

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. Deductibility of Provision for Warranty

In a recent judgment, the Supreme Court has held that provision for warranty created by the tax payer in its books of accounts is allowable as a deductible expense u/s 37 of the Income Tax Act. The Court observed that the tax payer has been engaged into manufacturing of sophisticated goods and the past trends established the existence of such warranty claims. While deciding the Court has placed reliance on its earlier judgment in the case of Bharat Earth Movers.

Source - Rotork Controls India (P) Ltd. v. CIT (2009) Supreme Court of India [CIVIL APPEAL NOS. 3506-3510 OF 2009]

2. Loss arising on Foreign Exchange Forward Contract

The Delhi High Court has held that loss incurred on foreign exchange forward contracts in respect of import of raw materials and spare parts is a revenue

loss. The Court specifically observed that the treatment in such cases can be no different from a situation wherein the tax payer earns income on foreign exchange forward contract which were offered to tax as business income.

Source - CIT vs Samtel India Ltd. (2009) High Court of Delhi (ITA No. 1120/2008)

3. Determination of Book Profit

The Mumbai Tribunal has held that provision for gratuity if created with reasonable certainty but without actual quantification would amount to 'ascertained liability' and hence treated as an expense for computation of 'book profits'.

Source - Dresser Valve India Pvt. Ltd. v. ACIT (2009) ITAT-Mumbai (ITA No. 6464/Mum/2007)

4. Withholding Tax applicability on Contracts involving Sale of Goods

The Central Board of Direct Taxes ("CBDT") has clarified that tax deduction at source is not required for payments made for sale contracts since no 'work' is involved in such transactions. Relying on this clarification, Mumbai Tribunal has held that in cases involving supply of goods which are fabricated as per customer specification, a contract of sale takes place and hence no deduction of tax at source u/s 194C is required. It is also important that in such cases the property in goods passes to the buyer upon delivery.

Source - Shemaroo Video Pvt. Ltd. Vs ITO (2009) ITAT - Mumbai (ITA NOS. 337 TO 340/MUMI/2007)

INDIRECT TAX

1. Exemption From Service Tax for units and developers of Special Economic Zones ('SEZs')

Notification no. 9/2009 was issued by the Central Board of Excise & Customs ('CBEC') which provided for exemption from service tax for units and developers of SEZs. However the exemption was available through a refund mechanism, whereby the unit or the developer was required to first pay the service tax to the service provider and thereafter claim a refund from the revenue authorities for the same.

Now the CBEC has made some further amendments by issuing notification no. 15/2009 dated May 20, 2009, whereby an unconditional exemption has been

provided from service tax in relation to services consumed by the units/developers within the SEZ. Therefore, the requirement of first paying the tax and thereafter claiming a refund has been dispensed with in respect of services consumed within the SEZ by the units/developers.

The unit or developer of SEZ is also required to maintain proper account of receipt and utilization of the taxable services for which exemption is claimed.

The earlier requirement is now limited to situations only when taxable services are provided to developers/units of SEZ and such services are consumed partially or wholly outside the SEZs.

Source: Notification no.15/2009-Service Tax, dated May 20, 2009

2. Drawback to Merchant Exporters

In case of merchant exporter who procures export goods from the open market and thereafter exports them, the benefit of all industry rates of duty drawback was restricted to the Customs allocation only, if any.

However, the CBEC has now decided that in case of merchant exporters who purchase goods from the local market shall be eligible to full rate of duty drawback (including the excise portion). However, such merchant exporters shall have to declare at the time of export, the name and address of the trader from whom they have purchased the goods. They also have to declare that no rebate (input rebate and also the final product rebate) shall be taken against the Shipping bills under which the goods are being exported by them.

Source: Circular No. 16/2009-Customs, dated May 25, 2009.

3. Outdoor catering services to be regarded as input services

The assessee, a manufacturing concern, paid service tax on outdoor catering services received by them in their factory canteens. Subsequently credit of such tax was claimed by the assessee which was disallowed by the revenue authorities and a demand was raised against the assessee. The assessee relied on the Tribunal's earlier decision in the case of CCE Vs GTC Industries Ltd., wherein the Tribunal had held that outdoor catering services was an input service for the manufacturer in as much as the cost of supply of

food to the employees formed part of cost of production of excisable goods in the factory. Relying upon its earlier judgment, the tribunal held that where expenses towards supply of subsidized food in a factory-canteen formed part of the cost production of the final products, the catering services employed in the canteen for the supply of such food had to be considered as input service relating to the business.

Source: Pudumjee Pulp and Paper Mills Ltd. and Pudumjee Industries Ltd. Vs. CCE (Mumbai CESTAT)

CORPORATE & OTHER LAWS

1. PAN requirement for transfer of shares in physical form

The Securities and Exchange Board of India (SEBI) vide circular ref. no. MRD/DoP/Cir-05/2007 dated April 27, 2007 made PAN the sole identification number for all participants transacting in the securities market, irrespective of the amount of such transaction. In continuation of the aforesaid circular, it is hereby clarified that for securities market transactions and off-market/private transactions involving transfer of shares in physical form of listed companies, it shall be mandatory for the transferee(s) to furnish copy of PAN card to the Company/RTAs for registration of such transfer of shares.

All Stock Exchanges are advised to:-

- implement the above by making necessary amendments to the bye-laws and Listing Agreement, as applicable;
- bring the provisions of this circular to the notice of the listed companies for necessary compliance and also to put the same on their website for easy access to the investors; and
- communicate to SEBI the status of the implementation of the provisions of this circular and the action taken in this regard in the Monthly Development Report.

All Registrars to an Issue and Share Transfer Agents are advised to:

- take necessary steps to implement the above decision.

- disseminate the provisions of this circular on their website.

This circular is issued to protect interests of investors in securities and to promote the development of, and to regulate the securities market.

Source : SEBI/MRD/DoP/Cir-05/2009 dated May 20, 2009

2. Amendment in E-forms

E-Forms 44 and 49 for the purposes of :

- delivering documents for registration by foreign company and
- alteration in the memorandum and articles of association, change in registered office and directors and secretary of a foreign company

have been revised vide Notification No. G.S.R 257(E) dated April 17, 2009.

E-Forms 19, 20, 20A wherein declaration of compliance with the provisions of Section.149(1)(a), 149(1)(b), 149(1)(c), 149(2)(b), 149(2A), 149(2B) have also been revised.

This notification shall come into force w.e.f. May 31, 2009

Source: MCA/G.S.R 257(E) dated April 17, 2009

FEMA

1. Policy Guidelines for issuance and operation of Prepaid Payment Instruments in India

Reserve Bank of India ('RBI') has notified the guidelines for 'Prepaid Payment Instruments in India'. These guidelines will ensure an orderly development and operations of prepaid payment instruments issued by banks and non-bank entities as a means of payment in India.

Source: RBI/2008-09/458 DPSS.CO.PD.No. 1873/02.14.06/2008-09 dated April 27, 2009

2. Loans to Non Residents or third party against security of Non Resident (External) Rupee Accounts

RBI has decided to increase the existing cap of Rs. 2 million to Rs. 10 million on loan against security of funds held in NR (E) RA and FCNR (B) deposits either to the depositor or third parties. Following the RBI's declaration, Banks are allowed to grant fresh

loans or renew existing loans against NR(E)RA and FCNR(B) deposits upto a maximum limit of Rs. 10 million.

Source: RBI/2008-09/462 A. P. (DIR Series) Circular No.66 dated April 28, 2009

3. Buyback or Prepayment of FCCBs

RBI has decided to enhance the total amount of permissible buyback of Foreign Currency Convertible Bonds ('FCCBs'), out of internal accruals, from USD 50 million to USD 100 million, under the approval route. Accordingly, 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 RBI, subject to a minimum discount of:

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

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

4. Investment Portfolio of Banks - Transactions in Securities

RBI has reviewed the policy regarding shifting of securities held as investment in Banks. It announced that interchanging of investment from permanent category to current category and vice-versa can only

be done once a year with the approval of the Board of Directors. It further added that such kind of shifting may normally be allowed at the beginning of the accounting year and further shifting will not be allowed during the remaining part of the year.

Source: RBI/2008-09/473 RPCD.CO.RF.BC.No. 104 / 07.37.02/2008-09 dated May 7, 2009

5. Asian Clearing Union (ACU) - Payment of interest on ACU USD/EUR Accounts

RBI has decided to allow banks operating in India to pay interest, at their discretion, on Asian Clearing Union ('ACU') Euro Vostro accounts in addition to ACU Dollar Vostro accounts maintained by them. The decision to pay interest and the rate at which it will be paid and other conditions will, however, be left to the discretion of each bank.

Source: RBI. No. 2008-09/472 DBOD. No. Dir. BC. 132/ 13.03.00/2008-09 dated May 7, 2009

6. Reconciliation of NOSTRO account and treatment of outstanding entries

RBI has reviewed the position regarding long pending outstanding debit and credit entries in these accounts because of practical difficulties and involvement of substantial expenditure in the elimination of outstanding entries in Nostro accounts after the lapse of certain time. Further, Banks are advised to minimize the number of Nostro accounts to have a better control over reconciliation and to leverage technology to avoid building up of unreconciled balances.

Source : RBI/2008-09/475 DBOD.BP.BC.No.133/21.04.018/ 2008-09 dated May 11, 2009

ASA & Associates

chartered accountants

Head Office

K S House 118 Shahpur Jat
New Delhi 110 049 INDIA
Tel : +91 11 4100 9999
Fax : +91 11 4100 9990
Email : info@asa.in

Mumbai Office

Navbharat Estate 'East Wing' 2nd Floor
Zakaria Bunder Road Sewri (W)
Mumbai 400 015 INDIA
Tel : +91 22 2410 4000
Telefax : +91 22 2410 6263
Email : infomumbai@asa.in

www.asa.in

Bangalore Office

A-2 Ground Floor
Akruti Antara Apartment
No 11/1 Haudin Road
Bangalore 560 042 INDIA
Tel : +91 80 4151 0751
Fax : +91 80 4113 5109
Email : infobangalore@asa.in