

TECHNICAL UPDATE

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The key amendments introduced in statutes, policies and procedures in respect of Direct Tax, Indirect Tax, Company Law & Accounting Standards, Foreign Exchange Management Act / Export Import Policy & Stock Exchange Board of India related matters are summarized hereunder

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DIRECT TAX

1. Liability to deduct TDS on commission paid to travel agent by assessee-airlines

The High Court of Delhi has held that the assessee-airlines are liable to deduct TDS on the standard and supplementary commission paid to its travel agents (per the provisions of section 194H of the Income Tax Act) since the relationship between the assessee-airlines and the travel agents is of principal and agent. However, while giving concessional tickets to travel agents, the difference between the full value of the ticket and the concessional ticket cannot be termed as commission and the transaction between the two is that of principal to principal. Hence, TDS is not required to be deducted for this arrangement.

Source: CIT v. Singapore Airlines Ltd. (2009) High Court of Delhi [ITA Nos. 306/2005 & 123/2006]

2. Treatment of loss on account of exchange rate fluctuation

The Hon'ble Supreme Court has held that profit or loss arises to an assessee on account of appreciation or depreciation in the value of foreign currency held by it, on conversion into another currency, such profit or loss would ordinarily be a trading profit or loss if the foreign currency is held by the assessee on revenue account or as a trading asset or as a part of circulating capital in the business. The Apex Court laid down the following parameters to consider for deciding the treatment of such exchange fluctuation

- (i) whether the system of accounting followed by the assessee is mercantile system,
- (ii) whether the same system is followed by the assessee from the very beginning and if there was a change in the system, whether the change was bona fide,
- (iii) whether the assessee has given the same treatment to losses claimed to have accrued and to the gains that may accrue to it,
- (iv) whether the assessee has been consistent and definite in making entries in the account books in respect of losses and gains,
- (v) whether the method adopted by the assessee for making entries in the books both in respect of losses and gains is as per nationally accepted accounting standards,
- (vi) whether the system adopted by the assessee is fair and reasonable or is adopted only with a view to reducing the incidence of taxation.

Source: CIT v. Woodward Governor India (P) Ltd (2009) Supreme Court of India (Civil Appeal No 2214 of 2009)

3. Taxability of an Australian company for providing basic engineering services to an Indian company

The Authority for Advance Ruling ('AAR') has held that the services rendered and work undertaken by the applicant-Australian company in terms of the Agreement for Basic Engineering and Procurement services fall within the scope of royalties as defined in Article 12(3) of the Double Tax Avoidance Agreement ('DTAA') between India and Australia and the receipts are taxable in India by virtue of Article 12(2) of DTAA. The exclusion clause under Article 12(4) of the DTAA is not attracted in view of the absence of the effective connection between its Permanent Establishment ('PE') and the services, and therefore, the royalty income is liable to be taxed

under Article 12(2) of the DTAA read with section 9(1)(vi) of the Income Tax Act.

Source: WorleyParsons Services Pty. Ltd., (2009) Authority for Advance Ruling (In re - AAR No. 747 of 2007)

4. Reasonable assumptions can be made while making adjustments to the Arm's Length Price charged in the course of an International Transaction

The Income Tax Appellate Authority, Pune ('ITAT') has held that where the business model of the assessee is different from that of the comparables, then appropriate adjustments are required to be made to the Arm's Length Price charged in the course of International Transactions. Where sufficient data to make such adjustments is not available in the public domain, then it is inevitable that some approximations and reasonable adjustments are made. The tribunal also agreed with the view of the assessee that a loss making company cannot be ignored while computing the Arm's Length Price alone for the reason that such a company is a loss making company.

Source: Skoda Auto India (P) Ltd. v. ACIT (2009) ITAT Pune (ITA No. 202/PN/07)

5. Selection of the Most Appropriate Method for computing the Arm's Length Price

The onus of proving that a particular method is the most appropriate method to compute the Arm's Length Price is on the assessee and the correctness of the same needs to be demonstrated by furnishing adequate records and data, irrespective of the fact whether they are statutorily required or not. Once the method adopted by the assessee is rejected, the revenue authorities are required to compute the Arm's Length Price by selecting the most appropriate method and the use of such method needs to be substantiated and justified.

Source: UCB India Private Limited v. ACIT (2009) ITAT Mumbai [ITA NOS. 428 & 429/MUM/2007]

INDIRECT TAX

1. Non-applicability of service tax on renting of immovable property

Service tax was levied by Finance Act 2007 on services rendered 'in relation to the renting of immovable property'. However the Delhi High Court observed that the service tax is primarily a value added tax. It is a tax on value addition provided by the service

provider, and as far as renting of immovable property for use in the course or furtherance of business or commerce is concerned, the court observed that there was no value addition done by the landlord in such an activity. Therefore, renting of immovable property by itself cannot be regarded as a taxable service, however, if some other services such as air – conditioning services are also provided along with renting of immovable property, then such services would fall within the ambit of taxable services.

Source: Home Solution Retail India Ltd and Anr. Vs. UOI and Ors., Delhi High Court

2. Applicability of service tax to clearing and forwarding agent

Service tax is applicable in respect of services rendered by ‘clearing and forwarding agents’ and not by ‘clearing or forwarding agents’. Therefore in order to be taxable the service provider should be providing services of both clearing as well as forwarding agent. The court held that reading the word ‘and’ as ‘or’ would amount to doing violence to the simple language used by Legislature which cannot be imputed ignorance of English language. Therefore the word ‘and’ should be understood in a normal conjunctive sense.

Source: CCE Panchkula Vs. M/s Kulcip Medicines (P) Ltd., Punjab and Haryana High Court

3. Payment of service tax through Cenvat Credit Account

The assessee had paid the service tax on Goods Transport Agency through Cenvat Credit Account, it was contended by the government authorities that such tax should have been paid in cash instead of paying it through the Cenvat Credit Account. The tribunal held that the assessee is entitled to utilize the Cenvat credit for payment of service tax on Goods Transport Agency.

Source: CCE Vs. Hero Honda Motors Ltd.

CORPORATE & OTHER LAWS

1. Uniform procedure for dealing with unclaimed shares – Insertion of clause 5A

It has been brought to the notice of the SEBI that there is a large quantum of shares issued pursuant to

the public issues, which remain unclaimed despite the best efforts of the Registrar to Issue or Issuers and that there is no uniform practice for dealing with such shares. It has been decided to provide a uniform procedure for dealing with unclaimed shares i.e., shares which could not be allotted to the rightful shareholder due to insufficient/incorrect information or any other reason. Accordingly, the new Clause 5A is to be inserted, which provides the following:

- The unclaimed shares shall be credited to a demat suspense account opened by the issuer with one of the depository participants.
- Any corporate benefit in terms of securities, accruing on unclaimed shares such as bonus shares, split etc., shall also be credited to such account.
- Details of shareholding of each individual allottee whose shares have been credited to such suspense account shall be properly maintained by the issuer.
- The allottee’s account shall be credited as and when he/she approaches the issuer, after undertaking the proper verification of identity of the allottee.
- The voting rights of these shares will remain frozen till the rightful owner claims the shares.
- Details (in aggregate) of shares in the suspense account including freeze on their voting rights, shall be disclosed in the Annual Report as long as there are shares in the suspense account.

Source: SEBI/CFD/DIL/LA/1/2009/24/04

2. Notice period for Record Date and Board Meeting - Amendments to Clause 16 and Clause 19

It has been decided to reduce the timelines for notice period for all corporate actions like dividend, bonus etc., for all scripts whether in demat or physical, whether in Future and Option segment or not. The notice period for record date has been reduced to 7 working days and for board meeting has been reduced to 2 working days.

Source: SEBI/CFD/DIL/LA/1/2009/24/04

3. Uniformity in dividend declaration - Insertion of clause 20A

It has been decided to mandate that listed companies shall declare their dividend on per share basis only. This is expected to bring uniformity in the manner of declaring dividend amongst the listed companies.

Source: SEBI/CFD/DIL/LA/1/2009/24/04

4. Shareholding pattern for each class of shares and voting rights pattern – Amendment to Clause 35

It is clarified that Clause 35 of the listing agreement which gives a format for disclosures of shareholding pattern, is required to be given for each class of security separately. Further, it has been decided to amend Clause 35 to provide an additional format for disclosures of voting rights pattern in the company.

Source: SEBI/CFD/DIL/LA/1/2009/24/04

FEMA

1. Guidelines for issuing preference shares as part of regulatory capital

Guidelines for Perpetual Non-Cumulative Preference Shares ('PNCPS') forming Tier I capital of commercial banks have been modified and accordingly dividend would no longer be treated as cumulative on PNCPS i.e., dividend missed in a year will not be paid in future years, even if adequate profit is available and the level of CRAR conforms to the regulatory minimum. Further, all instances of non-payment of dividend or payment of dividend at a lesser rate than prescribed are required to be reported by the issuing banks to the RBI, Mumbai.

Source: RBI/2008-09/425 DBOD.No.BP.BC. 120/21.01.002/2008-2009 dated April 02, 2009

2. ECB Policy – Liberalization Issue of Guarantee for operating lease

Reserve Bank of India ('RBI') has eased the External Commercial Borrowing ('ECB') norms for banks to issue no objection under the Foreign Exchange Management Act (FEMA), 1999. Under the relaxed norms, no objection by banks can be extended for issue of corporate guarantee in favor of the overseas lessee and for operating lease for import of aircraft, helicopters and engines. The RBI however has clarified that the no objection is issued only under the provisions of FEMA, 1999 and should not be construed as an approval by any other statutory authority.

Source: RBI/2008-09/438 A. P. (DIR Series) Circular No.62 dated April 20, 2009

3. Extension of Guarantee - Maturity beyond Ten years

RBI has allowed banks to issue guarantees for periods beyond 10 years. However, while issuing such

guarantees, banks are advised to take into account the impact of very long duration guarantees on their Asset Liability Management. Further, banks may evolve a policy on issuance of guarantees beyond 10 years as considered appropriate with the approval of their Board of Directors.

Source: RBI/2008-09/448 DBOD.No. BP. BC.127/21.04.009/2008-09 dated April 22, 2009

4. Guidelines on Outsourcing of Financial Services by Banks - Compliance Certificate

RBI has advised banks to submit an Annual Compliance Certificate giving the particulars of outsourcing contracts, the prescribed periodicity of audit by internal or external auditor, major findings of the audit and action taken through Board, to the concern office of RBI, Mumbai.

Source: RBI/2008-09/449 Ref. DBS.CO.PPD.BC. 5 / 11.01.005/2008-09 dated April 22, 2009

5. Transfer of securities by way of Sale - Modified Reporting Mechanism

RBI has revised form FC-TRS in order to capture the details of investment received by way of transfer of the existing shares or compulsorily and mandatorily convertible preference shares or debentures, of an Indian company. Accordingly, the proforma for reporting of inflows or outflows on account of remittances received or made in connection with the transfer, submitted by AD Category - I bank to RBI has also been modified. RBI further decided that form FC-TRS should be submitted to the AD Category – I bank, within 60 days from the date of receipt of the amount of consideration. The onus of submission of the form FC-TRS within the given timeframe would be on the transferor / transferee, resident in India.

Source: RBI/2008-09/447 A. P. (DIR Series) Circular No.63 dated April 22, 2009

6. Buyback/Prepayment of FCCBs

The current policy for Foreign Currency Convertible Bonds (FCCBs) buyback has been reviewed. The total amount of permissible buyback of FCCBs, out of internal accruals, has been increased from USD 50 million of the redemption value per company to USD 100 million, under the approval route by linking the higher amount of buyback to larger discounts. Indian companies may henceforth be

permitted to buyback FCCBs up to USD 100 million of the redemption value per company, out of internal accruals, with the prior approval of the Reserve Bank, subject to a:

- i) minimum discount of 25 per cent of book value for redemption value up to USD 50 million;
- ii) minimum discount of 35 per cent of book value for the redemption value over USD 50 million and up to USD 75 million; and
- iii) minimum discount of 50 per cent of book value for the redemption value of USD 75 million and up to USD 100 million.

All other terms and conditions stipulated in A.P. (DIR Series) Circular No. 39 dated December 8, 2008 will continue to be applicable. This facility shall come into force with immediate effect and the entire procedure of buyback should be completed by December 31, 2009 as specified in A.P. (DIR Series) Circular No. 58 dated March 13, 2009.

Source: RBI/2008-09/461 A. P. (DIR Series) Circular No 65 dated April 28, 2009

7. External Commercial Borrowings (ECB) Policy - Liberalisation

RBI in terms of its A.P. (DIR Series) Circular No. 46 dated January 2, 2009 relating to External Commercial Borrowings (ECB) dispensed with the requirement of all-in-cost ceilings on ECB, under the approval route, until June 30, 2009. Eligible borrowers, proposing to avail of ECB beyond the prescribed all-in-cost ceilings were required to approach the RBI, under the approval route.

In terms of the announcements made in the annual policy statement 2009 -10 considering the continuing pressure on credit spread in the international markets, such relaxation in all-in-cost ceilings, under the approval route, has been extended to December 31, 2009, subject to review in December 2009.

Source: RBI/2008-09/460 A. P. (DIR Series) Circular No 64 dated April 28, 2009

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