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A. Income Tax

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- Demonetization: Analysis
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Income Tax

Controversy with regards to Base year for indexation in the case of inherited or gift property.

On reading the Explanation 1(i)(b) to section 2(42A) together with sections 48 and 49 it becomes clear that object of the statute is not merely to tax the capital gain arising on transfer of capital asset acquired by the assessee by incurring cost of acquisition but also to tax the gain arising on transfer of capital asset, inter alia, acquired by the assessee under a gift or Will covered by section 49 where the assessee is deemed to have incurred the cost of acquisition.

Section 55(1)(b)(2)(ii) provides that where the capital asset became the property of the assessee by any of the modes specified under section 49(1) of the Act, not only the cost of improvement incurred by the assessee but also the cost of improvement incurred by the previous owner shall also be deducted from the total sale consideration for computing capital gains under section 48 of the Act. The question of deducting the cost of improvement incurred by the previous owner could be adopted only if the period for which the asset was held by the previous owner was also included in determining the period for which the asset was held by the assessee.

The expression 'Cost Inflation Index for the first year in which the asset was held by the assessee' contained in clause (iii) of the Explanation to section 48 has created enough controversy. The Revenue resorted to literal interpretation by making reference to the taxpayer who transfers the capital asset, whereas the assessee's have interpreted by seeking indexation benefit by taking the year of acquisition of such asset by the previous owner. The approach of the taxpayers cannot be faulted and the courts have consistently upheld their view point. The CBDT may think of providing a clarificatory circular to graciously accept the interpretation of the courts, thereby provide finality to the issue.

CBDT unveils final rule for computation of FMV of inventory converted into capital asset

Section 45 of the Income-tax Act, 1961 deals with taxability of capital gains arising on conversion of capital asset into stock-in-trade. There were not any defined provisions with respect to taxability in case of conversion of stock-in-trade into capital asset.

In order to provide symmetrical treatment, the Finance Act, 2018 brought about necessary amendments to Income-tax Act to provide symmetrical tax treatment on converting the inventory into capital asset. Now, any profit or gains arising from conversion of inventory into capital asset shall be charged to tax as business income under Section 28(via). For the purpose of computing the business profits, the FMV of the inventory as on the date of conversion, shall be deemed to be the full value of the consideration of such inventory.

Further, for the purposes of computation of capital gains arising from transfer of such converted capital assets, the FMV as on the date of conversion shall be the cost of acquisition as per Section 49 and the period of holding for such capital asset shall be reckoned from the date of conversion or treatment.

The Central Board of Direct Taxes (CBDT) has inserted a new Rule 11UAB in the Income-tax Rules, 1962 for determination of Fair Market Value (FMV) of the inventory converted into capital asset for the purpose of newly inserted section 28(via). The FMV of the inventory shall be as follows:-

1) In case of immovable property, the FMV shall be the value adopted or assessed or assessable by the stamp authorities for the purpose of payment of stamp duty in respect of such immovable property on date of conversion inventory into capital asset.

- 2) In case of jewellery, archaeological collections, drawings, paintings, sculptures, any work of art, shares or securities referred to in rule 11UA, the FMV shall be the value determined in the manner provided in rule 11UA(1) and the reference to the valuation date in the rule 11U and rule 11UA shall be the date on which the inventory is converted into capital asset
- 3) In case of property, other than one specified above, the FMV shall be the price that such property would ordinarily fetch on sale in the open market on the date on which the inventory is converted into capital asset.

Govt notifies 10% LTCG tax on IPO/FPO gains

The Income Tax Department has notified norms for applicability of concessional long-term capital gain tax. This will benefit investments made in initial public offerings (IPOs) and follow-on public offerings (FPOs). The new norms will come into effect from April 1, 2019, and will apply in relation to assessment year 2019-20 and subsequent assessment years. The notification talks about two types of transactions: First, those entered into before October 1, 2004, and second, those entered into on or after October 1, 2004, and not chargeable to securities transaction tax (STT).

Tax law panel may look to drop dividend distribution tax

Members of the task force set up to draft a new direct tax legislation appear to be in favour of abolishing the dividend distribution tax (DDT). The panel may revert to the classical method of taxing dividend in the hands of shareholders. One of the objectives is to boost investments from abroad, as DDT casts a heavy burden on foreign investors, sources close to the developments told TOI. Members of the task force set up to draft a new direct tax legislation appear to be in favour of abolishing the dividend distribution tax (DDT). The panel may revert to the classical method of taxing dividend in the hands of shareholders. One of the objectives is to boost investments from abroad, as DDT casts a heavy burden on foreign investors, sources close to the developments told TOI. Abolition of securities transaction tax (STT) to eliminate double taxation may also be on the cards, as Budget 2018 introduced tax on long-term capital gains exceeding Rs 1 lakh on sale of listed securities.

Recent case laws: Income Tax

1. No section 68 additions if identity of applicants was clearly revealed; Section 68 of the Income-tax Act, 1961 - Cash credit (Share capital) - In course of assessment, Assessing Officer noted that assessee was a sick company during relevant year but had nevertheless collected substantial amounts to extent of Rs. 12 crores invested by two share applicants - Assessing Officer took a view that identity of shareholders and genuineness of transaction had not been established and, accordingly, brought to tax said amount - Tribunal as well High Court found that even though assessee was a sick company earlier, yet it pulled out of woods in year 2010 - It was also noticed that identity of share applicants was clearly revealed but Assessing Officer did not conduct any enquiry except resting his conclusions on surmises - Accordingly, addition made by Assessing Officer was deleted - Whether on facts, SLP filed against order passed by High Court was to be dismissed - Held, yes [Para 2] [In favour of assessee] **Principal Commissioner of Income Tax v. Himachal Fibers Ltd. SLP dismissed [2018] 98 taxmann.com 173 (SC)**

2. Disallowance u/s 40(a)(ia)- The dispute between the assessee and Department is confined to the appropriate rate at which tax should have been deducted at source while making the payment of channel subscription charges. Thus, it is not a case of failure to deduct tax at source but, if at all, it is a case of deduction of tax at source at a lower rate. Provision of section 40(a)(ia) are not applicable to a case of short-deduction of tax at source. (in favour of Assessee).

Dish TV India Ltd. vs Assistant Commissioner of Income Tax (ITAT-Mumbai)

3. Capital or Revenue Expenses – Loss incurred by the assessee on account of encashment of bank guarantee by Delhi Transport Corporation for non fulfilment of the work awarded to the assessee is allowable as a business expenditure / loss; it cannot be said to be capital expenditure for the reason that the assessee failed to build bus shelters. (Favour of Assessee)

Green Delhi BOS Ltd. vs. Assistant Commissioner of Income Tax (ITAT – Delhi)

4. Search and seizure – Supervisory authority having himself admitted that he has accorded the approval u/s 153D mechanically without applying his mind to the facts of the case, the alleged approval does not constitute an approval envisaged by the provision of section 153D and, therefore, the impugned assessment u/s 153A is void and bad in law. (Favour of Assessee) **Geetarani Panda vs. Assistant Commissioner of Income Tax (ITAT-Cuttack)**

5. Capital Gain – Assessee having converted land held as capital assets into stock-in-trade, Commissioner of Income Tax (Appeal) rightly directed the Assessing Officer to take fair market Value determined by the valuation officer (Assessee Officer had adopted the valuation as per stamp valuation authority) as fair market value of assets on the date of conversion for purposes of section 45(2). **(Favour of Assessee) Income Tax Officer vs. Vilas Babanrao Rukari (HUF) (ITAT-Pune)**

6. Service of notices: When department had correct address of assessee furnished in return of income, sending notice at incorrect address available with bank and then drawing presumption of service of notice on ground that notice was not received back unserved, cannot be sustained

[2018] 96 taxmann.com 401 (Allahabad): Suresh kumar Sheetlani v. Income-tax Officer-1(3)

7. Section 68 of the Income-tax Act, 1961 - Cash credit (Share capital) - Assessment year 2009-10 - Section 68 addition was made in hands of assessee on ground that assessee company was not able to produce any of director, shareholders or principal officer of companies to whom shares were allotted and lenders from whom unsecured loans was taken - High Court deleted said addition holding that assessee had discharged its onus of establishing identity, genuineness and creditworthiness of both investors as well as lenders - Whether, on facts, SLP against said order was to be dismissed - Held, yes [Paras 4 to 6] [In favour of assessee] **[2018] 96 taxmann.com 403 (SC) Principal Commissioner of Income Tax-4 v. Hi-Tech Residency (P.) Ltd.**

8. Foreign allowance : Where assessee, an employee of Indian company, rendered his services outside India and during relevant year his residential status was non-resident, foreign assignment allowance received by him abroad, was not liable to tax in India under section 5(2) - **Deputy Commissioner of Income-tax (IT), Circle-2 (1), Kolkata v. Sudipta Maity - [2018] 96 taxmann.com 336 (Kolkata - Trib.)**

9. AO couldn't step into shoes of assessee to decide amount to be paid to avail a particular service

The ITAT held in favour of assessee as under:

1) There was no power of AO to reduce the claim. He could only examine whether the amount could be allowed in full or not. There was no dispute that the amount was paid for the purpose of business, as Assessing Officer had allowed the amount partly.

2) Since the provisions of section 37(1) do not have any restriction to allow the amount partly, so long as the expenditure is incurred for the purpose of the business wholly and exclusively, the same has to be allowed.

3) The restrictions placed in other provisions like that of section 36(1)(iii) for the purpose of interest, under section 40A (expenses or payment not deductible in certain circumstances) and also restrictions placed under sections 30 and 31 won't apply to the facts of the case.

4) Since the restrictions under section 37(1) were not applicable, the whole of the amount claimed was to be allowed as the expenditure was not of personal or capital in nature, as provided in the section itself. - **[2018] 96 taxmann.com 272 (Hyderabad - Trib.)**

10. Section 194A: Payment of interest by assessee for delayed delivery/allotment of plot was not in the nature of interest specified in Section 194A, and thus TDS provision was not applicable on it. **Commissioner of Income Tax, Kolkata Vs. West Bengal Housing Infrastructure Development Corporation Ltd.**

11. Jackie Shroff gets favourable tax ruling

Sum received for dropping criminal case against a person is capital receipt, not taxable : **Case of Asstt. CIT, Mumbai v. Jackie Shroff [2018] 97 taxmann.com 277 (Mumbai - Trib.)**

Difference between revenue and capital receipt: Concluding Remarks

Re: **Jackie Shroff case**

Categorization of such income

Some officials hold that compensation received, as in this case, for withdrawing criminal charges should be taxed under 'income from other sources.' But they are forgetting that the primary requirement is that it should be income. Then only the next question of 'taxing it under certain head' would arise.

Pros and Cons

Compensatory settlements, as in Jackie Shroff's case, always invite arguments on both sides of the divide:

Bouquets - Those who think that compensatory settlements, even in criminal matters are harmless negotiations across the table enunciate that these agreements reduce burden on courts. Besides, cases like these are just civil cases which have been given the garb of criminal suits. If the object is compensatory, it's a civil dispute, which can be negotiated, as said in *R. Vijayan v. Baby* [2012] 17 taxmann.com 77/111 SCL 270 (SC) case.

Brickbats - Those who argue against such compensation being called capital receipt propound that the very concept of settling criminal cases outside would amount to subsidizing the misdeeds of tricksters.

It is also said that mediation is resorted to for only one purpose - getting out of the clutches of law. Jackie Shroff slapped Anil Kapoor 17 times during the shooting of "Parinda" movie because Anil Kapoor was not satisfied with the takes and wanted 'perfection.' Now, if Jackie Shroff had slapped Anil Kapoor 17 times out of vengeance, perhaps, Anil Kapoor would have launched a criminal case. Jackie would have offered compensation in an agreement. Now, the compensation which Anil Kapoor would receive would be a revenue receipt. This is because the income-tax department would argue that the compensation was received during professional shooting !!!

The line between capital receipt and revenue receipt, indeed, is very thin. As it always involves disputes, the CBDT can bring out a detailed circular to clarify things.

The Revenue should remember what was said in *Dhruv N Shah v. CIT* [2004] 88 ITD 118 case, by the Apex Court, when compensation was sought to be taxed. The famous line was "all receipts are not taxable under Income-tax Act."

The gods too are surprised by the turn of events. Lord Brahma was heard saying to Lord Shiva, "Now-a-days, human beings are making strange wishes. They want to be cheated, have a settlement and then clinch the deal. Because being capital receipts, they won't be taxed by Income-tax department. People are now coming in droves to make this wish !"

IT officer can't adjust tax refund against outstanding demand without valid notice

As per the Income Tax Act, income tax officials need to serve a valid notice of demand to the concerned taxpayer before doing any adjustment against the demand. A valid notice means a notice which is served within the time-frame specified under the respective sections of the Income Tax Act. Thus, if you are one of those taxpayers who have not got a valid notice of tax demand, then you need not worry about the refund as that can't be adjusted against the outstanding demand. Here's what you need to know about a recent ruling of the Bombay High Court.

The Court said that it is present to adjudicate on questions of law and not to settle the routine issues of administration. Accordingly, such kind of errors made by the I-T officers would not be considered lightly as form the part of litigation and ultimately the court's judicial time is wasted.

The income tax law provides that a refund due to any person may, in lieu of payment of the refund, be set off against any outstanding tax demand. However, this can be done only after following the prescribed procedure, including giving a written intimation to the taxpayer of the action proposed to be taken.

As per the income tax law, in fact, it is the duty of every IT officer to ensure that along with the serving of notice, all the procedural requirements are complied with. A proof of service of demand is necessary before adjusting any refund due to the taxpayer against the outstanding demand. Further, with the advancement of technology now it is easy enough for the IT officers to provide a proof of service and also comply with other requirements of law.

Thus, without serving a valid notice of demand, the I-T officials cannot adjust refund of the amount due against the outstanding demand. If they do so, then a cost would be imposed upon them. According to tax experts, this is a highly-appreciated move of the High Court where the interest of the honest taxpayer has been upheld.

Indirect Taxes

Recent Developments: GST

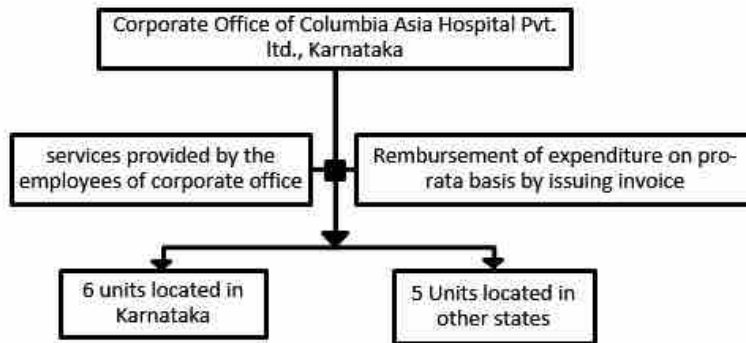
1. Services of direct selling agents (DSA's) to banks and NBFC'S are liable to tax under reverse charge The Central Government vide Notification No. 15/2018- Central Tax (Rate) dated 26th July, 2018; Notification No. 16/2018- Integrated Tax (Rate) dated 26th July, 2018 amended Notification no. 13/2017- Central Tax (Rate) dated 28th June, 2017 and Notification No.10/2017- Integrated Tax (Rate), dated the 28th June, 2017 respectively to provide that tax on the services supplied by individual Direct Selling Agents (DSAs) other than a body corporate, partnership or limited liability partnership firm to bank or non-banking financial company(NBFCs) shall be paid on reverse charge basis by a banking company or a non-banking financial company, located in the taxable territory. Also, an explanation has been inserted in the said notification which provides the meaning of renting of immovable property as allowing, permitting or granting access, entry, occupation, use or any such facility, wholly or partly, in an immovable property, with or without the transfer of possession or control of the said immovable property and includes letting, leasing, licensing or other similar arrangements in respect

of immovable property.” [Notification No. 15/2018- Central Tax (Rate) dated 26th July, 2018; Notification No. 16/2018- Integrated Tax (Rate) dated 26th July, 2018]

2. Supply by employees of a unit to another of a company is taxable under GST

Recently, M/s Columbia Asia Hospitals Pvt. Ltd. (AAR No.-KAR ADRG 15/2018) filed an application to sought an answer to the question whether the services provided by the employee of corporate office to the other units of the company is taxable plus charging consideration against allocation of common expenditure of units would tantamount to levy GST or not. The Karnataka AAR held the ruling in favor of revenue, briefing the findings in relation with the Entry 2 of Schedule I of CGST Act, 2017.

In the instance case, the applicant is a private limited company engaged in providing health care services categorizing them as In-patient (IP) and Out-patient (OP) services. The applicant is also engaged in supply of medicines (pharmacy) to in-patients and out-patients. The relevant facts on the basis of which ruling have been sought after are:-



As clarified by the applicants through the facts that the person delivering the service are employed by the corporate office & not by the other units of the applicant. Hence there is an employer-employee relationship with corporate office only and no relationship exists with the employees of the corporate office & other units of the applicant. Therefore, the entry no. 1 of schedule III of CGST Act, 2017 would not be applicable.

The services provided by such employees to the other units would be treated as the transaction between the corporate office & its units located in other states. Though the corporate office & its units are the distinct person u/s 25 of CGST Act, 2017, the transaction would be covered under the Entry no. 2 of Schedule I of CGST Act, 2017 i.e. "Supply of goods or services or both between related persons or between distinct persons as specified in section 25, when made in the course or furtherance of business" & therefore becomes taxable. The valuation of the transaction includes all cost incurred by the corporate office after considering employee cost in the form of salary, incentive & perquisites.

Additionally, corporate office raises an invoice for the allocation of the expenses such as rent, travel expense, consultancy, etc incurred on behalf of other units. Such reimbursement from the other units would be covered under the term 'TRANSFER' u/s 7(1)(a) of CGST act, 2017. Furthermore, the transaction between the distinct person without consideration is covered under the definition of the SUPPLY under Entry No. 2 of Schedule I of CSGT Act, 2017. Hence the reimbursement of the expenditure would be attracts the tax liability.

3. Supply of UPS along with battery could be considered as Mixed Supply: AAR

Switching Avo Electro Power Ltd., In re - [2018] 96 taxmann.com 106 (AAAR-West Bengal)

The assessee filed an application for Advance Ruling on whether the supply of UPS along with battery was to be considered as mixed supply as they are supplied under a single contract at a combined single price? It contended that UPS cannot function without battery because it is an integral part of UPS. Hence, it is naturally bundled and such supply should be treated as a composite supply and not as a mixed supply.

The Authority for Advance Ruling held that the storage battery had multiple uses and could be put to different uses. Therefore, when battery was supplied with UPS, then it could not be considered as a composite supply or a naturally bundled supply.

4. Failure to file Part-B of E-way bill would attract penalty on transporter: HC

The assessee was a transporter-company who transported the goods from Maharashtra to Noida via Indore and other places. The distance was more than 1200-1300 kilometers. But the assessee had not uploaded the Part-B of E-way bill, i.e., the

details of conveyance in the e-way bill. The competent authority initiated the proceedings and imposed penalty of Rs. 1,32,13,683. The assessee filed writ petition in the High Court on the ground that Part-B of the e-way bill could not be updated due to technical error and contended that the minor penalty of Rs. 5,000 should be levied.

The High Court held that no grievance had been raised by the assessee with regard to technical error. It could not be treated as a technical error when there was an option of raising a grievance on the GST portal. The minor penalty could be levied when the tax was upto Rs. 5,000. In the present case, tax liability was more than lakh of rupees. Therefore, the minor penalty of Rs. 5,000 could not be imposed. Thus, the department had rightly imposed the penalty of Rs. 1,32,13,683. Therefore, the writ petition filed by the assessee was dismissed. **Gati Kintetsu Express (P.) Ltd. v. Commissioner, Commercial Tax of MP - [2018] 95 taxmann.com 254 (Madhya Pradesh)**

5. TRANS-1: filing

Many High Courts has directed the GST council to provide an opportunity to the assessee to file the TRANS-I. Further, this case has not discussed that the CENVAT Credit is the vested right of the assessee and the same cannot be denied due to technical or procedural errors. **M/s. Apollo Screens Pvt Ltd Vs UIO 2018-TIOL-1831-HC-AHM-ST**

6. Include taxes which are in existence on entering into contract:

The terms inclusive of taxes shall be considered to include only the taxes which are in existence as on the date of entering into contract and it cannot be interpreted to include the future tax, since the same did not have the consensus ad idem among the parties of the contract. Link to GST: Many of the contracts entered prior to GST which are continuing in GST regime may not have mention about GST and the contracts were also not amended to incorporate the said clause. Further, in many cases the exemption provided to Government projects were removed in GST regime and tax rate was also high.

As per rationale of the above, the assessee can claim the reimbursement of GST as GST is not in existence as on the date of entering into agreement. **M/s. Speed Crafts Ltd Vs UIO - 2018- TIOL-1843-HC-DEL-CT**

7. Input on CSR Activities

CSR is generally understood as being the way through which the company achieves a balance of economic, environmental and social imperatives, while at the same time it addresses the expectations of stake holders and shareholders. Further, the provisions of Companies Act, 2013 made mandatory that every company should involve in the CSR activities. The rationale of the above decision can be applied in the GST regime also since the scope of Input tax credit is widened to allow the ITC on the goods/services used or intended to be used in the course or furtherance of business. **CA Lakshman Kumar CA Venkat Prasad Essel Propack Ltd. Vs. Commissioner of CGST-2018(9) TMI 247-CESTAT**

8. No GST exemption on educational courses offered by entities approved by NSDC

Functions of National Skill Development Corporation (NSDC) are in nature of encouraging and supporting private sector in skill development which is also one of its mandate and functions. Apart from this it is also implementing agency for various schemes such as Pradhan Mantri Kaushal Vikas Yojana , Sankalp, Udaan, etc. If services in relation to schemes as mentioned are provided through partner approved by NSDC, then only benefit of Notification as claimed would be applicable to applicant and it would not be applicable in respect of other services relating to skill development provided by applicant. In view of this it is found that NSD programme implemented by NSDC would cover only actual schemes and programmes of skill development that are undertaken by Government through its various ministries, departments, directorates, attached offices and organizations and cannot in any way be construed to be including each and every activity under the sun which enhances skills in one way or other. Thus, educational courses offered by applicant which have been approved by NSDC would not be construed as in relation to National Skill Development Programme implemented by NSDC. The educational courses for which qualification standards/framework i.e. QP/NOS has not been defined by NSDC and will be approved by NSDC as and when the relevant QP/NOS would be defined by NSDC, in the interim period ,though, NSDC has given exceptional approval on such courses, they will not be treated as in relation to National Skill Development Programme implemented by NSDC. Accordingly benefit of GST exemption as per Notification No. 12 of 2017-Central Tax (Rate), dated 28-6-June 2017 would not be available to applicant [2018] 98 taxmann.com 228 (AAR)

9. No GST exemption on contract of composite supply of goods and training services

To implement ICT project, applicant is not only imparting training but also providing composite supply of goods thus, could not term entire project as training programme not eligible for Nil rate exemption as per notification no 12/2017-Central Tax (Rate) [2018] 98 taxmann.com 231 (AAR)

Both Central and State tax authorities are authorized to initiate enforcement action against taxpayers

It is accordingly clarified that the officers of both Central tax and State tax are authorized to initiate intelligence based enforcement action on the entire taxpayer's base irrespective of the administrative assignment of the taxpayer to any authority. The authority which initiates such action is empowered to complete the entire process of investigation, issuance of SCN, adjudication, recovery, filing of appeal etc. arising out of such action.

In other words, if an officer of the Central tax authority initiates intelligence based enforcement action against a taxpayer administratively assigned to State tax authority, the officers of Central tax authority would not transfer the said case to its State tax counterpart and would themselves take the case to its logical conclusions.

Similar position would remain in case of intelligence based enforcement action initiated by officers of State tax authorities against a taxpayer administratively assigned to the Central tax authority.

It is also informed that GSTN is already making changes in the IT system in this regard.

Miscellaneous

Demonetization: Analysis

By T K Arun, ET Bureau

Small enterprises were the worst hit. It stands to reason that they would have had to borrow to tide over hard times.

Now that the RBI has admitted that 99.3% of all demonetized notes came back to the banking system (not counting what remains in Nepal and Bhutan), it is fairly clear that demonetization was a flop in economic terms. But it was a huge success in political terms for the prime minister personally and for his party in the Uttar Pradesh assembly elections. And that must be understood as having been the real goal of the demonetization exercise, all along.

The Economic Survey for 2016-17 estimated the loss in economic output arising from demonetisation to have been anything between a quarter of a percentage point to one percentage point of lost growth. GDP growth rate slowed from 8% in 2015-16 to 7.1% in 2016-17 to 6.7% in 2017-18.

There are those who quibble that growth lost steam for reasons other than demonetisation, such as introduction of GST in July 2017 and the twin balance sheet problem depressing investment in the economy, as banks refused to lend, groaning under their burden of bad debt, and large companies, squashed under unserviceable loans, the counterparts to the banks' bad loans, started few large projects. Yes, allocation of blame for deceleration to individual factors is not easy, although the Survey made its claim after some statistical exertions. What is not hard to identify is the common thread running through all three maladies — poor economic management.

Let us try to put a number to the loss in GDP arising from demonetisation. Take the midpoint of the range between 0.25% and 1% of GDP estimated by the Survey, and since GDP of both 2016-17 and 2017-18 were affected, take the average GDP for these two years. Output loss due to demonetisation is a little over Rs 1 lakh crore.

The latest annual report of the RBI, for 2017-18, has two additional statistics that damn demonetisation. One, household savings held in the form of currency shot up, from an average of 1.12% of Gross National Disposable Income (GNDI) in the pre-DeMo five years to 2.8% of GNDI in 2017-18. In other words, savings in the form of currency multiplied 2.5 times, not quite the less-cash result the government had hoped for. Worse is the increase in financial liabilities. In the five years prior to demonetization, household financial liability averaged 3.06% of GNDI. This went up sharply to 4% of GNDI in 2017-18. Liabilities went up by 83% from Rs 3,70,964 crore in 2016-17 to Rs 6,79,49 crore in 2017-18.

Small enterprises were the worst hit, and some of them presumably never recovered. It stands to reason that they would have had to borrow to tide over hard times. That would explain the rise in liabilities. The poor and the less well-off would have borne the brunt of it.

Demonetization would never have hit illicit wealth held as real estate, shares, gold, silver and foreign currency. Only smalltime concealers of income keep their money in cash. These include women hiding income from their men, to create a stash they could use to buy gold or in a health emergency. Demonetization hit such people hard, not the big fish.

What has been the gain from demonetization? A big jump in the number of tax filers has been attributed to it. GST would have increased the number of tax filers, in any case. GST creates multiple audit trails, leading to a big expansion in the base of direct tax. Digital payments rise when data networks become ubiquitous and when the government removes hurdles to digital payments. These should be taken out of demonetization gains.

What remains is the political impact. This columnist had written, a week after demonetisation was announced, that the goal was not ending black money or any other economic outcome but to position the PM as a champion of the poor who takes on the filthy rich on their behalf, and invites them to participate in this epic battle of redemption by standing in endless lines in front of banks.

The people of India bought that story, by and large. Even those who complained of the hardship they had to suffer on account of demonetization praised the PM for his courage, in taking on the rich and the powerful, and accepted their suffering as a price worth paying for it.

This expanded the BJP's support base. The poor and the not-so-poor, in whose breast class antagonism can be stirred, turned supporters, even as sections of the petty-trader support base suddenly experienced an unexpected improvement in their clarity of vision, as rosetinted glasses dropped off.

If demonetization is seen to not have achieved the goal of slaying the black money demon, even while raising the debt burden of the poor and the middle classes, it would impact the ruling party's popularity negatively. Hence the chorus in support of demonetization, never mind what the RBI annual report shows.

Forensic Audit In Banks

By definition, 'Forensic Audit' means "an examination and evaluation of a firm's or individual's financial information for use as evidence in court. A forensic audit can be conducted in order to prosecute a party for fraud, embezzlement or other financial claims". Thus, in the context of a bank, all financial transactions and decisions involving finance are analysed with a view to arrive at the truth. Forensic Report can be admitted in a court trial and forensic auditors may directly submit evidence in the court or depose before a judicial authority.

But, a forensic audit does not stop with mere audit of accounts. It goes a step further and find out the basis on which each decision was taken. Since decisions could be of myriad types that could directly impact the financial affairs of an institution, it is imperative that we shall probe all types of such decisions taken in the bank concerned.

One must start with the questions –

- (a) Whether the person who had taken the decision in question enjoyed expressly delegated authority?
- (b) Whether the decision was taken at the right moment (neither in haste nor after a delay)?
- (c) Whether the decision was promptly reported to the next higher authority?
- (d) Whether any mistakes of the past were repeated?
- (e) If the result of the decision made was just the opposite to what was intended, what were the remedial steps initiated?

1. Credit Decisions

Credit is the area where forensic auditors concentrate first and start their probe. Credit decisions must be compared with RBI policies and guidelines, individual bank's credit policy and finally the general laws of the land. If any deviation or violation is found in such a context, it is taken up for deeper investigation and reporting.

2. Investment Decisions

Investment decisions taken are compared with the objectives of investments made and actual returns are compared with anticipated returns. Other aspects like loss incurred if any and its magnitude and whether such loss could have been prevented are also analysed. In case of lower profit, causes for the fall in profit are gone into. It may be remembered that many investments escape the attention and scrutiny of concurrent auditors and statutory auditors as of now, due to paucity of time.

3. Income and Expenditure

Transactions involving both income and expenditure are taken up for investigation. Income/Revenue foregone/lost and Expenditure that exceeded the normal levels are specifically probed. The possible connection between a series of transactions is also analysed. If the loss was deliberate, the forensic audit will probe the background of the true beneficiary in all such cases.

4. Violation of Regulator's guidelines and prescriptions

Instances of deviation from/violation of the regulatory authority's rules and guidelines are probed. The fall out of these on the bank's image and reputation, discipline, financial risks and loss if any are examined. Obviously, the penalties levied by the regulator (RBI) for such deviation/laxity/violation are also covered in the report.

5. Unlawful activities

This is similar to Point No.4. In this case, any activities carried out by the bank in contravention of the laws of the land are analysed from various perspectives and all their dimensions are brought out. Ramifications of such activities, particularly the loss to the bank customers and general public and the possible threats to the nation's economy will be dealt with.

6. Wrong Persons Vs. Wrong Decisions

This is an important aspect to be looked into unfailingly. Mistakes made in placement will reverberate in all other areas. No average human being is infallible. But a person with a bad character and a history bad behaviour in the past can vitiate the whole atmosphere. So, a forensic auditor will look into this aspect too.

7. Illegality in Recruitment, Promotion and Transfers

Any illegality or irregularities noticed in recruitment, promotion and transfers must be subjected to further probe for necessary corrective measures.

8. Systems and Procedures

Forensic Audit also looks into the systems and procedures followed by each bank and compares them with the industry. Any deficiencies in the systems and lacunae in the procedures will weaken the bank. This is one sensitive area which if neglected will result in delays, growing customer complaints, monetary loss, frauds and uncertainty in many areas. So, forensic audit is to cover this topic also.

9. Strategy

Strategies adopted by the bank may not be as effective as was planned. So, changing of strategies may be prescribed by the forensic auditors. Dropping some product lines, pricing of products, adding new products in tune with the changing times and customers' preferences, packaging of each product with additional features etc. may be thought of and recommended. However, forensic auditor must act with extreme care and responsibility here, as otherwise he may compete with the bank's consultants.

10. Corporate Governance

Infusing more professionalism in the administration may be called for. Codification of corporate ethics, Transparency, Accountability and Truthfulness in the functioning of the bank and honesty in business transactions and simplified reporting of results in critical areas will achieve wonders. Therefore, the forensic audit will attempt to remove the veil of secrecy in all unwanted areas and shall suggest suitable ways to adhere to the corporate ethics chosen by the bank voluntarily.

In the end to be effective and successful, forensic audit must study various inter-related activities of the bank carefully and submit its report within a reasonable time.

Continued liquidity stress may have deeper impact on NBFCs

Non-bank financial companies (NBFCs) are likely to be impacted significantly if the liquidity situation, triggered by IL&FS default, continues to remain tight, according to a report.

Infrastructure Leasing & Financial Services (IL&FS) and its subsidiaries are facing liquidity crisis and has defaulted on debt repayment. The default by IL&FS has also impacted other NBFCs and also mutual fund players.

"Non-bank financial institutions (NBFI) will be significantly impacted if the liquidity distress in the country's capital markets, triggered by the default in September 2018 of IL&FS, prolongs for an extended period of time," rating agency Moody's said in a report.

The rating agency's vice president and senior credit officer, Srikanth Vadlamani, said the authorities will continue to take measures to limit the scope and duration of the prevailing liquidity challenges, while most NBFIs can cope with multi-weeks of tight liquidity conditions.

"However, prolonged liquidity distress will significantly erode the NBFIs' credit standing, and prove negative for the broader economy and structured finance sector," he said.

The report said liquidity tightness could lead to sharply higher financing costs for NBFIs, or even difficulty in rolling over their liabilities, because these companies have relied heavily on market borrowing to fund asset growth.

Any effects on the NBFIs will spill over to the broader economy mainly through the credit channel because NBFIs are a material provider of credit for the economy, with outstanding loans/GDP at end March 2018 registering 13 per cent versus banking system loans/GDP of 52 per cent.

"Consequently, a slowdown in credit growth provided by NBFIs will dampen overall consumption and economic growth," it said.

The report said NBFIs' liquidity management practices suggests that these companies are capable of coping with multi-week liquidity distress, but a prolonged period of liquidity stress will severely weaken the NBFIs' credit standings.

There will not be a significant impact on the credit quality of the country's structured finance sector, nor performance of asset-backed securities (ABS), it said.

RBI wanted to pull out nominees from public sector bank boards, Govt says no

The Finance Ministry is learnt to have turned down the Reserve Bank of India's demand for withdrawing its nominee directors from the boards of public sector banks, arguing that in these times of stress in the banking sector, the banking regulator's presence is important, sources familiar with the matter said. The RBI has been in communication with the government on these issues, with the correspondence picking up ever since the over Rs 13,000-crore Letters of Undertaking fraud at Punjab National Bank came to light.

Foreign investors make historic run from India! Over Rs 90,000 crore withdrawn from markets in 2018

Foreign institutional investors (FIIs) have given Indian capital markets a big thumbs-down this year, withdrawing Rs 90,746 crore so far, the highest ever. Interest rate hike by Federal Reserve and a falling rupee led the FIIs out of the Indian market. With two and a half months still remaining in the current calendar year, the net FII withdrawals could well cross the psychological mark of Rs 1 lakh crore.

Rupee may fall to 76 against US dollar by year-end: HSBC

The rupee could be significantly weaker than thought earlier at the ends of the current and next calendar years, HSBC Global Research said, even as it saw the Reserve Bank of India becoming 'more accommodative' of the currency's weakness. According to the firm, the steps taken by the government recently to support the rupee may not suffice to support it. Also, the option of financing the current account deficit (CAD) with more external debt could not only be sub-optimal but also rather difficult.

India's Sliding Rupee Has an Upshot: Rising Software Exports

The dark cloud hanging over India's economy from the rupee's rout is not without a silver lining.

The currency's double-digit drop against the dollar this year is helping the nation's services exports, according to HSBC Holdings Plc's chief India economist Pranjul Bhandari. So much so that the share of services exports, which mainly comprise software, has climbed to 7.3 percent of gross domestic product in June from 6.8 percent in March 2017, she said. That growth is reflected in the stock market, where the year-to-date gains for information technology stocks have outpaced the broad market index. While the MSCI India index is up about 3 percent, the information technology index has jumped nearly 37 percent. Infosys Ltd., Asia's second-most valuable exporter of software services, advanced 1.1 percent Tuesday, helping the benchmark S&P BSE Sensex index snap five days of losses.

India's Sensex Snaps Five Days of Losses as Rupee Aids Exporters

It's also helped to underpin the world's fastest growth rate of 8.2 percent in the June quarter given the services industry's 55 percent contribution to the overall economy.

The boost to services exports from a weaker currency is in contrast to overall shipments, which historically haven't benefited much from a weaker rupee.

The rupee is Asia's worst-performing major currency so far this year and that comes amid a global trade war that threatens exports. If anything, a slide in the rupee has ended up inflating India's import bill.

Another view: Weak Rupee Not Enough to Tip the Scale in Favor of India Exports

According to Bhandari, the main deterrents to goods exports, which account for 60 percent of overall shipments, are domestic bottlenecks, in particular the hit from the cash ban and the chaotic introduction of a nationwide consumption tax. Global growth and exchange rates are also factors.

"Exchange rates matter, but the least of the three, because India's import content of exports are rising," Bhandari said.

"On the other hand, the exchange rate matters much more for services exports," she said. "In that sense, 2018 is special. World growth is up and the exchange rate is more competitive than before."

India worst sufferer of declining trade & slow global growth: Suresh Prabhu

Commerce and industry minister Suresh Prabhu said India is the "worst sufferer" of declining trade and slow global economic growth as the country has a huge stake and its share in world trade is rising.

"No country can benefit from the decline in the world trade, and the slowing global economy is a concern for all nations, including India," Prabhu said at an ASSOCHAM event.

India's exports declined for the first time in the current fiscal, with shipments contracting 2.15% in September to \$27.95 billion. Prabhu said there was predictability in doing business globally in the past six-seven decades, but "we are seeing a dramatic change in global trade" in the past few months.

On Monday, commerce secretary Anup Wadhawan had said that global recovery was fragile and there was some element of risk from threats such as confrontational trade stances that major countries had taken.

Commenting on the World Bank's ease of doing business report, which is scheduled to be released soon, Prabhu said, "You will have a good news when World Bank will release its report."

Declaration

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