

TECHNICAL UPDATE

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The amendments introduced in statutes, policies and procedures in respect of Direct Tax, Indirect Tax, Company Law & Accounting Standards, FEMA / EXIM Policy & SEBI related matters are summarized hereunder

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DIRECT TAX

1. **Non-Residents having an Indian Liaison Office will not be treated to have a Business Connection in India**
Authority for Advance Ruling ('AAR') held that a non-resident will not be considered to have a business connection in India and hence not be taxable in India, if the LO of such non-resident is assisting in the purchase of goods and exporting it to other countries. Further, AAR held that such export of goods will be out of the ambit of business connection as provided through explanation 1 to section 9 of the Income Tax Act.

Source - Ikea Trading (Hong Kong) Ltd Vs DIT (2008) AAR (AAR No. 771 of 2008)

2. **Taxing Rights of the Contracting States under the Specific Provisions of the Tax Treaty**
Hon'ble Mumbai Bench of Income Tax Appellate Tribunal ('ITAT') held that the expression 'may be taxed in the other State' used in the Article 18 of Double Tax Avoidance Agreement entered between India and Canada ('DTAA') could not be interpreted to give an option to the other contracting States to tax such income. It also held that the expression 'may

be taxed in the other State', authorizes only the contracting State of source to tax such an income and by necessary implication the contracting State of residence is precluded from taxing such an income.

Source – Ms Pooja Bhatt Vs Deputy Commissioner of Income-tax – (2008) ITAT (Mumbai) (IT Appeal no. 7000 of 2005)

3. Determination of Nature of Expenditure incurred by an Assessee for acquiring Technical Information under a Contract

It has been held by the Hon'ble High Court of Delhi that where the assessee company had only acquired "access" to technical information under the agreement i.e. know-how which related to the process of manufacture, which was not, related to any secret process or patent rights or even the right to use a trademark or trade name under the agreement, the payments, can only be categorized as one made on revenue account.

Source – Commissioner of Income-tax Vs J K Synthetics Ltd – (2008) Delhi HC (ITR No. 139/1988 & ITR No. 202/1989)

4. Power of Income Tax Authorities to conduct Survey in Premises of a CA/ Lawyer/ Tax Practitioner of an Assessee

Hon'ble High Court of Orissa held that the income tax authority does not assume any power to enter the business premises/ office of the CA/Lawyer/Tax Practitioner to conduct survey under section 133A of Income Tax Act in connection with survey of the premises of their client unless the client state in the course of survey that his books of account/documents and records are kept in the office of his CA/Lawyer/Tax Practitioner.

Source – U K Mahapatra & Co Vs Income Tax Officer – (2008) Orissa HC [WP(c) No. 14018 of 2008]

5. Indian Tax Applicability on the Transfer of Shares of the Indian Company by Non-Residents

It has been held by the Hon'ble High Court of Mumbai that where the very purpose of entering into agreements between the two foreign companies is to acquire the controlling interest one foreign company held in the Indian company, the transaction would be subject to tax within the territory of India.

Source – Vodafone International Holdings B.V. Vs Union of India – (2008) Bombay HC (WP No. 2550 of 2007)

INDIRECT TAX

1. Reduction in Peak rate of Excise Duty

The Government has initiated a 4% cut in ad-valorem rates of central excise duty. The peak rate of excise duty of 14% has been reduced by 4%. The ad-valorem component of the excise duty rates in the automobile industry has been reduced from 24% to 20%. The rate of duty on cotton textiles and textile articles has been reduced from 4% to Nil.

Source: Notification No. 58/2008 – Central Excise dated December 7, 2008

2. Refund of Service Tax

Exporters are permitted refund of Service Tax paid by them in respect of certain services, attributable to export of goods. The benefit of such provisions is now available in respect of services provided to exporters. The refund of service tax was earlier restricted to actual amount of service tax paid or service tax calculated on 2% of FOB value of export goods, whichever is less. The ceiling limit of 2% has now been increased to 10%.

Source: Notification No. 33/2008 - Service Tax dated December 7, 2008

3. Exemption from Basic Customs Duty ('BCD')

In order to provide relief to power generation sector, naphtha imported for electricity generation has been fully exempted from Basic Customs Duty ('BCD'). However, the exemption is not available if such naphtha is used for generation of electrical energy for captive consumption. This exemption is only available upto March 31, 2009.

Source: Notification No. 128/2008 - Customs dated December 7, 2008

CORPORATE & OTHER LAWS

1. Rules eased for entry of foreign companies into India

The Ministry of Corporate Affairs (MCA) has removed the requirement of foreign companies/ foreign nationals to get consular verification in their country of origin for establishing place of business or setting up a subsidiary in India. This benefit will be available to only those foreign companies incorporated in a country that fall outside the

Commonwealth but a party to the Hague Apostille Convention 1961.

Source: www.thehindubusinessline.com/2008/12/26

2. Explanatory Memorandum Review of Schedule VI to the Companies Act 1956

In order to enable proper and adequate disclosures as well as to resolve the ambiguity in application of various rules which are to be observed by the company, the general disclosure requirements under Schedule-VI have been harmonized and synchronized with the prescribed accounting standards. The amended Memorandum along with its annexure is available at the Ministry's website at www.mca.gov.in.

Source: Ministry of Corporate Affairs

3. Parliament Passes Limited Liability Partnership (LLP) Bill 2008

Parliament has passed the Limited Liability Partnership (LLP) Bill 2008 on December 12, 2008. As proposed in the Bill, LLP shall be a body corporate and a legal entity separate from its partners. It will have perpetual succession. While the LLP will be a separate legal entity, liable to the full extent of its assets, the liability of the partners would be limited to their agreed contribution in the LLP.

Further, no partner would be liable on account of the independent or unauthorized actions of other partners, thus allowing individual partners to be shielded from joint liability created by another partner's wrongful business decisions or misconduct.

Source: Press release Dec 12, 2008

FEMA & OTHER LAW

1. Foreign Travel - Mode of payment in Rupees

Authorised Dealers Category I & II and Full Fledged Money Changers have been permitted to accept payments through debit cards or credit cards or prepaid cards by a person travelling outside India, against the sale of foreign exchange for travel abroad. This relaxation is in addition to the payment by Rupees or through crossed cheque or Banker's cheque or Pay order or Demand draft subject to the following conditions-

- (i) KYC or AML guidelines are complied with,
- (ii) Sale of foreign currency or issue of foreign currency travelers' cheques is within the limits (credit or prepaid cards) prescribed by the bank,
- (iii) The purchaser of foreign currency or foreign currency travelers' cheque and the credit /debit or prepaid card holder is one and the same person.

Source: A. P. (DIR Series) Circular No. 40, December 10, 2008

2. Buyback of Foreign Currency Convertible Bonds

The policy for premature buyback of Foreign Currency Convertible Bonds ('FCCBs') has been revised and it has been decided to liberalize the procedure and consider applications for buyback of FCCBs by Indian companies, both under the automatic and approval routes.

Under the Automatic Route :

- (i) The buyback value of the FCCB shall be at a minimum discount of 15 per cent on book value;
- (ii) The funds used for the buyback shall be out of existing foreign currency funds held either in India or abroad or out of fresh ECB raised in conformity with the current ECB norms; and
- (iii) Where the fresh ECB is co-terminus with the outstanding maturity of the original FCCB and is for less than three years, the all-in-cost ceiling should not exceed 6 months. In other cases, the all-in-cost for the relevant maturity of the ECB shall apply.

Under the Approval Route:

- (i) Buyback value of the FCCB shall be at a minimum discount of 25 per cent on the book value.
- (ii) Funds used for the buyback shall be out of internal accruals, to be evidenced by Statutory Auditor and designated AD Category – I bank's certificate, and
- (iii) Total amount of buyback shall not exceed USD 50 million of redemption value, per company. There are certain additional conditions that are

applicable for the both proposals, under the automatic and approval route.

Source: A. P. (DIR Series) Circular No. 39, December 08, 2008

3. Un-hedged foreign exchange exposure of clients

Banks are required to have a policy which explicitly recognizes and takes into account risks arising on account of un-hedged foreign exchange exposures of their clients. Besides foreign currency loans above USD 10 million or such lower limits can be extended by banks only on the basis of a well laid out policy of their Boards with regard to hedging of such foreign currency loans.

RBI has further advised that the Board policy of banks should cover un-hedged foreign exchange exposure of all their clients including Small and Medium Enterprises. Further, for arriving at the aggregate un-hedged foreign exchange exposure of clients, their exposure from all sources including foreign currency borrowings External Commercial Borrowings should be taken into account. Banks which have large exposures to clients should monitor and review on a monthly basis, through a suitable reporting system.

Source: DBOD.BP.BC. 96/21.04.103/2008-09, December 10, 2008

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