Editorial

We wish you a happy and prosperous 2011.

The new year begins with a positive outlook as the Indian economy witnessed a robust growth of 8.9% in the three months to September. The better than expected growth in GDP has raised hopes of the economy returning to 9% plus growth rates sooner than expected, possibly in the current fiscal. Industrial growth has bounced back into double digits to 10.8% in October after a gap of three months. Also, inflation eased in November to its lowest level in 2010. There is room for fiscal tightening and withdrawal of fiscal stimulus in the economy. We are clearly also subject to the uncertainty and volatility in the global arena including volatility in oil prices and the fiscal strain in several countries in Europe.

India has seen, in the recent past, visits by the world leaders from the United States, the United Kingdom, France, China and Russia. The leading nations now look to India, the booming Asian giant, for business opportunities.

The Reserve Bank of India has not revised key policy rates in its mid-quarter review of monetary policy, which was in line with general expectations. However, it has cut statutory liquidity ratio by 100 basis points. The Reserve Bank of India has released (on December 23) gist of the comments on the discussion paper on “Entry of new banks in the private sector”.

As reported in the press, the Ministry of Finance has taken a view that the International Financial Reporting Standards need to be adopted only while consolidating accounts of corporate groups as is the practice in Europe. It believes that the proposed fair-value-based accounting regime cannot be enforced on a stand-alone basis to individual companies as has been recommended by the Institute of Chartered Accountants of India and the Ministry of Corporate Affairs.

On the indirect tax front, with a fresh round of discussions between the Centre and the States, and a lack of consensus, it appears to be a challenge for the Government to roll out the Goods and Services tax in the next financial year.

There has been a spate of important decisions on taxation matters. Recently, the Mumbai bench of the Income-tax Appellate Tribunal (the “Tribunal”), in the case of DHL Express (India) Pvt. Ltd., held that application for stay of demand arising out of the assessment order passed by the tax officer in pursuance to the direction of the Dispute Resolution Panel (DRP) under section 144C of the Income-tax Act, 1961 is maintainable before the Tribunal even without making an application to the lower authorities. Filing of stay applications before lower authorities is directory, and not mandatory, for filing stay applications before the Tribunal. Also, the Delhi Bench of the Tribunal has taken
a negative view of cryptic orders passed by the DRP upholding the transfer pricing adjustments proposed by the TPO; the Tribunal has accordingly set aside the order of the DRP, in the case of GAP International Sourcing India Pvt. Ltd.

The past year has witnessed several noteworthy tax decisions and regulatory developments. We have analysed these in our annual publications “PwC Tax Glimpses – 2010” and “PwC Noteworthy Developments - 2010”. These will provide a snapshot of some significant landmark rulings and regulatory developments during the year.

We trust you will enjoy reading this India Spectrum. We would, as always, very much appreciate your feedback.

Ketan Dalal & Shyamal Mukherjee
Joint Leaders-TRS Practice

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Glossary

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Do mail your feedback at pwctrs.knowledgemanagement@in.pwc.com and we shall be pleased to respond
Case laws

Assessment proceedings

Interest on refund allowable for refund arising out of self-assessment tax paid

The assessee company, a tax resident of Mauritius, filed a revised return of income for the relevant assessment year ("AY"). The assessee had tax disputes which went up to the Income-tax Appellate Tribunal ("Tribunal") allowed relief to the assessee, while giving effect to the order of the Tribunal, the Tax Officer ("TO") granted refund arising on account of self-assessment tax, however, did not allow the interest under section 244A of the Act, it is clear that the payment of self-assessment tax is covered by clause (b) of section 244A of the Act. In this regard, the Tribunal followed the decisions in the cases of ACIT v. Grindwell Norton Ltd. [2006-TIOL-102-ITAT-MUM] and CIT v. Cholamandalam Investment & Finance Co. Ltd. [2007-TIOL-339-HC-MAD-IT]. Furthermore, it also referred to the Board Circular No. 549 dated 31 October, 1989, wherein it was stated that if the refund was out of any tax, other than advance tax or tax deducted at source or penalty, interest should be payable for the period starting from the date of payment of such tax or penalty and ending on the date of grant of refund.

ADIT v. Asia Today Ltd. [2010-TII-168-ITAT-MUM-INTL]

Business Expenses

Mutual Fund expenses borne by the Asset Management Company are allowable expenses

The assessee, a company engaged in the business of Asset Management, incurred certain mutual fund scheme related expenses. The expenses were charged to the mutual fund schemes in accordance with the limits prescribed under the Securities and Exchange Board of India ("SEBI") Mutual Fund Regulations. Expenditure in excess of the limits was borne by the assessee. The TO disallowed such excess amount by holding that the same was in contravention of law and hence, not allowable as business expenditure. On appeal, following the ratio of the Bombay High Court ("HC") in the case of DSP Merrill Lynch Investments Managers Ltd. ITA No. 1286 of 2008 dated 10 December, 2008 and referring to the observation of the Tribunal in ACIT v. DSP Merrill Lynch Investments Managers Ltd. [2007] 15 SOT 639 (Mum), the CIT(A) held that the expenditure that cannot be charged to the mutual fund scheme and has a direct nexus with the assessee’s business becomes the expenditure of the assessee; and allowed the expenditure. The Tribunal reiterated that since the expenditure incurred is for the purpose of assessee’s business and since there is nothing on record to suggest that the assessee had in any manner violated the Rules or Regulations set out by the said regulatory authority, the expenditure cannot be disallowed in assessee’s hands. It is not the case of the TO that the expenditure has no connection with assessee’s business and thus concluded in favour of the assessee.
**Business Income**

**Difference between market value and face value of shares held as pledge is not an income**

The assessee gave an interest-free loan of INR 500 million to Reliance Communication and Infrastructure Ltd. ("RCIL"). This loan was given against the pledge of 500 million equity shares of face value INR 1 of Reliance Infocom Ltd. ("RIC") owned by RCIL. RCIL transferred the shares of INR 500 million, offered as security, to the assessee's demat account. The TO held that the assessee acquired the shares of RIC in order to have control and management of RIC. Therefore, the shares of RIC were acquired at face value of INR 1 although the market value was INR 53.71 per share. Accordingly, the difference between the market value of the shares and the value at which the shares were purchased by the assessee was considered as the income of the assessee under section 2(24)(iv) of the Act.

The CIT(A) held that the transaction was in the nature of a pledge and not a case of sale of shares. In this regard, it observed that the assessee had returned the shares to RCIL on discharge of the loan and had also complied with the provisions of the Companies Act, 1956 ("Companies Act").

The Tribunal upon interpretation of the provisions of the Companies Act, SEBI regulations, Depositories Act, etc., and analysis of the concept of dematerialisation of shares upheld the order of the CIT(A) and held that,

- There was no transfer of 500 million shares of RIC held by RCIL to the assessee by way of sale and that the transfer was only by way of delivery of possession of shares as security for repayment of a loan provided to RCIL by the assessee.
- The assessee did not have absolute right over the shares held as a pledge. He could have sold the security in a manner contemplated by law. However, if the proceeds had been greater than the amount due to him, he would have had to pay the surplus to the pawnor. Consequently, the assessee would not have derived any benefit or perquisite, the value of which could have been brought to tax under section 2(24)(iv) of the Act.

**Capital or Revenue Expenditure**

**Lumpsum consideration paid for music rights is revenue in nature**

The assessee was engaged in the business of manufacturing and trading of pre-recorded music cassettes and compact discs. It had made original sound track ("OST") royalty payment for the songs and had claimed it as revenue in nature. The TO, following its order in the previous year, disallowed the claim. The CIT(A) was of the view that the lump sum payment included future benefits and the royalty amount paid was to be amortised over a period of five years. Dissatisfied with the order of the CIT(A), the assessee appealed before the Tribunal.

The Tribunal held that in earlier years, it had decided the same issue in the favour of the assessee on the ground that it was important for the nature of the business carried on by the assessee to have assignment of copyright, for making legal copies of the music and selling the same. Thus, in such a line of service, copyright acquired should be considered as revenue expenditure and not as capital expenditure. Accordingly, the Tribunal, in the absence of any contrary material brought on record, relied upon its earlier decision and held that the assessee was eligible to claim the expenses as revenue expenses.

**Sony Music Entertainment I P Ltd. v. ACIT [2010-TIOL-671-ITAT-MUM]**

**Capital Gains**

**No Taxability arises upon entering into a joint development agreement**

The assessee, a land owner, converted his land into stock-in-trade and entered into a Joint Development Agreement ("JDA") with a developer. Pursuant to the JDA, the assessee provided his land to the developer for development and in return, the assessee was entitled to a part of the constructed property. During subsequent years, the assessee sold the property and offered the income/loss to tax in the year of sale of the built-up property.

The TO was of the view that the long-term capital gains on transfer of land were assessable in the year in which the assessee handed over the possession of
the land to the developer pursuant to the JDA. On appeal, the CIT(A) upheld the order of the TO.

On further appeal, the Tribunal accepted the assessee’s contention and held that taxability in the case of conversion of capital asset to stock-in-trade arises only in the year in which the stock-in-trade is sold by the assessee. In the current context, the taxability arises only in the year in which the constructed property was sold by the assessee to ultimate buyers and not in the year of the JDA. It was further held that, since the development of the property was for residential purposes, when it was constructed as a residential building, the claim under section 54F of the Act should be allowed. The Tribunal rejected the TO’s contention that the assessee had not purchased or constructed a residential building as it was built by the developer under the JDA and therefore no exemption under section 54F of the Act should be allowed.

R Gopinath (HUF) v. ACIT [2009] 133 TTJ 595 (Chennai ITAT)

**Royalty**

**Right to make copies of software for programme operation within own business is not royalty**

The assessee company had purchased software for multiple users from a Singapore company. By purchasing the software, the assessee obtained a right to make copies of the programme to enable operation of the programme within its own business and no source code or programming language or technique would be provided with the software. As provided in section 195(2) of the Act, the assessee requested the TO to issue a certificate of nil withholding tax. The revenue contended that withholding tax was deductible on the payment made to the Singapore company as it was made towards ‘royalty’. The assessee contended that the payment in the hands of the foreign company was not taxable in India, either under the Income tax Act or under the Tax Treaty with Singapore since the seller had no permanent establishment (“PE”) in India. The assessee further contended that it had paid for purchase of goods, and therefore, it was not liable to withholding tax.

The Tribunal, by relying on the decisions in the cases of Tata Consultancy Services v. State of Andhra Pradesh [2004] 271 ITR 401 (SC), Samsung Electronics Co. Ltd. v. ITO [2005] 94 ITD 91 (Bangalore), Motorola Inc. v. DCIT [2005] 95 ITD 269 (Delhi) and Dassault Systems K.K., In re [2010] 322 ITR 125 (AAR), held that a computer software when put into a media and sold becomes goods like any other audio cassette or painting on a canvas or a book. The amount paid by the assessee towards the purchase of software for multiple users cannot be treated as towards payment of royalty taxable in India under Article 12 of the India-Singapore tax treaty. Therefore, the assessee would not be liable to withhold tax on the payment made to the Singapore company.

Kansai Nerolac Paints Ltd. v. ADIT [2010-TII-155-ITAT-MUM-INTL]
Case laws

While calculating the value of perquisite of accommodation, the amount of house rent allowance withheld from the employee is to be reduced

In a recent decision, the Mumbai bench of the Tribunal held that an employee would not lose the benefit of house rent allowance (“HRA”) merely because it has leased its premises to the employer company. The amount of HRA withheld should be treated as the amount recovered by the employer when computing perquisite value of rent-free accommodation.

Brief facts of the case are that BPCL introduced a self lease scheme under which employees owning house property were given an option of leasing it to the company. The company paid lease rent to the employees for the flats leased out and also reimbursed the share of maintenance charges. On verification of the returns, the TO noticed that many employees did not disclose the lease rent and maintenance charges received during the year in their tax returns. The TO issued notice under section 148 of the Act to such employees. The assessee did not disclose complete receipt of lease rentals even in the tax return filed in response to the notice. The TO taxed the lease rent income as income from house property and maintenance charges as income from other sources and also initiated penalty proceedings under section 271(1)(c) of the Act for concealment of income.

Before the CIT(A), the assessee submitted that on joining the self lease scheme, the employees had to forgo the HRA and were entitled to receive lease rent which was approximately 30% of the basic salary. However, while calculating the value of perquisites, the company failed to reduce the amount of HRA foregone by the employees and did not consider it as recovery of rent. The assessee also contended that the mistake of not disclosing lease rent and maintenance charges was bona fide as it was the responsibility of the employer to deduct the taxes on lease rent paid. The CIT(A) confirmed the action of the TO and also held that it is the responsibility of the assessee and not of the employer to disclose the correct income in the tax return to be filed.

The Tribunal held that the leasing of the flat by the employee to the corporation is a separate transaction. The lease rent received by the employee is taxed separately. The employee does not lose the benefit of HRA by leasing out their premises to their employer. The company withheld the HRA in lieu of the lease rent payable by the employee for the accommodation provided by the company. Therefore, in computing the value of perquisite for accommodation provided by the company, the HRA withheld should be treated as the amount recovered by the employer for providing accommodation. The TO was directed to rework the assessment in accordance with law.

Mrs Manghal Gaonkar v. ITO
[2010-TIOL-653-ITAT-Mum]

In computation of perquisite value of accommodation, HRA withheld from the employee to be reduced as rent paid
Withdrawal from provident fund by International Workers permissible only after retirement

Notifications/Circulars

For International Workers, withdrawal from provident fund permissible only after retirement

Under the Employee’s Provident Fund (Third Amendment) Scheme, 2008 and the Employee’s Pension (Third Amendment) Scheme, 2008, the Ministry of Labour and Employment of the Government of India (“MLE”) made it mandatory for international workers (“IW”) to contribute to the Indian social security. The Ministry has recently announced amendments under the Employees Provident Fund (Amendment) Scheme, 2010 and the Employee’s Pension (Amendment) Scheme, 2010, to provide that withdrawal will now be permitted on the retirement of the IW from the establishment after attaining the age of 58 years. In certain specified circumstances, an earlier withdrawal may be possible. The amended scheme also provides that where an IW is covered under a social security agreement (“SSA”), the payment of Provident Fund (“PF”) and pension is to be complied with in the manner specified in the SSA.

FAQs on Project Visas

The MLE has issued FAQs on Project Visas which are issued to foreign nationals coming to India for execution of projects. The Project Visa currently covers only the Power and Steel sector. Foreign nationals desiring to come to India on Project Visas have to make applications in the prescribed form.

Source: http://mha.nic.in

Clarifications with regard to Employment Visa Guidelines

The MLE issued Frequently Asked Questions (“FAQs”) on the granting of employment visas which provided a minimum salary limit of USD 25,000 per annum for the granting of an employment visa. Further clarifications have been issued specifying that the salary limit of USD 25,000 per annum includes salary and all other allowances paid to the foreign national in cash. Any perquisite received in kind is not included in this threshold limit. This salary threshold limit is applicable for the employment visas issued after 1 November, 2010. All foreign nationals who are already on an employment visa issued prior to 1 November, 2010 and drawing less than the minimum threshold limit of USD 25,000 p.a. may be allowed to continue in their present employment until the expiry of their present visa period.

Source: http://mha.nic.in
Depreciation on goodwill on purchase of business allowed if amount is paid for ensuring retention and continuity of business

The assessee purchased a hospital with its land, building, equipments, staff, name, trademark and goodwill on a going concern basis. The assessee claimed tax depreciation on goodwill arising on such purchase.

The TO held that “goodwill” was not covered by section 32(1)(ii) of the Act, and accordingly, denied claim of depreciation on goodwill. The HC observed that:

- The hospital was run in the same building and same name for several years prior to purchase
- All facilities and name continued to remain the same even after such purchase, to ensure continuity of the business with same reputation
- Purchase of hospital as a going concern with its name and trademark was nothing but acquisition of goodwill earned by the hospital, and thus, cannot be termed anything other than a commercial or a business right.

Thus, the HC held that goodwill was paid to ensure retention and continued business in the hospital. It was certainly for acquiring business and commercial rights and was comparable with trademark, franchise, copyrights, etc. referred to in section 32(1)(ii) of the Act, and thus, the assessee was entitled to claim tax depreciation on the same.

\[\text{B Raveendran Pillai v. CIT [2010] 194 Taxmann 477 (Kerala)}\]

Mergers and Acquisitions

Depreciation on goodwill on purchase of business allowable as deduction

The assessee company sold 99.75% shares of its subsidiary, VST Natural Products Ltd (“VST-NPL”), to Gujarat Gas Company Ltd. (“GGCL”) and claimed long-term capital loss. The supplemental agreement specified transfer of all assets and liabilities of VST-NPL to the purchaser.

The TO denied the loss on sale of shares to the assessee since the loss on sale of investments was nothing but a loss of capital invested in the subsidiary company. The CIT(A) held that the transaction was nothing but a slump sale, and thus, directed the TO to recompute the capital gains under section 50B of the Act.

The Tribunal, after going through the agreement, held that though the assessee transferred shares, it actually transferred the entire undertaking i.e. VST-NPL to GGCL by selling all the assets and liabilities of VST-NPL as a group. The Tribunal further held that various stipulations stated in the agreement made it clear that the parties intended to sell the subsidiary as an undertaking with all its assets, liabilities, licenses, permits, approvals, registration, contracts, employees, contingent liabilities, etc. for a lumpsum consideration. Accordingly, on the facts of the case, the Tribunal held that the transaction was squarely covered as a slump sale in terms of the provisions of section 50B of the Act.

\[\text{VST Industries Ltd. v. ACIT [2010] 41 SOT 415 (Hyderabad)}\]
Transfer of shares to a group company at prevailing market rate, to reduce taxable income, cannot be dubbed as a colourable device to evade taxes

The assessee transferred investment in shares of a company to a group company at its market value, which admittedly reduced its taxable income. The Tribunal reversed the order of the CIT(A) by holding that the transaction was genuine and was undertaken at the prevailing market rate. The Tribunal relied on the Supreme Court (“SC”) judgment in the case of Union of India v. Azadi Bachao Andolan (2003) 263 ITR 706 and Mcdowell & Co Ltd v. CTO (1985) 154 ITR 148.

On further appeal, the HC observed that a similar issue was considered in the case of Porrits and Spencer (Asia) Ltd. v. CIT (ITA No. 10 of 2004 decided on 31 March, 2010) where it was held that once the transaction is found genuine, then it cannot be dubbed as a colorable device. The HC further held that if a legally valid transaction forms part of tax planning, it cannot be ignored merely because it resulted in reduction of tax liability of the assessee. A tax payer will be within its right to resort to a device to divert the income before it arrives to him and the effectiveness of such a device would not depend upon considerations of morality. Accordingly, the HC decided in favour of the assessee.

CIT v. Pivot Finance Ltd. [2010] 236 CTR 111 (P&H)

Corporate Law

High Court has power to change appointed date if statutory proceedings are initiated after the end of the accounting year

A scheme of amalgamation of Shree Balaji Cinevision India Pvt. Ltd. with Balaji Electrical Insulators Pvt. Ltd was approved by the shareholders and creditors. The Official Liquidator and the Regional Director did not raise any objection to the scheme. The appointed date for the scheme was 1 April, 2008. The Board of Directors approved the scheme on 20 March, 2009 while application to Court under sections 391-394 of the Companies Act, for convening the meeting was filed in April 2009.

The HC, while approving the scheme, altered the appointed date to 1 April, 2009 from 1 April, 2008. It stated that while sanctioning the scheme, the Court had the power to alter/modify the scheme including modification/alteration of the appointed date.

The HC observed that if statutory proceedings for sanctioning the scheme are initiated after the end of a particular accounting year (2008-09 in this case) while the appointed date is the beginning of that accounting year (1 April, 2008), it may be a valid reason for the Court to consider that such a company has not approached the Court in good time seeking sanction of the proposed scheme.

The HC held that the relevant date would be the date of initiation of the statutory process i.e. convening of shareholders/creditors meeting by filing an application to the Court under sections 391-394 of the Companies Act, and thus, if the statutory process for convening the meeting was not initiated, the appointed date in the scheme should not be accepted beyond the date of beginning of such accounting year.

Shree Balaji Cinevision (India) Pvt. Ltd., In re [2010] 99 CLA 80 (Guj)
The sixth round of Transfer Pricing Assessments for financial year 2006-07 have come to a close with the Revenue Authorities being successful in raising a tax demand of INR 8 billion (approx). Now it is for the taxpayers who have had to face adjustments on their international transactions to take a decision as to whether to file objections against the adjustments before the Dispute Resolution Panel ("DRP") or to file an appeal before the CIT(A). Both these dispute resolution mechanisms have their own pros and cons. Although the DRP offers a fast-track resolution and the tax demand is deferred, it is binding on the revenue, and hence, unlikely to vary from the original assessment. A decision from the CIT(A), on the other hand, could take a longer time to be forthcoming. Hence, the taxpayers have to take a judicious decision on this matter.

Over the past month, we have observed a plethora of cases relating to transfer pricing disputes being adjudicated by the Tribunal across the country. In this communiqué, we present to you a summary of these decisions.

Case Laws

Non-value adding or pass-through costs, should not be included in the cost base while computing a return/mark-up on costs

The assessee, a wholly owned Indian subsidiary, was primarily engaged in the business of rendering advertising services to its Associated Enterprises ("AEs") against payment of commission. The assessee applied the Transactional Net Margin Method ("TNMM") to confirm the arm’s length pricing of its inter-company transactions and selected Operating Profit/Value added expenses ("OP/VAE") as the Profit Level Indicator ("PLI"). As part of its business of consultancy services relating to advertisement, the assessee also facilitated placement of such advertisements in print/electronic media. For this purpose, the assessee made payment to third parties like advertisement agencies, printing presses, etc. on behalf of its customers, namely the AEs and recovered the same from them. In its audited financial accounts, the assessee recognised the revenue on net basis, i.e., it recognised the commission received as ‘revenue’ and treated the ‘gross media spends’ passed on to the customers/AEs, as ‘pass-through costs’, thereby not including such third party costs in its profit and loss account and operating margin computation.

During the course of assessment proceedings, the TPO disregarded the net basis of accounting followed by the assessee in its financial statements and considered gross receipts/reimbursements of costs as operating in nature and TPO also held that the Operating Profit/Total Cost ("TC") should be taken as the PLI, where TC included the cost of placing advertisements on behalf of the AE’s which were reimbursed by the AEs to the assessee on actual basis. On comparing the revised OP/TC markup of the assessee with that of comparables on a full cost basis, the TPO made an upward adjustment to the Transfer Price of the assessee. Dissatisfied with the TPO’s order, the assessee appealed before the CIT(A). The CIT(A) agreed with the contentions of the assessee and rejected the TPO’s action of computing the assessee’s profitability
at gross level and reversed the adjustment made by the TPO.

On appeal, the Tribunal held that:
- The net basis of accounting followed by the assessee was accepted and also agreed that in the assessee’s case, mark-up was to be applied on the cost incurred by the assessee in performing the agency functions and not on the gross media spends.
- The assessee facilitated the placement of advertisements for its customers/AEs and was not engaged in the business of selling advertising slots to the customers/AEs.
- It was also noted that the advertising space was let out by third party vendors directly in the names of the customers/AEs, who finalised the terms of advertising.
- The Tribunal endorsed the OECD’s view that while applying TNMM, the costs to be considered should be the costs incurred in relation to the value added activity i.e., the costs relating to the agency function in the instant case. The pass-through costs ought not to be marked up.

The Tribunal, upholding the order of the CIT(A), decided the case in favour of the assessee.

**Argued by PwC Tax Litigation Team**

DGIT v. Cheil Communications India Pvt. Ltd. [2010-TII-60-ITAT-DEL-TP]

Legally binding agreements cannot be disregarded without assigning cogent reasons

The assessee was engaged in the manufacture of car seat belts in technical collaboration with a Japanese collaborator. The assessee imported completely knocked down kits (“CKD”) from the collaborator, then assembled the CKD kits, adding indigenous raw material to manufacture the finished products which were then sold to third party car manufacturers. The assembly and manufacturing activity was carried out on the basis of technical know-how provided by the collaborator. In the course of transfer pricing assessment proceedings before the TPO, the assessee provided an internal comparability analysis comparing the gross profit margins earned from the sale of car seat belts manufactured from the kits supplied by the Collaborator (“controlled transaction”) vis-a-vis the gross profit margin earned from the sale of car seat belts manufactured using third party raw materials supplies (“uncontrolled transaction”) to demonstrate that the purchase price paid by the assessee on the controlled transactions was at arm’s length.

The TPO however, did not agree with the calculations presented by the assessee and proposed an adjustment at the entity level for the transactions involving purchases of raw materials, royalty payment and technical know-how fees, contending that no transfer of technology and know-how had taken place, and the price of raw material has already factored in the cost of technology and know-how. Dissatisfied with the TPO order, the assessee filed an appeal before the CIT(A). The CIT(A), while retaining the adjustments made by the TO to the royalty and technical fee transactions, enhanced the transfer pricing adjustments for purchase of raw material, on the basis of updated financial data for comparable companies obtained by the TPO. Dissatisfied with this, the assessee filed an appeal before the Tribunal.

On appeal, the Tribunal held that:
- The joint venture agreement between the taxpayer and the collaborator was approved by the Reserve Bank of India (“RBI”) and other Regulatory bodies. Hence, legally binding agreements entered into between the parties, with a commercial objective, cannot be disregarded without assigning cogent reasons.
- The revenue authorities cannot intervene in the commercial needs and expediencies involved in an arrangement, the decisions on which should be left to the taxpayer.
- The assessee was correct in asserting that the import of machinery cannot by itself be considered sufficient for the taxpayer to be able to use the machinery, and that the technical know-how and assistance would be required for the use of machinery under normal circumstances. Hence, the payment towards technical know-how was justified.
- Transfer Pricing adjustments should be made only on the result of international transactions, and therefore, insisted on a clear segmentation of the results for domestic and international transactions.
- Relying on similar judgements, the best comparibility for a controlled transaction is the transaction of the tested party itself.

Accordingly, the Tribunal ruled in favour of the assessee and directed the TO to cancel the adjustment made to the taxpayer’s transfer prices.

Abhishek Auto Industries Ltd. v. DCIT [2010-TII-54-ITAT-DEL-TP]
Filing stay application before lower tax authorities is directory and not mandatory for filing stay application before the Tribunal.

The assessee, on receipt of the direction from the DRP and subsequently the TO’s order, filed an appeal before the Tribunal. The assessee also filed a stay application before the Tribunal requesting for stay against recovery of outstanding demand raised by the TO. However, the assessee had not approached the revenue authorities requesting for stay against the recovery of outstanding demand. The revenue, relying on the Mumbai Tribunal decision in the case of RPG Enterprises Ltd., insisted that the assessee ought to have approached the revenue authorities for grant of stay of the disputed demand, which would give the revenue an opportunity to study the case, gather necessary data and protect its interest, before approaching the Tribunal. Accordingly, the revenue contested that the assessee should be directed to pay forthwith the demand raised.

The Tribunal ruled in this matter as follows:

- The TO’s order had been framed in conformity with the directions of the DRP and therefore, the assessee had filed an appeal directly before the Tribunal.
- It was not mandatory on the part of the assessee to move an application before the revenue authorities for granting stay of outstanding demand. Such a requirement is directory and not mandatory.
- The Tribunal directed the assessee to pay around 20% of the outstanding demand and stayed the recovery of the balance demand until the disposal of the appeal, or for a period of six months form the date of order, whichever was earlier.

The Tribunal had granted an out-of-turn hearing of the appeal.

_Argued by PwC Tax Litigation Team_
DHL Express (India) P Ltd. v. ACIT [2010-TII-58-ITAT-MUM-TP]

Infosys Technologies cannot be compared with a captive software developer

The assessee was engaged in the business of providing contract software development services to its AE in the USA. During the course of assessment proceedings, the TPO introduced new comparables and arrived at a mark-up of 27.08%, thereby proposing an adjustment to the income of the assessee. Dissatisfied with the order of the TPO, the assessee filed its objections before the DRP. The DRP dropped one of the comparables proposed by the TPO and directed the TO to recompute the ALP at 25.6%.

On Appeal, the Tribunal agreed to the assessee’s argument of excluding Infosys from the TPO’s comparable set due to difference in risk profile, higher ad spend, owning of products, etc. (function, asset and risk criteria). The Tribunal did not comment on other high risk comparables as the assessee complied with the arm’s length after excluding Infosys.

_Argued by PwC Tax Litigation Team_
ITO v. Agnity India Technologies Pvt. Ltd. [ITA No. 3856(Del)/2010]
Sale of helium gas to Bombay high is taxable as inter-State sales

The Maharashtra Sales-tax Tribunal has held that sale of helium gas to Bombay high was an inter-state sale covered under section 3(a) of the Central Sales-tax Act, 1956, as although the Bombay high is situated beyond 12 nautical miles from the coast, it is nevertheless part of the Indian territory and also because there were no export of goods in such a situation.


Battery charger sold along with the mobile phone as a composite package was eligible to concessional rate of tax

The Punjab & Haryana HC has held that a battery charger sold along with the mobile phone as a composite package, and without any extra charge, was eligible to the concessional rate of tax under the entry description of mobile phones and parts thereof.


Process of purification and filtration of acid to make the product marketable would be covered by the definition of manufacture

The Mumbai HC has held that the incidental process of purification and filtration of acid to make the product marketable would be covered by the definition of manufacture under section 2(f) of the Central Excise Act, 1944 and would be subject to excise duty.

CCE v. Alok Enterprises [2010] 259 ELT 333 (Mum)

Provisions relating to reversal of input tax credit where goods have been sold at a price less than the purchase price in the state of Tamil Nadu have been introduced with retrospective effect

Provisions pertaining to reversal of input tax credit over and above the output tax, where goods have been sold at a price less than the purchase price, which were earlier introduced with effect from 19 August, 2010 have now been made applicable retrospectively with effect from 1 January, 2007.

Tamil Nadu Ordinance No. 7 of 2010 dated 29 October, 2010

Parties cannot be said to be related to each other merely for the reason that the entire production was sold to one company or the premises of the buyer were rented to the assessee

The Bangalore Cutoms, Excise and Service Tax Appellate Tribunal (“CESTAT”) has held that in the absence of any evidence, the parties to the transaction cannot
be said to be related to each other merely for the reason that the entire production was sold to one company or that the premises of the buyer was rented out to the assessee.

RAD-MRO Manufacturing Pvt. Ltd. v. CCE [2010] 258 ELT 235 (Bang)

No requirement of inclusion of sale proceeds of scrap in value if the duty has been discharged by job worker on the cost of material, plus job work charges

The Bangalore CESTAT has held that where the job worker has discharged the duty on the cost of materials plus job work charges, as in the Ujagar Print’s case, there was no further requirement of inclusion of the value of scrap arising during the process.

Campco Chocolate Factory v. CCE [2010] 258 ELT 273 (Bang.)

Service Tax

Case Law

Levy of service tax on equipment lease and hire-purchase transactions is constitutionally valid

The SC has held that “financial lease” and “hire-purchase” were services, and the levy of service tax on these transactions was within the powers of the Parliament, even though VAT was chargeable thereon as well.

Association of Leasing & Financial Service Companies v. UOI [2010-TIOL-87-SC-ST-LB]

Erection, commissioning and installation services under a composite contract for manufacture and supply not liable to service tax

The Ahmedabad CESTAT has held that where excise duty has already been paid on full value of the machinery, no service tax is to be paid on the erection, commissioning and installation services provided, as these services are incidental to the manufacture and sale of machinery.

Alidhara Texspin Engineers v. CCE&C [2010] 20 STR 315 (Ahm)

Additional requirements prescribed under CBEC circular not to be used to deny benefits under notifications

The Ahmedabad CESTAT has held that any additional requirements prescribed under a CBEC circular cannot be made the basis for denial of substantive rights accruing to an assessee under a notification.

CST v. Transformers & Rectifiers (India) Ltd. [2010-TIOL-1371-CESTAT-AHM]

Customs/Foreign Trade Policy

Case Law

Predominant function to be the basis of classification for goods performing composite functions

The SC has held that the predominant function test should be the basis of classification for imported goods which perform composite functions

Xerox India Ltd. v. CC [2010-TIOL-97-SC-CUS]

Post import reduction in the price cannot result in reduction of transaction value

The Ahmedabad Tribunal has held that post import reductions in the value, in terms of an addendum to the contract of sale, cannot result in a reduction in the transaction value.


Date of export order is the relevant date for determination of rate of customs duty

The Bombay HC has held that the date of determination of the rate of duty was the date on which the let export order was given and not the date on which the loading of goods for exportation was made.

Narayan Bandkar & Sons Pvt. Ltd. v. CC [2010] 259 ELT 362 (Bom)

Notification/Circulars

Imports from Brunei Darussalam have been notified for duty concessions under the India ASEAN Foreign Trade Agreement

The Central Government has notified Brunei Darussalam under the India ASEAN Foreign Trade Agreement (“FTA”). Goods imported from Brunei Darussalam with effect from 1 November, 2010, will be eligible for customs duty benefits under the terms of the FTA. Furthermore, the Central Government has also notified Brunei Darussalam under the Customs Tariff [Determination of Origin of Goods under the Preferential Trade Agreement between the Government of Member States of Association of Southeast Asian Nations (“ASEAN”) and the Republic of India] Rules, 2009.

Customs Notification No's 115/2010 dated 8 November, 2010 and 94/2010-NT dated 3 November, 2010
Easy Exit Scheme 2011

The Ministry of Corporate Affairs ("MCA") has re-launched the “Easy Exit Scheme, 2011” ("EES 2011") to enable defunct companies to be dissolved under a simple process. The EES 2011 would be effective from 1 January, 2011 till 31 January, 2011. The scheme is similar to the "Easy Exit Scheme, 2010" ("EES 2010").

The EES 2011 provides a good opportunity for defunct companies to be dissolved without going through the complex, and often time consuming, process of winding-up through a Court.

A “defunct company” has been defined to mean a company registered under the Companies Act and:
- has not carried out any business activity or operations since 1 April, 2008; and
- includes a company which has not raised its paid-up capital to the minimum paid-up capital requirement under the companies Act.

For this purpose, the defunct company is to make an application to the Registrar of Companies (“RoC”) along with an Affidavit (confirming that the company is defunct/inoperational) and an Indemnity Bond (against future liabilities). Both the Affidavit and the Indemnity Bond should be signed by all the directors of the company.

DNBS (PD) CC. No. 204 /03.05.002 / 2010-2011 dated 1 December, 2010
Source: www.mca.gov.in

Financial Sector

Payment of New Pension Scheme contribution in a single premium

New Pension Scheme ("NPS") subscribers will, henceforth, have the option to pay their yearly NPS subscriptions in a single installment as opposed to the stipulated minimum four installments in a year.
Source: www.pfrda.org.in

Submission of Balance Sheet and Profit & Loss account

In terms of Para 12 of Non-Banking Financial (Deposit Accepting) Companies Prudential Norms Directions, 2007 and Non-Banking Financial (Non-Deposit Accepting) Companies Prudential Norms Directions, 2007, the RBI has announced that all Non-Banking Financial Companies ("NBFCs") shall be required to finalise their balance sheet within a period of three months from the date to which it pertains.

DNBS (PD) CC. No. 204 /03.05.002 / 2010-2011 dated 1 December, 2010
Source: www.rbi.org

Yearly premium payment under the New Pension Scheme