

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 & Securities and Exchange Board of India related matters are summarized hereunder

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DIRECT TAX

1. Taxability of Income from Shipping Business by Non-Resident

Profits from international shipping operations are not covered by the Indo-Swiss Double Taxation Avoidance Agreement ('DTAA'). The Authority for Advance Ruling ('AAR') has observed that Article 7 of the Indo-Swiss DTAA specifically excludes the

profits earned through international shipping operations and the same is also not covered by Article 22 dealing with residuary items of income on the ground that such profits have been consciously kept out of the provisions of the DTAA & that such income is only a species of business profits and not a separate item of income, and therefore cannot be brought within the purview of the residuary article. Such profits are therefore taxable as per the provisions of the Indian Income Tax Act 1961.

Source: Gearbulk AG vs DIT (2009) Authority for Advance Rulings (AAR No 803 of 2009)

2. Independent Sub-Contractor not to be considered as Permanent Establishment

Workplace of a sub-contractor entrusted to execute the contract awarded to a non-resident cannot be treated as the permanent establishment of the non-resident. A German company ('the Applicant') was awarded a contract for design, supply, installation and maintenance of solar operated navigational lighting equipment. The applicant subcontracted the work to an independent sub-contractor. The applicant also deputed its engineers for onshore installation for a period less than 60 days. The AAR observed that although the sub-contractor is acting as a nominee of the applicant in carrying out the work which would otherwise had been performed by the Applicant, the workplace of the sub-contractor cannot be treated as the permanent establishment of the Applicant, unless the subcontractor is a dependent agent.

Source: Pintsch Bamag vs DIT (2009) Authority for Advance Rulings (AAR No 790 of 2008)

3. No Penalty for Bonafide Transfer Pricing Adjustment

The Transfer Pricing Officer ('TPO') while evaluating the pricing of international transactions undertaken by the Assessee with its Associated Enterprises ('AE'), made an adjustment to the transaction price. The Assessee was charging its AE on an operating cost plus mark up basis. While computing the operating cost, the Assessee excluded the expense incurred in account of 'Provision for Bad Debts' from the Operating Costs. The TPO disagreed with the contention of the Assessee, that such an expense was extra-ordinary and accordingly made an adjustment to the transfer price. Penalty

was levied by the Assessing Officer on such adjustment on the ground that the Assessee has not disclosed the real operating cost. The tribunal held that treatment of such an provision is debatable issue, for which two different opinions are possible.

Further, the Assessee had made full disclosure of all the relevant facts and therefore the Assessee acted under a boafide belief and with due diligence, therefore no penalty for concealment of income is leviable under such circumstances.

Source: DCIT vs Vertex Customer Services (India) Pvt Ltd. (I.T.A No. 1506/Del/2008)

4. No Depreciation on Stock Exchange Membership Cards

Depreciation is allowable on intangible assets, per the provisions of Section 32 of the Income Tax Act, 1961. The section allows depreciation on specific intangible assets, which are primarily of the nature of Intellectual Property Rights ('IPRs')/ right to use IPRs. Amongst others, the section also allows depreciation on licenses. It was contended on behalf of the Assessee that stock exchange membership cards are in the nature of licenses to carry on trade. However, the court held that section 32 allows depreciation on assets which are generically IPRs, therefore relying on various judgments of the Supreme Court, the court held that, the term license has to be interpreted to mean licenses to acquire or use IPRs. Since, the stock exchange membership cards are not a license to use or acquire any IPR, no depreciation is allowable on the same.

Source: Commissioner of Income Tax vs Techno Shares and Stocks Limited and others (ITA (L) No. of 971 of 2006)

5. Purchase of Plant Know-how from Non-Resident

The tax-payer entered into an agreement with a Singapore Company to purchase plant know-how in the form of technical and engineering data, design data, drawings, sketches, photographs etc. The technical documents were handed over to the tax-payer in Singapore and payment was also made in Singapore. Given these facts, the question before High Court was to examine whether the agreement to transfer all such know-how falls within the meaning of 'Royalty' or can be considered as outright sale of the plant. Relying on past rulings, the High

Court observed that the drawings, designs, processing data etc constitute plant within the meaning of Income Tax Act. Considering the facts of the case that Singapore Company had no Permanent Establishment in India and that the agreement was executed in Singapore, the High Court held that the payment may not be considered as royalty or fee for technical services. Accordingly, no tax liability arises in India.

Source – CIT Vs Maggronic Devices (P) Ltd (2009) High Court of Himachal Pradesh

6. Taxability of Demurrage Charges Paid to Non-Resident Shipping Company

The tax-payer had made payment towards demurrage charges to a shipping company (non-resident in India). No tax was withheld on such payment and therefore the tax-officer disallowed the same per section 40(a)(i) of the Act. The question before High Court was to decide whether demurrage charges payable to non-resident for delay in loading the goods on the ship is liable to be taxed under the provisions of the Act. Relying on the Circular issued by CBDT, High Court held that the demurrage charges received by any non-resident shipping company are taxable per provisions of section 172 of the Act and hence tax-payer was required to withhold the tax at source. Accordingly, the disallowance made by the tax-officer was confirmed.

Source – CIT Vs Orient (P) Ltd (2009) High Court of Bombay (Tax Appeal No 7 of 2005)

7. Taxability of Telecasting and Broadcasting Services by Foreign Companies

The tax-payer was engaged in the business of providing transponders capacity (operated through telecommunication satellites) to Indian telecasting companies. The Indian companies used such transponders for data transmission by uplinking and downlinking programmes. The issue before the Delhi ITAT (Special Bench) was to examine if the income received by the tax-payer for use of their satellites for telecommunication and broadcasting qualifies as 'Royalty' and hence taxable in India. The Tribunal held that the use of process involved in the transponder for telecasting and broadcasting services amounts to 'Royalty' within the meaning of section 9 of the Income Tax Act and relevant tax treaty.

Accordingly, the income was held taxable as 'Royalty'.

*Source – New Skies Satellites NVVs ADIT (2009) Delhi ITAT – Special Bench
Shin Satellite Public Co Ltd Vs DDIT (2009) Delhi ITAT – Special Bench*

8. Cost of Granting Stock Options to Employees

The tax-payer granted stock options to its employees and recognised the difference between the market price and issue price as 'deferred employee compensation' in its books of accounts. The tax-officer disallowed the deferred employee compensation on the basis that no actual liability had arisen or paid by the tax-payer. The Delhi ITAT observed that issuing shares at below market price does not result in incurring any expenditure. It rather amounts to short receipt of 'share premium'. Accordingly, the Tribunal upheld the disallowance made by the tax-officer.

Source – Ranbaxy Laboratories Ltd Vs DCIT (2009) Delhi ITAT (ITA No 1666/2006)

INDIRECT TAX

1. Interest recoverable if CENVAT credit is wrongly taken

It has been clarified by the Board that even in cases where CENVAT credit has been wrongly taken, but not utilized and reversed by the assessee before utilization, interest is recoverable on the amount of credit wrongly taken. Rule 14 of the CENVAT Credit Rules, 2004, is clear and unambiguous in this position.

Source : Circular No. 897/17/2009-CX dated 3.9.2009

2. Exemption from the whole of service tax

Services provided by a sub-broker u/s 65(105) (zzb) to a stock broker u/s 65(101) in relation to the sale and purchase of securities listed on a recognized stock exchange has been exempted from the whole of service tax.

Source: Notification no 31/2009-Service Tax dated 1st September 2009.

Services provided by any person u/s 65(105) (zzb) to a client as defined u/s 65(19) in relation to the manufacture of pharmaceutical products, medicines, perfumery, cosmetics or toilet preparations containing

alcohol which are charged to excise duty under medicinal and toilet preparations (Excise Duties) Act, 1955 exempted from the whole of service tax.

Source: Notification no 32/2009-Service Tax dated 1st September 2009.

3. Services in relation to works contract in respect of canals exempted

Service referred to in sub-clause (zzzz) of clause (105) of section 65 of the said Act, in relation to execution of a works contract in respect of canals, other than those primarily used for the purposes of commerce or industry, has been exempted from the whole of service tax leviable thereon under section 66 of the said Act.

Source: Notification No. 41/2009-Service Tax dated 23rd October 2009

4. Minor ports and foreign post office not required to send documents for audit to major Custom Houses

The Board's instructions issued vide F.No. 8/6/67-Cus.III dated 05.11.1977 stands rescinded. These instructions provided that various documents such as Bills of Entry, postal imports of certain categories, refund claims of certain categories, drawback shipping bills of certain categories etc., pertaining to various minor ports and foreign post offices should be sent for audit to major Customs Houses like Mumbai, Cochin etc.

Source: CBEC Instruction dated 8th October 2009

5. Duty-paid packing materials permitted to be brought into export warehouse

The Board has clarified that the duty paid packing material can be allowed to be brought in the export warehouse to be used for packing of export goods. The exporter will be required to obtain permission from the jurisdictional Excise Officer and also to maintain proper account of such goods. However, he shall not be entitled to claim any export benefit like rebate of duty paid on the said material.

Source - Circular No. 900/20/2009-CX dated 6th October 2009

6. Assessable value under Central Excise for good manufactured on job-work

It has been clarified by The Board that where stock

transfer is made by the principal manufacturer to the job worker for producing the final product, who then transfers back the final product to the principal manufacturer for onward sale, the assessable value for payment of duty should remain same for both principal manufacturer and job worker, such value being the end sale price.

Source - Circular No. 902/22/2009-CX dated 20th October 2009

CORPORATE & OTHER LAWS

1. E-payment of stamp duty

In order to make the transactions more faster and to dispense with the requirement of physical submission of the documents at Registrar of Companies, the Central Government has introduced the scheme for making e-payment of stamp duty via MCA 21 portal on the below stated statutory documents:

- Form 1, Memorandum and Articles of Association
- Form 5 for increase in Share Capital
- Form 44 for LO, BO, PO

This scheme is effective from September 14, 2009.

Source: S.O. 2276 (E) Ministry of Corporate Affairs dated September 07, 2009

2. Amendment in e-form 24B, e-form 25 A under Companies Act, 1956

Ministry of Corporate Affairs vide notification no. G.S.R 649 (E) dated September 08, 2009, have amended the following e-forms:

- E-form 24 B for filing an application to the Central Government for obtaining prior consent for holding of any office or place of profit in the Company.
- E- Form 25 A for filing an application to the Central Government for approval of appointment or re-appointment and remuneration or increase in remuneration or waiver for excess or over payment to managing or whole time director or manager.

Revised e-forms will be effective from September 13, 2009.

Source: Company Affairs Notification No. G.S.R 649 (E) dated September 08, 2009

FEMA

1. Foreign Exchange Management (Transfer or Issue of Any Foreign Security) (Fourth Amendment) Regulations, 2009, notified.

RBI has made amendments in the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 to issue Foreign Exchange Management (Transfer or Issue of Any Foreign Security) (Fourth Amendment) Regulations, 2009, permitting an Indian Party engaged in financial services sector in India to make investment in an entity outside India provided that the Indian party

- a) has earned net profit during the preceding three financial years from the financial services activities;
- b) is registered with the regulatory authority in India for conducting the financial services activities;
- c) has obtained approval from the concerned regulatory authorities both in India and abroad, for venturing into such financial sector activity;
- d) has fulfilled the prudential norms relating to capital adequacy as prescribed by the concerned regulatory authority in India.

Source: Notification No. FEMA 196/2009-RB dated July 28, 2009

2. Acceptance of Deposits by Chit Fund Companies

Miscellaneous Non-Banking Companies ('MNBCs') are prohibited from accepting deposits from public except from the shareholders subject to some conditions. RBI has further clarified that any deposit accepted and held by the MNBCs other than from its shareholders as on date shall be repaid on maturity and shall not be eligible for renewal.

Source: RBI/2009-10/133 DNBS (PD) CC No. 159/03.03.01/2009-10 dated August 28, 2009

3. Gold Card Scheme for Exporters

RBI has dispensed with the requirement of overdue export bills not exceeding 10 per cent of the previous year's export turnover, for one year i.e. from April 1, 2009 to March 31, 2010 in order to minimize the difficulties faced by exporters on account of weakening of external demand and in realizing the dues within the stipulated time.

Source: RBI/2009-10/149 DBOD No Dir (Exp). BC. 39/04.02.001/2009-10 dated September 7, 2009

4. Foreign Currency Account by diplomatic missions - Credit of Visa Fees

RBI has permitted diplomatic missions to credit the visa fees collected in India in Indian rupees by way of transfer from the rupee account to the accounts maintained in foreign currency. This is in addition to proceeds of inward remittances received from outside India through normal banking channels.

Source: RBI/2009-10/156 A. P. (DIR Series) Circular No.08 dated September 14, 2009

5. Prior RBI approval for acquisition/ transfer of control of NBFCs

RBI has decided that any takeover or merger or amalgamation or acquisition of shares of a deposit taking Non Banking Financial Corporation ('NBFC') would need to comply with the guidelines laid and would require prior approval of RBI.

Source: RBI/2009-10/162 DNBS (PD) CC No 160/03.10.001/2009-10 dated September 17, 2009

6. Lending to enterprises under the MSMED Act, 2006 categorized as Priority Sector Lending

Government of India has decided to include loans granted by banks in respect of various consultancy and Management services under Micro and Small (Service) Enterprises within the priority sector, provided such enterprises satisfy the definition of Micro and Small (Service) Enterprises in respect of investment in equipments. It further categorized Retail Trade as the part of the Small (Service) Enterprise.

Source: RBI/2009-10/164 RPCD CO Plan BC 24 /04.09.01/2009-10 dated September 18, 2009

7. Guidelines for Foreign Investment in Commodity exchange

Date for divestment of foreign equity, exceeding the composite ceiling for foreign investment of 49 per cent, extended to 31.03.2010. It has been further clarified that such extension would be the last opportunity to comply with the provisions of press note 2 (2008) dated March 12, 2008 by all Commodity Exchanges.

Source: IPP F.No. 12(58)/2005-FC dated September 26, 2009

8. Issue of Bank Guarantee on behalf of Service Importers

RBI has liberalised the procedure for import of

services, it has been decided to increase the limit for issue of guarantee by AD Category-I banks from USD 100,000 to USD 500,000. Accordingly, AD Category-I banks are now permitted to issue guarantee for amount not exceeding USD 500,000 or its equivalent in favour of a non-resident service provider, on behalf of a resident customer who is a service importer.

Source: RBI/2009-10/176 A.P. (DIR Series) Circular No.11 dated October 5, 2009

9. Cash withdrawal at Point of Sale

Presently cash withdrawal facility using plastic cards is available only at ATMs. As a step towards enhancing the customer convenience in using the plastic money, RBI decided to permit cash withdrawals at Point of Sale terminals irrespective of whether the card holder makes a purchase or not. This facility will be available to all debit cards issued in India, upto Rs. 1000/- per day. Banks may obtain the approval of their Board of Directors for offering this facility.

Source: RBI/2009-10/179 UBD.CO.BPD.No. 13/09.18.300/2009-10 dated October 5, 2009

10. Advance Remittance for Import of Services

RBI has clarified that the increase in the limit for advance remittance for all admissible current account transactions for import of services without bank guarantee is not applicable for a Public Sector Company or a Department/ Undertaking of the Government of India/ State Governments as they would require approval from the Ministry of Finance, Government of India for any such advance remittance.

Source: RBI/2009-10/175A.P. (DIR Series) Circular No.10 dated October 5, 2009

11. Submission of certificate from Statutory Auditor to the Bank

RBI has decided that the Non Banking Financial Companies may submit the certificate from its Statutory Auditor stating that it is engaged in the business of non-banking financial institution and showing the position of the company as at end of the financial year ended March 31 within one month from the date of finalization of the balance sheet but not later than December 30th of that year.

Source: RBI/2009-10/187DNBS (PD) CC. No. 162/03.05.002/2009-2010 dated October 22, 2009

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