

We are publishing hereunder the best of the answers to the queries published in July 2005 Issue of our Journal as received by us from a large number of readers. All the Members of the ICAI, whose answers are published in the journal, will be awarded One hour CPE Credit for each answer.

ACCOUNTING STANDARDS

Q.1. As per Accounting Standard 10 "Accounting for Fixed Assets" (AS-10), issued by the Institute of Chartered Accountants of India (ICAI), the cost of Fixed Assets includes its purchase price, import duties and other non-refundable taxes or levies and any directly attributable cost of bringing the asset to its working condition for its intended use. In such a case whether Fringe Benefit Tax (FBT) paid on an expenditure incurred by an employee of an enterprise towards foreign travel undertaken towards the purchase of the Fixed Asset be included in the cost of the Fixed Asset (assuming it is ultimately decided by the government/courts that FBT will have to be paid on traveling expenses on the ground that it is "incurred" by an assessee irrespective of whether such an expenditure is debited to the Profit and Loss of an assessee).

ANSWER: As per the case FBT is paid for on Foreign travel for purchase of asset. If it is clarified that FBT for expenses in capital in nature also is to be debited to P & L account by the government, then there is no question of adding to the cost of asset. But this will contradict AS-10. Hence this view will not be taken by the government.

From AS 10 perspective, the word "import duties & other non-refundable taxes or levies

and any directly attributable cost of bringing the asset to its working condition for its intended use" draws attention for considering FBT. From the case given, it is evident that travel of an employee is absolutely essential (i.e. cost attributable to the asset to bring it to its working condition) for the purchase. So the travel cost is to be capitalized. FBT for that matter is a non-refundable tax on expenditure incurred (Travel Expenses of employee) for acquiring the fixed asset.

Conclusion: Hence in my view, FBT is to be included in the cost of the fixed asset for the purpose of complying with AS-10 requirements.

The Union Finance Ministry had clarified that FBT is not payable on expenditure incurred to acquire any capital asset on which depreciation is allowable under Section 32. So there will not be any FBT on Travel Expenses if it is capitalized.

Please refer the related CIRCULAR NO.8/2005, dt 29-08-2005

—(K.S.Sathyanarayanan, M.No. 212906)

TAXATION

Q.2. A firm of Chartered Accountants situated in Delhi is conducts audit of a client in Chennai. The firm of Chartered Accountants sends an audit team to Chennai and incurs a sum of Rs.60,300 as expenses towards carrying out

the audit. The break up of expenses is as under:

- a. Rs.40,150 incurred by the partner of the firm; and
- b. Rs.20,150 incurred by the firm's audit assistants and articled clerks.

The audit firm submits a bill to the client for Rs.60,300 and the client reimburses the expenditure only to the extent of Rs.58,500 (due to absence of bills etc.) i.e. Rs.38,750 towards expenses incurred by the Partner and Rs.19,750 towards expenses incurred by the audit assistants and articled clerks.

The amount spent by the firm is initially debited to "Traveling Expenses" account, which is revenue account, and the amount of reimbursement received from the client is credited to the same account.

In such a situation whether any amount would be payable as a Fringe Benefit Tax. If yes, would it be:

- (i) Rs.60,300 being the total expenses incurred; or
- (ii) Rs. 20,150 being the amount incurred by the firm's audit assistants and articled clerks; or
- (iii) Rs.1,800 being the difference between amount claimed and the amount received from the bank); or
- (iv) Rs. 400 (being the difference between the amount claimed from the bank towards employees and amount paid by the Bank; or
- (v) Any other amount.

Would your answer be different if the firm had debited the amount spent initially to the client's account, credited the amount of reimbursement received from the bank to the same account and only debited

the difference to the traveling expenses account of the firm.

Alternatively, whether nothing would be chargeable since the expenditure has been incurred by the CA firm on behalf of a client.

ANSWER: The prerequisites for levying FBT is as follows:

1. The person should be employer.
2. The person who is an employer should have employees based in India.
3. The person is a company or a firm.

As it is mentioned that it is a firm of Chartered Accountant in Delhi, the said firm will be governed by the provisions of FBT.

However, as it is not clear whether the firm has employees on its payroll, the payment of FBT will be as follows:

CASE 1: If audit assistants are on retainer basis and are not on employed in the firm i.e. they do not have employer employee relationship, then it will be a case where the firm does not have any employees. The partners and articled clerks are not employees. So in this case there are no employees in these firms.

As there are no employees in this firm, the firm will not have to pay any FBT as one of the prerequisites has not been complied. The FBT to be paid will be NIL.

CASE 2: If the audit assistants or any one assistant are/ is employees/ employee of the firm, then it is a case where the firm has employees working for it. In this case therefore the FBT will have to be paid on full amount of Rs. 60,300 by the firm. This is due to sub section (2) of section 115 WB which states that 'fringe benefits shall be deemed to have

been provided' by the employer if he has incurred any expense on conveyance tour and travel (including foreign travel); use of hotel, boarding and lodging facilities (clauses F & G).

The circular 8/2005 issued by CBDT has clarified that, FBT will have to be paid on the total amount, and the amount will not have to be bifurcated between employees (audit assistants) and others i.e. partners and articled clerks.

So the FBT in CASE 2 will have to be paid on total Rs. 60,300 by the firm of Chartered accountants, Chennai.

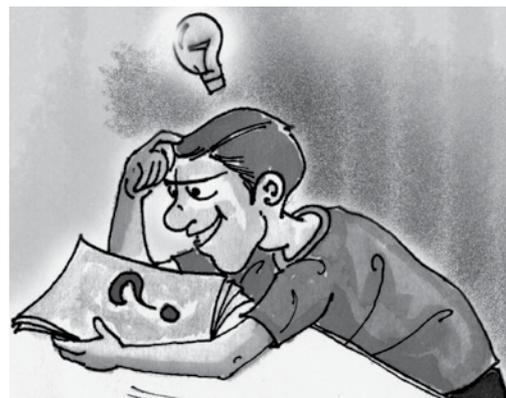
The circular 8/2005 also states that if the expenditure on traveling, hotel, etc. is incurred by the company/firm and not by the client, the company/firm is liable to FBT in respect of such expenditure. However, the client will not be liable to FBT in respect of payment for such expenditure.

The nature of accounting followed is irrelevant in determining whether FBT is payable or not. Also, the extent of amount reimbursed by client is also irrelevant in determining payment of FBT.

—(*Sanjay Hede, M. No. 43647*)

Q.3. As per the definition of Business Auxiliary Service under section 65 (19) of the Finance Act, 1994 (the "Act"), a Business Auxiliary Service means any service in relation to:

- (i) Promotion or marketing or sale of goods produced or provided by or belonging to the client; or
- (ii) Promotion or marketing of services provided by the client; or
- (iii) Any customer care service provided on behalf of the client; or
- (iv) Procurement of goods or



services, which are inputs for the client; or

- (v) Production of goods on behalf of the client; or
- (vi) Provision of service on behalf of the client; or
- (vii) A service incidental or auxiliary to any activity specified in sub-clauses (i) to (vi), such as billing, issue or collection or recovery of cheques, payments, maintenance of accounts and remittance, inventory management, evaluation or development of prospective customer or vendor, public relation services, management or supervision.

If a person does not carry any of the activities specified in clauses (i) to (vi) hereinabove but carries on the activities specified in clause (vii), whether the income received from such a service would be chargeable to tax under the Act.

ANSWER: Business Auxillary has been defined to include six type of services and the seventh provision is incidental or auxillary to any services specified in sub clause (i) to (vi). As such when a service is done of the seventh type alone without any service activity involved in the first six types of services it will be out of the Business Auxillary Service.

—(*P.S. Rajaram, M.No. 27725*)



Ethical Issues

Q.4. Firm A is the Statutory Auditor of a public company listed in Stock Exchanges in India and the aforesaid company appoints Firm B to do a translation of its audited accounts prepared under the Indian Accounting Standards to Generally Accepted Accounting Practices of United States of America ("US GAAP") for circulation amount prospective investors, investment bankers in the United States of America. Whether Firm B needs to take no objection from Firm A before accepting the assignment.

ANSWER: Clause 8 of Part 1 of 1st Schedule states: "A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct if he accepts a position as AUDITOR previously held

by another Chartered Accountant or a restricted State Auditor without first communicating with him in writing".

As per the Chartered Accountants Act, 1949, previous communication with auditor is necessary only if the position taken over is as Auditor of the entity. Audit might be for any engagement like statutory audit or Income tax audit or Internal audit, etc. In our present case as the assignment is only for preparation of accounts under USGAAP, as per the Act no previous communication is necessary.

But the Council of the ICAI has laid out a few guidelines on the subject and the Council in those guidelines defined "previous auditor" as follows;

"The term previous auditor means the immediately preced-

ing auditor who held same or similar assignment comprising same/similar scope of work.'

Thus from the above definition the work assignment can be construed to include not only audit but also certification work. Therefore, from the above discussions the communication with previous auditor is mandatorily required for accepting all types of audit assignments and is a healthy practice to communicate for certification work.

In our present example it is a healthy practice for Firm B to communicate with previous auditor (if any) who has handled the translation of accounts prepared under Indian Accounting Standards to US-GAAP, which need not necessarily be Firm A.

- (Chaitanya Kumar (M. No.215621)) □

FOR YOUR INFORMATION

No. 1-CA(7)/88/2006

January 13, 2005

(TO BE PUBLISHED IN THE GAZETTE OF INDIA , PART III, SECTION 4) NOTIFICATION (Chartered Accountants)

In partial modification of Notification No. 1-CA(7)/85/2005 published in the Gazette of India dated May 14 – 20, 2005, notifying the setting up of a branch of WIRC at Thane w.e.f. 22nd January, 2005, it is hereby notified that the jurisdiction of Thane Branch of WIRC has been enlarged and the same shall now comprise of, besides Thane City, the following cities/towns falling within a radius of 50 kms., from the Municipal limits of Thane City:-

- | | |
|-----------------------|----------------------|
| 1. Balkum | 2. Bhatvanagar |
| 3. Kalyan City | 4. Dandekarwadi |
| 5. Dombivili Ind.Est. | 6. Kulgaon |
| 7. Kopri Colony | 8. Ambarnath |
| 9. Thana H.O. | 10. Ulhasnagar No. 2 |
| 11. Ulhasnagar No. 5 | 12. Shahad |
| 13. Sarawali | 14. Vartak Nagar |
| 15. Vidyashram | 16. Vishnunagar |
| 17. Manpada | 18. Murbad |
| 19. Naupada | 20. Partur |
| 21. Manda | 22. Washind |

The rest of the contents of Notification No. 1-CA(7)/85/2005 shall remain unchanged.

(Dr. Ashok Haldia)
Secretary