

TECHNICAL UPDATE

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The key amendments introduced in statutes, policies and procedures in respect of Direct Tax, Indirect Tax, Corporate Laws & 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. Dispute Resolution Scheme - Notified

The Finance Act, 2009 had introduced the concept of an Alternate Dispute Resolution Scheme to address the grievances of foreign companies or of those Indian entities where an adverse Transfer Pricing adjustment is proposed by the Transfer Pricing Officer. Section 144C was introduced in the Income Tax Act 1961 ('the Act') empowering the Central Board of Direct Taxes ('CBDT') to constitute a Dispute Resolution Panel ('DRP') to adjudicate upon such cases. CBDT has now notified the rules for regulating the procedure to be followed by the DRP while disposing the objections of the Appellant. The procedure to be followed while approaching the DRP viz. the forms to be used, filing of additional evidence etc has also been notified. DRPs will presently be constituted at eight cities. It is noteworthy that the order of DRP is appealable by the Assessee before the Income Tax Appellate Tribunal.

Source: Notification No 84 dated November 20, 2009

2. Liability to Withhold Tax on Payment to Non-Residents

The tax-payer had made payments for acquisition/purchase of copyrighted article from non-residents without withholding of tax u/s 195 of the Income Tax Act ('Act'). The tax-payer took a view that since nature of payments was 'trading receipts', which could not have been taxable in India in the absence of a 'Permanent Establishment' ('PE'), such payments were not subject to taxation in India. The tax-officer, on the other hand, considered such payments as royalty and held that the same were taxable in India. The question before the High Court was to examine whether there was an obligation of tax withholding in terms of section 195 of the Act in respect of remittances made to the non-resident. Relying on

the past judgment of the Apex Court, the High Court held that section 195 of the Act mandates compulsory withholding of tax while remitting any sum to non-residents even when only a part of the payment has the character of income and tax-payer cannot be absolved from this responsibility on the basis of non-taxability of payment in India. The court further clarified that the tax-officer has no right to decide the final taxability of non-residents and the tax-payer should have exercised the option granted in sub-section (2) of section 195 i.e. to make an application before the tax-officer to allow a lower/nil rate of withholding tax prior to making such payment. In effect, this ruling sets precedence that payments to non-residents, which are apparently not subject to taxation in India, must be examined by the tax-officer beforehand.

Source: CIT vs Samsung Electronics Co Ltd (High Court of Karnataka)

3. Nexus of Expenditure incurred with the Exempted Income

The tax-payer company earned dividend income which was exempt from tax. Based on these facts, the tax-officer disallowed certain expenditure per provisions of section 14A of the Act read with Rule 8D of the Income Tax Rules on a presumption and without establishing any nexus of expenditure with the exempted income. The High Court held that expenditure which has been proved to be incurred in relation to earning of tax free income can be disallowed u/s 14A of the Act and the disallowance cannot be extended to expenditure which is assumed to have been incurred for earning tax free income. Therefore, common expenditure incurred cannot be broken artificially to attribute for apportioning a part thereof to earning of tax free income on assumption that such part of common expenditure was incurred in relation to tax free income.

Source: CIT Vs Hero Cycles Ltd (2009) (High Court of Punjab & Haryana)

INDIRECT TAX

1. Exemption from submission of the annual installed capacity statement

Exemption has been provided to the following

industries from submission of the annual installed capacity statement -

- (i) biris, manufactured without the aid of machines
- (ii) matches manufactured without the aid of power
- (iii) reinforced cement concrete pipes

Source: Notification No. 26/2009 - Central Excise (N.T.) dated 18th November 2009

2. Exemption from the whole of service tax

Services provided by any person u/s 65(105)(zzb) to any other person in relation to one or more of the specified process during the course of manufacture of parts of cycles or sewing machines have been exempted from the whole of service tax, subject to certain conditions.

Source: Notification No. 42/2009-Service Tax dated 12th November 2009

3. Applicability of indirect taxes on packaged software.

Further to notification no. 22/2009-CE dated 07.07.2009 and 80/2009-Customs dated 07.07.2009, CBEC has issued instructions to provide exemption from excise duty / CVD in the case of shrink wrapped packaged software on such portion of the value which represents the consideration for the transfer of the right to use for commercial exploitation (cost of IPR), as distinct from the portion of value towards cost of actual software on a media. The value attributable to cost of IPR shall be subject to service tax and there should not be dual taxation. There is no rationale for the department to deny splitting of the total value of such packaged software unless there are reasons to believe that such a splitting has been done in order to evade payment of duty.

Source: Instruction F.No.354/189/2009-TRU- CBEC dated 4th November 2009

FEMA

1. Export Credit Refinance Facility

Reserve Bank of India ('RBI') has reduced the eligible limit of Export Credit Refinance ('ECR') to 15 per cent from 50 per cent of the outstanding rupee export credit eligible for refinance. Accordingly, modifications in the part A of the reporting format have also been made.

Source: RBI/2009-10/193 Ref. MPD No.1437/02.01.005/2009-10 dated October 27, 2009

2. Provisioning Requirement for Standard Assets

RBI has reduced the provisioning requirement for all types of standard assets to 0.40 per cent except in the case of direct advance to Agriculture and Small Manufacturing Enterprise, it has been reduced to 0.25 per cent. RBI has also increased the provisioning requirement for advances to the Commercial Real Estate Sector to 1.00 per cent from 0.40 per cent.

Source: RBI 2009-10/209 DBOD No BP.BC 58 /21.04.048/2009-10 dated November 5, 2009

3. Section 24 of the Banking Regulation Act, 1949- Shortfall in Maintenance of Statutory Liquidity Ratio (SLR)

RBI has withdrawn the relaxation to scheduled commercial banks in the maintenance of Statutory Liquidity Ratio ('SLR') for an extent upto 1.5 per cent with effect from October 27, 2009.

Source: RBI/2009-10/207 Ref: DBOD.Ret.BC.No.56/12.02.001/2009-10 dated November 05, 2009

4. Transparency of transactions in the marketing products by banks

RBI has decided that the banks should disclose to the customers, details of all the commissions or other fees (in any form) received, if any, from the various mutual funds, insurance or other financial companies for marketing or referring their products so that the transparency of the transactions in their interest is being maintained.

Source: RBI/2009-10/225 DBOD No FSD.BC 60/24.01.001/2009-10 dated November 16, 2009

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