Tax & Corporate law Bulletin

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MARCH 2011

From the Editor's Desk...
Dear Reader,
Greetings for the season.
New month, new challenges, new hopes, new goals…We hope you beat every challenge and achieve your goals for this month successfully.
Here are some of the updates regarding this month: Substitution of rule 28aa, Amendments in Rule 3-CENVAT Credit, CRAR (Capital to Risk Assets Ratio) requirements for NBFCS, RBI allows IRFs on 91-day Treasury Bills and read many more…
We eagerly await your feedback on the bulletin.
Yours truly,
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Table of contents

DIRECT TAX 3-5

RECENT JUDGEMENT

INDIRECT TAX 5-8

- SERVICE TAX
- CENTRAL EXCISE

CORPORATE LAWS 8-10

INTERNATIONAL TAXATION 10-13

POLICY WATCH 13-14

INDUSTRY WATCH & CORPORATE HIGHLIGHT 15

GLOSSARY 17

"Adapting swiftly to the global business environment"

DIRECT TAX

- **Section 43(5), Clause (I)(i) of Explanation to Clause (D) of Proviso of The Income-Tax Act, 1961– Speculative Transaction– Recognized Stock Exchange– Notified Recognized Stock Exchange**

Notification no. 12/2011 [F.NO. 142/20/2010-SO (TPL)], dated February 25th, 2011

The Central Government has notified the United Stock Exchange of India Limited as a recognized stock exchange for the purpose of the said clause with effect from the date of publication of this notification in the Official Gazette.

- **Section 143 of The Income-Tax Act, 1961 – Assessment – General –Processing of returns of A.Y. 2010-11 –Steps to clear backlog**

Instruction No. 2/2011F.NO.225/25/2010/ITA-II], dated February 9th, 2011.

The issue of processing of returns for Assessment. Year 2010-11 and giving credit for TDS has been considered by the Board. In order to clear the backlog of returns, the following decisions have been taken:-

a) In all returns (ITR-1 to ITR-6), where the difference between the TDS claim and matching TDS amount reported in AS-26 data does not exceed 1 lakh, the TDS claim may be accepted without verification.

b) Where there is zero TDS matching, TDS credit shall be allowed only after due verification. However, in case of returns of ITR-1 and ITR-2, credit may be allowed in full, even if there is zero matching, if the total TDS claimed is five thousand or lower.

c) Where there are TDS claims with invalid TAN, TDS credit for such claims is not to be allowed.

d) In all other cases TDS credit shall be allowed after due verification.

- **Order under Section 119(2)(B) Regarding Extension Of Time Limit For Filing ITR-V Forms For A.Y. 2010-11**

Order [F.No. 225/25/2010/ITA-II], dated February 10th, 2011

The CBDT has extended the time limit for filing ITR-V forms relating to income-tax returns for A.Y. 2010-11 filed electronically (without digital signature) on or after 1st April, 2010. These ITR-V forms can now be filed up to 31st July, 2011 or within a period of 120 days from the date of uploading of the electronic return data, whichever is later. These directions issued to mitigate the hardship and grievances of the tax payers who have been prevented by reasonable causes to file the ITRV.

- **Certificate for deduction at lower rate or no deduction of tax from income other than dividend–Substitution of rule 28aa and form 13 in appendix ii and amendment in rule 31a**

The CBDT vide notification No. 16/2011 dated 29th March, 2011 gives the Income Tax (Second Amendment) Rule, 2011. It substitutes rule 28AA by

Prescribing new procedure for certificate of deduction at lower rate or no deduction of tax from income other than dividend. It also substitutes Form 13 being application by person for a certificate under section 197 and / or section 206C (9) of the Income-Tax Act for no deduction / collection of tax or deduction / collection of tax at a lower rate.

It also amends Rule 31A inserting clause Nos. (v) and (vi) prescribing to furnish the particulars of amount paid / credited on which tax was not deducted in view of the issue of certificate under section 197 / 194C (6) of the Income-Tax Act. The amendment came into force from April 1st, 2011.

➢ Section 268A of the Income-Tax Act, 1961 – revision of monetary limits for filing of appeals by the department before income tax appellate tribunal, high courts and supreme court– measures for reducing litigation

Instruction No. 3/2011 [F.NO.279/MISC. 142/2007-ITJ], dated February 9th, 2011

Appeals shall not be filed by the Department in cases where the tax effect does not exceed the monetary limits given here under:-

Sr. No.	Appeals in Income-tax matters	Monetary Limit (In ₹)
1	Appeal before Appellate Tribunal	3,00,000
2	Appeal u/s 260A before High Court	10,00,000
3	Appeal before Supreme Court	25,00,000

It is also clarified that an appeal should not be filed merely because the tax effect in a case exceeds the monetary limits prescribed above. Filing of appeal in such cases is to be decided on merits of the case.

RECENT JUDGEMENT

➢ Tata Communications Ltd vs. ACIT (ITAT Mumbai-Special Bench) March 30th, 2011

In Ronak Industries, the Tribunal held, relying on Narang Industries, that the Tribunal has the power to extend stay beyond 365 days. This decision of the Tribunal was challenged by the department in the Bombay High Court by specifically raising a question as to the applicability of the Third Proviso to section 254(2A) as amended w.e.f October 1st 2008. The High Court, vide order dated October 22nd, 2010, dismissed the department's appeal. As such, the Tribunal's order holding that there was power to extend stay even after 365 days stood affirmed.

➢ TNT India Private Limited vs. ACIT (ITAT Bangalore) March 27th, 2011

In respect of FY 2001-02, the assessee used data pertaining to AYs 1999-2000 & 2000-01. While the argument that at the time of TP study, the data relating to relevant comparable for FY 2001-02 is acceptable, the assessee has to adopt the data available for the TP study at the time of filing of the return. By the time of filing of return, the data relevant to FY 2001-02 was available. Further, prior year data is relevant only if the assessee is able to prove that the pricing pattern of the assessee for the relevant financial year has been influenced by the market conditions/business cycle/product life cycle of the earlier years (which is not there in the courier business). The OECD guidelines are not of binding nature and even the Proviso to Rule 10B (4) provides that any subsequent year data cannot be considered. The contemporaneous data of relevant financial year is to be used for making the comparable analysis for arriving at the ALP unless it is proved otherwise.

➢ CIT vs. Niraj Amidhar Surti (Gujarat High Court) dated March 17th, 2011

The AO held the transaction to be an "adventure in the nature of trade" and not normal investment on the basis that

- Assessee had borrowed funds at an exorbitant rate of 30% and
- The shares were held by the lender till the entire loan was paid. However, this reasoning loses sight of the fact that merely because the shares had been purchased from borrowed funds obtained on high rate of interest would not change the nature of the transaction from investment to one in the nature of an "adventure in the nature of trade".

Moreover, as the shares were held for a long-period of 14 months, the intention of the assessee had always been that of making investment in shares and not dealing in shares. This is also apparent from the fact that the shares had not been treated as stock in trade by the assessee. The fact that the shares were in the physical possession of the lender was not relevant because the assessee was the owner thereof.

- **Tata Sons Limited vs. DCIT (ITAT Mumbai) March 9th, 2011**

While s. 91 allows credit for Federal & State taxes, the DTAA allows credit only for Federal taxes. The result is that the s. 91 is more beneficial to the assessee & by virtue of s. 90(2) it must prevail over the DTAA. Though s. 91 applies only to a case where there is no DTAA, a literal interpretation will result in a situation where an assessee will be worse off as a result of the provisions of the DTAA which is not permissible under the Act. S. 91 must consequently be treated as general in application and must prevail where the DTAA is not more beneficial to the assessee. Accordingly, even an assessee covered by the scope of the DTAA will be eligible for credit of State taxes u/s 91 despite the DTAA not providing for the same.

- **GVK Industries Ltd vs. ITO (Supreme Court -5 Judge Bench) March 1st, 2011**

Parliament is constitutionally restricted from enacting legislation with respect to extra-territorial aspects or causes that do not have, nor expected to have any, direct or indirect, tangible or intangible impact(s) on or effect(s) in or consequences for: (a) the territory of India, or any part of India; or (b) the interests of, welfare of, well-being of, or security of inhabitants of India, and Indians. In all other respects, Parliament may enact legislation with extra-territorial effect. This power is not subject to tests of "sufficiency" or "significance" or in any other manner requiring a pre-determined degree of strength. All that is required is that the connection to India be real or expected to be real, and not illusory or fanciful

INDIRECT TAX

SERVICE TAX

- **Changes Effective from 1st January, 2011**

Central Government vide Notification No.2/2011-ST dated 1st March, 2011 inserted Rule 2B in the service tax (Determination of value) Rules, 2006 providing for determination of value of service in relation to money changing. The various provisions inserted are as following:-

- In case of currency which is exchanged from or to Indian Rupee, value of taxable service shall be the difference between buying/selling rate & RBI reference rate for the currency for that day multiplied by total units of currency exchanged

- Where RBI reference rate is not available for a currency, value of taxable service shall be 1% of the gross amount of Indian Rupee provided or received.

- Where services are not for exchange of Indian Rupee, value of taxable service shall be equal to 1% of the lower of two amounts, the person changing the money would have received by converting both the currencies into Indian Rupee at the RBI reference rate of that day. Central Government vide Notification No.3/2011-ST dated 1st March, 2011 made following amendments in Service tax Rules, 1994.

Domestic (Economy)	From Rs. 100 to Rs. 150
Domestic (others)	Standard rate of 10%
International (Economy)	From Rs. 500 to Rs. 750

- inserted Rule 2B in Rule 4A(1) amended whereby the bill/challans/invoice is to be issued within 14 days from the date of provision of service or receipt of any payment towards value of taxable service, whichever is earlier.

- Rule 5B inserted whereby the rate of service tax shall be the rate prevailing at the time service is deemed to have been provided as per Point of Taxation Rules, 2011.

- Rule 6(1) is amended whereby the payment of service tax is to be made to the treasury of Central Government by the due date following the calendar month/quarter, as the case may be, "in which the service is deemed to be provided as per the Point of Taxation Rules, 2011."

- Rule 6(3) substituted whereby excess service tax paid by the service provider in respect of services not so provided either wholly or partially, is allowed to be adjusted against his liability for subsequent period subject to conditions that:

- Assessee has refunded the payment or part thereof, along with service tax there on to the receiver of service; or

- Assessee has issued a credit note for value of service not so provided.

- Rule 6(4B) is amended whereby the present limit for adjustment of excess service tax paid is increased to Rs.2 Lacs from erstwhile limit of Rs.1 Lac

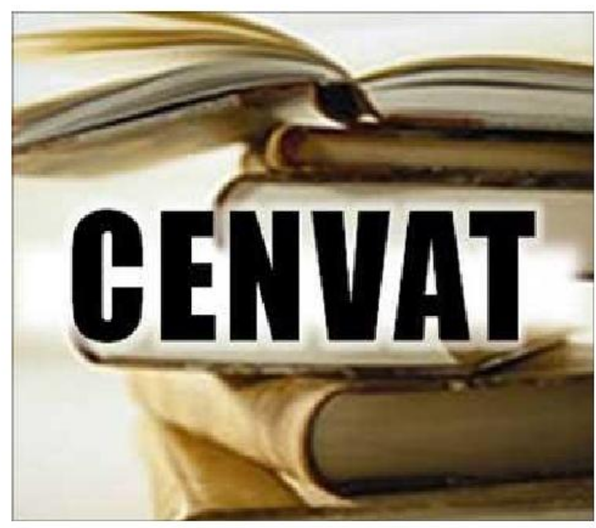
- Rule 6(6A) inserted whereby when service tax is not paid in full by the assessee based on his self assessment, the same shall be recovered in the manner prescribed in Section 87 of the Finance Act, 1994 and not U/s.73 as provided erstwhile.

- Rule 6(7B) is amended whereby the rate of composition is reduced to 0.1% from the present limit of 0.25% for discharging service tax liability by foreign exchange broker/dealer/money changer. The erstwhile condition of not showing service charges separately in the invoice by the service provider for taking benefit of composition is omitted. Central Government vide Notification No.4/2011-ST dated 1st March,2011 amended the limit of payment of service tax under the category of "transport of passengers" by air service is revised as follows:

Central Government vide Notification No.8/2011-ST dated 1st March, 2011 granted Exemption to taxable service of "transport of goods by air (Section 65(105) (zzn))"

➢ Amendments in CENVAT Credit Rules, 2004:-

Amendments in Rule 2: Definition



- **2(a):** 'Capital goods' also to include the goods used for generation of electricity for captive use within the factory even if they are outside the factory of the manufacturer. (Effective 1st April, 2011)

- **2(d):** 'Exempted goods' also to include the 130 items introduced as per Notification 01/2011 – CE dated 01st March, 2011

- **2(e):** 'Exempted services' to include the following:

  a) Taxable services on which abatement is claimed;
  b) Trading. (Effective 1st April, 2011)

- **2(k):** Definition of 'inputs' has been overhauled. A list for classification of a good as "input" has been introduced. Moreover, any goods primarily used for the personal use or consumption of the employees have been

excluded from the definition of 'inputs'. (Effective 1st April, 2011).

- **2(l):** 'Input services' to exclude services like Port Services, Architect Services, etc. used as inputs in provision of services like Construction Services. (Effective 1st April, 2011).

- **2(naa):** 'Manufacturer or Producer' to include job-worker or merchant trader under Chapter 61, 62 and 63 of Central Excise Tariff Act. (Effective 1st March, 2011)

Amendments in Rule 3: CENVAT Credit

- **3(1):** CENVAT Credit not to be allowed on newly introduced 130 items under Notification 1/2011CE. Also, CENVAT Credit to the extent of 85% only shall be allowed on CVD (additional duty of Customs) on ships, boats and other floating structures for braking up falling under tariff item 89080000. (Effective 1st March, 2011)

- **3(4):** CENVAT will not be allowed to be utilized in the payment of Excise Duty on the newly introduced 130 goods under Notification 1/2011 –CE (Effective 1st March, 2011).

- **3(5):** No payment of CENVAT to be required on the goods removed from the premises for the purpose of providing free warranty on final products. (Effective 1st April, 2011).

- **3(5B):** CENVAT Credit shall not be allowed if the Credit is written off partially or any provision to write it off partially has been made. (Effective 1st March, 2011)

Amendments in Rule 4: Conditions for availing CENVAT Credit

- **4(2):** CENVAT of up to 50% in the first year and the remaining subsequently can be availed on goods, which are used for generation of electricity outside the factory premise, without its actual receipt in the factory premise. (Effective 1st March, 2011)

- **4(7):** A proviso has been inserted which payment of CENVAT availed on Input Services, if such payment of Input Service has been returned by the manufacturer or provider of taxable service. (Effective 1st April, 2011)

Explanations to Rule 4: Following explanations have been inserted to Rule 4:-

- The time-limit for payment of CENVAT have been specified similar to the due-dates of payment of Service Tax.

- Recovery procedures may be initiated for non-payment of CENVAT.

- Persons who pay excise duty/service tax quarterly may reverse the CENVAT quarterly. (Effective 1st April, 2011)

Amendments in Rule (6): Obligation of manufacturer of dutiable and exempted good sand provider of taxable and exempted services

- **6(2):** Has been substituted to specify the records to be maintained by manufacturer or producer of final products and a provider of taxable service. (Effective 1st April, 2011).

- **6(3):** Has been amended as follows :-

  a) Option available to manufacturer / provider of taxable service not maintaining separate books of accounts to pay CENVAT at 6% of value of exempted services has been reduced to 5%.

  b) One more option to pay CENVAT availed in the production of exempted goods or provision of exempted service has been introduced on the basis of the records maintained in Rule 6(2).

c) Explanation 2 substituted to emphasize that no CENVAT shall be allowed of goods or services used in relation to manufacture or provision of exempted goods / services (Effective 1st April, 2011)

- **6(3B):** Has been introduced to mandate reversal of 50% CENVAT availed on inputs and input Services in the respective month by Banking companies and Financial Institutions. (Effective 1st April, 2011).

- **6(3C):** Has been introduced to mandate reversal of 20% CENVAT availed on inputs and input Services in the respective month by a Life insurer or Manager of Investment or ULIP.(Effective from 1st April, 2011)

- **6(3D):** Has been inserted to clarify that where any CENVAT has been reversed in order to avail any exemption under a Notification, then such CENVAT shall amount to 'CENVAT not availed'. (Effective 1st April, 2011).

Explanations to Rule 6(3) to 6(3D): Earlier explanations have been substituted with new explanations covering the following:-

a) Meaning of the word "value";

b) The manner of payment of CENVAT;

c) Recovery of CENVAT. (Effective 1st April, 2011).

- **6(5):** Availment of CENVAT of 16 specified services even if used in the manufacture of exempted goods or services stands withdrawn. (Effective 1st April, 2011).

- 6A: Has been inserted to allow CENVAT on the output services to SEZ units or Developer of a SEZ for their authorised operations. (Effective 1st March, 2011).

CORPORATE LAW

➢ CRAR (Capital to Risk Assets Ratio) requirements for NBFCS

The RBI has issued Notification No. DNBS.224/CGM (US) - 2011 dated February 17th, 2011 stating that under the current dispensation, every deposit taking NBFC shall maintain a minimum capital ratio consisting of Tier I and Tier II capital, which shall not be less than 12% of its aggregate risk weighted assets on balance sheet and of risk adjusted value of off balance sheet items. However, in terms of paragraph 16 of Non Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007, dated February 22nd, 2007, every systemically important non-deposit taking NBFC (NBFC-ND-SI) has to maintain a minimum capital ratio consisting of Tier I and Tier II capital, which shall not be less than 15% of its aggregate risk weighted assets on balance sheet and of risk adjusted value of off-balance sheet items by March 31st, 2011.

The RBI has now decided to align the minimum capital ratio of all deposit taking as well as systemically important non-deposit taking NBFCs to 15%, and hence, all deposit taking NBFCs shall maintain a minimum capital ratio consisting of Tier I and Tier II capital, which shall not be less than 15% of its aggregate risk weighted assets on Balance Sheet and risk adjusted value of off-balance sheet items w.e.f. 31st March, 2012.

➢ Recognition Of Permanent Diminution In The Value Of Investments In Banks' Subsidiaries/Joint Ventures

The RBI has issued Circular No. BP.BC.79/21.04.141/2010-11:-

a) On the happening of an event which suggests that impairment has occurred. This would include:-

- The company has defaulted in repayment of its debt obligations.

- The loan amount of the company with any bank has been restructured.
- The credit rating of the company has been downgraded to below investment grade.

b) When the company has incurred losses for a continuous period of three years and the net worth has consequently been reduced by 25% or more.

c) In the case of new company or a new project when the originally projected date of achieving the breakeven point has been extended i.e., the company or the project has not achieved breakeven within the gestation period as originally envisaged. When the need to determine whether impairment has occurred arises in respect of a subsidiary, joint venture or a material investment, the bank should obtain a valuation of the investment by a reputed/qualified valuer and make provision for the impairment, if any. These guidelines would be applicable with immediate effect.

No Government Approval for Managerial Remuneration for Unlisted Companies with No Profits

The Ministry of Corporate Affairs (MCA) has issued Notification No. 70(E) dated. 8th February, 2011 in relation to managerial remuneration in unlisted companies having no profits/inadequate profits and it is now provided that in the case of unlisted companies, so long as the conditions specified in Schedule XIII, including special resolution of shareholders and absence of default on payment to creditors, are fulfilled, approval of the MCA will not be needed hereafter. Accordingly, Schedule XIII of the Companies Act 1956 is being amended to provide that unlisted companies (which are not subsidiaries of listed companies) shall not require government approval for managerial remuneration in cases where they have no profits/inadequate profits, provided they meet the other conditions stipulated in the Schedule XIII.

Revised Schedule VI to the Companies Act, 1956

The Ministry of Corporate Affairs (MCA) has released the Revised Schedule VI to the Companies Act, 1956. This revised Schedule VI has been framed as per the existing non-converged Indian Accounting Standards notified under the Companies (Accounting Standards), Rules, 2006 and has nothing to do with the converged Indian Accounting Standards. This will apply to all the companies uniformly for the financial statements to be prepared for the financial year 2010-11 and onwards.

Directions under Section 212 For Attaching Subsidiaries' Financial Statements

The MCA has issued General Circular No. 2 /2011 dated 8th February, 2011 and stated that section 212 of the Companies Act, 1956 requires holding companies to attach with their balance sheet a copy of the balance sheet, profit and loss account etc of each of its subsidiaries and that in recent years, with the globalization of the Indian economy, there has been a large increase in the number of holding companies and subsidiaries. Accounting policies and practices have also evolved, and accounting standards have been issued regarding preparation of consolidated financial statements. The MCA is receiving many applications seeking permission not to attach the accounts of subsidiaries which are granted on case-by-case basis on the basis of certain conditions which are intended to protect the interests of investors. Now, in the context of the emerging trends in the economy and regulatory and accounting practices, it has been decided that the permission may be granted on a general basis wherever the board of directors of the holding company gives its consent and the conditions, prescribed by the MCA are complied with, like,

- The board of directors of the company has by resolution given consent for not attaching the balance sheet of the subsidiary concerned;

- The company shall present in the annual report, the consolidated financial statements of holding company and all subsidiaries duly audited by its statutory auditors;

- The consolidated financial statement shall be prepared in strict compliance with applicable accounting standards and, where applicable, listing agreement as prescribed by the SEBI;

- The company shall disclose in the consolidated balance sheet the following information in aggregate for each subsidiary including subsidiaries of subsidiaries:- (a) capital (b) reserves (c) total assets(d) total liabilities (e) details of investment (except in case of investment in the subsidiaries) (f) turnover (g) profit before taxation (h) provision for taxation (i) profit after taxation (j)proposed dividend;

- The holding company shall undertake in its annual report that annual accounts of the subsidiary companies and the related detailed information shall be made available to shareholders of the holding and subsidiary companies seeking such information at any point of time. The annual accounts of the subsidiary companies shall also be kept for inspection by any shareholders in the head office of the holding company and of the subsidiary companies concerned and a note to the above effect will be included in the annual report of the holding company. The holding company shall furnish a hard copy of details of accounts of subsidiaries to any shareholder on demand;

- The holding as well as subsidiary companies in question shall regularly file such data to the various regulatory and government authorities as may be required by them;

- The company shall give Indian rupee equivalent of the figures given in foreign currency appearing in the accounts of the subsidiary companies along with exchange rate as on closing day of the financial year.

➢ **Directions under section 212 for attaching subsidiaries financial statements –year of applicability**

The MCA has issued General Circular No. 3/2011 dated February 21st, 2011 clarifying that the MCA Circular No. 2/2011 dated February 8th, 2011 shall be effective in respect of balance sheet and profit and loss accounts prepared regarding the financial year ending on or after the 31st March, 2011.

INTERNATIONAL TAXATION

➢ **Asia Satellite Tele communications Co. Ltd**

Facts of the case

The taxpayer, a company incorporated in Hong Kong, enters into contract with the television channels, etc (the customers) for providing the transponder capacity of its satellites.

The customers have their own relay facilities outside India for up-linking the signal to the satellite. The

signal is received, amplified and re-sent by the transponder through a different frequency without any change in signal content. Then the signal is received for down linking by the cable operators, etc. The taxpayer does not have any facility, assets or presence in India. Further, the tracking, tele-metering and control operations in respect of the satellites were performed by the tax payer from Hong Kong.

Issues

Applicability of Section 9(1) (i) of the Act to the payments received by the taxpayer.
Whether payment received by the taxpayer can be regarded as "royalty" under section 9(1) (vi) of the Act?

Whether the payment by the taxpayer can be regarded as Fee for technical Services under section 9(1) (vii) of the Act?

High Court's Ruling

The High Court considered the clauses of the Agreement between the tax payer and its customers and observed that:-

- Programmers are uplinked by the customers outside India;
- Amplification of signals takes place at the satellite, which is not located in Indian airspace; and
- The amplified programme signals are relayed over the foot print area, which includes India, for the cable operators to downlink the signal and pass on the same for viewing by Indian population.

In light of the above, the High Court held that relay of the programmes in India does not amount to operations being carried in India by the taxpayer. Further, as the taxpayer did not have any facility, assets or presence in India, the provisions of Section 9(1) (i) of the Act are not attracted.

Further, the High Court held that various clauses of the agreement clearly indicate that the control over the transponders was always with the taxpayer. It was observed that the taxpayer had merely given access to a broadband/ capacity available with the transponder to its customers. Hence replying on the ruling of the Authority of Advance Rulings in the case of ISRO Satellite Centre [ISAC], [In re (2008) 307 ITR59] it held that the payments for use of transponder capacity would not qualify as royalty under the Act.

The High Court also held that the transponder is an in-severable part of the satellite. It cannot function without the continuous support of various systems and components of the satellite. Consequently, it is wrong to assume that the control and constructive possession of the transponder can be handed over by the satellite operator to its customers. The transponder being a part of satellite, playing how so ever important role cannot be termed as equipment.

The High Court held that there was no use of the transponder/ process in India. Merely because the satellite had a footprint in India would not mean that the process took place in India. Reliance was placed on the decision of the Supreme Court in the case of Ishikawajima-Harima Heavy Industries Company Limited [2007] 288 ITR 408 (SC), in which it was held that sufficient territorial nexus with India was sine qua non for attracting taxation. Therefore, payments from TV channels could not be taxed in India as there was insufficient territorial nexus with India.

The High Court also held that where the technical terms used in the OECD Model Convention are the same as appearing under the domestic tax laws, OECD commentary can be relied upon for better understanding.

Based on the above the High Court held that the said payments do not constitute royalty and are not taxable in India.

No argument was advanced by the tax department on the ground relating to Fee for technical Services under section 9(1) (vii) of the Act. Hence, the High Court did not adjudicate on this matter.

- **SET Satellite (Singapore) Pvt. Ltd. v. ADIT**

Facts

The taxpayer, a tax resident of Singapore, entered into an agreement with Global Cricket Corp Pte Ltd (GCC), also a tax resident of Singapore, for acquiring rights to broadcast cricket matches in licensed territories, including India. The matter went to Tribunal on the issue as to whether the payment made by the taxpayer to GCC was subject to withholding tax in India.

The Mumbai Tribunal allowed taxpayer's appeal and held that, even if the payments are in the nature of royalty, it does not arise in India under Article 12(7) of the tax treaty as in absence of economic link between the payment of royalties and taxpayer's alleged Permanent Establishment (PE) in India, the payment cannot be said to have been incurred "in connection" with the PE in India or "borne by" the PE in India.

Pursuant to the above order, the taxpayer filed a miscellaneous application before the Tribunal. In its miscellaneous application, the taxpayer requested the Tribunal to provide a specific finding that the provisions of the Limitation of Benefits (LOB) Article cannot be applied in the present case and the tax treaty benefit would be available.

Issues

Whether LOB article can be applied in the present case?

Held

The Tribunal observed that the provisions of Article 24(1) of the tax treaty apply only to income paid from sources in one Contracting state (India in this case), where they are exempt from tax or enjoy tax at a reduced rate, to a recipient resident in the other Contracting State (Singapore in this case) who is taxable on a remittance basis in the Singapore. The Tribunal held that Article 24 of the tax treaty was not applicable in the present case on account of following:-

- Even if the payments made to the GCC are construed as royalty, such royalty does not arise in India under Article 12(7) of the tax treaty, further as per the OECD Commentary on Article 11, the state of source of the royalties is the state of which the payer of royalties is resident. In this case, the state of source of royalties is Singapore as the payer is a resident of Singapore. The royalties are not therefore 'income from sources in India'.

- There is a distinction between income 'exempt from tax' and income which is 'not taxable'. In the present case, there is no question of income being exempt from tax in India.

- The payment made by the taxpayer to GCC, in Jersey, was subject to tax in Singapore under its domestic laws.

- **Citicorp Banking Corporation, Bahrain v. ADIT [2011-TII-40-ITAT-MUMINTL] Dated 25th February, 2011**

Facts

The taxpayer, a foreign company was registered as a Foreign Institutional Investor ('FII') with the Securities and Exchange Board of India (SEBI). Further, the taxpayer is a branch of Citicorp Banking Corporation, Bahrain and is tax resident of USA.

The taxpayer earned Long-Term Capital Gain on sale of shares held in UTI Limited of INR 804 million. Against this gain, the taxpayer set off net loss which arose due to cancellation of exchange contract. Accordingly, the taxpayer offered the net long-term-capital gain for taxation at 10 percent as per the provisions of section 115AD of the Act.

The AO held that exchange contract cannot be considered as a capital asset and the gain or loss that accrues from an exchange contract cannot be considered for taxation under section 115AD of the Act. Therefore, the AO declined to give benefit of the set off in respect of the loss on cancellation of the exchange contract against long term capital gains.

Issues

Whether losses accruing to FIIs on account of cancellation of foreign exchange forward contract having direct nexus with investment are capital losses.

Held

The Tribunal relied on the Delhi Special Bench decision in the case of Apollo Tyres Ltd. vs. ACIT [2004] 89 ITD 235 (Del)(SB) wherein the issue was in respect of gain on cancellation of foreign contract.

The Tribunal observed that the tax authorities had not challenged the fact that the dominant purpose for entering into foreign exchange forward contract was to hedge against the depreciation of the foreign currency and that it has direct nexus with the investments made.

Accordingly, the Tribunal held that the loss accrued / arising on account of cancellation of exchange contract is capital loss having direct nexus with the investment of the taxpayer and hence the taxpayer is entitled to set off the same.

Section 115AD of the Act decides the quantum of the tax payable by the FIIs on the income from securities or capital gains and it has nothing to do with the determination of the nature of gain or loss. It does not take in account whether loss/gain is on account of capital or revenue.

POLICY WATCH

- **Government gives itself power to quickly levy export duty**

Government has taken the power to quickly levy export duty on some of India's most popular farm commodities overseas. The Budget has introduced export tariff lines on tea, coffee, basmati, cotton, tobacco, groundnut and spices. Once the Finance Bill is passed, the export duty can be imposed immediately through a notification if it becomes necessary to prevent trade and cool local market prices. The government also issued an exemption notification. The specific and ad valorem duties introduced in the Finance Bill are the maximum customs tariff that can be imposed by the government on farm products leaving the country. Introduction of these tariff lines by the finance ministry has been a bolt from the blue for the commerce ministry, in charge of overseeing farm exports.

- **Government to raise Rs 4,170 billion from borrowings**

Prospects of tax buoyancy on the back of robust economic growth has lowered the government's dependence on market borrowings, pegged at Rs 4,170 billion for 2011-12, against Rs 4,470 billion as per the revised estimates of the current fiscal. Lower government borrowings will have a positive impact for the private sector. The government borrowings next fiscal would not crowd out resources for the private sector, as much as it did in 2010-11. Analysts say it would also help in controlling inflation as the government returns back to path of fiscal consolidation. During the current fiscal, the government resorted to gross market borrowing of Rs 4,470 billion, Rs 100 billion lower than the Budget estimate of Rs 4,570 billion.

- **CCI gets power to approve big M&As**

The Competition Commission of India (CCI) will now be able to investigate and approve big Mergers and Acquisitions (M&A) in the country, with the government notifying the key provisions of the Competition Act.

The provisions, Sections 5 and 6 would grant the competition watchdog the powers to scrutinize amalgamation proposals of companies with a threshold of 15 billion. The CCI would take a maximum of 180 days to investigate mergers. The preview of Competition Commission of India (CCI) was passed by the cabinet and will be placed before Parliament in this session.

- **RBI allows IRFs on 91-day Treasury Bills**

The Reserve Bank of India has allowed Interest Rate Futures (IRFs) trading on 91-day Treasury Bills (T-Bills). The central bank has decided to introduce interest rate futures on 91-day Treasury Bills issued by the Government of India. The 91-day T-Bill is a liquid short-term instrument. Hence, trading in futures on T-bills will give an indication about the interest rate trend at the short of the curve. The central bank has allowed cash settlement in futures on T-Bills.

The contract shall be cash-settled in Indian rupees. This feature was not available in futures on the 10-year gilt. Instead, the contract was settled by physical delivery, resulting in the dull off take of the instrument. Since the time of inception, volumes have remained thin in IRFs on 10-year gilt as they were considered illiquid by market players. Thus, the introduction of IRFs on Treasury Bills will help develop the market. The central bank had also issued directions regarding the same. The final settlement price of the contract shall be based on the weighted average price or yield obtained in the weekly auction of the 91-Day Treasury Bills on the date of expiry of the contract.

- **RBI agrees for limited flexibility in pricing of convertible instruments**

The Reserve Bank of India has agreed to give companies limited flexibility in pricing of convertible instruments for raising funds overseas, a move that will improve foreign direct investment (FDI) flows into the country. The current FDI policy states that the price at which a convertible instrument is to be swapped for equity shares should be locked at the time of issue. Companies say this rule denies them the benefit of getting better conversion terms if their business does well. The RBI has agreed to some flexibility in pricing of FDI-compliant convertible instruments.

- **Government approves Goods and Services Tax Bill**

The Union cabinet has approved the Constitutional Amendment Bill to roll out the Goods and Services Tax (GST), the cabinet has given its nod to introduce the Bill in the Parliament. The GST seeks to replace multiple indirect taxes, such as the central excise duty and services tax, and state taxes including value-added tax, entry tax and purchase tax, with a neat single levy.

The proposed tax will have two components, one levied by the centre and the other by the states, implying that both will need to have concurrent powers to tax a good or service. At present, the centre can impose taxes on goods at the factory gate and services while states can only tax goods at retail level. States do not have the power to levy tax on services.

INDUSTRY WATCH & CORPORATE HIGHLIGHT

- **Railways project 16.5% rise in earnings**

The railways have projected an increase in passenger earnings by over 16.5% to Rs 304 billion. For the financial year 2011-12, the railways have projected a 17.1% increase in upper-class passenger revenues and 16.4% in second-class revenues, over a passenger growth of 6.4%. During financial year 2010-11, with a 5.3% increase in passenger numbers, the railways' revenue is set to grow 11.2%. The Indian Railways is hopeful of achieving the target with an increase in passenger numbers and capacity. Assuming 6.4% growth in the originating number of passengers and higher traffic output due to the proposed induction of a large number of new trains in the non-suburban segment, the target for next year is achievable.

- **Direct tax collections up 20.75% in April-Feb**

NET direct tax collections grew by 20.75% to Rs 33,611 billion during the April-February period of the current financial year. Direct tax collections stood at Rs 27,841 billion in the same period last fiscal. Corporate income tax collections grew by 24.01% to Rs 22,361 billion during the review period from Rs 18,031 billion in the corresponding period a year ago. Furthermore, personal income tax grew by 14.76% to Rs 11,211 billion; Securities Transaction Tax (STT) revenue grew by 1.72% to Rs 60 billion during the 11-month period ending February, 2011.

- **Forex reserves raise $1.8 billion to $302.59 billion**

The country's foreign exchange reserves have gone up by $1.8 billion to $302.59 billion for the week ended March 4, as per the data released by Reserve Bank of India. The reserves have gone up for the third consecutive week. On February 25, forex reserves increased by $158 million to $300.786 billion.

The foreign currency assets increased by $1.5 billion to $272.964 billion. The increase in reserves is mainly on account of currency revaluation. Foreign currency assets expressed in US dollar terms include the effect of appreciation or depreciation of non-US currencies such as the euro, sterling and yen, held in reserves. The country's reserve position has also increased by $12 million to $2.28 billion. Gold reserves also increased by $219 million to $22.14 billion.

- **Bharti Airtel launches 3G service in Delhi circle**

The country's largest telecom player, Bharti Airtel launched 3G service in Delhi circle, enabling subscribers to access high speed internet and video telephony. The company launched its third Generation of Mobile services on the back of a robust network powered by over 1,800 3G sites in the National Capital Region spanning Delhi, Gurgaon, Faridabad and Noida.

Bharti Airtel is the third private operator after Tata Teleservices and Reliance Communications to launch 3G services in the country.

Statuary compliance calendar for the month of December 2014			
Statuary compliance under Act	**Particulars**	**Due date**	**Governing authority**
Service Tax	Payment of monthly service tax by all tax payers other than individuals, proprietors and partnership firms (Payment by 6th in case of e-payment).	05/12/2014	Central Board of Excise and Custom
Central Excise	Payment of monthly central excise duty on goods by assessee other than SSI units (Payment by 6th in case of e-payment).	05/12/2014	Central Board of Excise and Custom
Income Tax Act -1961	Deposit of Income Tax TCS and TDS deducted in previous month.	01/12/2014	Central Board of Direct Tax.
NBFC-D	Monthly return of exposure to capital market in form NBS-6 by NBFC having total assets of ` 100 crore and above.	07/12/2014	Reserve Bank of India.
NBFC-ND-SI	Monthly return of source and application of fund profit and loss account, asset classification.	07/12/2014	Reserve Bank of India
Central Excise	Monthly central excise return in form ER-1/ER-2 by other that SSI.	10/12/2014	Central Board of Excise and Custom.
Central Excise	Monthly return of receipts and consumption of Principal Inputs by specified manufacturers of excisable goods in form ER-6.	10/12/2014	Central Board of Excise and Custom
SEBI	Un-audited quarterly financial results and Limited Review Report from auditors for previous quarter to stock exchange as per clause 41 of Listing Agreement.	10/12/2014	The securities and exchange board of India Act-1992
Income tax Act -1961	Quarterly TDS certificate by Government in form 16A.	15/12/2014	Central Board of Direct Tax.
Provident Fund	(a) Payment of monthly dues of Provident fund. (b) Monthly return in form 5 for employees joining Provident fund during previous month along with declaration in form 2 furnished by the employees . (c) Monthly return of PF in form 10 of employees leaving the service during preceding month.	15/12/2014	The Central Board of Trustees , The Employees' Provident Fund Scheme,1952
The employees' state insurance Act-1948.	Payment of ESIC contribution.	21/12/2014	The employees' state insurance Act-1948. Ministry of labour and employment.
Provident fund	Monthly contribution statement (abstract) in form 12A, along with copy of receipted challans regarding payment of contribution.	25/12/2014	The Central Board of Trustees , The Employees' Provident Fund Scheme, 1952
Income Tax Act -1961	Annual information return under section 285BA in form 61A.	31/12/2014	Central Board of Direct Tax.

Glossary

AAR	Authority of Advance Rulings
ADR	American Depository Receipt
ALP	Arm's Length Price
AO	Assessing Officer
AP	Association of Persons
APA	Advance Pricing Agreement
ATM	Automated Teller Machine
AY	Assessment Year
BCD	Basic Customs Duty
BI	Body of Individuals
BP	Balance of Payments
CA	Chartered accountant
CAD	Current Account Deficit
CBDT	Central Board of Direct Taxes
CBEC	Central Board of Excise & Customs
CENVAT	Central Value Added Tax
Customs Act	Customs Act, 1962
CIT	Commissioner of Income Tax
CPI	Consumer Price Index
CSR	Corporate Social Responsibility
CD	Countervailing Duty
DDT	Dividend Distribution Tax
DTA	Domestic Tariff Area
ECB	External Commercial Borrowings
ESI	Employee's state insurance
FDI	Foreign Direct Investment
FEMA	Foreign Exchange Management Act
FERA	Foreign Exchange Regulation Act
FII	Foreign Institutional Investors
FIPB	Foreign Investment Promotion Board
FPI	Foreign Portfolio Investment
FTS	Fees for Technical Services
FY	Financial Year
GDP	Gross Domestic Product
GDR	Global Depository Receipt

LCD	Liquid-crystal Display
MP	Madhya Pradesh
MP	Market price
MF	Mutual fund
MSME	Micro Small and Medium Enterprises
NBFC	Non Banking Finance Company
NHAI	National Highway Authority of India
NPS	National Pension Scheme
NRI	Nonresident in India
NABARD	National Bank for Agriculture and Rural Development
OEM	Original Equipment Manufacturer
OET Act	Odessa Entry Tax Act, 1999
PSU	Public Service Undertakings
P&L	Profit & loss
PF	Provident fund
POTR	Point of Taxation Rules
QE	Quantitative Easing
QFI	Qualified Foreign Investor
RBI	Reserve Bank of India
REF	Renewable Energy Fund
REIT	Real Estate Investment Trust
Rules	Income-tax Rules, 1962
SA	Standard on Auditing
SAD	Special Additional Duty
SC	Scheduled Caste
SC	Supreme Court
SEBI	Securities and Exchange Board of India
SEZ	Special Economic Zone
ST	Scheduled Tribes
ST	Service Tax
STP	Software Technology Park
STR	Service Tax Rules
STCG	Short Term Capital Gain
TIN	Transaction identification number
TNNM	Transactional Net Margin Method
Tribunal	Income tax Appellate Tribunal

BUSINESS ADVISORY

- Growth Planning
- Succession Planning.
- Strategic Decision Appraisal
- Risk, Uncertainty and Change Management Services
- Strategic Decision Implementation – National and Global Platform
- Wealth Management Services.

AUDIT & ASSURANCE

- Statutory Audit including Tax Audit &VAT Audit
- Internal Audit and Concurrent Audit
- Management Audit and Operational Audit
- Cost Audit/Reviews
- System and process control reviews.
- Secretarial Audit.

RBI, FEMA, SEBI Services

- Setting up Liaison Office, Branch Office and Project Office.
- RBI Consulting
- Private Equity Finding Advisory.
- Project Financing.
- Credit Rating.
- Business Asset Valuation.
- Due Diligence.

TAXATION SERVICES

- Direct Taxation Advisory
- Service Tax, Excise duty, VAT Registration Services
- Tax Planning Strategy– Optimum use of Corporate Tax Incentives.
- Implementing and Operating in the tax consolidation regime
- Preparation of return of Income Tax, Service Tax, Excise Duty and VAT.

OUTSOURCING ACCOUNTANTS

- Annual financial report preparation
- Preparation of general and special purpose statutory accounts
- Processing Payroll
- Cash management reporting
- Accounting system reviews
- Financial analysis
- General Accounting Support, as required by client.

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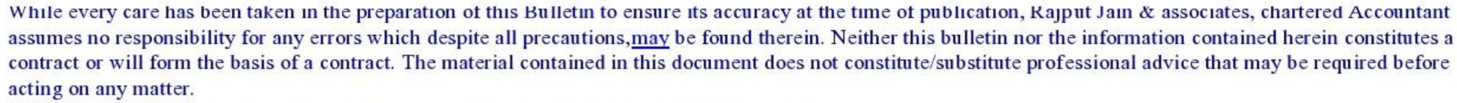

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