. In the case of "original works," tax shall be payable on 40% of the total amount charged for the works contract; in the case of works contracts entered into for "maintenance or repair or reconditioning or restoration or servicing of any goods," service tax shall be payable on 70% of the total amount charged for the works contract; and in the case of "other works contracts" not covered under either of the two heads mentioned above, service tax will be payable on 60% of the total amount charged for the works contract.

Therefore, with effect from June 1, 2007, for the first time, the Finance Act and the Rules issued thereunder defined what a works contract is, provided for the levy of service tax on the execution of works contracts, and set out the method for determining the value on which tax would be payable.

Rival Contentions.

The assessees challenged the validity of the levy of service tax on works contracts executed prior to June 1, 2007, on the ground that an indivisible works contract cannot be split

into its constituent parts without the concerned legislation permitting such splitting. According to the assessees, before June 1, 2007, there was no charging provision or any machinery provisions that permitted the Union to split an indivisible works contract and levy service tax on the service portion thereof. Therefore, the assessees contended that the pre-June 2007 provisions contemplated the levy of service tax on only pure service contracts and not hybrid contracts involving the sale of goods and the rendering of service.

On the other hand, the Revenue's contention, simply put, was that the 46th Constitutional Amendment itself provided the necessary machinery for the Union to split an indivisible contract for the purpose of levying service tax on the labour/ service element. Therefore, according to the Revenue, when the Constitution itself provided the necessary machinery, there was no requirement for the Finance Act to define what a works contract is and permit the Union to split such contracts.

The Supreme Court's Judgment.

The Supreme Court's analysis of the issues raised in this case was based primarily on the Court's landmark judgment in Gannon Dunkerley v. State of Rajasthan, (1993) 88 STC 204 (SC). In the Court's words, "crucial to the understanding of the issue at hand is the second *Gannon Dunkerley* judgment," wherein "the modalities of taxing composite indivisible works contracts was gone into." After extracting a substantial portion of the judgment in Gannon Dunkerley, the Court observed as follows:

> *"This judgment, therefore, clearly and unmistakably holds that unless the splitting of an indivisible works contract is done taking into account the eight heads of deduction, the charge to tax that would be made would otherwise contain, apart from other things, the entire cost of establishment, other expenses, and profit earned by the contractor and would transgress into forbidden territory namely into such portion of such cost, expenses, and profit as would be attributable in the works contract to the transfer of property in goods in such contract. This being the case, we feel the learned counsel for the assessees are on firm ground when they state that the service tax charging section itself must lay down with specificity that the levy of service tax can only be on works contracts, and the measure of tax can only be on that portion of works contracts which contain a service element which is to be derived from the gross amount charged for the works contract less the value of property in goods transferred in the execution of the works contract. This not having been done by the Finance Act, 1994, it is clear that any charge to tax under the five heads in Section 65(105) noticed above would only be service contracts simpliciter and not composite indivisible works contracts."*

The Court, therefore, held that since the Finance Act did not provide for the bifurcation of an indivisible contract for the purpose of levying service tax, the levy of tax prior to June 1, 2007, must be restricted to pure service contracts and cannot be extended to indivisible works contracts.

In this regard, the Court further observed that a works contract is a separate species of contract and, therefore, the assessees were right in contending that, prior to June 1, 2007, the Finance Act did not contain a charging provision that permitted the levy of tax on works contracts. Relying on the wording of the charging provision, namely Section 65(105), the Court observed that, "what is referred to in the charging provision is the taxation of service contracts simpliciter and not composite works contracts." Thus, the Court found that, in the absence of a charging section providing for the levy of tax specifically on works contracts, the contracts that were sought to be taxed prior to June 1, 2007, could only have been service contracts simpliciter and not composite works contracts.

Therefore, as per the Court's ruling, an erection, installation, and commissioning contract that was composite in nature and contemplated the supply of goods in addition to rendering of services could not have been brought to tax prior to June 1, 2007. In order to be exigible to service tax, the contact ought to have been a pure service contract. It was only after the introduction of "works contract service" as a taxable service that the Union was permitted to bifurcate an indivisible composite works contract and levy service tax on the service element involved in it.

The Court further proceeded to make some very important observations regarding the taxing power of the Union and the States in our federal structure. The relevant observations are as follows:

> *"[T]he moment the levy contained in a taxing statute transgressed into a prohibited exclusive field, it is liable to be struck down. In the present case, the dichotomy is between sales tax leviable by the States and service tax leviable by the Centre. When it comes to composite indivisible works contracts, such contracts can be taxed by Parliament as well as the State legislatures. Parliament can only tax the service element contained in these contracts, and the States can only tax the transfer of property in goods element contained in these contracts. Thus, it becomes very important to segregate the two elements completely for if some element of transfer of property in goods remains when a service tax is levied, the said levy would be constitutionally infirm."*

The Court found that, prior to June 1, 2007, the Finance Act did not contain any machinery provisions that permitted the Union to remove from the total value of the contract, the

amounts received for rendering of services. In this regard, the Court observed that, "[i]t will also be noticed that no attempt to remove the non-service elements from the composite works contracts have been made by any of the aforesaid Sections by deducting from the gross value of the works contract the value of the property in goods transferred in the execution of a works contract." According to the Court, it is the scheme provided under Rule 2-A of the Service Tax (Determination of Value) Rules, 2006, "alone which complies with the constitutional requirements in that it bifurcates a composite indivisible works contract and takes care to see that no element attributable to the property in goods transferred pursuant to such contract, enters into computation of tax."

The Revenue relied extensively on the judgment of the Supreme Court in MahimPatram Pvt. Ltd. v. Union of India, (2007) 3 SCC 668, in support of the proposition that even when rules are not framed to provide for the method of computation of tax, the levy of tax would still be sustainable. The Court, however, held that the judgment in MahimPatram was of no relevance to the case on hand. In MahimPatram, the argument of the assessee was that no tax could be levied under the provisions of the Central Sales Tax Act, 1956 ("CST Act"), in the absence of any rule prescribing the manner of computing the turnover on which tax is leviable. The Court, however, repelled the arguments of the assessee in MahimPatramand held that Section 9(2) of the CST Act conferred power on the officers to utilize the machinery provisions of the respective sales tax statutes for the purpose of levy and assessment of tax.

The Court, therefore, held that the judgment in MahimPatram was distinguishable and not applicable to this case. The Court, thereafter, relied on its earlier judgment in Heinz India v. State of Uttar Pradesh, (2012) 5 SCC 443, and held that where there is no machinery for assessment provided under the Act or the Rules, application of the law would be left to the whims of the assessing officers, and the same would result in the arbitrary assessment of tax. The Court, accordingly, concluded that there can be no levy of tax in the absence of the requisite machinery provisions.

An additional contentionwas raised by the Revenue by placing reliance on McDowell and Co. v. Commercial Tax Officer, (1985) 2 SCC 230. The contention in this regard was, essentially, that post 1994, all indivisible works contracts were made with the specific intent of evading or avoiding tax and that, therefore, such contracts were contrary to public policy and the principles laid down in McDowell should apply to make such "so-called indivisible contracts taxable under the Finance Act, 1994." This contention, too, was rejected by the Court by observing that, "in view of our finding that the said Finance Act lays down no charge or machinery to levy and assess service tax on indivisible works contracts, such argument must fail."

Discussion.

Apart from providing relief to a number of assessees in respect of tax periods prior to June 1, 2007, this judgment is of vital importance because of the manner in which the Court had lucidly dealt with the issue of separation of taxing powers between the Union and the States. Pertinently, the Court lays the onus on the legislature, be it the Parliament or the State, to clearly demarcate the turnover which it seeks to tax, failing which the levy would be constitutionally invalid. The observations of the Court in this regard will most certainlybe useful to assessees in cases where there is a dual levy of sales tax and service tax on the same transaction.

The judgment has also exhaustively dealt with the question of the charge of tax and the measure of tax, and reiterated the well-settled position of law that in the absence of a charge or machinery provisions to levy and assess tax, the tax would not be sustainable. As suggested in the opening paragraph of this article, the observations of the Court in this regard would have a bearing on the levy of VAT on sales of apartments and units pursuant to development agreements. In paragraph 115 of the Supreme Court's judgment in Larsen & Toubro v. State of Karnataka, (2013) 65 VST 1 (SC), it has been observed that "the activity of construction undertaken by the developer would be works contract only from the stage the developer enters into a contract with the flat purchaser." According to the Court, "the value addition made to the goods transferred after the agreement is entered into with the flat purchaser can only be made chargeable to tax by the State Government." Therefore, as per the Court's judgment, the value of goods used in the development of the project prior to entering into a contract with the purchaser cannot be brought to sales tax/ VAT.

In one of my earlier articles[1], I had explained that after the Supreme Court's judgment, the Maharashtra State Government amended the MVAT Rules in order to give effect to the observations contained in the judgment, and the validity of those Rules were upheld by the Bombay High Court in CREDAI - Maharashtra v. State of Maharashtra, WP No. 4520/2014.

Among various other amendments, the Maharashtra Governmentinserted Rule 58(1-B), which reads as under:

> *"Rule 58(1-B)(a) Where the dealer undertakes the construction of flats, dwellings, buildings or premises and transfers them in pursuance of an agreement along with the*

[1] See June 2015 KSCAA News Bulletin

land or interest underlying the land then, after deductions under sub-rules (1) and (1-A) from the total contract prices, the value of the goods involved in the works contract shall be determined after applying the percentage provided in column (3)of the following Table depending upon the stage at which the purchaser entered into contract."

The table appended to the above rule provides the following 5 stages during which the developer enters into a contract with the prospective purchaser, and specifies the corresponding percentage of the contract receipts to be the value of goods involved in the execution of the works contract:

(a) Before issue of commencement certificate: 100%

(b) From the commencement certificate to the completion of plinth value: 95%

(c) After the completion of plinth level to the completion of 100% of the RCC framework: 85%

(d) After the completion of 100% RCC framework to the occupancy certificate: 55%

(e) After the occupancy certificate: Nil

Rule 58(1-B) has clearly been inserted keeping in mind the observations of the Supreme Court in paragraph 115 of the Larsen & Toubro(65 VST 1) judgment, wherein the Supreme Court held that only the value addition made to the goods transferred after the agreement is entered into with the flat purchaser can be brought to tax. Recognizing that it would be very difficult, and rather arbitrary, to determine the exact value addition to the goods after the developer enters into a contract with a purchaser, the Maharashtra Government has adopted an ad hoc percentage to denote the value of goods transferred to the purchaser depending on which stage it enters into a contract with the developer.

Therefore, Rule 58(1-B) is the machinery provision that ensures that only the transfer of property in goods after the agreement is entered into between the flat purchaser and the developer is brought to tax. Interestingly, most States, including Karnataka, do not contain similar machinery provisions. In light of the recent judgment in Larsen & Toubro (the service tax judgment), holding that tax is not leviable if the Act or the Rules do not contain the necessary machinery provisions to provide for the levy of tax, it is arguable that, in the absence of any machinery provisions such as Rule 58(1-B), the levy of tax by the State on construction and sales of apartments is unsustainable. In short, it can be argued that in the absence of machinery provisions to remove from the taxable value, the turnover of goods used in the development of the project before the developer and the purchaser enter into a contract, the application of the law would be left to the whims of the assessing officers, and the same would result in the arbitrary assessment of tax.

Conclusion.

In sum, this is an excellent judgment, not merely because the Court held in favour of the assessee, but because important legal principles have been discussed and analyzed with great clarity, and these legal principles will be of great assistance to assessees who are liable to pay not only service tax but also VAT.

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Recent Decisions of The Supreme Court and High Courts on Income Tax

(Contd. from page 7)

CAPITAL GAINS

The Bombay High Court has in CIT v. Nitish Rameshchandra Chordia (2015) 374 ITR 531 (Bom) ruled that the amendment made in section 2(14) by the Finance Act, 2013 providing that the distance of the agricultural land from the municipal limit should be measured aerially is prospective in nature applicable in respect of the assessment year 2014-15 and subsequent years and does not apply to earlier assessment years.

HIGH COURT

In Somerset Place Co-operative Housing Society Ltd. v. ITO (2015) 374 ITR 307 (Bom) where the assessee did not prefer an appeal to the High Court against the order of the Tribunal though there were decisions of other High Courts in its favour but filed an appeal after five years after the jurisdictional High Court rendered a favourable decision, the Bombay High Court expressed the view that the delay in filing the appeal could not be condoned.

TAX DEDUCTION AT SOURCE

The Gujarat High Court has in CIT v. City Gold Entertainment (P) Ltd. (2015) 276 CTR (Guj) 539 held that payments made by the assessee running a theatre to the distributor under an agreement in terms of which the assessee would exhibit films provided by the distributor and the distributor was to get a part of the amount collected by the assessee from sale of tickets for the films was not liable for deduction of tax at source under section 194C as the distributor got his share because he had acquired the rights of distribution of the films in the particular area and he had not carried out any work for which the payment is made.

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Indirect Taxes Update – Aug 2015

CA C.R. Raghavendra, *B.Com, FCA, LLB, Advocate* and
CA J.S. Bhanu Murthy, *B.Com, FCA, LLB, Advocate*

Important Decisions

1. **CCE Vs. Hindustan Lever Ltd. 2015-TIOL-194-SC-CX**

   Issue: The issue involved in the appeal is as to whether Vaseline Intensive Care Heel Guard is to be treated as merely a skin care preparation or it is a medicament having curing properties.

   Held: Hon'ble Supreme Court holding the product as medicament observed that on examination of both entries it would come out that if a product is for care of the skin, then it would fall under Chapter Heading 3304.00 as skin care product, whereas if it is for the cure of skin disease then the product in-question would be medicament. In the case of 'Heel Gaurd' in question the same is manufactured as a solution to cracked heel based on the research conducted in house by the company. Further product was manufactured under a drug licence as drug authorities had treated the same as a medicament. Based on the above, it is clear that the product is in the therapeutic in nature.

2. **CCE Vs. M/s INDORAMA SYNTHETICS (I) LTD & C 2015-TIOL-190-SC-CX**

   Facts: The assessee had supplied goods to a particular type of buyers at much lower price than the price charged from the general buyers in the normal course of trade as it had obtained the facility of invalidating of advance licences from such buyers and procured imported raw material (duty free) against such licences for manufacturing of finished goods. It is, therefore, alleged by the department that the assessee received additional consideration in the form of duty free imports and such additional consideration should also be added to the value for the purpose of discharge of duty of excise.

   Held: The Supreme Court agreeing with the contention of the department that the invalidation of licenses in favour of the assessee by the buyer shall be considered as additional consideration observed that the Commissioner has rightly come to the conclusion with regard to the fact that additional monetary consideration, in the nature of transfer of advance import licence in favour of the seller by the buyer. The invalidation would enable the seller of the goods to effect duty free import of the raw materials and bringing down the cost of production/procurement, is a consideration, the monetary value of which has to be considered under the provisions of Rule 6 of Central excise valuation rules.

3. **CCE Vs Larsen & Tubro Ltd. 2015-TIOL-187-SC-ST**

   Issue: Whether service tax could be levied on the composite contracts / works contract prior to 1.6.2007, from the date when separate entry under service tax legislation was introduced.

   Held: The Supreme Court based on the following observations held that no service tax could be levied on works contracts prior to 1.6.2007:

a) In the lists contained in the 7th Schedule to the Constitution, taxation entries are to be found only in lists I and II. This is for the reason that in our Constitutional scheme, taxation powers of the Centre and the States are mutually exclusive. There is no concurrent power of taxation. This being the case, the moment the levy contained in a taxing statute transgresses into a prohibited exclusive field, it is liable to be struck down. In the present case, the dichotomy is between sales tax leviable by the States and service tax leviable by the Centre. When it comes to composite indivisible works contracts, such contracts can be taxed by Parliament as well as State legislatures. Parliament can only tax the service element contained in these contracts, and the States can only tax the transfer of property in goods element contained in these contracts. Thus, it becomes very important to segregate the two elements completely for if some element of transfer of property in goods remains when a service tax is levied, the said levy would be found to be constitutionally infirm.

b) Works contract is a separate species of contract distinct from contracts for services simpliciter recognized by the world of commerce and law as such, and has to be taxed separately as such

c) As held by the Supreme Court in the case of Mathuram Agarwal, 1999 8 SCC 667, the statute should clearly and unambiguously convey the three components of the tax law i.e. the subject of the tax, the person who is liable to pay the tax and the rate at which the tax is to be paid. If

there is any ambiguity regarding any of these ingredients in a taxation statute then there is no tax in law. Then it is for the legislature to do the needful in the matter.

d) Charging section under service tax legislation itself must lay down with specificity that the levy of service tax can only be on works contracts, and the measure of tax can only be on that portion of works contracts which contain a service element which is to be derived from the gross amount charged for the works contract less the value of property in goods transferred in the execution of the works contract. As this not having been done by the Finance Act, 1994,(prior to 1.6.2007) it is clear that any charge to tax under the other heads in Section 65(105) would only be of service contracts simplicitor and not composite indivisible works contract.

e) Judgment of High Court in the case G.D Builders is wholly incorrect in its conclusion that the Finance Act, 1994 contains both the charge and machinery for levy and assessment of service tax on indivisible works contracts

4. Poonam Spark Pvt Ltd Vs. CCE, 2015-TIOL-158-SC-CX

Facts: Filter Housing and Cartridges are imported by the Assess through M/s Cuno Asia Pte Ltd, Singapore and UV based Filtration and Purification unit from Rathi Brothers/ IWT Poona. The appellants undertake the job of assembling all the items received from M/s. Perfect Drug Ltd. on a base plate and thus brings into existence a new and commercially different commodity known as Water Purification & Filtration System. The issue is whether the said process would amount to manufacture.

Held: Based on the facts, the Supreme Court concurred with the findings of the Tribunal that the process of assembly undertaken by the appellant would amount to manufacture as a new commodity known as water purification & filtration system would emerge.

5. **Union of India Vs. DSCL Sugar 2015(322)ELT 769(SC)**

Issue: Whether Bagasse, generated during the course of crushing of sugarcane, could be treated as mainufactured product and in terms of Rule 6 of Cenvat Credit Rules, 2004 payment of 6%/8%/10% of value of is required as Bagasse carries NIL rate of duty.

Held: The Supreme Court held that the Bagasse is not an excisable product as the process of generation of Bagassee cannot be termed as manufacture. Therefore, once the Bagasse is not a manufactured product, the provisions of Rule 6 does not apply. The Court further, held that the once the goods are not at all manufactured products concept of deemed marketability in terms of Section 2(d) of Central Excise Act, 1944 would have no importance.

6. **CCE Vs. CESTAT Chennai, 2015(322)ELT 697(Mad.)**

Facts: Assessee is engaged in manufacture of machine tools on job-work for principal manufacturer as well as on their own. The goods manufactured on job-work are cleared to principal manufacturer without payment of duty, whereas the goods manufactured on their own are cleared on payment of duty. The assessee was availing credit on inputs and capital goods.

Dispute: The contention of the department is that the assessee is clearing the goods without payment of duty to principal manufacturer and hence they have to reverse proportionate credit in terms of Rule 6 of Cenvat Credit Rules, 2004

Held: The High Court concurring with the view of the CESTAT observed that the goods cleared on job work cannot be equated to exempted goods and hence the provisions of Rule 6 cannot be made applicable. The Court relied upon the decision of Supreme Court decision in the case of Escorts Ltd. Vs. CCe, 2004(171)ELT 145 and Bombay High Court decision in the case of Sterlite Industries Ltd.

7. **Condon Power Products P Ltd. VS. CCE, 2015(322) ELT 755(Tri.-Delhi)**

Facts: The finished products cleared on payment of duty were returned by the customer on account of quality reasons. The assessee availed cenvat credit of such duty paid on the returned goods in terms of Rule 16(1) of Central Excise Rules, 2002 and used the parts of the such returned goods in manufacture of the other finished products. The department contended that the said credit needs to be reversed as the defective goods were not sent back after repairs.

Held: The Tribunal held that Rule 16 provides for availment of credit on return of duty paid finished products and reversal of credit so availed on clearance after repair or rectification if such process does not amount to manufacture and in any other case, to pay applicable duty on clearance. On the basis of this, the Tribunal in the present case held that the defective goods received back were used in manufacture of new final products and hence the conditions of Rule 16 have been fulfilled by the assessee. Therefore, credit cannot be denied.

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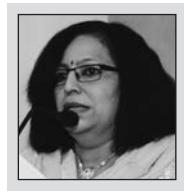
Epic Women from the Epics



CA Roopa Venkatesh

Dear Professional Colleagues,

Continuing our earlier conversation, here is a "learning" sketch from the Mahabharata (the Epic of Epic proportions).

The Indian psyche is embedded with the presence of the Epics – the Ramayana and the Mahabharata.

Today's world is changing. Today there are women in the workforce. Yet, we find that they are often limited to, or restricted to certain roles and functions. At home we find that the girl child is making sacrifices for her brothers all the time. In society we find that women are being marginalized – ignored at best, and ill treated at worst.

Of course the circumstances and trials of these women may be different, yet there is a lesson to be learnt. The emotions are the same, the feelings are similar. The background varies, but they are all in the background of the same canvas of close relationships.

We may use the example of one powerful woman from the Epic of Mahabharata.

Draupadi

She is the daughter of one of the most powerful kings in Aryavartha – Drupada. She is also called Agni jyotsna (the light of the fire) or Krsnaa Draupadi (the dark complexioned one) or Yajnaseni (born of the sacred fire).

Fiery, feisty, and devoted to her father and later her husbands, she is beautiful and intelligent. She is dark, endowed with enchanting bodily fragrance and rivetingly lovely. She is well versed in the art of war and the court. She is a capable administrator and fine judge of persons.

Birth is an incident, does not define your future

It is true that leaders are made not always born. Draupadi seems to signify that principle**.**

She is married to not one but five of the most influential kings in Aryavartha – the Pandavas. Yet she suffers untold miseries and rises above them. Birth is an incident, and does not define your future.

Polyandry (one woman with many husbands) was not common in those times. Yet, she is put in circumstances which force her to accept five husbands. There is an interesting story about why this happens. Apparently, in her earlier birth as Nalayani (daughter of Nala and Damayanti) she prayed to Lord Shiva asking for a husband with 14 qualities. Lord Shiva was pleased with her devotion but conceded that it would be difficult to find one husband with all these qualities, so blessed her with five husbands!! (shows that we should be careful in what we aspire for!! She certainly ended up with more than she bargained for!!)

Wholly unconventional she accepts the challenge of having five husbands. Without falling into a rut of self doubt or self pity, she manages to convert even this challenge into a personal triumph, thru her choices.

Leadership is about knowledge and reasoning.

Yudhishtira agrees to a game of dice with his cousin – Duryodhana. And wagers his property, and himself and his brothers and loses them to Duryodhana. But when the villain is winning, he is on a roll!! He even loses his wife Draupadi and loses her.What follows after that can be considered a defining moment of the Epic, as well as one of the foundations of the war which follows much later.

Draupadi is dragged into court. On being told of her fate, in a situation where any other woman would have collapsed in hysterics, Draupadi displays her immense understanding of the tenets of Dharma and courtly behaviour.

She questions the upholders of Dharma, whether her husband lost her before or after he wagered himself. If it was after he lost himself as a bet, then he technically could not wager anything else, as he is not an owner anymore. If he wagered his wife before himself, then it was wrong, because he had sworn before the sacred fire that he would protect her from all hardships by putting himself first before trouble. So either way he could not put her as a wager.

Duryodhana, drunk with power and the euphoria of winning, demands that as the Pandavas are now his slaves, they should be dressed accordingly – and wanted to disrobe Draupadi.

Imagine a woman, inherently strong, who has an influential and powerful father and extraordinarily brave brother, five powerful husbands, but none to protect her – an example, that ultimately, what matters is yourself and your destiny.

She prays to Krishna, who blesses her with unending clothing. Of course there are many versions of this – the original Epic talks of the intervention of "Dharma" – which could mean either Bhishma, or Vidura, Vikarna, (all of these people were referred to as Dharma).

This incident highlights that pedigree will take you only that far, it does not guarantee how fairly you will be treated by life

Leaders are excellent communicators:

Communication is the grease which keeps the human factory running!! And effective communication could mean a world of difference.

Draupadi was kidnapped by Jayadratha, who she first tries to physically overcome (she is a strong woman), but when that fails, she uses her skills of communication, to strike fear into him – extolling the virtues of her husbands, who would certainly pursue and kill him for kidnapping her. She uses these delaying tactics, describing at length the troubles he would be inviting by kidnapping her. Her eloquent description of the strength of each of her husbands strikes fear into the heart of Jayadratha, who is more than willing to return her to her husbands.

Timing is of essence

Draupadi's suffering is almost unimaginable. Though a queen, humiliated in the court of Hastinapura, molested publicly in the court of Virata by Keechaka, asked to "not make a scene" by her husband – Yudhishtira, any lesser mortal would have gone insane.

To add insult to injury, her husbands want to forgive the perpetrators of the crimes!

But yet, she remains loyal to them, keeps them united, and ensures that the spirit of revenge does not die. Her character remains fiery and controlled. She is the uniting and motivating force behind her husbands.

But her patience does pay. When Krishna is going as a peace negotiator to avoid war, she makes it clear, that she is on the side of "war" as only that will avenge the many wrongs done to her. Her ability to touch the right chord with Krishna, is obvious, when an excited Krishna, who is going on a peace mission exclaims:

"Consider those you disfavour as already dead ! The Himavant hills may move, the earth shatter in a hundred pieces, the heavens may collapse; But my promise stands. You will see your enemies killed"

She is astute enough to know when to use the powers of her unrivalled charms and intellect to achieve her ends. She is courteous, and concerned. After the war, she devotedly serves Gandhari even though her sons caused her so much suffering.

Draupadi is also an empathetic mother. After Abhimanyu's death, she consoled his grieving widow, Uttara, by encouraging his widow, Uttara to gather her strength for the sake of her and Abhimanyu's child, whom she was carrying at the time. And yet, she herself was mourning – she lost all her 5 sons in the war.

Draupadi was a multifaceted personality: she could be fiery and angry when the situation called for it, but she still had a compassionate nature. She encouraged people to face life with the same inner strength that she did.

She was constantly guiding, uniting, communicating and leading the Pandavas on the path of Dharma – Duty.

Truly she was an EPIC woman, who shall continue to be a role model for all womanhood for times immemorial.

Today, when we read the story of Mahabharata we can empathise with Draupadi's character. We find that women today face the same challenges – working in a "man's world", facing bias, both at home and the work place, yet, if we look deep within, we can find the same resilience and strength she displayed.

I am sure most women can identify with and learn from this wonderful character.

Management of Co-operative Society and Audit Engagement – Fraud and Audit Risk under the Karnataka Co-operative Societies Act, 1959

CA G. Sathyanarayana

With the 97th constitutional amendment bill, the audits of co-operative societies are entrusted to Chartered Accountants to carry out statutory audit of co-operative societies.

The Karnataka Co-operative Societies Act, 1959 is suitably amended to provide for provisions relating to audit of a co-operative by substituting the sections related with the audit by passing the Act no. 3 of 2013, w.e.f 11-02-2013 to audit the accounts of a co-operative society by Chartered Accountant/ C.A. Firms. The same provisions are amended to include Cost accountants also to conduct the audit by passing the Act No. 35 of 2014 w.e.f 6th September 2014.

Hence the professionals gained the entry into the field of co-operatives to conduct the audit to a large extent in addition to departmental auditors. The legal provisions stated with audit of co-operative societies are enumerated in the following paragraphs:-

Legal provisions: Chapter VIII of the Karnataka Co-operative Societies Act, 1959

Section 63: Audit

(1) Every Co-Operative society shall get its accounts audited at least once in a year before the first of September following the close of the co-operative year by an auditor or an auditing firm appointed by the general body of the co-operative society from a panel of auditors or auditing firms approved by the Director of co-operative audit;

Provided that the Director of co-operative audit shall be the authority competent to prepare and maintain a list of auditors and auditing firms who satisfy the prescribed qualification and experience for undertaking the audit of accounts of co-operative societies in the State:

Provided further that, the National Bank shall prepare a list of auditors and auditing firms who satisfy the prescribed qualification and experience for undertaking the audit of accounts of State Co-operative Bank and District Central Co-operative Banks.

(2) The general body of every co-operative society shall at its general meeting appoint an auditor or auditing firm to audit the accounts of the society for the co-operative year in which the general meeting held:

Provided that, if the Director of Co-operative audit is satisfied that the society has failed to appoint an auditor or an auditing firm to audit its accounts for a Co-operative year in their general body and to intimate the same, the Director of Co-operative Audit, after giving an opportunity in writing to such society and after confirming that the society has not appointed an auditor or auditing firm, may appoint an auditor or an auditing firm to audit the accounts of that society from the approved panel of auditors or auditing firms and such appointed auditor or auditing firm shall be deemed as the auditor or the auditing firm for the purpose of conducting audit of that society for that particular co-operative year under consideration.

Provided, further that in case of Government auditors mentioned in the panel of auditors or auditing firms maintained by the director of Co-operative audit, they shall be mentioned by designation only and that in case of a Co-operative Society selecting a Government auditor from the empanelled list, the Co-operative Society shall intimate to the concerned deputy director of the Co-operative audit of the concerned district to cause the audit from a departmental auditor mentioning the auditors designation only.

(3) The manner of preparation of the list of auditors and auditing firms by the Director of the co-operative audit and the procedure for giving the panel to each co-operative society shall be such as may be prescribed.

(4) The audit under sub-section (1) of the Section or under Section 98-U or Section 98-V shall include an examination of overdue debts, if any, the physical verification and valuation of the assets and liabilities, verification of the cash balance and securities, certification of the profits or the losses, compliance with the transparency law and the other laws applicable to the co-operative societies including the instruction and directives of NABARD or Reserve Bank of India and an examination of the working and the other prescribed particulars of the society.

(5) The auditor or the auditing firm shall at all times have access to all the books, accounts, documents, papers, securities, cash and other properties belonging to the society or in the custody of any member of the board or the office-bearer or the Chief Executive or any other employee of the society and may summon any person in possession or responsible for the custody of any such books, accounts, documents, papers, securities, cash or

any other properties to produce the same at the registered office of the society or any branch thereof or at any public office at the headquarters of the society.

(6) Every person who is, or has at any time been, an officer or employee of the society and every member and past member of the society shall furnish such information in regard to the transaction and working of the society as the Auditor or Auditing firm approved by the Director of Co-operative Audit may require.

(7) The board of every co-operative society shall ensure that the annual financial statements like the receipts and the payments or income and expenditure, profit and the loss and the balance sheet along with the such schedules and other statements as prescribed as at the end of a co-operative year are prepared and the presented for audit before the auditor or auditing firm within thirty days of the closure of that co-operative year.

(8) The auditor or auditing firm shall conduct and complete the audit of accounts as provided for in this Act, or in the rules and send copies of the audit report and communicate the results of audit to the co-operative society, the Registrar, the Director of co-operative audit and to the financing bank or credit agency, and if the society is affiliated to any other co-operative society, to such co-operative society, as early as possible but within the first day of the September every year.

(9) The auditor or auditing firm shall have right to receive all notices and every communication relating to the general meeting of the co-operative society and, at the cost of the co-operative society, shall be entitled to attend such meeting and to be heard at the general body meeting, in respect of all or any part of the business with which he is concerned as auditor or auditing firm.

(10) If the result of the audit held under sub-section (1) discloses any defects in the working of the society, the board shall take steps to rectify the defects and the remedy irregularities pointed out in the audit report and place the audit report along with the action taken report before the general meeting to be held before Twenty-fifth day of the September every year and explain therein the said defects or the irregularities. The board shall continue to take steps for rectification of all the defects of and the remedying of all the irregularities in the audit report and appraise the general meetings every year till all the defects are rectified and the irregularities are remedied. The board shall send report of action taken to the Registrar and Directors of Co-operative Audit within thirty days from the date of general meeting.

(11) The Director Co-operative Audit shall submit the audit reports of an Apex co-operative society to the State Government annually for being laid before the legislature in the manner prescribed.

(12) If it appears to the general body of the co-operative society that there is *prima facie* case of fraud or misappropriation or embezzlement of funds not detected or properly examined by the auditor during the regular audit or misclassification of accounts, the general body may resolve to provide for a re-audit of any account of the society with a view to truly reflect the financial position of the society and the provision of the Act, and the rules applicable to the audit shall apply to such re-audit.

(13) If it appears to State Government on an application by a co-operative society or otherwise that it is necessary or expedient to re-audit the accounts of the society, the State Government may, by an order provide for such re-audit and the provision of the act, and the rules applicable to the audit shall apply to such re-audit :

Provided that such re-audit shall be ordered only when there is a *prima facie* case of fraud or misappropriation or embezzlement of funds not detected or properly examined by the auditor or auditing firms during regular audit or misclassification of accounts or for any other valid reasons with a view to truly reflect the financial position of the society.

(13A) Notwithstanding anything contained in the preceding sub-sections, the Director of Co-operative Audit subject to the approval of State Government shall have power to re-examine or re-verify particular account or accounts of the audited accounts of any Co-operative Society pertaining to preceding three years and instruct the concerned auditor to rectify the lapses observed during such re-examination or re-verification in the next audit report to be issued.

(14) Without prejudice to the provision of sub section (5) and (6), the auditor shall inquire:

(a) Whether loans and advances made by the co-operative society on the basis of security have been properly secured and whether terms on which they have been made are not prejudicial to the interests of the co-operative society or its members.

(b) Whether the transactions of the co-operative society which are represented merely by book entries are not prejudicial to the interest of co-operative society;

(c) Whether the personal expenses have been charged to revenue account;

(d) Where it is sated in the books and papers of the co-operative society that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account

books and the balance sheet is correct, regular and not misleading; and

(e) Whether any special issue or subject matter referred to for enquiry by the Reserve Bank or National Bank has been duly enquired into and report thereof is submitted to Reserve Bank or National Bank as the case may be.

(15) The auditor shall make report to the co-operative society on the accounts examined by him and on every balance sheet and profit and loss account and on every other document required to be part of or annexed to the balance-sheet or profit and loss account. The report shall state whether, in his opinion and to the best of his information and according to the explanations given to him, the said accounts give the information required by this Act, in the manner so required and give a true and fair view-

(a) In the case of balance-sheet, of the state of the co-operative society's affairs as at the end of the year; and

(b) In the case of the profit and loss account of the profit or loss for the year.

(16) The auditor's report shall also-

(a) State whether he has obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit;

(b) State whether in his opinion, proper books of accounts have been kept by the co-operative society so far as appears from his examination of those books and proper returns adequate for the purpose of his audit have been received from branches or offices of the co-operative society not visited by him;

(c) State whether the report on the accounts of any branch office audited by a person other than the co-operative society's auditor has been forwarded to him and how he has dealt with the same in preparing the auditor's report;

(d) State whether the co-operative society's balance sheet and profit and loss account dealt with by the report are in agreement with the books of accounts and returns;

(17) The audit report shall have –

(a) All particulars of the defects or the irregularities observed in audit and in case of financial irregularities and misappropriation or embezzlement of funds or fraud, the auditor/auditing firm shall investigate and report the *modus operandi*, the entrustment, amount involved, and fix the responsibility for such misappropriation or embezzlement of funds or fraud, on the members of the board or the employees of the society or any other person as the case may be with all necessary evidence;

(b) Accounting irregularities and their implications on the financial statements to be indicated in detail in the report with the corresponding effect on the profit and loss;

(c) The functioning of the general body, the board and sub committees of the co-operative society to be checked and any irregularities or violations observed reported duly fixing the responsibilities for such irregularities or violations;

(d) All schedules and other statements as may be prescribed.

(18) Where any of the matters referred to in clause (a) and (b) of the sub section (14) or in clauses (a) and (b) of sub section (15) or clauses (a) to (d) of sub section (16) is answered in negative or with a qualifying observation, the auditor's report shall state the reason for the answer.

(19) The remuneration of the auditor or auditing firm of a co-operative society shall be borne by the society and shall be at such rates as may be fixed by the general body of the society based on the working capital and turnover of the society as per the guidelines issued by Director of Cooperative audit from time to time.

(20) The Director of Co-operative Audit shall maintain a list of co-operative societies district-wise, the list of working societies, the list of societies whose accounts are audited, the list of societies whose accounts are not audited within a prescribed time and the reason thereof. He shall co-ordinate with the co-operative societies and the auditors or auditing firms and ensures the completion of audit of accounts of all the co-operative societies in time every year.

Explanation- For the purpose of this section –

(i) 'Auditor' means an auditor or an officer of the Department of Co-operative Audit who has passed, in addition to the graduation or post-graduation degree, Higher Diploma in co-operative management/Diploma in Co-operative audit/General Diploma in Co-operative Management and who has completed the period of probation successfully and who has a working knowledge of Kannada language ; or a Chartered Accountant within the meaning of Chartered Accountants Act, 1949 who shall have a fair knowledge of the functioning of co-operative societies and shall have an experience of at least three years in auditing of which the auditor would like to be included in the panel and Chartered Accountants shall have working knowledge of the Kannada language or a Cost Accountant within the meaning of Cost and Works Accountant Act, 1959, who shall have fair knowledge of the functioning of the Cooperative societies and an experience of at least three years in auditing and working knowledge of Kannada language.

(Continue in next issue)

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Overview of Income Computation and Disclosure Standards (ICDS)

CA Prashanth Kumar N

Cross section of participants

Tax Audit – Issues and Solutions and Deemed Sales under KVAT Act 2003

CA A.S. Vishnu Bharath

CA Raghavendra T N.

Congratulations

On being elected as
President of
Bangalore CA's Toastmasters Club

CA Yusuf Mohammed

Mentors Meet at Bangalore City Institute

"Registered" News Bulletin for India vide No.KA/BGGPO/2542/2015-17
RNI Regn. No. KARENG/2013/51293
Licensed to post without prepayment License No. WPP-309
Total No. of Pages Printed : 20
Date of Posting 14th or 15th of the month, Place of Posting at Bangalore PSO, Mysore Road, Bangalore 560026

KSCAA NEWS BULLETIN English Monthly Printed, Published & Edited by CA. Raghavendra Puranik, Vice President on behalf of **Karnataka State Chartered Accountants Association,** # 7/8, 2nd Floor, Shoukath Building, S.J.P. Road, Bengaluru-560 002. **Ph : 2222 2155, Tel. Fax : 2227 4679, e-mail : info@kscaa.co.in, Website : www.kscaa.co.in**
Printed at **Jwalamuki Mudranalaya Pvt. Ltd.,** 44/1, K.R.Road, Basavanagudi, Bengaluru- 560 004, Ph : 080-2660 1064, e-mail: jwalmuki@gmail.com.
Published at # 7/8, 2nd Floor, Shoukath Building, S.J.P.Road, Bengaluru-560 002. Editor : **CA. Raghavendra Puranik**