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India Spectrum

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In this issue

Corporate tax 06

Personal taxes 12

Mergers and acquisitions 14

Transfer pricing 16

Indirect taxes 19

Regulatory developments 21

Editorial

We are delighted to present another issue of India Spectrum.

Following the budgetary announcements, the budget document was placed before the Parliament. Bowing to uncertainty in its application, the government deferred its plan to bring General Anti Avoidance Rules (GAAR) by a year and it would now be effective from 1 April, 2013. Importantly, the onus to prove a transaction to be impermissible is shifted on the revenue department. However, the retrospective amendment relating to capital gains on sale of assets located in India through indirect transfer abroad was left as it is. A reprieve was provided by clarifying that reopening of cases will not take place where the assessments are completed.

The Reserve Bank of India (RBI) announced its monetary policy and expects the overall economic growth in India to improve moderately in 2012-13. And while inflation is moderate, risks remain. The growth rate at the industry level is also expected to be moderate, with the index of industrial production (IIP) hovering around 4.1% in February, up from 1.1% in January 2012 and 1.8% in December 2011. Following the announcement by the RBI to cut the repo rate by 50 bps to 8%, a turnaround in IIP growth is likely.

On the global front, the US economy continues to show signs of modest recovery while large-scale liquidity infusions by the European Central Bank have significantly reduced the stress in global financial markets. However, a sustainable solution to the Euro-area debt problem is yet to emerge as sovereign debt challenges, such as that in the case of Spain, will continue to weigh on the global economy.

Shyamal Mukherjee

Ketan Dalal

The Department of Industrial Promotion and Production issued the consolidated foreign direct investment policy, which clarified inter alia that shares will now be allowed to be issued only against the import of new capital goods, machinery or equipment since capitalisation of second-hand capital goods, machinery or equipment has been discontinued. The policy stated that institutional investors, who were permitted to invest up to a maximum of 23% within the overall limit of 49%, would no longer require approval from the Foreign Investment and Promotion Board.

On the judicial front, in the case of Jet Airways India Pvt. Ltd., the Mumbai Income-tax Appellate Tribunal (the Tribunal) held that a mere relation between the business of a non-resident and the activity in India that facilitates or assists the carrying on of the business of the non-resident would also result in a business connection and hence would be liable to tax. The Tribunal also held that receipt of income alone is adequate for a resident to be treated as an agent of a non-resident, and that the liability of the non-resident to be taxed in India need not be established. In another ruling in the case of R. Nagaraja Rao, the Karnataka High Court held that shares transferred to a family member under a family arrangement or partition cannot be construed as a 'transfer' under section 2(47) of the Act; hence, no capital gains tax would be chargeable in such cases.

We hope you enjoy this issue. As always, we look forward to hearing from you.

Ketan Dalal and Shyamal Mukherjee
Joint Leaders, Tax and Regulatory Services

Analysing tax issues
Corporate tax

Royalty or fees for technical services

Reimbursement of travel expenses to be considered for computing taxable gross receipts

The assessee company is a resident of Singapore with no place of business in India. It was receiving income from licensing software to four customers in India, one of which was CSC India Pvt Ltd, a 100% subsidiary of the assessee. The assessee offered to tax all sums received from India as royalty and fees for technical fees (FTS) on 'receipt' basis under the Double Taxation Avoidance Agreement (the tax treaty) between India and Singapore. Furthermore, the assessee received reimbursement from its subsidiary for the travel expenses of its employees who came to India to assist the subsidiary company on a cost-to-cost basis.

During the course of assessment proceedings, the tax officer (TO) held that the reimbursement of travel expenses should be a part of the gross receipts for computing the amount of royalty or FTS and will be liable to tax. The order of the TO was upheld by the Dispute Resolution Panel (DRP).

The Income-tax Appellate Tribunal (the Tribunal) held that the travel expenses were incurred to earn royalty or FTS which was in connection with the technical service agreement. These receipts are taxable on gross basis. If the assessee was allowed deduction of expenses incurred while computing royalty or FTS, the principle of taxation on gross basis, as provided in Article 12 of the tax treaty, would be violated.

Furthermore, since the provisions of the tax treaty were more beneficial to the assessee, the royalty or FTS was taxable on a gross basis and no deduction for expenses was permitted under Article 12 of the tax treaty. Reliance was placed on the decision in the case of CIT *v.* Hallibuton Offshore Services Inc [2008] 300 ITR 268 (Uttarakhand) where it was held that the reimbursement of expenses will be included in receipts for arriving at the presumptive income. Therefore, the reimbursement of travel expenses has to be considered while computing the gross receipts taxable under Article 12 of the tax treaty.

CSC Technology Singapore Pte Ltd *v.* ACIT [TS-94-ITAT-2012 (Del)]

Installation work which is ancillary to the use of equipment taxable as FTS

The applicant, a tax resident of Singapore, entered into a contract with Indian Oil Corporation Ltd (IOCL) to install a terminal for the discharge of crude oil from the sea vessels to the onshore tank.

Furthermore, Larsen & Toubro (L&T) entered into a contract with ONGC for installation and construction work which was sub-contracted to the applicant.

The applicant sought an advance ruling on the taxability of payments received under the above contracts and contended the following:

- Both the contracts were for installation work representing business income and would be taxable only on the existence of a permanent establishment (PE) in India.
- Since the installation work continued in India for less than 183 days and it did not have any office or premises in India, it would not constitute a PE in India in terms of Article 5 of the India-Singapore tax treaty.
- Even though the activities carried out under the contract with L&T were in connection with the prospecting, extraction or production of mineral oils, in the absence of a PE, there would be no liability under section 44BB of the Income-tax Act, 1961 (the Act).

The Revenue contended the following:

- Services imparted by the applicant under both the contracts were post exploration services which, being technical in nature, would be taxable as FTS under the tax treaty as well as under the Act.
- The equipment mobilisation and de-mobilisation expenses for the L&T contract were a part of the composite contract. Therefore, they were taxable.
- Furthermore, the receipts from L&T, even though they were in connection with the production of mineral

oils, cannot be taxed under section 44BB of the Act as this was under a sub-contract.

The Authority for Advance Rulings (AAR) observed that in the case of IOCL, the contract was not only for installation work as only 25% of the receipts were received for it while the rest related to the use of the vessels to carry out the installation work. Even though it was a composite contract, IOCL was paying for each of the items separately.

In the case of Ishikawajma-Harima Heavy Industries Ltd *v.* DIT [2007] 288 ITR 408 (SC), it was held that where the consideration of each portion of the contract is separately specified, the receipts are independently taxable on the basis of the source and the nature of the receipt.

In the case of State of Madras *v.* Richardson & Cruddas Ltd [1968] 21 STC 245 (SC), it was held that the mobilisation and de-mobilisation expenses relate to the use of equipment for undertaking installation work. Hence, it is taxable as a royalty under Article 12(3)(b) of the tax treaty. As the installation was ancillary and subsidiary to the use of equipment and availing the right for such use, the payment for the installation was taxable as FTS under Article 12(4)(a) of the tax treaty.

Furthermore, as per the contract with L&T, the scope of work included various preparatory services such as surveys, drawings, engineering, etc. These services go beyond installation and include pre- and post-installation services. The duration of performing such preparatory activities cannot be excluded while calculating the duration of a PE in India under Article 5(5) of the tax treaty.

Since the activities of the applicant, including the preparatory services, extended beyond a period of 183 days, it constituted a PE in terms of the deeming provisions of Article 5(5) of the tax treaty and was liable to tax under section 44BB of the Act.

Global Industries Asia Pacific Pte Ltd *v.* DIT [TS-89-AAR-2012]

Consideration for sale of software applications through independent reseller in India taxable as royalty

The applicant company, incorporated in Japan, was a subsidiary of Acclerys, USA and was providing scientific informatics software and services.

It entered into an arrangement with an independent Indian company for the reselling its products (copyrighted software applications) in India. The reseller company withheld tax under section 195(1) of the Act on the consideration remitted to the applicant.

The applicant contended that the end-user was authorised only to have the benefit of data or modules of the copyrighted software on a non-exclusive and non-transferable basis. Therefore, payments received from independent resellers for any transfer of rights in copyrighted software would be taxable as business income under Article 7 of the India-Japan tax treaty. However, in the absence of the applicant having a PE in India, this business income would not be taxable in India.

The Revenue contended that the right to use the software given to end-users involved the right to use copyright applications. Hence, the consideration would constitute a royalty under Article 12 of the tax treaty.

The AAR observed that, in the case of Citrix Systems Asia Pacific Pvt Ltd, *In re* [TS-82-AAR-2012], it was held that there can be no use of copyrighted software without the use of copyright.

Therefore, the payment for the use of copyright can only be a royalty. Furthermore, it was held that the payment made by the seller on behalf of the end-user and the direct payment by the end-user both take the character of royalty.

Accordingly, the AAR held that the payment received by the applicant from the sale of software products to its end-users through its independent reseller in India would be taxable as royalty under Article 12 of the India-Japan tax treaty.

Acclerys KK, *In re* [TS-119-AAR-2012]

Tax withholding

No tax withholding on guarantee commission paid to a bank

The assessee, a company engaged in stock broking, is a member of the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE). It furnished bank guarantees in lieu of margin deposits to the BSE and NSE. The assessee paid certain charges to the bank as bank guarantee commission. During survey proceedings under section 133A of the Act, the TO noticed that the assessee had failed to withhold tax on the guarantee commission paid to the bank. The TO disallowed the commission paid and treated the assessee as an 'assessee-in-default' and levied interest under sections 201(1) and 201(1A) of the Act. The CIT(A) upheld the TO's order.

On further appeal, the Tribunal held that tax was not required to be withheld on the commission and brokerage paid to banks where a principal and agent relationship does not exist. This was an essential condition to invoke the provisions of section 194H of the Act. Hence, no tax was required to be withheld under section 194H of the Act.

The Tribunal observed that the context in which the expression 'commission' appears in section 194H of the Act, along with the expression 'brokerage', significantly restricts the additional meaning of both the terms. As per common parlance, the meaning of the expression 'commission' does not extend to the payment of fees for a product or service and it should be restricted to the payment in the nature of a reward for effecting sales or for business transactions.

Therefore, the Tribunal held that commission and brokerage are exclusive of each other and do not mean anything other than the normal meaning of the terms. Accordingly, the Tribunal held that the guarantee commission paid to the bank was not liable to withholding tax.

Kotak Securities Ltd *v.* DCIT [TS-62-ITAT-2012 (Mum)]

Tax withholding applicable on payment of export commission to non-resident agent

The applicant, an Indian company, manufactured and supplied rice par boilers and dryer plants. It received an export order from a non-resident company through its non-resident agents to whom it paid commission.

The applicant contended that the commission was paid to non-resident agents outside India for services rendered by them outside India. Hence, no income accrued to the agents in India under the provisions of section 5(2)(b) read with section 9(1) of the Act. Accordingly, the agents were not liable to tax in India. Hence, the assessee was not required to withhold tax under section 195 of the Act on the payment of export commission.

The Revenue contended that the income accrued to the agents in India at a time when the right to receive such income became vested on execution of the order. Therefore, the export commission was liable to be taxed in India requiring the assessee to withhold tax on such commission under section 195 of the Act.

The AAR relied on its decision in the case of Rajiv Malhotra *In re* [2006] 284 ITR 564 (AAR) where it was held that if the source of income is situated in India, the non-resident agent was liable to tax in India.

In the applicant's case, though the agents rendered services and solicited orders abroad, the right to receive commission accrued in India only upon execution of the order by the applicant in India.

Accordingly, the AAR ruled that the export commission payable to non-resident agents would be income deemed to have accrued or arisen in India and would be taxable under section 5(2)(b) read with section 9(1)(i) of the Act. Therefore, the applicant was required to withhold tax on the export commission under section 195 of the Act.

SKF Boilers and Driers Pvt Ltd, *In re* [2012-TII-08-ARA-INTL]

Capital gain or loss

Loss on transfer of non-convertible portion of partly convertible debentures not speculative in nature

The assessee held shares in Tube Investments of India Ltd (the company). The company came out with an issue of partly convertible debentures (PCDs) for its

existing shareholders. The face value of each PCD worth INR 100 consisted of two parts: a convertible portion of INR 50 consisting of an equity share of INR 10 issued at a premium of INR 40 and a non-convertible portion of INR 50 having a coupon rate of 15% per annum redeemable at par on maturity.

Under an arrangement, the Hongkong Bank agreed to purchase the non-convertible portion of debentures at a discount upon allotment. On the date of allotment, the bank cancelled the loan given to the assessee and based on the authorisation given by the assessee the company directly transferred the non-convertible portion of debentures to the bank. In the process, the assessee incurred a loss on the non-convertible portion of the debentures which it claimed as capital loss in the return filed for AY 1993-94.

The TO treated the loss as speculative under section 43(5) of the Act as there was no actual delivery of the non-convertible portion of debentures. The CIT(A) also upheld the order of the TO. On appeal to the Tribunal, it held that there was an element of constructive delivery of the non-convertible portion of debentures to the assessee followed by constructive delivery in favour of the bank by the assessee. Hence, it was a case of capital loss and not speculative loss.

On further appeal, the HC observed that the expression 'speculative transaction' under section 43(5) of the Act covers shares, commodities and stocks. A non-convertible portion of debenture is neither a share nor a commodity or a stock, and hence, it is not a speculative transaction under section 43(5) of the Act. Accordingly, the loss on the non-convertible portion of PCD would be treated as capital loss and not speculative loss.

CIT *v.* New Ambadi Estates Pvt Ltd [TS-141-HC-2012 (Mad)]

Carry forward or set-off

Loss of an eligible unit under section 10B can be set-off against profit of non-eligible units

The assessee company was eligible to claim deduction under section 10B of the Act for its 100% export-oriented unit (EOU). For the relevant AY, the EOU incurred a loss on account of current depreciation which was set-off against the profit of non-eligible units.

The TO held that the eligible unit was independently entitled to claim deduction under section 10B of the Act. Therefore, the loss of the eligible unit cannot be set-off against the profit of non-eligible units. The CIT(A) confirmed the TO's order. The Tribunal reversed the CIT(A)'s order.

The HC observed that in the case of Hindustan Lever Ltd *v.* DCIT [2010] 325 ITR 102 (Bom), it was held that the original provisions of section 10B of the Act which were introduced by the Finance Act, 1988 w.e.f. 1 April 1989 provided for an 'exemption' i.e., the profits and gains derived by the assessee from EOU were to be excluded from the assessee's total income. However, the provisions of section 10B of the Act were substituted by the Finance Act, 2000 by providing a 'deduction' of the profits derived by the EOU from the assessee's total income. Therefore, the AO's contention was not sustainable.

Furthermore, section 70 of the Act provides for the setting-off of loss from one source of income against any other source under the same head of income. Section 10B of the Act does not prohibit setting-off loss from one source under the head of profit and gains of business against income from any other source under the same head of income.

Also, under section 80-IA(5) of the Act, profits and gains of a business eligible under section 80-IA(1) of the Act are to determine the quantum of deduction to be computed if such eligible business is the only source of income of the assessee for the initial AY and every subsequent AY. However, a similar provision was not introduced by the legislature at the time of enactment of section 10B of the Act. The fact that unabsorbed depreciation can be carried forward to a subsequent year will not prohibit the assessee from setting-off loss of an eligible unit against the income arising from other units under the same head of profits and gains of business or profession.

Hence, in the absence of any statutory prohibition the assessee would be entitled

to set-off the loss of eligible units against the profits of non-eligible units in terms of the provisions of section 70 of the Act.

CIT *v.* Galaxy Surfactants Ltd [2012-TIOL-142-HC-MUM-IT]

Capital loss arising on sale of shares as per statutory direction is allowed to be carried forward

The assessee, a non-banking finance company (NBFC), was engaged in the business of hire purchase financing and leasing of commercial vehicles. During the year, a notification was issued by the Reserve Bank of India directing NBFCs to discontinue activities not related to its core business. Accordingly, the assessee was compelled to divest shares held by it as investment to its group concern and the resulting loss was carried forward.

The TO rejected the claim of the assessee on the ground that the sale was made to its group concern and not through the stock exchange. Furthermore, the TO declined the carry forward of loss as the basis of arriving at the sale value was not furnished. On appeal, the assessee contended that most of the shares were not quoted on the stock exchange and there were no ready buyers. The assessee further contended that the genuineness of sale of shares was not questioned by the TO. The CIT(A) allowed the assessee's appeal.

On further appeal, the Tribunal observed that the shares were not quoted on a stock exchange. Hence, the price had to be fixed by mutual agreement. It further observed that the TO had not doubted the genuineness of the transaction. The Tribunal had ruled favourably in the assessee's own case in preceding years. The Tribunal held that the TO had not provided an alternate computation and a commercial transaction could not be ignored and had to be dealt with as per law even if they were between two entities belonging to the same group. Thus, the Tribunal allowed the capital loss to be carried forward arising on sale of shares.

ACIT *v*. Shriram Transport Finance Co Ltd [2011] 9 ITR 543 (Chennai)

Share brokers eligible for bad debts claim on unrecovered balance of share transactions carried on behalf of clients

The assessee, a share broker, submitted its return of income claiming a deduction of INR 2.82 million on account of bad debts, representing amounts receivable from clients on transactions in shares effected on their behalf.

The TO disallowed the deduction holding that the business in respect of which the debts had arisen ceased to exist in the year under consideration and also on the ground that no action was taken against the clients to recover the amount due. However, the CIT(A) and the Tribunal held in favour of the assessee.

On appeal by the Revenue, it was contended that since the assessee had credited only the amount of the brokerage to the profit and loss account, the conditions stipulated in section 36(2) of the Act were not satisfied and the assessee was not entitled to claim deduction in respect of the bad debts under section 36(1)(vii) of the Act.

The Bombay HC, relying on the judgments of the SC in the cases of TRF Ltd *v*. CIT [2010] 323 ITR 397 (SC), CIT *v.* T Veerabhadra Rao [1985] 155 ITR 152 (SC) and of the Delhi HC in the case of CIT *v.* Bonanza Portfolio Ltd [209] 320 ITR 178 (Delhi), held that the value of shares transacted by the assessee as a stock broker on behalf of clients is as much a part of debt as is the brokerage charged by the assessee on the transactions. As the brokerage had been credited to the profit and loss account of the assessee, it was evident that a part of the debt was taken into account while computing the income of the assessee. The requirements of section 36(2)(i) of the Act were fulfilled and, accordingly, the assessee was entitled to deduction of bad debts under section 36(1)(vii) of the Act.

CIT *v.* Shri Shreyas S Morakhia [TS-134-HC-2012 (Bom)]

Lease equalisation charges

No disallowance where lease equalisation charges accounted under generally accepted accounting principles

The assessee company claimed deduction of lease equalisation charges (LEC)

for AYs 1996-97 to 2000-01 which were accounted as per the guidance note (GN) issued by the Institute of Chartered Accountants of India (ICAI).

The TO disallowed the LEC on the ground that it was merely a provision made to determine the profitability of the assessee's business and cannot be claimed as a deduction. The CIT(A) confirmed the TO's order. The Tribunal reversed the CIT(A)'s order.

The HC held that the lease equalisation charge is a method of adjusting the difference between the lease rentals and the depreciation claimed by the assessee. This method results in squaring-off the lease equalisation charges over the term of the lease period, thereby reflecting the true and correct picture of business profitability.

Even though accounting standard (AS) 19 for leases issued by the ICAI was applicable from 1 April 2001, the GN for the same was applicable prior to 1 April 2001 i.e., for the relevant AYs.

The LEC were accounted based on the GN issued by the ICAI which is a recognised authority vested with the powers of issuing ASs for the presentation of financial statements. These GNs reflect the best practices adopted by accountants globally.

The proviso to section 211(3C) of the Companies Act, 1956 (the Companies Act) specifies that until such time the central government prescribes, the AS issued by the ICAI will be deemed to be the relevant AS. Therefore, the method followed by the assessee reflected a true and fair view of the accounts which is a statutory requirement under section 211(2) of the Companies Act. Hence, the LEC were eligible for deduction.

CIT *v*. Virtual Soft Systems Ltd [2012-TIOL-189-HC-DEL-IT]

Swap loss

Swap cost on account of exchange rate difference not a deductible loss

The assessee, a foreign bank, received an FCNR deposit of INR 0.25 million on 14 January 2000, which was converted into Indian rupees by selling it in the open market at INR 43.565 per dollar. On the same day, the assessee entered into a forward contract to buy (on 29 December 2000) an equal number of dollars at INR 45.165 per dollar. The difference between the rates of INR 43.565 and INR 45.165, when multiplied with US$ 0.25 million, resulted in a loss of INR 0.4 million for the period of 14 January 2000 to 29 December 2000. Of the total loss, on a pro-rata basis from 14 January 2000 to 31 March 2000, INR 0.085 million was claimed by the assessee as swap cost in financial year (FY) 1999-2000.

In support of its claim, the assessee relied on the Special Bench decision of the Mumbai Tribunal in the case of DCIT *v.* Bank of Bahrain and Kuwait [2010] 41 SOT 290 (Mumbai), where it was held that when a forward contract is entered into by an assessee to buy or sell foreign currency at an agreed price at a future date falling beyond the last date of the accounting period, the loss incurred by the assessee on account of evaluation of the contract on the last date of the relevant accounting period, i.e. before the date of the maturity of the forward contract, is allowable as a deduction.

The Tribunal expressed its inability to appreciate how the ratio of the Special Bench order in the case of Bank of Bahrain and Kuwait applied to the facts of the instant case. Adverting to the facts of the case, in the view of the Tribunal, there was no relation between the transaction of the assessee receiving a foreign currency non-resident deposit of US$ 0.25 million and converting it into Indian rupees, with the transaction of entering into a forward contract. The Tribunal stated that both these transactions were independent of each other. It was further observed that there is absolutely no basis to determine the loss by considering the rate at which the assessee converted US$ on receipt of the deposit with that for which it entered into an agreement at a future date. The Tribunal rejected the assessee's claim for deduction of the swap cost.

Siam Commercial Bank PCL *v.* DDIT [2012] 134 ITD 463 (Mum)

Assessing personal tax

Personal taxes

Salary or perquisite

Notification

Exemption to specified persons from furnishing tax return for AY 2012-13

As per the recent notification issued by the central government, individuals whose total income for the AY 2012-13 does not exceed INR 0.5 million and consists of only income chargeable to income-tax under the heads of income of salaries and income from other sources, by way of interest from a savings bank account not exceeding INR 10,000, have been exempted from furnishing a return of income under section 139(1) of the Act, subject to the fulfillment of specified conditions.

The conditions include the discharge of tax liability through taxes withheld by the employer. The assessee would therefore have income from only one employer and no refund is due to the assessee.

However, this exemption from filing tax is not available where a tax return is required to be filed in pursuance of a notice issued under section 142(1) or section 148 or section 153A or section 153C of the Act.

Notification no 9/2012 [F. no.225/283/2011-ITA(II)] dated 17 February 2012

Case laws

Carry forward and set-off of business losses only allowed to a person who has actually incurred it

In a recent decision, the Delhi HC held that section 78(2) of the Act only provides for the carry-forward and setting-off of business losses in the hands of a person other than the person who has actually incurred the loss in the event of a change in constitution of a firm or upon succession. Under no other circumstance is the setting-off of such a business loss allowed to a person who has not actually incurred such a loss.

The assessee, an individual, took over the running of the business of a partnership firm. He was a partner in the firm prior to its dissolution. He filed his tax return for AY 2005-06 by setting-off the loss of INR 2,240,193 suffered by the partnership firm (constituted by the assessee and his brother) in accordance with section 78(2) of the Act. Upon dissolution (18 September 2004), the assessee took over the fixed and current assets and current liabilities.

The assessee's claim of setting-off the business losses incurred by the partnership firm against the income generated by carrying on the business as a sole proprietor was denied by the lower appellate authorities. Aggrieved by the findings, the assessee approached the HC where he relied on section 78(2) of the Act and the SC rulings in the cases of CIT *v.* Madhukant M Mehta [2001] 247 ITR 805 (SC) and Saroj Aggarwal *v.* CIT [1985] 156 ITR 497 (SC).

The HC held that the assessee's case was not a case of succession by inheritance as the partnership firm ceased to exist upon dissolution. Furthermore, he continued the business of the partnership firm in the capacity of a sole proprietor which is separate and distinct from the partnership firm. Also, through the application of section 170(1) of the Act, a partnership firm was assessable to income from 1 April 2004 to the date of dissolution and the assessee from the date after dissolution until 31 March 2005. Since there is no contradiction between sections 78(2) and 170(1) of the Act as both cover different situations, the assessee's appeal was dismissed.

Pramod Mittal *v.* CIT [2012-TIOL-149-HC-DEL-IT]

Property held with an intention to let out is not taxable

In a recent decision, the Bangalore Tribunal held that where a property is held during the relevant tax year with an intention to let it out and efforts are made by the assessee to let it out, such property will be considered as 'let out property' and its annual letting value (ALV) will be worked out in accordance with the provisions of section 23(1)(c) of the Act.

The assessee, a non-resident individual, filed her income tax return for AY 2007-08. Out of the total taxable income of INR 5.52 million, income reported from house properties was INR 2.03 million. In the tax return, the assessee disclosed rental income from eight house properties of which four were let out properties, one a self-occupied property and three properties with ALV as 'NIL'. The tax return was processed under section 143(1) of the Act but was later selected for detailed scrutiny by serving notice under section 143(2) of the Act.

During the course of the assessment proceedings, for three house properties whose ALV was shown as 'NIL' in the tax return, the assessee submitted that the house property located at Eldarado, Mumbai, was old and not in a habitable condition because of which it could not be let out during AY 2007-08. No tenant could be found for the property located at Vastu Apartments, Mumbai, despite her best efforts and the property located at Andheri East, Mumbai, was acquired during the AY 2007-08 and was lying vacant during the year. The TO, in the absence of evidence to support her contention, computed the notional rent at 70% of the rent received against these properties in the AY 2008-09. On appeal, the CIT(A) confirmed the order of the TO.

Aggrieved, the assessee filed an appeal to the Tribunal placing reliance on the decision in the case of Indu Chandra *v.* DCIT (ITA No. 96 /Lkw/2011, order dated 29 April 2011). In this case, the Tribunal had set aside the order of the CIT(A) and interpreted the words as 'property is let' in clause (c) of section 23(1) of the Act and held that these expressions do not refer only to actually let out but also an intention to let out. If the property is retained by the owner for letting out and efforts are made to let it out, then that property is covered by the provisions of section 23(1)(c) of the Act. Where, despite having made continuous efforts to let out the property, no tenant could be found and rent received or receivable from the property was 'NIL', the ALV of the property should be considered as 'NIL' in order to compute the income from house property', and the assessee's appeal was allowed.

Shakuntala Devi *v.* DDIT [TS-753-ITAT-2011 (Bang)]

Case laws

Minimum alternative tax not applicable to amalgamation reserve created out of the profit-and-loss account

Pursuant to a scheme of amalgamation of two subsidiaries into the assessee company, the work in progress of amalgamating companies was recorded at market value and the excess of assets over liabilities taken over on amalgamation was credited to the general reserve.

The TO added the reserve on amalgamation for computing book profits under section 115JB of the Act, contending that as per explanation 1(b) to section 115JB of the Act, any amount carried to the reserves, regardless of its name, has to be added back.

The assessee contended that only reserves created out of the profits can be adjusted for computing book profits. A notional increase by way of revaluation of work-in-progress cannot be considered.

The Tribunal relied on the SC ruling in the case of the National Hydroelectric Power Corporation Ltd *v.* CIT [2010] 320 ITR 374 (SC) where it was held that for adding reserves for computing book profits under section 115JB of the Act, both of the following two conditions need to be satisfied:

- Such an amount should be debited to the profit and loss account.
- The amount debited should be carried to the reserves.

The Tribunal observed that since the amalgamation reserve was created as per Accounting Standard 14 and not out of the profits, no addition on that account can be made to compute book profits under section 115JB of the Act. Thus, the Tribunal decided the matter in favour of the assessee.

ITO *v.* United Estates Pvt Ltd [TS-68-ITAT-2012 (Mum)]

Transfer of tenancy rights not liable to deemed valuation under stamp duty regulations

The assessee (along with another person) had acquired leasehold rights in a residential property in FY 1992 for 99 years. In FY 2007, the owner, the lessees and the purchasers entered into a registered tripartite sale deed, following which the owner and the lessees transferred all the rights and interest in the property to the purchasers.

The TO noted that the stamp duty valuation of the property was greater than the stated sales consideration. Accordingly, the TO invoked the provisions of section 50C of the Act and adopted the stamp duty valuation as the sales consideration and notionally divided the amount against the owner and the lessees in the ratio in which the actual consideration was divided. Aggrieved, the assessee filed an appeal before the CIT(A), who decided the matter in favour of the assessee.

The case was then referred to the Tribunal, which observed that the consideration for the transfer of tenancy rights cannot be treated as consideration for ownership rights merely because payment was made upon sale of the property. To apply section 50C of the Act, the transfer must be of a capital asset, being land or building or both. Hence, section 50C of the Act cannot be invoked where tenancy rights in a land or building are transferred.

Hence, the Tribunal also ruled in favour of the assessee.

DCIT *v.* Tejinder Singh [2012-TIOL-147-ITAT-KOL]

Transfer of shares by enforcing non-compete agreement taxable as capital gains

During the year, a Dutch company acquired all the shares held by the assessee in Mandhana Bornemann, pursuant to a share purchase agreement. Although the agreement provided a non-compete clause, no separate consideration was provided for it.

The assessee treated the entire gains on the sale of shares as capital gains. The TO, however, allocated a part of the consideration towards non-compete fees liable to tax as business income under section 28(va) of the Act. The CIT(A) upheld the action of the TO, but reduced the amount attributed to non-compete fees.

The Tribunal noted that the assessee was not actively engaged in business but was a shareholder in the company carrying on the business. The Tribunal held that section 28(va) of the Act would apply where the assessee was carrying on business and not where the assessee only had a right to carry on the business in the form of a capital asset. Thus, the Tribunal held that the amount attributable to non-compete fees was taxable as capital gains. Since the assessee had already offered the entire gains as capital gains, it was not necessary to divide the consideration into parts attributable to the sale of shares and non-compete fees. The Tribunal relied on the decision in the case of Hami Aspi Balsara *v.* ACIT [2010] 126 ITD 100 (Mum).

ACIT *v.* Savita N Mandhana [TS-593-ITAT-2011 (Mum)]

Waiver of right to acquire shares against capital advances taxable as capital gains

The assessee had made certain advances to a company, KPCL, and further to an agreement had the right to convert the advances into KPCL's equity shares. During the previous year, the assessee received compensation for foregoing its right to convert these advances into shares.

The TO treated the compensation as short-term capital gains and not as a capital receipt, as claimed by the assessee.

The CIT(A) held that the compensation is taxable as income from other sources.

The Tribunal observed that the assessee, further to the agreements entered into with a third party, received its advances back along with interest and also agreed to waive its right to convert the advances into shares for a consideration of INR 100 million.

The Tribunal held that the expression 'property of any kind' used in section 2(14) of the Act is wide in scope. Thus, the right to convert advances into shares is a capital asset under section 2(14) of the Act. The Tribunal also held that since the assessee relinquished the right to acquire shares, this would constitute a 'transfer' under section 2(47) of the Act.

The Tribunal held that the SC decision in CIT *v.* B C Srinivasa Setty [1981] 128 ITR 294 (SC), relied upon by the assessee, is not applicable to the case, since the assessee acquired the right in consideration of the advances given to KPCL from time to time. Therefore, it could not be said that the cost of acquisition was unascertainable.

The Tribunal concluded that the entire amount of INR 100 million was to be taxed as capital gains, which would then be computed as long-term or short-term on a pro-rata basis depending upon the investment and advances made by the assessee.

DCIT *v.* Natco Pharma Ltd [TS-122-ITAT-2012 (Coch)]

Pricing appropriately
Transfer pricing

Case laws

Important transfer-pricing principles on characterisation and rewards for overseas selling activity upheld

The assessee, a global software solutions provider, was engaged in providing offshore and onsite solutions to clients. The assessee operated through overseas subsidiaries in various countries. The assessee's subsidiary in the UK acted as a distributor for the software solutions of the assessee and earned a return on sales. In the transfer pricing (TP) documentation, the assessee selected its UK subsidiary as a tested party and benchmarked the return on sales with comparable distributors. During the course of the assessment proceedings, the TPO re-characterised the UK subsidiary as solely a marketing service provider by stating that the subsidiary did not bear any inventory, foreign exchange or profit risk. Based on this, the TPO proposed a TP adjustment which was upheld by the DRP. Aggrieved, the assessee appealed before the Tribunal.

The Tribunal ruled as follows:

- The agreements between the parties based on commercial expediency cannot be disregarded without assigning a cogent reason, unless the agreement was not genuine.
- The subsidiary in the UK was not merely a front-end entity but was in a position to negotiate with customers and handle the scope and timing of deliverables and assumed credit and market risk. Consequently, it acted as a distributor rather than a marketing service provider.
- Furthermore, the return-on-sales agreement created an incentive for the subsidiary to generate more revenue. Such an agreement was necessary since the assessee generated a significant share of revenue in the UK.
- The distributors were not always required to have a fluctuating percentage of profit. A fixed percentage would still lead to fluctuating absolute profits based on sales generated.
- Relying on the UK HMRC Guidance, the Tribunal concluded that the distributors would need to be compensated on a return-on-sales basis and not on a cost-plus basis.
- The OECD TP guidelines emphasise functional similarities over product similarities. Thus, the assessee's comparability analysis identifying comparable distributors of software products was appropriate.
- The assessee had no incentive to shift the tax burden to the UK by resorting to the return-on-sales methodology when it actually enjoyed a tax holiday in India.
- In relation to the interest charged by the TPO on late recoveries from associated enterprises (AEs), the Tribunal recognised that after taking into account the commercial considerations and market practice, there was no justification to charge interest from AEs.
- On the secondement of employees by the assessee, the TPO had held that the secondement was a recruitment service for which the assessee should earn a fee. The Tribunal held that it was in the assessee's business interest to second the employees and a negative inference cannot be drawn merely because the AEs benefitted as long as benefits were derived by the assessee.

Mastek Ltd *v.* ACIT [TS-127-ITAT-2012 (Ahd)]

Editor's note: The PwC Litigation team assisted in this case.

Admission of additional evidence filed by the assessee upheld

The assessee was providing a range of services, including R&D, IT support, corporate shared support (back office support) and global sourcing, to its affiliates. In order to justify the arm's length basis for its international transactions,

the assessee had applied the transactional net margin method (TNMM) using operating profit or operating costs as the profit-level indicator (PLI). During the course of the assessment proceedings, the TPO rejected the use of multiple-year data and proposed to compute the operating mark-up of comparable companies with contemporaneous financial data of FY 2003-04. In relation to the IT support services, the TPO rejected the comparables selected by the assessee and introduced a new set of comparables, thereby proposing an adjustment to the transfer price of the assessee. The TPO rejected the comparables, citing reasons such as insufficient financial data, functional differences, absence of foreign exchange revenues, persistent loss-making, ceased or inactive business operations and substantial related-party transactions. Aggrieved, the assessee filed an appeal before the CIT(A). The CIT(A) re-determined the adjustment determined by the TPO. The assessee then filed an appeal before the Tribunal.

On appeal, the Tribunal ruled as follows:

- Relying on the decision in the case of Genisys Integrating Systems (I) Pvt Ltd, the Tribunal directed the TO to decide whether the case was applicable to the facts of the assessee. Based on the applicability of the Tribunal ruling, the comparables would then stand to be rejected or retained.
- The issue of standard deduction of 5% was covered as per the orders of the Tribunal, namely, Genisys Integrating Systems (I) Pvt Ltd [2011-TII-96-ITAT-BANG-TP], SAP Labs India Pvt Ltd v. ACIT [2010-TII-44-ITAT-BANG-TP] and Philips Software Centre Pvt Ltd v. ACIT [2008-TIOL-471-ITAT-BANG], and MSS India Pvt Ltd [2009-TII-07-ITAT-PUNE-TP].
- On the assessee's petition for filing the additional evidence for the exclusion of two of the companies as comparables, the Tribunal held that the documents furnished by the assessee were vital and had to be admitted in the interest of natural justice. The TO was directed to examine the documents.

The case was remitted back to the file of the AO.

Timken Engineering and Research India Pvt Ltd *v.* DCIT [TS-131-ITAT-2012 (Bang)]

Editor's note: This case was argued by the PwC Litigation team.

Adjustments to be made to comparables and not tested party under the transactional net margin method

The assessee was primarily a supplier of telecommunications equipment as well as a provider of telecommunications solutions to customers in India. The assessee had benchmarked its international transactions adopting TNMM as the most appropriate method. During the course of the assessment proceedings, the TPO accepted the assessee's transaction of receipt of technical services and the provision of manpower hiring and other services to be at arm's length. However, with respect to the transaction of the import of finished goods, the TPO rejected the PLI of adjusted profit to sales adopted by the assessee and recomputed the margins of the comparable companies using the ratio of operating profit to operating revenue as the PLI, thereby proposing an adjustment to the transfer price of the assessee. On appeal before the CIT(A), the assessee was granted adjustment on account of the start-up costs. A certain percentage of the start-up expenses were considered as extraordinary expenses and thus excluded for the computation of operating margin. As the assessee's transfer price was within the +/-5% range, the transaction was held to be at arm's length. Aggrieved, the

revenue authorities filed an appeal with the Tribunal.

On appeal, the Tribunal ruled as follows, upholding the contentions of the revenue authorities:

- The uncontrolled transaction or comparables selected should not have any material differences from the tested party. If material differences exist, the comparables should be rejected.
- Furthermore, if there are differences, then only 'reasonable accurate adjustments' can be made to eliminate differences, Rule 10(B)(3) of Income-tax Rules, 1962 (Rules) mentions the comparables and does not provide scope for adjustments to the assessee or the tested party.
- The order of the CIT(A) was a non-speaking order as it did not provide reasons for making adjustments to the operating results of the assessee. The CIT(A) also failed to provide reasons for considering a certain percentage of the assessee's expenses as extraordinary.
- The assessee had also not claimed any adjustment on account of specified expenses in the TP study.

Based on the above, the Tribunal remitted the case back to the CIT(A) for fresh adjudication.

DCIT *v.* Marconi Telecommunication India Pvt Ltd [TS-92-ITAT-2012 (Del)]

Taxing of goods and services
Indirect taxes

VAT, sales tax, entry tax and professional tax

Case law

Sale of goods to inbound and outbound passengers by duty-free shops at international airport not liable to sales tax

The SC has held that sales by duty-free shops in international airports both to inbound and outbound passengers were made before or after the goods had crossed the customs frontiers of India. Consequently, these sales were not liable to sales tax since they qualify as a sale in the course of import or export covered by section 5 of the Central Sales Tax Act, 1956.

Hotel Ashoka *v.* Assistant Commissioner of Commercial Taxes & Anr. [2012] VIL 03 (SC)

Reimbursement of the cost of parts to dealers in lieu of warranty arrangement between manufacturer and customer liable to sales tax

The Bombay HC has held that the transactions involving free-of-cost (FOC) replacement of spare parts under the warranty arrangement where the cost of such spare parts are subsequently reimbursed by the manufacturer by issue of credit note, are covered by the definition of sales, and hence liable to sales tax.

Navnit Motors Pvt Ltd *v.* State of Maharashtra [2012] 47 VST 511 (Bom.)

Notification

Input tax credit on declared goods on account of stock transfer reduced from 50 to 40% in Delhi

Input tax credit on declared goods on account of stock transfer has been reduced from 50 to 40% of the tax paid on the purchase of such goods.

Notification no. F.3 (23)/Fin (Rev-I)/ 2011-12/DSIII/68 dated 27 January 2012

CENVAT

Case law

CENVAT credit on capital goods used in captive power plant admissible, even if only a part of the electric power used in the manufacture of the dutiable final product

The Chhattisgarh HC has held that Central Value Added Tax (CENVAT) credit on capital goods used in captive power plant is admissible, even if the major portion of the electric power is sold by the assessee and only a part of it is used in the manufacture of the dutiable final product.

UOI *v.* HEG Ltd. [2012] 275 E.L.T. 316 (Chatt)

Supplementary invoice raised on account of a price variation clause to attract interest liability from the original date of clearance of goods

The Mumbai Custom Excise and Service Tax Appellate Tribunal (CESTAT) has held that a supplementary invoice raised on account of a price variation clause will attract interest liability from the original date of clearance of the goods.

Gammon India Ltd *v.* CCE (A) [2012] 275 E.L.T. 442 (CESTAT - Mum)

Notification

Area-based exemptions in Himachal Pradesh and Uttarakhand not affected by change in ownership

The Central Board of Excise and Customs (CBEC) has clarified that area-based exemptions in Himachal Pradesh and Uttarakhand will continue even after the transfer of ownership of the factory to a new owner.

Circular no. 960/03/2012-CX dated 17 February 2012

Service tax

Case law

The term 'business' in section 65(105) to cover all services undertaken as occupation regardless of profit

The Punjab and Haryana HC has held that for tax statutes, the expression 'business' need not necessarily imply a profit element and will cover all services undertaken as a matter of occupation.

Punjab Ex-Servicemen Corporation *v.* UOI [2012] 25 S.T.R. 122 (P&H)

Customs and foreign trade policy

Case law

Royalty and license fee, not related to imported goods, not includible in the value of imported goods

The Mumbai CESTAT has held that the royalty and license fee is not includible in the value of the imported goods in case the royalty and license fee is related to goods manufactured in India and not to imported goods.

CC *v.* Bridgestone India Pvt. Ltd. [2012-TIOL-166-CESTAT-MUM]

No bar of unjust enrichment on duty refunds relating to short landing of goods

The Ahmedabad CESTAT has held that unjust enrichment is not applicable on duty refunds relating to short landing of goods; hence, the refund of duty should be given to the importer and not transferred to the Consumer Welfare Fund.

Petronet LNG Ltd. *v.* CC [2012] 275 ELT 568 (CESTAT – Ahd)

Customs duty benefit under advance licence cannot be denied where inputs not utilised as per the notified norms

The Mumbai HC has held that custom duty benefits available under an advance licence cannot be denied to the exporters in case the inputs have not been utilised as per the norms notified under the foreign trade policy on account of advancements in technology.

Arkema Catalyst India Pvt. Ltd. *v.* UOI [2012] 276 E.L.T. 206 (Mum.)

Customs duty benefits cannot be extended where goods cleared to a Domestic Tariff Area unit are not similar to exported goods

The Chennai CESTAT has held that the benefits of concessional customs duty cannot be extended on goods cleared from a 100% Export Oriented Unit (EOU) to the Domestic Tariff Area (DTA), in case goods cleared to the DTA are not similar to the goods exported by the 100% EOU.

Abi Turnamatics *v.* CCE [2012-TIOL-228-CESTAT-MAD]

Notification

Instruction issued for strict compliance with the guidelines issued for time-bound clearance of goods from ports, land customs stations and ICDs

The central government has instructed the customs authorities to strictly follow the guidelines regarding time-bound clearance of goods from ports, land customs stations and inland container depots (ICDs) as directed by the SC. Furthermore, the customs authorities must intimate the importer or exporter to keep the goods in the warehouse, in case clearance is not possible due to any unavoidable reason.

F. No. 450/160/2011-STO dated 13 February 2012

Goods covered under FTA, if sold on high seas, entitled to FTA benefit

The Mumbai Commissionerate has clarified that goods covered under the free trade agreement (FTA), if sold on high seas, should be entitled to FTA benefits, subject to the fulfilment of the conditions provided under the relevant FTA.

Standing order no. 06/2012 dated 20 February 2012

Following the rulebook
Regulatory developments

FEMA

Liberalisation and rationalisation in overseas direct investment (ODI)

A. By Indian party

1.1 Investment modes

The RBI allows an Indian party (i.e. a company incorporated in India, a body created under an Act of Parliament or a partnership firm registered under the Indian Partnership Act, 1932) to invest in a foreign entity directly outside India by way of contribution to the capital or subscription to the Memorandum of Association or purchase of existing shares either through a market purchase, private placement or stock exchange.

The RBI has now permitted Indian parties to invest in a joint venture (JV) or wholly owned subsidiary (WOS) set up outside India through the modes in the table.

	Modes of investment	Conditions prescribed
1	Compulsorily convertible preference share (CCPS)	• CCPS would be treated at par with equity shares
2	Creation of charge in the form of pledge, mortgage or hypothecation on the immovable or movable property and other financial assets of the Indian party and its group companies within the overall limit of 400% of net worth	• Approval of RBI will be required • No objection certificate will be required to be submitted by the Indian party and its group companies from their Indian lenders
3	Bank guarantee issued by a resident bank on behalf of overseas JV or WOS of the Indian party, which is backed by a counter guarantee or collateral by the Indian party	• Bank guarantee must be reckoned for the computation of the financial commitment of the Indian party
4	Issuance of personal guarantee by the indirect resident individual promoters of the Indian party will be allowed under general permission	• Personal guarantee by the indirect resident individual promoter shall be subject to stipulations applicable to the personal guarantee extended by the direct promoters
5	Financial commitment (loan or guarantee) without equity contribution	• Approval of the RBI will be required • Laws of the host country permit incorporation of a company without equity participation by the Indian party

A.P. (DIR Series) circular no. 96 dated 28 March 2012

1.2 Annual Performance Report (APR)

In cases where the law of the host country does not require the auditing of books of account of the JV or WOS, the APR may now be submitted by the Indian party based on the un-audited annual accounts of the JV or WOS provided the following conditions are satisfied:

- The statutory auditors of the Indian party certify that the unaudited annual accounts of the JV or WOS reflect the true and fair picture of the affairs of the JV/WOS.
- The unaudited annual accounts of the JV or WOS have been adopted and ratified by the board of the Indian party.

A.P. (DIR Series) circular no. 96 dated 28 March 2012

1.3 Foreign currency account for the purpose of overseas direct investment

The RBI has now permitted the Indian party to open a foreign currency account (FCA) abroad for the purpose of making overseas direct investments (ODI) subject to the following conditions:

- The host country regulations stipulate that the investments into the country are required to be routed through a designated account.
- The FCA shall be opened, held and maintained as per the regulations of the host country.
- The remittances sent to the FCA by the Indian party should be utilized only for making overseas direct investments into the J or WOS abroad.
- Any amount received in the account by way of dividends

and/or other entitlements from the subsidiary shall be repatriated to India within 30 days from the date of credit.

- The Indian party shall submit the details of debits and credits in the FCA on a yearly basis to the designated authorised dealer (AD) bank with a certificate from the statutory auditors of the Indian party certifying that the FCA was maintained as per the host country laws and the extant FEMA regulations and provisions as applicable.

The FCA opened would need to be closed within 30 days from the date of disinvestment from the JV or WOS or its cessation.

A.P. (DIR Series) circular no. 101 dated 2 April 2012

B. By resident individuals

The RBI has decided to liberalise the guidelines for outbound investments by resident individuals as below:

- Acquiring shares of a foreign company towards professional services or in lieu of director's remuneration is now permitted under the automatic route.
- The cap of 1% of the paid up capital of the foreign company for acquisition of qualification shares is now removed. The resident individual can now acquire qualification shares up to the limit prescribed by the law of the host country.
- The RBI has done away with the condition requiring the foreign company to hold a 51% equity stake directly or indirectly in the Indian company, to enable the resident individual to acquire shares under the Employee Stock Ownership Plan (ESOP) scheme which is offered by the foreign company globally on a uniform basis.

A.P. (DIR Series) circular no. 97 dated 28 March 2012

Liberalisation for Authorised Dealers Category-II

A. Issue of foreign currency prepaid travel cards

- In addition to Authorised Dealer Category - I banks, Authorised Dealers Category-II are now permitted to issue foreign currency prepaid cards to residents travelling on private or business visits abroad, subject to adherence of KYC/AML/CFT requirements.

However, settlement in respect of these cards may be effected through the AD Category-I banks.

B. Opening of nostro account

- Authorised Dealers Category-II are now permitted to open nostro accounts subject to the following conditions:
  - One nostro account for each currency can be opened.
  - Balances in the account can be utilized only for the settlement of remittances sent for permissible purposes and not for the settlement in respect of foreign currency prepaid cards.
  - No idle balance shall be maintained in the account.
  - The accounts will be subject to reporting requirements as prescribed from time to time.

A.P. (Dir Series) circular no. 104 dated 4 April 2012

Overseas borrowing: Revision of all-in-cost ceilings

In November 2011, the all-in-cost ceilings for external commercial borrowings (ECB) and trade credits were revised upwards as besides:

Instrument	Maturity period	All-in-cost over six month LIBOR*
ECB	Three years and up to five years	350 basis points (bps)
	More than five years	500 bps
Trade credit	Up to one year	350 bps
	More than one year and up to three years	

(* for the respective currency of credit or applicable benchmark)

These ceilings were subject to review on 31 March 2012. Upon review, the RBI has decided to continue with the above ceilings for six more months i.e. up to 30 September 2012.

A.P. (Dir Series) circular no. 99 and 100 dated 30 March 2012

NRE/FCNR(B) account: Permissible credit and repayment of loan

The AD Category-I banks are now permitted to credit the repayment of loans taken by individual residents in India from their close relatives outside India, to the non-resident external (NRE) or foreign currency non-resident (Bank) [FCNR(B)] account of the lender concerned subject to the following conditions:

- The loan to the resident individual must have been extended by way of inward remittance in foreign exchange through normal banking channels or by debit to the NRE/FCNR(B) account of the lender.
- The lender must be eligible to open a NRE/FCNR(B) account.

A.P. (Dir Series) circular no. 95 dated 21 March 2012

Prepaid travel cards: Immediate redemption of unutilised balance

The issuers of foreign currency prepaid travel cards are now directed to immediately redeem (when requested by the card holder) the unutilised balance in the cards, subject to retention of:

- the amounts that are authorised and remain unclaimed or not settled by the acquirers as of the date of redemption until the completion of the respective settlement cycle
- a small balance not exceeding 100 USD, for meeting any pipeline transactions until completion of the respective settlement cycle, and
- transaction fees or service tax payable in India in rupees.

A.P. (Dir Series) circular no. 102 dated 2 April 2012

Export of goods: Discontinuation of sale of hard copies of GR Forms

Given the increase in Internet access by the general public, the RBI has decided to discontinue supplying and selling printed exchange control declaration (GR) forms across the counter at its regional offices. Effective 1 July 2012, GR forms shall be available only online at the RBI website.

A.P. (Dir Series) circular no. 98 dated 30 March 2012

Financial services

Amendments to the valuation of debt and money market instruments and advertisement norms

SEBI has directed mutual funds and asset management companies (AMCs) to compute and carry out the valuation of investment made by its schemes in accordance with investments valuation norms provided by the SEBI (Mutual Funds) Regulations, 1996.

Furthermore, as per the SEBI circular dated 2 February 2010, floating rate securities with floor and caps on coupon rates and residual maturity of up to 91 days were to be valued on an amortisation basis taking the coupon rate as the floor.

SEBI had mandated mutual funds and AMCs to value debt and money market securities with a residual maturity of up to 91 days at the weighted average price at which they are traded on the particular valuation day.

As per the circular, the above-mentioned period of 91 days has been changed to 60 days. Therefore, this clarification would be applicable to floating rate securities with maturity periods of up to 60 days. This amendment will be effective from 30 September 2012.

Furthermore, SEBI has mandated certain disclosure requirements for the AMCs in relation to debt and money market securities transacted (including inter-scheme transfers) in its schemes portfolio, as per the specified format.

Additionally, SEBI has prescribed certain revised norms for advertisement to be followed by the mutual funds.

SEBI circular – CIR/IMD/DF/6/2012 dated 28 February 2012

Due diligence of distributors and clarification on conflict of interest

The SEBI has clarified that due diligence of distributors is the responsibility of the mutual funds and AMCs and these cannot be outsourced. However, a mutual fund or AMC can take the assistance of an agency of repute while carrying out the due diligence.

As per the earlier amended SEBI (Mutual Funds) Regulations, 1996, it was mandated that the AMCs should appoint separately a fund manager for each fund managed by them unless the investment objectives and assets allocations are the same and the portfolio is replicated across all the funds managed by the fund manager.

However, SEBI has decided that replication of a minimum of 70% of the portfolio value will be considered adequate for having a common fund manager across all the funds managed. However, the AMC should have in place a written policy for trade allocation and the fund manager should not take opposite positions in the different schemes managed by him.

The circular also provides for additional disclosure requirements to be followed by AMCs.

SEBI circular – CIR/IMD/DF/7/2012 dated 28 February 2012

Guidelines issued on implementation of provisions of Foreign Contribution (Regulation) Act, 2010

The RBI has issued certain guidelines on the Foreign Contribution (Regulation) Act, 2010 and Foreign Contribution (Regulation) Rules, 2011.

The Act prohibits certain classes of persons from receiving foreign contributions. It also restricts certain classes of persons from accepting foreign hospitality while visiting any country or territory outside India, without the prior permission of the central government.

The key features are:

- The Act casts certain obligations on banks in relation to the receipt of foreign contributions.
- It mandates registration for the acceptance of foreign contributions.
- It also prohibits or restricts the receipt, transfer and utilisation of foreign contributions.
- The foreign contribution is to be received through a scheduled bank.

RBI circular – RBI/2011-12/388 dated 6 February 2012

SEBI - Informal guidelines

Share transfer among promoters amounts to equity sale

Company S was listed on the BSE and NSE. The promoter group entities had executed certain *inter se* transfers of shares (in accordance with the Securities Exchange Board of India (SEBI) takeover code). There had been no change in the combined promoter shareholding further to the above *inter se* transfers.

Provisions of regulation 72(2) of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009

'The issuer shall not make preferential issue of specified securities to any person who has sold any equity shares of the issuer during the six months preceding the relevant date.'

Query

Guidance was sought on whether shares transferred pursuant to *inter se* transfer will be considered as a 'sale' under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.

Guidance

The SEBI held that any transfer of shares, even within the promoter group of a company, will be considered as an equity sale. Thus, the promoters of a listed company will not be eligible for preferential allotment of shares or warrants if there has been any *inter se* transfer of shares among the promoter group in the preceding six months.

Informal guidance dated 14 February 2012 sought by Strides Arcolab Ltd

Guidelines on offer for sale through stock exchange mechanism amended

The SEBI has amended the guidelines on offer for sale through stock exchange and clarified the following:

- Cumulative orders and bid quantity information will be made available online by the exchanges at specific time intervals.
- The indicative price will be disclosed by the exchanges only during the last half an hour of the duration of the offer for sale. This indicative price will reflect the volume-weighted average price of all the bids that have exhausted the quantity offered.

Furthermore, the SEBI has also clarified that the content of the advertisement for sale will be the same as the content of the notice sent to the stock exchanges.

SEBI circular no. CIR/MRD/DP/ 7/2012 dated 23 February 2012 and circular no. CIR/MRD/DP/ 8 /2012 dated 27 February 2012

Glossary

AAR	Authority for Advance Ruling
AEs	Associated enterprises
ALP	Arm’s length price
AY	Assessment year
CENVAT	Central value added tax
CESTAT	Customs, Excise and Service Tax Appellate Tribunal
CIT(A)	Commissioner of Income-tax (Appeals)
Companies Act	The Companies Act, 1956
DRP	Dispute Resolution Panel
FTS	Fees for technical services
FY	Financial year
HC	High Court
PE	Permanent establishment
RBI	The Reserve Bank of India
SC	Supreme Court
SEBI	The Securities and Exchange Board of India
The Act	The Income-tax Act, 1961
The Rules	The Income-tax Rules, 1962
The tax treaty	Double Taxation Avoidance Agreement
The Tribunal	The Income-tax Appellate Tribunal
TNMM	Transactional Net Margin Method
TO	Tax officer
TP	Transfer pricing
TPO	Transfer Pricing Officer

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