INDIA BUDGET 2014

Nanubhai Desai & Co.

For private circulation & for internal use only.
This booklet summarises the important proposals included in the budget speech made by the Honourable Finance Minister on 10th July, 2014. Whilst every care has been taken in the preparation of this document it may contain inadvertent errors for which we shall not be held responsible. It must be stressed that the finance bill may contain proposals which have not been referred to in the budget speech and additionally, the detailed proposals are liable to amendment during the passage of the finance bill through Parliament. The information given in this document provides a bird's-eye view on the changes proposed and should not be relied for the purpose of economic or financial decision. Each such decision would call for specific reference of the relevant statutes and consultation of an expert.

INDEX

FOREWORD, EXECUTIVE SUMMARY AND RECENT DEVELOPMENTS

FOREWORD….. 2

EXECUTIVE SUMMARY.. 3

BACKDROP TO THE BUDGET AND RECENT DEVELOPMENTS 6

ECONOMIC SURVEY

OVERVIEW OF ECONOMIC SURVEY 133

KEY BUDGET PROPOSALS

INCOME TAX RATES 134

FOREIGN POLICY ANNOUNCEMENTS 136

DOMESTIC TAXATION 137

INTERNATIONAL TAXATION 149

SERVICE TAX.. 152

CUSTOMS 155

CENTRAL EXCISE 157

INDUSTRY SPECIFIC ANALYSIS

INDUSTRY SPECIFIC ANALYSIS.. 159

FOREWORD....

The Hon'ble Finance Minister, Shri Arun Jaitley, in his maiden Budget Speech on July 10, 2014, attempted to touch upon almost all the important sectors of the economy and thereby appeared to spread the agenda a bit too wide!

The positives of the Budget were the major allocation to road infrastructure, liberalisation of FDI regime the real estate and affordable housing sectors, boost to manufacturing sector & an assurance to reduce litigation by removing bottlenecks in the transfer pricing regime and amendments relating to Advance Pricing Agreements. The common man and senior citizens were given relief in the form of higher exemption limit and higher deduction for savings.

The Finance Minister was hopeful of introducing the GST regime by end of the year. The much expected deletion of the retrospective operation of the provisions relating to indirect transfers, however, failed to materialize.

All in all, a good effort from a six week old government the Finance Minister has ticked all the boxes. The proof of the pudding, however, lies in the eating!!

Thursday, July 10, 2014

Mumbai
INDIA

EXECUTIVE SUMMARY

DIRECT TAX PROPOSALS

- Basic exemption limit increased by Rs. 50,000 for all individual tax payers, except super senior citizens (aged eighty years or more).
- No change inrate of surcharge for corporate, individuals, HUFs and firms.
- Education cess to continue at 3 per cent.
- Investment limit under section 80C raised from Rs 1 lakh to Rs 1.5 lakh.
- Deduction limit on account of interest on loan in respect of self occupied house property raised from Rs 1.5 lakh to Rs 2 lakh.
- Conducive tax regime to Infrastructure Investment Trusts and Real Estate Investment Trusts to be set up in accordance with regulations of the Securities and Exchange Board of India.
- Investment allowance at the rate of 15 per cent to a manufacturing company that invests more than Rs 25 crore in any year in new plant and machinery. The benefit to be available for three years i.e. for investments up to 31.03.2017.
- Investment linked deduction extended to two new sectors, namely, slurry pipelines for transportation of iron ore, and semi-conductor wafer fabrication manufacturing units.
- 10 year tax holiday extended to the undertakings which begin generation, distribution and transmission of power by 31.03.2017.
- Income arising to foreign portfolio investors from transaction in securities to be treated as capital gains.
- Concessional rate of 15 per cent on foreign dividends without any sunset date to be continued.
- The eligible date of borrowing in foreign currency extended from 30.06.2015 to 30.06.2017 for a concessional tax rate of 5 per cent on interest payments. Tax incentive extended to all types of bonds instead of only infrastructure bonds.
- Introduction of a “Roll Back” provision in the Advanced Pricing Agreement (APA) scheme so that an APA entered into for future transactions is also applicable to international transactions undertaken in previous four years in specified circumstances.

- Introduction of range concept for determination of arm's length price in transfer pricing regulations.
- To allow use of multiple year data for comparability analysis under transfer pricing regulations.
- Long term capital gains increased from 10 per cent to 20 per cent on transfer of units of Mutual Funds, other than equity oriented funds.
- Income and dividend distribution tax to be levied on gross amount instead of amount paid net of taxes.
- In case of non-deduction of tax on payments, 30 per cent of such payments will be disallowed instead of 100 per cent.
- Government to review the DTC in its present shape and take a view in the whole matter.
- 60 more Ayakar Seva Kendra's to be opened during the current financial year.Net Effect of the direct tax proposals to result in revenue loss of Rs 22,200 crore.

INDIRECT TAX PROPOSALS

☐ **Service tax**

- Sale of space/time on media such as internet, films,billboards, etc. made, subject to service tax.
- Services by air-conditioned contract carriages and technical testing of newly developed drugs on human participants brought under service tax.
- Services provided by Indian tour operators to foreign tourists in relation to a tour wholly conducted outside India to be taken out of the tax net.
- Services provided by the Employees' State Insurance Corporation for the period prior to 1st July 2012 exempted, from service tax.
- Exemption available for specified micro insurance schemes expanded to cover all life micro-insurance schemes where the sum assured does not exceed Rs 50,000 per life insured.
- 'Indian Customs Single Window Project' to facilitate trade, to be implemented.
- The scheme of Advance Ruling in indirect taxes to be expanded to cover resident private limited companies.

☐ **Excise Duty**

- Reduction in excise duty on specified food processing and packaging machinery from 10 per cent to 6 per cent.
- Reduction in the excise duty from 12 per cent to 6 per cent on footwear of retail price exceeding Rs 500 per pair but not exceeding Rs 1,000 per pair.

- Withdraw concessional excise duty (2 per cent without Cenvat benefit and 6 per cent with Cenvat benefit) on smart cards and a uniform excise duty at 12 per cent.
- To develop renewable energy, various items exempted from excise duty.
- Specific rates of excise duty increased on cigarettes in the range of 11 per cent to 72 per cent.
- Excise duty increased from 12 per cent to 16 per cent on pan masala, from 50 per cent to 55 per cent on unmanufactured tobacco and from 60 per cent to 70 per cent on gutkha and chewing tobacco.
- Levy of an additional duty of excise at 5 per cent on aerated waters containing added sugar.
- Clean Energy Cess increased from Rs 50 per tone to Rs 100 per tone.

☐ **Customs**

- To address the issue of inverted duties, basic customs duty (BCD) reduced on certain items.
- To encourage new investment in the chemicals and petrochemicals sector, basic customs duty reduced on certain items.
- Concessional basic customs duty of 5 per cent extended to machinery and equipment required for setting up of a project for solar energy production.
- Concessional basic customs duty of 5 per cent on machinery and equipment required for setting up of compressed biogas plants (Bio-CNG).
- Anthracite coal, bituminous coal, coking coal, steam coal and other coal to attract 2.5per cent basic customs duty and 2 per cent CVD to eliminate all assessment disputes.
- Basic customs duty on semi processed, half cut or broken diamonds, cut and polished diamonds and coloured gemstones rationalized at 2.5 per cent. To encourage exports, pre-forms of precious and semi-precious stones exempted from basic customs duty.

INCOME TAX

DOMESTIC TAXATION

CIRCULARS/ NOTIFICATIONS/PRESS RELEASE

Information to be furnished while making payment to a Non-Resident:

Rule 37BB of the Income-tax Rules for remittances outside India was issued by the CBDT with effect from 1 July 2009. The existing Rule provides for electronic furnishing of information by the Remitter in Form 15CA (self-declaration), while making payment to the nonresident, based on a certificate from a Chartered Accountant in Form 15CB (CA Certificate).

In August 2013, the CBDT had amended Rule 37BB of the Rules to broaden the requirement of collecting information and reporting requirements for all remittances outside India. On 2 September 20132, the CBDT has substituted the earlier Notification which has further revised the scope and the format of reporting of information under Rule 37BB of the Rules. It provides that the person responsible for making any payment including any interest or salary or any other sum chargeable to tax under the Act shall be required to furnish details in the prescribed forms. The amended Rule shall come into force from 1 October 2013. The key amendments are summarized as follows:

- Part A of Form 15CA, the amount of remittance does not exceed Rs 50,000 and aggregate of such payments made during the financial year does not exceed Rs 2,50,000.

  It includes information about the remitter and recipient like name, address etc., details of remittance to be made, tax deducted and the aggregate amount of remittance made during the financial year including the proposed remittance. It is also mandatory to provide the PAN of the remitter if tax has been deducted. There is no requirement to obtain Form 15CB. Remitter is also required to verify the genuineness of information furnished and undertake to co-operate with tax authority by furnishing requisite documents for determining income of recipient or tax withholding liability.

- In Part B of Form 15CB, the payments other than those covered under Part A, after obtaining a CA Certificate or withholding orders from Assessing Officer (AO) are required to be reported. The contents cover the details about the Remitter, Recipient, Bank, CA Certificate/withholding orders and expansive information about the remittance and its taxability under the Act as well as the applicable tax treaty.

- Once the remitter furnishes the above information on Government's website, a signed hard copy of Form 15CA is required to be submitted to the Authorized Dealer Bank prior to the remittance. The revised Rule also empowers any tax authority to obtain a copy of Form 15CA from the remitting Bank for the purpose of any proceedings under the Act.

The reporting has now been reduced for small remittances up to a certain limit and for those remittances which are not chargeable to tax. Certificate from accountant under Form 15CB which was earlier mandatory for all remittances outside India is not required to be furnished for remittances which are not taxable and covered in the specified list or in the cases where a certificate or order is obtained from tax authorities. However, the remitter has to undertake to provide requisite details and documents to enable tax authorities to evaluate tax liability in India and also pay the requisite withholding tax along with interest and penalty in case of any wrong declaration.

[Notification NO. 67/2013, dated 02-09-2013]

CBDT notifies statement to be furnished in respect of income distributed by a securitization trust

CBDT has inserted special provisions relating to tax on distributed income by securitization trusts. The amount of income distributed by the securitization trust to its investors will be chargeable to tax and the trust shall be liable to pay additional income tax on such distributed income. Pursuant to this, the CBDT has notified a statement to be furnished in respect of income distributed by a securitization trust in Form 63AA. This Form is to be furnished to the Tax Authority and it contains details of the trust along with details of income distributed, tax and interest paid thereon with a requirement of enclosing audited annual accounts of the trust.

[Notification NO. 68/2013, dated 04-09-2013]

Form of application for obtaining an advance ruling under section 245Q (1) of the Income-tax Act, 1961 -"FORM No. 34EA"

The Central Board of Direct Taxes has inserted new form 34EA for filling application to seek Advance Ruling under section 245.

[Notification NO. 76/2013, dated 24-09-2013]

Reverse Mortgage (Amendment) Scheme, 2013

Central Board of Direct Taxes (CBDT) has by the notification made the following changes to the erstwhile scheme.

- Disbursement of Loan

  After the amendment, the lending institutions, in addition have been authorized to make payment to Life Corporation of India (LIC) or any other insurer registered with IRDA for the purpose of making periodic payments by way of annuity to the reverse mortgagor.

- Period of Reverse Mortgage Loan

  After the amendment, the lending institutions can disburse the loans for lifetime of the borrower for periodic payments of annuity by insurer registered with IRDA.

[Notification NO. 79/2013, dated 07-10-2013]

Notified Jurisdictional Area

In exercise of the powers under section 94A of the Income tax Act, 1961, Central government specifies “Cyprus “as ‘Notified Jurisdictional Area’.

[Notification NO. 86/2013, dated 01-11-2013]

Rajiv Gandhi Equity Savings Scheme, 2013 [Section 80CCG]

The deduction under the Scheme shall be available to a new retail investor who complies with the conditions of the Scheme and whose gross total income for the financial year in which the investment is made under the Scheme is less than or equal to Rs 12,00,000. The eligible securities brought into the demat account, as declared or designated by the new retail investor shall be under a lock-in for a period of 3 years. Deduction under section 80CCG can be claimed of 50 per cent of the amount invested or maximum Rs 25,000 and subject to other conditions.

[Notification NO. 94/2013, dated 18-12-2013]

CLARIFICATION REGARDING TDS ON SERVICE TAX COMPONENT COMPRISED OF PAYMENTS MADE TO RESIDENTS

In exercise of the powers conferred under section 119 of the Act, the Board has decided that wherever in terms of the agreement/contract between the payer and the payee, the service tax component comprised in the amount payable to a resident is indicated separately, tax shall be deducted at source under Chapter XVII-B of the Act on the amount paid/payable without including such service tax component. {Judgement of the Hon’ble Rajasthan High Court dated 1-7-2013, in the case of CIT (TDS) Jaipur v. Rajasthan Urban Infrastructure.

[Notification NO. 1/2014, dated 13-01-2014]

Clarification regarding disallowance of expenses under section 14A in cases where corresponding exempt income has not earned during the FY

CBDT in exercise of the powers under section 119 of the Act hereby clarifies that Rule 8D read with section 14A of the Act provides for disallowance of the expenditure even where the tax payer in a particular year has not earned the exempt income.

[Notification NO. 5/2014, dated 11-02-2014]

Additional Income Tax on distributed Income under Section 115R of the Income Tax Act

Section 115R is placed under chapter XII-E of the Act, which is titled as “Specific Provision Relating to Tax on Distributed Income”.

As per sub-section (2) of section 115R, any amount of income distributed by specified companies or by mutual funds to its unit holders shall be chargeable to tax at the rates prescribed therein.

Redemption/Repurchase of units or allotment of Bonus units would not be subjected to levy of additional income tax under sub-section (2) of section 115R.

[Notification NO. 6/2014, dated 11-02-2014]

DIRECT TAX CODE 2013

Background

Recently, the Finance Minister has released the Direct Taxes Code, 2013 (DTC 2013) for public discussion/comments. The first version of DTC was introduced in August 2009 when Government unveiled the DTC along with a discussion paper to replace the Income-tax Act, 1961 (the Act) and the Wealth Tax Act, 1957. In June 2010, the Government released the revised discussion paper incorporating several changes to address concerns over some major issues arising there from.

In August 2010, the Government tabled a revised version in the form of DTC 2010 in the Lok Sabha which was then referred to the Standing Committee on Finance (SCF) for its review and comments. The Standing Committee after deliberating with the recommendation given by various stakeholders submitted their report to the Parliament on 9 March 2012.

Thereafter, in September 2012, Kelkar Committee in its report on 'Road Map for Fiscal Consolidation' suggested a comprehensive review of DTC. Hence, Government decided to revise the DTC after considering suggestions given by SCF and present the revised version in the parliament. As per news reports, out of 190 recommendations made by SCF, 153 are proposed to be accepted wholly or in part. Some of the key recommendations accepted include exemption to taxation of income from indirect transfer for shareholders having small shareholdings (up to 5 per cent), modification in definition of place of effective management, broad based General Anti avoidance Rules (GAAR), etc. The following paragraphs give an overview of the provisions of DTC 2013. We trust you would find these useful.

International Tax

- ***Indirect transfer of shares of an Indian company***

  DTC 2013 has provided that an asset or a capital asset, being any share or interest in a company or entity registered outside India shall be deemed to be situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets (whether tangible or intangible) located in India.

  The share or interest shall be deemed to derive its value substantially from the assets (whether tangible or intangible) located in India, if on the specified date, the value of such assets:

  - Exceeds the amount as may be prescribed; or

  - Represents at least twenty per cent of the Fair Market Value (FMV) of all the assets owned by the company or entity, as the case may be.

DTC 2010 provided for a 50 per cent threshold of global assets to be located in India for taxation of income from indirect transfer in India. Based on the recommendation of SCF, that the threshold was too high, the DTC 2013 now provides for a threshold of 20 per cent of global assets to be located in India for taxation of income from indirect transfer in India.

DTC 2013 proposes to exempt small shareholder who does not hold the right of management or control exceeding 5 per cent directly or indirectly and on satisfaction of certain prescribed condition. This was also recommended by SCF. However, recommendations related to exemption on transfer of listed shares outside India and overseas intragroup restructuring are not accepted.

SCF had also recommended that the criteria for computing the FMV of the assets could be applied on a particular date instead of any time during the 12 months preceding the transfer. This recommendation is accepted in DTC 2013 which provided the definition of 'specified date' as the date on which accounting period of company /entity whose share/interest is transferred ends and which immediately precedes the date of transfer of the asset share/interest in the company.

- ***Place of effective management***

DTC 2013 has provided that a foreign company is considered to be a resident in India if its Place of Effective Management (POEM) at any time in the year is in India.

POEM has been defined to mean the place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are in substance made. However, under the Act, foreign company is treated as resident in India only when its place of control and management of its affairs is situated wholly in India.

The definition of POEM has been changed from earlier version of DTC. This change is in line with the SCF's recommendation that that term 'executive directors', and 'officers' may be removed from the definition of POEM and the definition should be more objective and in line with internationally accepted standards.

Accordingly, a foreign company having POEM in India will be treated as a tax resident in India and would be consequently liable to be taxed in India on its global income.

- ***Widening of source rules***

The scope of 'royalty' under the Act has been extended retrospectively with effect from 1 June 1976. These provisions have been proposed to be introduced under DTC 2013. In addition to that, DTC 2013 further expanded the scope of royalty to include consideration for the use or right to use transmission by satellite, cable, optic fibre or similar technology, use or right to use ship or aircraft, transfer of all or any rights (including the granting of a license) in respect of live coverage of any event and cinematographic films or work on films, tapes or any other means of reproduction.

Further, the Act provides for taxation of interest payable by the non-resident in respect of any debt incurred and used for the purpose of business carried on by the non-resident in India. DTC 2013 expanded the scope of this provision to include interest payable by the non-resident in respect of any debt incurred and used for the purpose of earning any income from any source in India. Thus, interest paid, though not claimed as deduction in India, would still be taxable by virtue of the extended source rule.

- ***Availment of tax treaty benefit***

The tax treaty related provisions under DTC 2013 are in line with the provisions of the Act. The beneficial provisions of the tax treaty would prevail over the Act.

However, beneficial provisions of the tax treaty may not apply where GAAR, branch profit tax and

Controlled Foreign Company (CFC) related provisions are invoked. DTC 2013 provides that liability of foreign company on account of branch profit tax cannot be treated as discriminatory.

Under DTC 2013, the taxpayer can claim tax treaty benefit only if it obtains Tax Residency Certificate (TRC) from the specified authority of the foreign territory. Further, such taxpayer also needs to obtain\ other documents and information, as may be prescribed. The Indian Government is empowered to issue notification defining terms which are not defined under DTC 2013 or the tax treaty and the same meaning will be deemed to take effect from the date when the concerned tax treaty came into force.

- ***Levy of branch profit tax***

Under DTC 2013, every foreign company, in addition to income-tax payable, is liable to pay branch profit tax at the rate of 15 per cent in respect of branch profits of a financial year. As compared to the provisions of the Act, DTC 2013 reduces corporate income-tax rate for foreign companies from 40 per cent to 30 per cent, which is in line with the tax rate of domestic companies. However, branch profit tax is levied additionally.

Branch profit tax is levied on income attributable, directly or indirectly, to the Permanent Establishment (PE) or an immovable property situated in India, as reduced by the amount of income-tax payable on such attributable income. Branch profit tax is applicable irrespective of the tax treaty. Accordingly, the effective tax rate for a foreign company would be 40.5 per cent on income attributable to its Indian PE.

- **General Anti-Avoidance Rules**

Provisions of GAAR were originally introduced in DTC 2009. Subsequently, GAAR has been included in the Act with certain modifications. GAAR applies to transaction which are ‘impermissible avoidance arrangement’. The proposed GAAR provisions under DTC 2013 are in line with the Act with a few modifications. DTC 2013 proposes to expand the definition of ‘connected person’ to include company carrying on business or profession in which the holding company has substantial interest.

Under the Act, the entire arrangement may be declared as impermissible arrangement even if a part of arrangement is impermissible arrangement. The SCF had proposed that it needs to be clarified only that part of the arrangement would be invoked which is proved as ‘impermissible’. However, the same has not been accepted in DTC 2013.

The Standing Committee had recommended that the onus of proof should rest on the tax authority invoking GAAR.

However, DTC 2013 proposes to rest the onus of proof on the taxpayers.

- **Controlled Foreign Company**

  CFC provisions were first introduced in DTC 2010 to limit artificial deferral of tax by using offshore low taxed entities. It enables to tax the income of foreign companies situated in low tax jurisdiction but are controlled by the resident entities. The CFC provisions are as follows:

  The total income of a resident taxpayer to include income attributable to a CFC, which is defined to mean a foreign company:

  - which is a resident of a 'territory with lower rate of taxation' (i.e. where taxes paid are less than 50 per cent of taxes on such profits as computed under DTC);
  - whose shares are not listed on any stock exchange recognized by such territory;
  - which is individually or collectively controlled by persons resident in India (through capital, voting power, income, assets, dominant influence, decisive influence, etc.); and
  - Which is not engaged in active trade or business (i.e. it is not engaged in commercial, industrial, financial undertakings through employees/personnel) and more than 251 per cent of its income comprises passive income (dividend, interest, etc.) The above provisions continue to be in line with DTC 2010, except the following:
  - DTC 2013 provides that in computing the rate of tax in the foreign jurisdiction, for the purpose of determining coverage under the CFC regime, the credit of foreign taxes paid by the foreign entity shall be included in taxes paid.
  - It lowers the threshold of 'passive income' proportion of the foreign company, to 25 per cent of its income (from 50 per cent in DTC 2010).
  - It includes a provision empowering the Central Government to notify a country or specified territory outside India as not being 'a territory with lower rate of taxation' having regard to tax rates and tax exemptions prevailing therein.

The specified income of CFC shall be treated as 'Nil' if it is negative or less than INR 2.5 million. DTC 2013 provides that no adjustment shall be made to the income attributable to CFC on account of transfer pricing adjustment in respect of the international transaction between Indian resident entity and CFC.

Dividend received in a subsequent year from a foreign company to whom provisions of CFC apply, will be reduced from the total income to the extent it has been taxed as CFC attributable income in any preceding financial year.

Corporate Tax

- ***Computation of income from business***

DTC 2013 has proposed that certain businesses for e.g. as covered under section 80-IA, 80-IB, 80-IC (certain specified undertakings) etc of the Act shall be treated as distinct and separate business and its income shall be computed separately. SCF recommendations have not been accepted in this regard.

The profits from any business, other than Specified businesses whose income is dealt by the relevant schedules, shall be the gross earnings from the business as reduced by the amount of business expenditure incurred.

Gross earnings are listed in detail in DTC 2013 and include accruals and receipts connected with business. Key inclusions are as follows:

- Amount received on cessation, termination or forfeiture of any agreement entered into in the course of business.
- Consideration for transfer of carbon credits.
- Profits on transfer of business capital assets.
- Any amount accrued or received as advance or security deposit from a log-term lease or transfer of a business asset.
- Outstanding stagnant balance of creditor for more than five years, except where recovery suit/ arbitration is pending or where beneficiary is a sick industrial company.

Business expenditure in DTC 2013 is broadly classified into the following three mutually exclusive categories: (a) Operating expenditure, (b) Permitted financial charges, (c)

Capital allowances. There is a detailed listing of qualifying operating expenditure which also includes a residuary clause to cover any other expenditure if it is laid out or expended wholly for the business purpose and is not capital in nature.

DTC 2013 clarifies that a person who has acquired the assets on a finance lease will be deemed to be the owner of the asset.

DTC 2013 has reduced the weighted deduction for scientific research and development allowance from 200 per cent to 150 per cent. However, unlike DTC 2010 which allowed deduction to all the companies, DTC 2013 allows deduction only to the company engaged in the business of biotechnology or in the business of manufacture or production of any article or thing, not being an article or thing specified in Fourteenth Schedule.

- ***Deduction for corporate social responsibility related expenditure***

Under the Companies Act, 2013, any specified company should mandatorily spend 2 per cent of their net profits in every financial year on CSR activities.

DTC 2010 and the Act do not include specific provisions for allow ability of the expenditure incurred on CSR activities.

Accordingly, the Committee had recommended that tax deduction for CSR expenditure in backward regions and districts may be provided to encourage more CSR activities in places where it is required. However, the DTC 2013 does not provide for allow ability of CSR expenditure. The website of the Income-tax department2 provides a rational that the CSR expenditure cannot be allowed as a business deduction as it is an application of income. Further, allowing deduction for CSR expenditure would imply that the government would be contributing one third of this expenditure, as revenue foregone.

- ***Minimum alternate tax***

DTC 2013 proposes to levy MAT at the rate of 18.5 per cent as against the earlier rate of 20 per cent provided under DTC 2010. MAT is levied if the tax liability under the regular provisions is lower than 18.5 per cent of the book profits (after prescribed additions/deletions). The provisions of MAT are applicable to Insurance, Banking and Electricity companies as well. However, income from life insurance business is not covered under the MAT provisions of DTC 2013.

The carry forward of MAT credit is allowed for 10 years under DTC 2013 as compared to 15 years prescribed in DTC 2010.

DTC also allows carry forward of MAT paid under the provisions of Act. This is in line with SCF's recommendations.

- ***Alternate minimum tax***

DTC 2013 proposes to introduce the provisions of Alternate Minimum Tax (AMT) applicable to a firm in line with the existing provisions under the Act. AMT is levied at the rate of 18.5 per cent if the tax liability under the regular provisions is less than the 18.5 per cent of the adjusted total income.

The adjustments relate to various investments and deductions as allowed in the computation of the normal income. The carry forward for AMT is allowed for a period of 10 years. DTC 2013 also allows carry forward of AMT paid under the provisions of Act. This is in line with SCF's recommendations.

- **Tax on dividend received in excess of INR 10 million**

DTC 2013 proposes to introduce an additional levy of 10 per cent on the resident shareholder if the total amount of dividend received exceeds INR 10 million. Under the current provisions of the Act, once a domestic company has paid Dividend Distribution Tax (DDT) at the rate of 15 per cent, no tax is further required to be paid by a shareholder on such dividend received.

This dividend income subject to an additional levy of 10 per cent above falls under the category of 'special source' of income and no deduction of expenditure is allowed to be set-off against such income. The additional tax is to be paid by the resident shareholder over and above the DDT paid by the distributing company.

- **Income distribution tax on Mutual Funds, Securitization Trusts and Insurance companies**

DTC 2013 proposes to cast an obligation on the non-equity oriented mutual funds and Securitization Trusts to pay tax on the distribution of income at the following rates:

- 25 per cent where the payment is made to an individual/Hindu Undivided Family (HUF); and
- 30 per cent where the payment is made to any other person.

Correspondingly, the income is not taxable in the hands of recipient unit holders of mutual fund; therefore, there is no need to withhold tax.

In case of Securitization Trusts, no distribution tax is required to be paid where the payment is made to any person who is not liable to tax. The provisions pertaining to taxation of Securitization Trusts in DTC 2013 are in line with the provisions of the Act.

DTC 2013 proposes that income distribution by the life insurers to the policy holders will attract distribution tax at following rates:

- In case of an approved equity oriented insurance scheme at the rate of 5 per cent; and
- In case of scheme other than an approved equity oriented insurance scheme at the rate of 25 per cent if the payment is made to an individual/HUF and at the rate of 30 per cent if the payment is made to any other person.

Any income received from a life insurer on which the distribution tax has been paid by the life insurer is not taxable in the hands of the policy holder. Income arising under a life insurance policy is not taxable where the amount is received on completion of the original period of contract of insurance and the premium paid or payable in any of the year does not exceed 10 per cent of the capital sum assured. Tax is not required to be deducted in case of payment of income by life insurers to policy holders under any scheme. SCF had recommended that the capital sum assured should be at least 10 times of the annual premium as a pre-condition for granting tax exemption in relation to the proceeds / benefits of the life insurance policies.

The recommendations of SCF about capital sum assured being at least 10 times of the annual premium has been accepted.

☐ **Capital Gains**

DTC makes a distinction between ‘investment assets’ and ‘business assets’ and provides that gains arising from the transfer of ‘investment assets’ are taxable under the head ‘capital gains’.

DTC 2013 has proposed that ‘investment asset’ has been amended to include any self-generated capital asset in the course of business and any security held by a qualified foreign investor.

In line with the recent introduction of certain provisions3 of the Act, the scope of transfer of ‘investment asset’ is widened to include the disposing of an asset or any interest therein, or creating any interest in any asset in any manner whatsoever, directly or indirectly, voluntarily or involuntarily, by way of an agreement (whether entered into in India or outside India) or otherwise, notwithstanding the fact that such transfer of rights has been characterized as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India.

In line with the certain other provisions4 of the Act, DTC 2013 has proposed exemption for income arising on transfer of any 'investment asset' by a firm to a company as a result of succession by a company in the business carried on by the firm subject to certain conditions. SCF had recommended exemption for income arising on succession of a firm by a company as well as on transfer of asset by a firm to a company. DTC 2013 has been amended in relation to transfer of assets but not in relation to succession. It is proposed that in respect of assets acquired prior to 1 April 2000, appreciation in value till 1 April 2000 is kept out of the taxable net.

While DTC 2013 continues with exempting specified transfers, it has made provisions only for substitution of cost base, while not including specific provision providing the benefit of holding period of the transferor. Under the Act, there is litigation as to whether indexation benefit may be availed by a successor when asset is acquired under gift, inheritance, succession, etc. DTC 2013 is more specific permitting benefit of indexation from the year of acquisition of asset by the previous owner. Under the DTC 2013 for all assets other than listed securities, the applicable threshold for the asset to turn long-term is 1 year reckoned from the end of the financial year in which asset is acquired. The asset may, therefore, turn long term if held for a period of 1 year 1 day to close to two years depending on the date of acquisition of the asset.

Benefit of indexation in respect of long term capital gain may be claimed by all taxpayers. Individuals and HUF may also be entitled to the benefit of roll over exemption. Long term capital gain is however, taxed at normal rate (as against concessional tax rate in the Act)

It is proposed that in case of non-resident, any income arising from transfer of an investment asset, being a security purchased in foreign currency shall be computed in foreign currency and reconverted to Indian rupees.

Further where the full value of consideration of an 'investment asset' is not ascertainable or cannot be determined, then FMV of the said 'investment asset' on the date of transfer would be deemed to be the full value of consideration.

DTC 2013 has also proposed that 'Cost of Acquisition' of an 'investment asset' acquired on dissolution of an unincorporated body or on distribution of any asset on the liquidation of a company shall be the fair market value or the stamp duty value, as the case may be, on the date of distribution of the asset. SCF recommendation is accepted in this regard.

DTC 2013 has proposed that 'Cost of Acquisition' of an 'investment asset' acquired through any of the prescribed modes of acquisition, shall be the full value of consideration for such acquisition. The SCF had recommended that in cases of exempt transactions which are subsequently taxed on account of noncompliance of conditions, the cost in the hands of the transferee should be the full value of consideration.

Though the recommendation was in relation to those transactions which are subsequently taxed, condition of being taxed has been skipped, and replacement of higher cost is allowed to all the transactions. DTC 2013 has proposed that 'Cost of Acquisition' should include prescribed expenditure incidental to purchase, if borne by the person. In this relation, the SCF recommendations have been accepted. This a restrictive provision, till now all such expenditure were allowed. DTC 2013 has proposed that the specified deemed income, taxable as capital gains, shall be deemed to be the income of the successor, if the predecessor ceases to exist in the financial year in which the transfer is taxable. SCF recommendation is accepted in this regard. DTC 2013 has proposed that for computation of indexed cost of acquisition / improvement, the benefit of period of holding

by the previous owner, in case of transfer by special modes, should be provided and thereby increasing such indexed cost. SCF recommendation is accepted in this regard. DTC 2013 has proposed that any amount by way of advance, security deposit or of similar nature received and retained on account of negotiations for transfer of whole or part of, or any interest in, any ‘investment asset’ is made as gross residuary income. DTC 2013 has proposed that in case of compulsory acquisition, the period for acquiring new asset or the period for depositing the amount for claiming rollover benefit, shall be reckoned from the date of receipt of the compensation. SCF recommendation is accepted in this regard. DTC 2013 proposes an exemption from capital gains tax arising on conversion of an Indian branch of a foreign bank into a subsidiary company.

The following recommendations of the Standing Committee have not been accepted:

- For the purposes of determining the cost of an ‘investment asset’ received on retirement by a participant from an unincorporated body, the FMV on the date of distribution to be considered as cost of acquisition.

- The security held by Foreign Institutional Investors (FII) should not be included in the definition of ‘investment asset’.

☐ **Conversion of partnership firm into LLP/Company**

Presently, conversion of a partnership firm into a Limited Liability Partnership (LLP) or a company is exempt from tax under the Act on fulfillment of certain conditions. There was no clarity on this aspect in the earlier version of DTC. The Committee had recommended that tax neutrality may be provided on conversion of a partnership firm into a LLP or a company.

DTC 2013 has provided that transfer of any investment asset by a firm to company as a result of conversion of the firm into LLP/company in accordance with the provisions of relevant Act shall be exempt if specified conditions are satisfied.

☐ **Residuary Income**

DTC 2013 proposes to tax the amount of voluntary contribution received by a person, other than an individual or a HUF or a non-profit organization, by including it in the gross residuary income. Further it proposes to include any income of a resident attributable to CFC as a residuary income. DTC 2013 also proposes to include any amount received as advance, security deposit or otherwise, from the long-term leasing of any interest in any investment asset, etc. as the residuary income.

☐ **Carry forward and set-off of losses**

Losses brought forward under the head, income from house property, income from business or profession, income from speculation business and income from activity of owning and maintaining race horses under the Act shall be set-off and carried forward against the income computed under DTC 2013 in a prescribed manner. Losses brought forward under the head capital gains (whether short term or long term) under the Act shall be set-off and carried forward against the income computed under the head capital gains in DTC 2013 up to 8 financial years. SCF‘s recommendation on carried of forward capital loss is accepted. In respect of losses incurred in subsequent years, DTC 2013 provides intra-source and intra-head set-off of loss from

ordinary sources for an unlimited period. However, speculative loss, capital loss, loss from activity owning and maintaining of horses, tonnage tax scheme, etc. can be carried forward for limited period. There are special rules which regulate losses incurred in investment linked tax holiday activities.

Loss incurred by the predecessor/transferor entity can be carried forward by successor entity in case of business reorganization of residents (amalgamation and demerger), corporatization of non-corporate entities and conversion into LLP, etc. provided the predecessor was in the business for at least 3 years and the successor satisfies the continuity of the business test by continuing the business of the predecessor for 5 years. Further specific provisions on quantification of loss to be transferred on demerger have been proposed in DTC 2013.

- **Collection and recovery of tax**

DTC 2013 requires a person to deduct tax on the specified payments to a non-resident at the appropriate rate. However, for the payments which are not specified, an amount paid is to be deducted only if it is chargeable to tax. Under the Act, payments to non-resident which are chargeable to tax are subject to deduction of tax at source. SCF had recommended to bring these provisions in line with the Act which has not been accepted.

Under DTC 2013, a person shall not be called upon to pay tax himself to the extent tax is deductible and has been so deducted from payment made to him. This is in accordance with the recommendations made by SCF. The provisions similar to those under the Act with respect to prescribing of time limit for passing an order for default in deducting/collecting taxes at source, higher deduction of tax for non-furnishing of Permanent Account Number (PAN), higher deduction of tax for transactions with persons located in Notified Jurisdictional Area, issue of lower/nil tax deduction certificate by Assessing Officer, non-deduction of tax on certain payments on furnishing of declaration, etc. are now proposed under DTC 2013.

In line with the Act, the payments made to a non-resident of a country with which India has entered into a tax treaty, and where the tax treaty provides for a lower rate of tax, then such lower rate is to be adopted for deduction of tax. The concern raised due to the language of DTC 2010 as regards time for deduction of tax has been clarified in DTC 2013 by deeming a specified payment to be made, if such payment has been made by credit to the account of the payee or any other account, whether called suspense or by any other name. The change is in line with the recommendation made by SCF. DTC 2013 proposes a significant amendment to allow an employer to consider any other income of the employee while deducting tax under the head 'income from employment', provided the income does not have the effect of reducing the tax deductible on income under the head 'Income from employment'. A threshold has been proposed for non-deduction of tax in respect of the following payments:

- Royalty, fees for professional/ technical service and non-compete fees paid to residents - INR 30,000
- Consideration paid for transfer of immovable property - INR 500,000
- Interest received on time deposits by senior citizens – INR 20,000 DTC 2010 requires every seller, who is receiving an amount in cash for sale of bullion or jewellery to collect 1 per cent of sale consideration from the buyer subject to a prescribed ceiling.

SCF recommended definitions of various terms such as commission, brokerage, rent, professional service, etc. The same have been accepted under the DTC 2013.

The rates for deduction of tax proposed under DTC 2013 are as follows:

Interest (other than specified interest)	20per cent
Specified Interest (interest to FII or QFI between 1 June 2013 and 1 June 2015, interest on monies borrowed in foreign currency, interest on infrastructure debt fund payable to a non-resident)	5per cent
Dividend other than dividends subject to DDT	20per cent
Royalty or Fees for Technical Services (FTS)	25per cent
Winning from lottery, or crossword puzzle or card game or any other game of gambling or betting	30per cent
Winning from race, including horse race	30per cent
Payment to non-resident sports person and by way of guarantee money to a non-resident sports association or institution in relation to any game or sport played in India	10per cent
Payment to non-resident entertainer in respect of his performance in India	10per cent
Payment by way of insurance including reinsurance	20per cent
Any other sum, if chargeable to tax	30per cent

Computation of total income

Under DTC 2013, income is broadly classified into two categories for computing total income i.e. 'ordinary sources' and 'special sources'. The income classified under 'ordinary sources' is in line with the Act viz. income from employment, house property, business income, capital gains and residuary sources. However, the income from special sources includes investment income, royalty/FTS, etc. Accordingly, total income of taxpayer is an aggregate of total income from 'ordinary source' and 'special source' DTC 2013 proposes to expand the scope of 'special source' income so as to include within its ambit the value of investments; value of bullion jewellery, other valuable article or money owned; amount credited in books; amount of expenditure incurred if one of the following conditions is satisfied viz. there is no explanation; an explanation is offered but there is a failure to substantiate the same; or the explanation offered is not to the satisfaction of the AO.

- **Transfer Pricing**

On the Transfer Pricing front, DTC 2013 has not been significantly amended vis-à-vis DTC 2010. Consequential amendments in relation to international transactions, Specified Domestic Transactions (SDT), tolerance band, safe harbor, Advance Pricing Agreements (APA), etc. have been proposed to be in line with the existing provisions of the Act.

One of the significant change is an expansion in the definition of 'associated enterprise' to include 'associated persons' in respect of SDT (i.e. persons covered under Section 40A (2) (b) of the Act). In the absence of profit linked deductions under DTC 2013, SDT is not applicable in respect of transactions under profit linked deductions.

However, DTC 2013 is silent as regards grandfathered profit linked deductions. As compared to elaborate definition of 'intangible property' under the Act, DTC 2013 has provided a shorter and inclusive definition of this term.

A few recommendations made by SCF on APA that it is to be concluded in a time bound manner and it should be a part of the tax treaties have not been accepted in DTC 2013.

Tax on income received from Venture Capital Company and Venture Capital Fund

The provisions relating to taxability of income of Venture Capital Fund (VCF) or Venture Capital Company (VCC) under DTC 2013 have been aligned with the following provisions of the Act:

- Only Securities and Exchange Board of India (SEBI) registered Category I Alternate Investment Fund (AIF), sub category VCF and existing VCFs/VCCs registered under the SEBI VCF regulations are per se eligible for the automatic tax pass through.
- The tax pass through is available only in respect of income from venture capital undertakings (VCU). Sectoral restrictions have been dispensed with and the definition of VCU has been made in line with the definition of VCU under the respective SEBI regulations.
- Income of the qualifying AIF/VCF/VCC will be subject to tax in the hands of investors on an accrual basis irrespective of actual distribution thereof by the qualifying AIF/VCF/VCC to the investors. The Act provides for a withholding tax exemption on income paid by qualifying AIF/VCF/VCC to its investors. However, such withholding tax exemption is not provided for in DTC 2013 (nor was such an exemption present in DTC 2010).

☐ **Wealth Tax Provisions**

Under the Wealth Tax Act, 1957, tax is payable in respect of the net wealth on the corresponding valuation date by every individual, HUF and Company. The wealth tax is levied at the rate of 1 per cent of the amount by which the net wealth exceeds INR 3 million. Further, the wealth tax is levied with reference to only certain specified assets subject to certain exemptions.

Under DTC 2013, every individual, HUF and private discretionary trust, will be liable to pay tax on the net wealth on the valuation date of a financial year. It also provides a list of assets which are not subject to wealth tax. The proposed asset base is very wide compared to the present Wealth-tax Act. DTC 2013 captures all assets, physical or financial (including listed and unlisted shares), for wealth tax as against only unproductive assets captured in DTC 2010. Nonresidents, foreign citizens and foreign companies may not be required to pay wealth tax in respect of assets situated outside India. Further, valuation rules may be prescribed for determining the value of net wealth. Individuals, HUF's and private discretionary trusts are subject to wealth tax at rate of 0.25 per cent. Further, in case of individuals and HUF threshold limit is prescribed as INR 500 million. However, DTC 2010 had provided for threshold limit of INR 10 million and tax rate of 1 per cent of net wealth exceeding that limit

Clarification in case where income of the firm is exempt

It is clarified that the Total Income of the Firm for sub-section (2A) of Section 10 of the Act, income which is exempt or deductible under various provisions of the act, is to be taxed in the hands of the firm only and the same under no circumstances be taxed in the hands of its Partners.

Accordingly entire profit credited to partners' capital account in the firm would be exempt from tax in the hands of such partners even if the income chargeable to tax in the hands of the firm is Nil on account of any exemption or deduction.

[Notification NO. 8/2014, dated 31-03-2014]

Guidelines for approval of agricultural extension project under section 35CCC

- The agricultural extension project shall be considered for notification if it fulfils all of the following conditions, namely:-
  - the project shall be undertaken by an assessee for training, education and guidance of farmers;
  - the project shall have prior approval of the Ministry of Agriculture, Government of India; and
  - An expenditure (not being expenditure in the nature of cost of any land or building) exceeding the amount of Rs 25,00,000 is expected to be incurred for the project.
- Before undertaking any agricultural extension project, an assessee shall make an application in Form No.3C-O to the Member (IT), Central Board of Direct Taxes for notification of such project under sub-section (1) of section 35CCC.
- The application referred to in sub-rule (2) shall be accompanied by the following, namely:-
  - a detailed note on the agricultural extension project to be undertaken by the assessee;
  - details of the expenditure expected to be incurred on the project and expected date of completion of the project; and
  - A letter approving the project and specifying the amount of expenditure expected to be incurred on the project from the Ministry of Agriculture, Government of India.
- Where any defect is noticed in the application referred to in sub-rule (2) or a relevant document is not attached thereto, the Central Board of Direct Taxes shall, before the expiry of the month from the date of receipt of the application in its office, intimate the defect to the applicant for its rectification.
- The applicant shall remove the defect within a period of fifteen days from the date of such intimation or within such further period as may be extended by the Central Board of Direct Taxes, on an application made in this behalf by the applicant, so however, that the total period for removal of defect does not exceed thirty days, and if the applicant fails to remove the defect within such period as allowed, the Central Board of Direct Taxes shall pass an order treating the application as invalid.
- If the application form is complete in all respects, the Central Board of Direct Taxes shall, within a period of one month from the end of the month in which it receives the application form complete in all respects, issue under sub-section (1) of section 35CCC, a notification in form No. 3CP to be published in Official Gazette specifying the agricultural extension project, subject to the conditions mentioned in rule 6AAE or such other conditions, as it may deem fit, to be effective for such period not exceeding three assessment years.

- The assessee may, atleast two months before the expiry of the effective period of the notification issued under sub-rule (6), make an application to the Central Board of Direct Taxes for notification of such project for a further period.

- The Central Board of Direct Taxes shall, after receiving the application under sub-rule (7), call for a report from the Commissioner of Income-tax or the Director of Income-tax, as the case may be, having jurisdiction over the case regarding the activities of the agricultural extension project during the period of notification and fulfillment of conditions mentioned in rule 6AAE and any other conditions subject to which the agricultural extension project was notified under sub-rule (6).

- On being satisfied with the report received under sub-rule (8) on the agricultural extension project, the Central Board of Direct Taxes may, within a period of three months from the end of the month in which it receives application referred to in sub-rule (7), notify the said project for a further period not exceeding three assessment years.

- A copy of the notification issued under sub-rule (6) or, as the case may be, under sub-rule (9) shall be sent to the applicant, the Ministry of Agriculture, Government of India, the Commissioner of Income-tax or the Director of Income-tax, as the case may be, the Department of Agriculture of the concerned State and the Agricultural Technology Management Agency of the concerned District.

- The Central Board of Direct Taxes may, on being satisfied that the assessee has ceased its activities, or that its activities are not genuine or that its activities are not being carried out in accordance with all or any of the relevant provisions of the Act or this rule or rule 6AAE, or its activities are not being carried out in accordance with all or any of the conditions subject to which the notification was issued, pass an order for rescission of the notification issued under sub-rule (6) or sub-rule (9).

- Before any order is passed treating the application as invalid or rejecting it or rescinding the notification, an opportunity of being heard in the matter shall be given to the assessee.

- A copy of the order invalidating or rejecting the application or rescinding the notification shall be sent to the applicant, the Ministry of Agriculture, Government of India, the Commissioner of Income-tax or the Director of Income-tax, as the case may be, the Department of Agriculture of the concerned State and Agricultural Technology Management Agency of the concerned district."

[Notification NO. 18/2014, dated 21-03-2014]

Press Note on Standard Operating Procedures

Detailed instructions have been issued by the CBDT to all the assessing officers laying down a Standard Operating Procedure (SOP) for verification and correction of demand by the AOs. As per this SOP, the taxpayers can get their outstanding tax demand reduced/deleted by applying for rectification along with the requisite documentary evidence of tax/demand already paid. The SOP also makes special provisions for dealing with the tax demand upto Rs 1,00,000 in the case of Individuals and HUFs in order to accommodate certain extra ordinary situations. The SOP is expected to mitigate the long standing grievances of taxpayers by way of reduction/deletion of tax demands.

The CBDT has further noted that many taxpayers are committing mistakes while furnishing their tax credit claims in the return of income. Such mistakes include quoting of invalid/incorrect TAN; quoting of only one TAN against more than one TAN tax credit; furnishing information in wrong TDS Schedules in the Return Form; furnishing wrong challan particulars in respect of Advance tax, Self-assessment tax payments etc. As a result of these mistakes, the tax credit cannot be allowed to the taxpayers while processing returns despite the tax credit being there in 26 AS statement. The CBDT, therefore, desires the taxpayers to verify if the demand in their case is due to tax credit mismatch on account of such incorrect particulars and submit rectification requests with correct particulars of TDS/tax claims for correction of these demands. The rectification requests have to be submitted to the jurisdictional assessing officer in case the return was processed by such officer, or the taxpayer is informed by CPC, Bangalore that such rectification is to be carried out by Jurisdictional assessing officer. In all other cases of processing by CPC, Bangalore, an online rectification request can be made by logging in to e-filing website http://incometaxindiaefiling.gov.in as per the procedure given in detail in its Help Menu.

[Notification NO.-, dated 17-04-2014]

Treatmentof Expenditure incurred for Development of Roads/ Highways in Build-Operate-Transfer (BOT) Agreements

- The CBDT clarifies that the cost of construction on development of infrastructure facility of roads/highways under BOT projects may be amortized and claimed as allowable business expenditure under the Act.

- The amortization allowable may be computed at the rate which ensures that the whole of the cost incurred in creation of infrastructural facility of road/highway is amortized evenly over the period of concessionaire agreement after excluding the time taken for creation of such facility.

- In the case where a taxpayer has claimed any deduction out of initial cost of development of infrastructure facility of roads/highways under BOT projects in earlier year, the total deduction so claimed for the Assessment Years prior to the Assessment Year under consideration may be deducted from the initial cost of infrastructure facility of roads /highways and the cost 'so reduced' shall be amortized equally over the remaining period of toll concessionaire agreement.

- The Circular also clarifies that it is applicable only to those infrastructure projects for development of road/highways on BOT basis where ownership is not vested with the assessee under the concessionaire agreement.

[Notification NO. 09/2014, dated 23-04-2014]

New form for PAN application

Under Income-tax Rules, 1962, new Forms 49A & 49AA have been substituted instead of the old forms for Application for allotment of Permanent Account Number.

[Notification NO. 26/2014, dated 16-05-2014]

Cost of Inflation Index

Cost of Inflation Index has been issued for the F.Y. 2014-2015(A.Y. 2015-2016) as ‘1024’

[Notification NO. 31/2014, dated 11-06-2014]

Form of Return of Wealth

CBDT has prescribed new Wealth Tax Return ‘Form BB’ w.e.f. A.Y. 2014-2015 instead of old ‘Form BA’. CBDT has also prescribed that this form can be filed online with or without digital signature. For certain class of Assessee i.e. Individual/HUF not liable to tax audit, e-filing is optional but for other class of Assessees i.e. Individual/HUF liable to audit and Companies, return of net wealth in Form BB shall be furnished electronically under digital signature.

[Notification NO. 32/2014, dated 23-06-2014]

Draft SEBI (Real Estate Investment Trusts) Regulations, 2013

Background

India’s real estate sector has witnessed rapid growth in recent years underlined by robust economic growth in the country. Real Estate Investment Trusts (REITs) are common investment vehicles globally which pool monies of investors and invest primarily in completed, revenue-generating real estate assets (such as buildings, offices, warehouses, malls, etc.) and distribute a major part of the earnings among the investors. REITs are critical as they provide an exit avenue for the developers of commercial properties who can channel such monies to further commercial projects.

Previously, the Securities and Exchange Board of India (SEBI) had attempted to introduce REITs in India wherein it had issued draft regulations in 2008 but withdrew it later. Further, when the concept was revisited again, SEBI was more in favour of the mutual fund model for real estate investment. However, the same also could not materialize.

SEBI has recently issued a press release wherein it has revived an over five-year old proposal of REIT by issuing draft SEBI (Real Estate Investment Trusts) Regulations, 2013 [SEBI (REIT) Regulations]. Public comments have been invited on the same by 31 October 2013.

Key highlights of the draft SEBI (REIT) Regulations are provided below:

Structure of the REIT

- The REIT shall be set up as a Trust and shall not launch any schemes.
- The relevant parties in a REIT structure would be trustee (registered with SEBI), sponsor and manager.
- The REIT is required to be registered with SEBI.

Offer of units to the public and listing of units

Particulars	Requirements
Method /manner of raising funds	Initial Offer*
Listing	Mandatory
Conditions for Initial Offer	Asset size >= Rs. 10,000million
	Minimum Initial Offer size –Rs. 2,500 million
	Minimum public float of 25per cent
Eligible Investors	Resident or Non-resident (Initially shall be offered only to HNIs/institutions)
Minimum subscription size / unit size	Rs. 0.2 million / Rs. 0.1 million

*REIT should come out with initial offer within 18 months of registration with SEBI.

Key eligibility criteria for Sponsor and Manager of REIT

Sponsor

- Sponsor should have minimum net worth of INR 200 million on a consolidated basis.
- Sponsor should hold at least 25 percent of the total units of the REIT prior to initial offer.
- Minimum holding of 25 percent of the sponsor will be locked in for three years from the date of listing and balance holding will be locked in for one year.
- Sponsor should hold at least 15 percent of the outstanding units of the REIT at all times. If sponsor proposes to sell the units below 15 percent after three years from the date of listing, it shall arrange for other person / entity to act as the re-designated sponsor.
- Sponsor should have atleast five years of experience in the real estate industry on a standalone basis.

Manager

- Manager should have minimum net worth of INR 50 million.
- Manager should have atleast five years of specified relevant experience.
- Manager should have minimum two key personnel in its investment committee with five years of specified relevant experience.

Eligible Investors

- REITs may raise funds from any investor, whether resident or foreign (subject to guidelines specified by RBI and government).

- However, initially, till the market develops, it is proposed that the units of the REITs may be offered only to HNIs / institutions and therefore, it is proposed that the minimum subscription size shall be INR 2 lakhs per investor and the unit size shall be INR 1 lakh.

- REITs should have a minimum of 20 investors (other than related parties).

Investment conditions and dividend policy

- Investment by a REIT shall only be in properties or securities in India

- At least 90 percent of the value of the REIT assets shall be in completed (i.e. occupancy certificate received) and rent generating properties (i.e. 75 percent rented / leased out); and

- Balance can be invested in the specified assets [like developmental properties, listed or unlisted debt, mortgage backed securities (MBS), equity shares of real estate companies, government securities or money market instruments, etc, subject to specified conditions].

- REITs will not be permitted to invest in vacant land or agricultural land or mortgages (other than MBS).

- REITs will be permitted to invest in properties through a Special Purpose Vehicles (SPV) if SPV holds atleast 90 percent of their assets directly in specified real estate properties and

- REIT has control over the SPV.

- REITs are permitted to invest entire corpus in one project.

- REITs cannot undertake investment in other REITs.

- Atleast 75 percent of the revenues of the REIT (other than gains arising from disposal of properties) shall be from rental, leasing and letting real estate assets at all times.

- In case of co-investment with any person, few conditions are specified which, inter alia, includes that the investment by other person shall not be at terms more favourable than those of REIT.

- Atleast 90 percent of the net distributable income after tax of the REIT should be distributed to the unit holders.

Borrowings and deferred payments

- Aggregate consolidated borrowings and deferred payments of the REIT have been capped at 50 percent of the value of the REIT assets.

- If the same exceeds 25 percent of the REIT assets, credit rating from SEBI registered credit rating agency and approval of unit holders would be required.

Valuation of assets

- Full valuation including a physical inspection of the properties should be carried out at least once a year (with every six monthly updation in the valuation).
- For any purchase of a new property or sale of an existing property, full valuation to be undertaken and the transaction shall not be less than 90 percent / not more than 110 percent of the assessed value of the property for sale / purchase of assets respectively.

Other Key Aspects

- All unit holders of the REIT shall enjoy equal voting rights.
- Rights of Investors and specified matters (like change in manager or sponsor, transaction value exceeding 15 percent of REIT assets, etc.) wherein approval of investors are required have been specified.
- Stringent conditions have been imposed for related party transactions including detailed disclosures, valuation requirements, investor approval, etc.
- Detailed disclosure norms have been specified (including mandatory disclosure requirements in the offer document, valuation report, annual and half yearly report).

INCOME TAX – DOMESTIC TAXATION

SUPREME COURT DECISION

SECTION 36(1)(v): APPLICATION OF THE PRINCIPLES OF REASONABLE CONSTRUCTION TO GIVE EFFECT TO THE PURPOSE AND INTENTION OF ANY PARTICULAR PROVISION OF THE ACT

In the case of CIT vs. Textool Co., Supreme Court held that a strict construction of a provision does not rule out the application of the principles of reasonable construction to give effect to the purpose and intention of any particular provision of the Act. From a bare reading of Section 36(1)(v), it is manifest that the real intention behind the provision is that the employer should not have any control over the funds of the irrevocable trust created exclusively for the benefit of the employees. On facts, it is evident that the assessee had absolutely no control over the fund created by the LIC for the benefit of the employees of the assessee and further all the contribution made by the assessee in the said fund ultimately came back to the Textool Employees Gratuity Fund, approved by the CIT. Thus, the conditions stipulated in section 36(1) (v) were satisfied and the assessee company was entitled to a deduction u/s. 36(1) (v) in respect of payment made directly to LIC towards employees Group Gratuity Fund duly approved by CIT. **[2013] 35 taxmann.com 639 (SC)**

SECTION 2(47)/ 54: IF AN AGREEMENT TO SELL IS ENTERED INTO WITHIN THE PRESCRIBED PERIOD, THERE IS A TRANSFER OF SOME RIGHTS IN FAVOUR OF THE VENDEE. FACT THAT SALE DEED COULD NOT BE EXECUTED WITHIN THE TIME LIMIT OWING TO SUPERVENING PROBLEM IS NOT A BAR FOR SECTION 54 EXEMPTION

In the case of Sanjeev Lal vs. CIT, Supreme Court held that exemption u/s. 54 should be given if agreement to sell is entered into by the purchaser and sale deed could not be executed within time limit owing to supervening problem. The Apex court observed as under:

- The consequences of execution of the agreement to sell are very clear and they are to the effect that the appellants could not have sold the property to someone else. There are events when a person, even after executing an agreement to sell an immoveable property in favour of one person, tries to sell the property to another. Such an act would not be in accordance with law because once an agreement to sell is executed in favour of one person, the said person gets a right to get the property transferred in his favour by filing a suit for specific performance and therefore, some right, in respect of the said property, belonging to the appellants had been extinguished and some right had been created in favour of the vendee/transferee, when the agreement to sell had been executed.

- A right in respect of the capital asset in this case had been transferred by the appellants in favour of the vendee/transferee on 27.12.2002. The sale deed could not be executed for the reason that the appellants had been prevented from dealing with the residential house by an order of a competent court, which they could not have violated.

- A purposive interpretation of the provisions of the Act should be given while considering a claim for exemption from tax and one can very well interpret the provisions of Section 54 read with Section 2(47) of the Act, i.e. definition of "transfer", which would enable the appellants to get the benefit under Section 54 of the Act. **[Unreported]**

SECTION 80HHC: MEANING OF THE WORD "TURNOVER" IN SECTION 80HHC EXPLAINED. SALE PROCEEDS OF SCRAP IS NOT "TURNOVER" FOR SECTION 80HHC. REVENUE SHOULD ENCOURAGE ASSESSEES TO BRING IN FOREIGN EXCHANGE

In the case of CIT vs. Punjab Stainless Steel Industries, it was held by the Apex Court as under:

- The word "turnover" means only the amount of sale proceeds received in respect of the goods in which an assessee is dealing in.

- The sale proceeds from the scrap may either be shown separately in the Profit and Loss Account or may be deducted from the amount spent by the manufacturing unit on the raw material. When such scrap is sold the sale proceeds of the scrap cannot be included in the term 'turnover' for the reason that the unit is engaged primarily in the manufacturing and selling of steel utensils and not scrap of steel.

- Hence, the proceeds of such scrap would not be included in 'sales' in the Profit and Loss Account of the assessee. The situation would be different in the case of a person who is primarily dealing in scrap. **[2014] 46 taxmann.com 68 (SC)**

SECTION 132B(4)(b)/240/244A: ASSESSEE IS ENTITLED TO INTEREST ON CASH APPROPRIATED DURING SEARCH EVEN IF REFUND IS DIRECTED IN APPEAL PROCEEDINGS

In the case of Chironjilal Sharma HUF vs. UOI**,** Supreme Court held that the assessee is entitled to simple interest on cash appropriated during search. The Apex Court observed as under:

- The department's argument that the refund of excess amount is governed by Section 240 and that Section 132B (4) (b) has no application is not acceptable. Section 132B (4) (b) deals with pre-assessment period and there is no conflict between this provision and Section 240 or for that matter Section 244A.

- The former deals with pre-assessment period in the matters of search and seizure and the later deals with post assessment period as per the order in appeal.**[Unreported]**

SECTION 133(6): ASSESSING OFFICER EMPOWERED TO LAUNCH FISHING AND ROVING ENQUIRY WITH A VIEW TO DETECT TAX EVASION

In the case of Kathiroor Service Co-operative Bank Ltd vs. CIT, the Supreme Court held that the legislative intention behind Section 133(6) was to give wide powers to the IncomeTax Department to gather general particulars in the nature of survey and store those details in the computer so that the data so collected can be made use of for checking evasion of tax effectively. It would not fall under the restricted domains of being "area specific" or "case specific." Section 133(6) does not refer to any enquiry about any particular person or assessee, but pertains to information in relation to "such points or matters" which the assessing authority issuing notices requires. The information of general nature can be called for and names and addresses of depositors who hold deposits above a particular sum are certainly permissible.**[2013] 39 taxmann.com 49 (SC].**

SECTION 158BC/ 158BD: LAW ON HOW AND WHEN "SATISFACTION" HAS TO BE RECORDED BY ASSESSING OFFICER TO ATTAIN JURISDICTION OVER NON-SEARCHED PERSON EXPLAINED

In the case of CIT vs. Calcutta Knitwears, the Apex Court held as under:

- For the purpose of Section 158BD, a satisfaction note is sine qua non and must be prepared by the Assessing Officer before he transmits the records to the other Assessing Officer who has jurisdiction over such other person. The satisfaction note could be prepared at either of the following stages:

    - At the time of or along with the initiation of proceedings against the searched person u/s 158BC of the Act.

    - Along with the assessment proceedings u/s 158BC of the Act.

    - Immediately after the assessment proceedings are completed u/s 158BC of the Act of the searched person. **[2014] 43 taxmann.com 446 (SC)**

SECTION 244A: DEDUCTOR ENTITLED TO INTEREST ON REFUND OF EXCESS TDS FROM DATE OF PAYMENT

In the case of UOI vs. Tata Chemicals Ltd, it was held by the Apex Court as under:

- Providing for payment of interest in case of refund of amounts paid as tax or deemed tax or advance tax is a method now statutorily adopted by fiscal legislation to ensure that the aforesaid amount of tax which has been duly paid in prescribed time and provisions in that behalf form part of the recovery machinery provided in a taxing Statute.

- Refund due and payable to the assessee is debt-owed and payable by the Revenue. The Government, there being no express statutory provision for payment of interest on the refund of excess amount/tax collected by the Revenue, cannot shrug off its apparent obligation to reimburse the deductor's lawful monies with the accrued interest for the period of undue retention of such monies.

- The obligation to refund money received and retained without right implies and carries with it the right to interest. **[2014] 43 taxmann.com 240 (SC)**

SECTION 260A(4): HIGH COURT HAS POWER TO HEAR THE APPEAL ON QUESTIONS NOT FORMULATED AT THE STAGE OF ADMISSION

In the case of CIT vs. Mastek Limited*, the Apex court held that the proviso following the main provision of Section 260A(4) of the Act states that nothing stated in subsection (4), i.e., 'The appeal shall be heard only on the question so formulated' shall be deemed to take away or abridge the power of the Court to hear, for reasons to be recorded, the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.

The High Court's power to frame substantial question(s) of law at the time of hearing of the appeal other than the questions on appeal has been admitted remains under Section 260A(4). This power is subject, however, to two conditions:

- The Court must be satisfied that appeal involves such questions.

- The Court has to record reasons therefore.

***[2013] 32 taxmann.com 380 (SC).**

SECTION 271(1)(c): UNDER EXPLANATION 1 TO SECTION 271(1)(c), VOLUNTARY DISCLOSURE OF CONCEALED INCOME DOES NOT ABSOLVE ASSESSEE OF SECTION 271(1)(c) PENALTY IF THE ASSESSEE FAILS TO OFFER AN EXPLANATION WHICH IS BONA FIDE AND PROVES THAT ALL THE MATERIAL FACTS HAVE BEEN DISCLOSED

In the case of Mak Data P. Ltd vs. CIT, Supreme Court held that the Tribunal has not properly understood or appreciated the scope of Explanation 1 to Section 271(1)(c). The question is whether the assessee has offered any explanation for concealment of particulars of income or furnishing inaccurate particulars of income. Explanation to Section 271(1)© raises a presumption of concealment, when a difference is noticed by the Assessing Officer, between reported and assessed income. The burden is then on the assessee to show otherwise, by cogent and reliable evidence. When the initial onus placed by the explanation, has been discharged by him, the onus shifts on the Revenue to show that the amount in question constituted the income and not otherwise. **[2013] 38 taxmann.com 448 (SC)**

SECTION 276CC: PROSECUTION FOR OFFENCE U/S 276CC FOR FAILURE TO FILE RETURN OF INCOME CAN BE INITIATED DURING THE PENDENCY OF ASSESSMENT PROCEEDINGS. THE STATEMENT IN THE INDIVIDUAL RETURNS OF THE PARTNERS THAT THE FIRM HAS NOT FILED A RETURN OF INCOME AS ITS ACCOUNTS ARE NOT FINALIZED DOES NOT ABSOLVE THE FIRM OF PROSECUTION FOR NON-FILING OF

RETURN OF INCOME

In the case of Sasi Enterprises vs. ACIT, Supreme Court held as under:

- ☐ The offence u/s 276CC is attracted on failure to comply with the provisions of Section 139(1) or failure to respond to the notice issued u/s 142 or Section 148 within the time limit specified therein. The contention that pendency of the appellate proceedings is a relevant factor for not initiating prosecution proceedings u/s 276CC is not acceptable.

- ☐ Section 276CC contemplates that an offence is committed on the non-filing of the return and it is totally unrelated to the pendency of assessment proceedings except for second part of the offence for determination of the sentence of the offence, the department may resort to best judgment assessment or otherwise to past years to determine the extent of the breach.

- ☐ The language of Section 276CC is clear so also the legislative intention. If it was the intention of the legislature to hold up the prosecution proceedings till the assessment proceedings are completed by way of appeal or otherwise the same would have been provided in Section 276CC itself. **[2014] 41 taxmann.com 500 (SC)**

DESPITE PRONOUNCEMENT OF VERDICT IN OPEN COURT AND SIGNING OF DRAFT JUDGEMENT, JUDGE ENTITLED TO ALTER VERDICT UNTIL JUDGEMENT IS SIGNED AND SEALED

In the case of Kushalbhai Ratanbhai Rohit vs. State of Gujarat, the Apex Court held that up to the moment the judgment is delivered, judges have the right to change their mind. There is a sort of 'locus paenitentiae' and indeed last minute alterations often do occur. Therefore, till judgment is formally delivered as the judgment of the Court, it will be a draft judgment even if it is signed beforehand. It follows that the Judge who "delivers" the judgment, or causes it to be delivered by a brother Judge, must be in existence as a member of the Court at the moment of delivery so that he can, if necessary, stop delivery and say that he has changed his mind. He may not be physically present in court but he must be in existence as a member of the Court and be in a position to stop delivery and effect an alteration should there be any last minute change of mind on his part. If he hands in a draft and signs it and indicates that he intends that to be the final expository of his views. Those are still his views at the moment of delivery if he is alive and in a position to change his mind but takes no steps to arrest delivery. It is frequently the practice to send a draft, sometimes a signed draft, to a brother Judge who also heard the case. This may be merely for his information, or for consideration and criticism. The mere signing of the draft does not necessarily indicate a closed mind. It would be against public policy to leave the door open for an investigation whether a draft sent by a Judge was intended to embody his final and unalterable opinion or was only intended to be a tentative draft sent with an unwritten understanding that he is free to change his mind should fresh light drawn upon him before the delivery of judgment. **[2014] 45 taxmann.com 250 (SC)**

IMPORTANT PRINCIPLES ON DISTINCTION BETWEEN "CONTRACT FOR SALE OF GOODS" AND "WORKS CONTRACT" EXPLAINED

In the case of Kone Elevator India Pvt. Ltd vs. State of Tamil Nadu, a five judge member of the Apex Court explained the important principles distinguishing "contract for sale of goods" and "works contract" as under:

- ☐ The works contract is an indivisible contract but, by legal fiction, is divided into two parts, one for sale of goods, and the other for supply of labour and services;

- The concept of “dominant nature test” or, for that matter, the “degree of intention test” or “overwhelming component test” for treating a contract as a works contract is not applicable;

- The term “works contract” as used in Clause (29A) of Article 366 of the Constitution takes in its sweep all genre of works contract and is not to be narrowly construed to cover one species of contract to provide for labour and service alone; and

- Once the characteristics of works contract are met with in a contract entered into between the parties, any additional obligation incorporated in the contract would not change the nature of the contract. **[2014] 45 taxmann.com 150 (SC)**

HIGH COURT DECISIONS

SECTION 40A (3): NO SECTION 40A (3) DISALLOWANCE FOR CASH PAYMENTS EVEN IF RULE 6DD (j) EXCEPTION DOES NOT APPLY IF THERE IS NO DISPUTE AS TO GENUINENESS OF PAYMENT AND BUSINESS COMPULSION

In the case of Anupam Tele Services vs. ITO*, Gujarat High Court observed as under:

- Section 40A (3) and Rule 6DD are not intended to restrict business activities. The terms of Section 40A (3) are not absolute. Considerations of business expediency and other relevant factors are not excluded. Genuine and bona fide transactions are not taken out of the sweep of the section.

- It is open to the assessee to furnish to the satisfaction of the Assessing Officer the circumstances under which the payment in the manner prescribed in Section 40A (3) was not practicable or would have caused genuine difficulty to the payee. It is also open to the assessee to identify the person who has received the cash payment.

On facts, the Court held that though the case of the assessee did not fall within the exclusion clause in Rule 6DD (j), Section 40A (3) will not apply due to following reasons:

- There is no doubt as to the genuineness of the payment nor the identity of the payee.

- The assessee was compelled to pay cash owing to the insistence of its principal and if it had not abided by the direction, the business would have suffered and

- The exceptions in Rule 6DD are not exhaustive and the rule must be interpreted liberally.

***[2014] 43 taxmann.com 199 (Gujarat)**

SECTION 41(1): UNCLAIMED LIABILITIES (OF EARLIER YEARS), WHICH ARE SHOWN AS PAYABLE IN THE ACCOUNTS, ARE NOT TAXABLE AS INCOME EVEN IF CREDITORS UNTRACEABLE AND LIABILITIES ARE NON-GENUINE

In the case of CIT vs. Bhogilal Ramjibhai Atara, it was held by Gujarat High Court observed that Section 41(1) would apply in a case where there has been remission or cessation of liability during the year under consideration. In this case, the court observed as under:

- There was nothing on record to suggest there was remission or cessation of liability in the AY 2007- 2008. It was undoubtedly a curious case. Even the liability itself seems under serious doubt. The Assessing Officer undertook the exercise to verify the records of the socalled creditors. Many of them were not found at all in the given address. Some of them stated that they had no dealing with the assessee. In one or two cases, the response was that they had no dealing with the assessee nor did they know him.

- Of course, these inquiries were made ex parte and in that view of the matter, the assessee would be allowed to contest such findings. Nevertheless, even if such facts were established through bi-parte inquiries, the liability as it stands perhaps holds that there was no cessation or remission of liability and that therefore, the amount in question cannot be added back as a deemed income u/s 41(1) of the Act.

- This was one of the strange cases where even if the debt itself was found to be non-genuine from the very inception, at least in terms of Section 41(1) of the Act there was no cure for it.

Hence, it was held by the Court in this case that addition u/s. 41(1) cannot be made. **[2014] 43 taxmann.com 55 (Gujarat)**

SECTION 45: WRITE-OFF OF IRRECOVERABLE ADVANCES IS NOT A "TRANSFER" AND THE LOSS CANNOT BE CLAIMED AS A CAPITAL LOSS U/S 45

In the case of Crompton Greaves Limited vs. DCIT, it was held by Bombay High Court that having regard to the definitions of terms "capital asset" and "transfer" in Sections 2(14) and 2(47), in order to be eligible for carry forward of capital loss, the capital asset should be of the nature defined in Section 2(14) and should be transferred in the manner defined in Section 2(47). Equally, it should be subjected to tax as per Section 45(1) of the Income-tax Act. The advances given to the parties and written off are not the capital assets nor there any transfer. Therefore, they were not allowed to be carried forward to subsequent years. It is a capital loss and should be ignored. **[Unreported]**

SECTION 45(4): SECTION 45(4) DOES NOT APPLY IF THE RETIRING PARTNER TAKES ONLY MONEY TOWARDS THE VALUE OF HIS SHARE AND THERE IS NO DISTRIBUTION OF CAPITAL ASSETS AMONG THE PARTNERS

In the case of CIT vs. M/s Dynamic Enterprises, Full Bench of Karnataka High Court laid down conditions for applicability of Section 45(4) as under:

- There should be a distribution of capital assets of a firm;

- Such distribution should result in transfer of a capital asset by firm in favour of the partner;

- On account of the transfer there should be a profit or gain derived by the firm and

- Such distribution should be on dissolution of the firm or otherwise.

In other words, the capital asset of the firm should be transferred in favour of a partner, resulting in firm ceasing to have any interest in the capital asset transferred and the partners should acquire exclusive interest in the capital asset. On facts, the partnership firm purchased the property and it was not in the name of any partner. No partner brought that capital asset as capital contribution into the firm. Also, there was no dissolution of the firm because the firm continued to exist even after the retirement of some partners. What was given to the retiring partners is cash representing the value of their share in the partnership. No capital asset was transferred on the date of retirement. In the absence of distribution of a capital asset and in the absence of transfer of capital asset in favour of the retiring partners, no profit or gain arose in the hands of the partnership firm and so the question of the firm being assessed u/s 45(4) would not arise. **[2013] 40 taxmann.com 318 (Karnataka) (FB)**

SECTION 50B: APPLIES ONLY TO A "SALE" FOR A "MONETARY CONSIDERATION" AND NOT TO A CASE OF "EXCHANGE" OF THE UNDERTAKING FOR SHARES UNDER SECTION 391/394 SCHEME OF ARRANGEMENT

In the case of CIT vs. Bharat Bijlee Ltd, Bombay High court held that Section 2(42C) is not applicable to a case of exchange but to a case of sale. The definition of the term "*slump sale*" in Section 2(42C) means the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sale. The facts of the scheme of arrangement shows that the transfer of the undertaking took place in exchange for issue of preference shares and bonds. Merely because there was quantification when bonds/preference shares were issued, does not mean that monetary consideration was determined and its discharge was only by way of issue of bonds/preference shares. Hence, this is not a case where the consideration was determined and decided by parties in terms of money but its disbursement was to be in terms of allotment or issue of bonds/preference shares. All the clauses read together and the entire Scheme of Arrangement envisages transfer of the Lift Division not for any monetary consideration. Thus, it was a case of exchange and not a sale. Therefore, Section 2(42C) of the Act was inapplicable. Hence, Section 50B was also inapplicable. **[2014] 45 taxmann.com 104 (Bombay)**

SECTION 50C: EXTENT TO WHICH RELIANCE CAN BE PLACED BY ASSESSING OFFICER ON STAMP DUTY VALUATION EXPLAINED

In the case of CIT vs. Chandra Narain Chaudhri, Allahabad High Court held that Section 50C is a rule of evidence in assessing the valuation of property for calculating capital gains and is rebuttable. It is well known that an immovable property may have various attributes, charges, encumbrances, limitations and conditions. The Stamp Valuation Authority does not take into consideration the attributes of the property for determining the fair market value and determines the value in accordance with the circle rates fixed by the Collector. The object of valuation by the Stamp Valuation Authority is to secure revenue on such sale and not to determine the true, correct and fair market value for which it may be purchased by a willing purchaser subject to and taking into consideration its situation, condition and other attributes such as it occupation by tenant, any charge or legal encumbrances. **[2013] 38 taxmann.com 275 (Allahabad)**

SECTION 54F(4): EXTENDED LIMIT U/S. 139(4) IS AVAILABLE FOR MAKING DEPOSIT IN THE CAPITAL GAINS ACCOUNT SCHEME

In the case of CIT vs. Jagtar Singh Chawla, Punjab and Haryana High Court observed that though Section 54F(4) provides that the amount not appropriated towards purchase of the new asset has to be deposited in the capital gains account scheme before the due date for filing the return u/s 139(1), sub-section (4) of Section 139 is in the nature of a proviso to Section 139(1). Section 139(4) provides that a person who has not furnished a return within the time allowed to him under section 139(1) may furnish the return at any time before the expiry of one year from the end of

the relevant assessment year or before the completion of the assessment whichever is earlier. The extended time limit for filing return of income is available for making deposit in the capital gains account scheme.

The Court held that as the assessee had invested the consideration in purchase of a new house before that date, the exemption has to be allowed. **[2013] 215 Taxman 154 (Punjab and Haryana)**

SECTION 80-IB (10): IF DEVELOPER DOES NOT (WITHOUT JUST CAUSE) DEVELOP TO FULL EXTENT OF FSI, A PART OF THE SALE PROCEEDS HAS TO TREATED AS BEING FOR SALE OF FSI AND DENIED SECTION 80-IB (10) DEDUCTION

In the case of CIT vs. Moon Star Developers, the assessee, engaged in development of housing projects, constructed a residential project. Though total FSI of 15312 sq. meters was available for construction, the assessee utilized only 3573 sq. meters. The residential units were constructed only on the ground floor. The said residential units were sold and the entire surplus was claimed u/s 80-IB (10) as profits derived from activity of developing housing project. The Assessing Officer and CIT (A) held that a part of the consideration received by the developer was relatable to the unutilized FSI and had to be excluded from the profits eligible for Section 80-IB (10) deduction.

It was affirmed by Gujarat High Court which observed as under:

- For any commercial activity of construction, be it residential or commercial complex maximum utilization of FSI is of great importance to the developer. Ordinarily, therefore, it would be imprudent for a developer to underutilize available FSI. Sale price of constructed properties is decided on the built up area. It can thus be seen that given the rate of constructed area remaining same, non-utilization of available FSI would reduce the profit margin of the developer;

- When a developer therefore utilizes only say 2 per cent of FSI and sells the unit leaving 75 per cent FSI still available for construction, he obviously works out the sale price bearing in mind this special feature. Thus, therefore, when a developer constructs residential unit occupying a fourth or half of usable FSI and sells it, his profits from the activity of development and construction of residential units and from sale of unused FSI are distinct and separate and rightly segregated by the Assessing Officer;

- It is true that Section 80IB (10) does not provide that for deduction, the undertaking must utilize 100 per cent of the FSI available. The question however is, can an undertaking utilize only a small portion of the available area for construction, sell the property leaving ample scope for the purchaser to carry on further construction on his own and claim full deduction u/s 80IB (10) on the profit earned on sale of the property? If this concept is accepted, in a given case, an assessee may put up construction of only 100 sq. ft. on the entire area of one acre of plot and sell the same to a single purchaser and claim full deduction on the profit arising out of such sale u/s 80IB (10) of the Act. This cannot be stated to be development of a housing project qualifying for deduction u/s 80IB(10);

- This is not to suggest that for claiming deduction u/s 80IB (10), invariably in all cases, the assessee must utilize the full FSI and any shortage in such utilization would invite wrath of the claim u/s 80IB (10), being rejected. The issue has to be seen from case to case basis. Marginal under-utilization of FSI certainly cannot be a ground for rejecting the claim u/s 80IB (10). Even if there has been considerable under-utilization, if the assessee can point out any special grounds why the FSI could not be fully utilized, such as, height restriction because of special zone, passing of high tension electric wires overhead, or any such similar grounds to justify under utilization, the case may stand on a different footing. However, in cases where the utilization

of FSI is way short of the permissible area of construction, looking to the scheme of s. 80IB (10) and the purpose of granting deduction on the income from development of housing projects envisaged thereunder, bifurcation of such profits arising out of such activity and that arising out of the net sell of FSI must be resorted to. On facts, none of the assessees have made any special ground for non-utilization of the FSI.**[2014] 45 taxmann.com 181 (Gujarat]**

SECTION 147: BALD STATEMENT THAT ASSESSEE HAS FAILED TO MAKE A FULL AND TRUE DISCLOSURE OF MATERIAL FACTS NOT SUFFICIENT. DETAILS MUST BE GIVEN AS TO WHICH FACT WAS NOT DISCLOSED

In case of Bombay Stock Exchange Ltd vs. DDIT, Bombay High Court observed as under:

- ☐ The reasons for initiating re-assessment proceedings do state that there was a failure on the part of the Petitioner to disclose fully and truly all material facts necessary for its assessment.

- ☐ However, merely making this bald assertion was not enough. The Assessing Officer must disclose in the reasons as to which fact or material was not disclosed by the assessee fully and truly necessary for assessment of that assessment year, so as to establish the vital link between the reasons and evidence.

- ☐ On facts, there were no details given by the Assessing Officer as to which fact or material was not disclosed by the Petitioner that led to its income escaping assessment. There is merely a bald assertion in the reasons that there was a failure on the part of the Petitioner to disclose fully and truly all material facts without giving any details thereof.

The Court held that this being the case, the impugned notice is bad in law and on this ground alone the Petitioner is entitled to succeed in this Writ Petition**. [Unreported]**

SECTION 194H TDS DOES NOT APPLY TO ALL SALES PROMOTIONAL EXPENDITURE. IT APPLIES ONLY IF RELATIONSHIP BETWEEN PAYER AND PAYEE IS THAT OF PRINCIPAL AND AGENT

In the case of CIT vs. Intervet India Pvt. Ltd., Bombay High Court observed as under:

- ☐ The assessee had undertaken sales promotional scheme viz. Product discount scheme and Product campaign under which it offered an incentive on case to case basis to its stockists / dealers / agents. A deduction was claimed towards expenditure incurred under the said sales promotional scheme.

- ☐ The relationship between the assessee and the distributor / stockists was that of principal to principal and the distributors were the customers of the assessee to whom the sales were effected either directly or through the consignment agent. As the distributor / stockists were the persons to whom the product was sold, no services were offered by the assessee and what was offered was a discount to buy the assessee’s product.

- ☐ The distributors / stockists were not acting on behalf of the assessee and that most of the credit was by way of goods on meeting of sales target.

The Court held that the Product discount scheme and Product campaign under which it offered an incentive could not be said to be a commission payment within the meaning of Explanation (i) to Section 194H of the Income-tax Act,1961. **[Unreported]**

SECTION 220: AFTER REJECTING STAY APPLICATION ASSESSING OFFICER MUST GIVE REASONABLE TIME BEFORE TAKING STEPS FOR COERCIVE RECOVERY

In the case of Sony India Pvt. Ltd Vs. ACIT, Delhi High Court held that having said that Assessing Officer, having rejected the stay application, should wait for a reasonable period before he takes coercive steps to recover the amounts since the petitioner, faced with an order rejecting the stay application, may need some time to make arrangements to pay the entire tax demand or come up with proposals for paying the same in installments. The Assessing Officer is a prospector of the revenue and he is expected to protect the interests of the revenue with the rules of fair play and an anxiety to ensure that an opportunity is not lost to the assessee to make alternative arrangements for clearing the tax dues, once the stay applications filed under section 220(3) are rejected. **[2014] 44 taxmann.com 234 (Delhi)**

SECTION 254: IF A LEGAL ISSUE IS RAISED (EVEN FOR THE FIRST TIME) TRIBUNAL HAS THE DUTY TO DEAL WITH IT AND CANNOT REMAND IT TO LOWER AUTHORITIES

In the case of Kansai Nerolac Paints Ltd vs. DCIT, Bombay High Court held that the Tribunal should answer the legal issue itself even if it is raised for the first time if this legal issue goes to the root of the matter. High Court observed as under:

- The issue was that if penalty proceedings were initiated prior to the order of the winding up passed or the scheme of amalgamation being sanctioned, then, whether the subsequent act of a order sanctioning the scheme would permit continuation of the proceedings against an entity or company which is wound up and in terms of the provisions contained in the Act. This was a clear legal issue.

- It should have been answered by the Tribunal, particularly when it had admitted the question or ground and also the additional evidence filed by the assessee. The only two documents which required to be looked into were the scheme of amalgamation and the order passed in pursuance thereof by this Court. If that was the admitted factual position and based on which the legal issue was raised, then, the Tribunal was obliged to answer the legal question. Its omission to answer it, therefore, is vitiated in law.

The Tribunal is a last fact finding Court and equally if it could have been approached by the assessee both on law and fact, then, in the given circumstances, the Tribunal should have answered this issue and its failure to do so can safely be termed as not performing its duty in law. The direction to remit and to remand it to the Assessing Officer is not justified and in the peculiar facts and circumstances noted above. **[Unreported]**

SECTION 269SS/269T IS NOT ATTRACTED TO BOOK ENTRIES NOT INVOLVING CASH TRANSACTIONS

In the case of CIT vs. Saurabh Enterprises, Allahabad High Court held that as in this case, the transactions of loans and advances were not cash transactions and were merely book entries by way of adjustment entries, there was no violation of Section 269SS/269T of the Act and hence no penalty u/s 271D/ 271E is to be levied.

TRIBUNAL HAS NO POWER TO DISMISS APPEAL FOR NON-APPEARANCE OF APPELLANT. IT HAS TO DEAL WITH THE MERITS. AN APPLICATION FOR RECALL OF AN EX-PARTE DISMISSAL ORDER IS UNDER SECTION 254(2) AND MUST BE FILED WITHIN 4 YEARS FROM THE DATE OF THE ORDER. THE TRIBUNAL MUST PERMIT "MENTIONING" OF MATTERS

In the case of Bharat Petroleum Corporation Ltd vs. ITAT, nobody appeared on the day when the assessee's appeal was fixed for hearing before the Tribunal. Hence, the Tribunal dismissed the appeal for want of prosecution. The assessee filed a Miscellaneous Application (MA) before the Tribunal seeking to recall the exparte order. The Tribunal dismissed the MA on the ground that the application for recall had been filed beyond a period of 4 years from the date of the ex-parte order. The assessee filed a Writ Petition contending that the Tribunal had no power under Rule 24 to dismiss an appeal for want of prosecution and an application for recall of an ex-parte order does not fall u/s 254(2) and the time limit of 4 years does not apply to it. It was also contended that the Tribunal ought to allow the system of "*mentioning*" matters as is done in the High Court. Bombay High Court dismissed the petition and held as under:

- It is a little strange that the Tribunal does not permit the practice of mentioning matters at any time of the day. If it had done so, the exercise of filing an application for recall may not have been necessary. The ultimate object of the Tribunal is to decide a dispute between the revenue and assessee in accordance with law to ensure that justice is done. In the aid of ensuring that justice is done, the Tribunal cannot as a matter of practice bar any Advocates/representative from mentioning their matters before the Tribunal. The mentioning of matters should be allowed by the Tribunal. It is of course in the Tribunal's discretion to allow the request made by the parties while mentioning but prohibiting mentioning of matters before a Court/ Tribunal is a likely recipe for injustice. The Tribunal was requested to do away with such a practice and allow mentioning of matters;

- Under Rule 24, the Tribunal has no power to dismiss an appeal for non-appearance of the assessee. It has to decide the appeal on merits. The dismissal order is consequently erroneous and the assessee is entitled to have the order set aside;

- However, because dismissing an appeal for non-prosecution in the face of Rule 24 is an error apparent on the face of the record, an application to set right the error of dismissal for non-prosecution is an application u/s 254(2) and not u/s. 254(1). Where Parliament has provided a specific provision to deal with a particular situation, it is not open to ignore the same and apply some other provision. Such an application has to be filed within a period of 4 years from the date of the order;

- Though the Proviso to Rule 24 empowers the Tribunal to recall an ex-parte order without specifying any period of limitation, this applies only where the appeal is decided ex-parte on merits. Where the appeal is dismissed ex-parte for non-prosecution, it is a case of an erroneous order which only be rectified u/s 254(2). Also an order passed in breach of Rule 24 is an irregular order but not a void order. Assuming the said order is a void order, yet it continues to be binding till it is set aside by a competent authority. **[2014] 42 taxmann.com 25 (Bombay)**

COURT ON ITS OWN MOTION VS. CIT

In the case of Court on Its Own Motion vs. CIT, Delhi High Court observed as under:

- The Central Board of Direct Taxes (CBDT) has accepted that incorrect and wrong demands have been uploaded on the CPC arrears portal. The Commissioner of Income Tax, CPC, has expressed his concern on account of uploading of incorrect and wrong data in the CPU and the problem faced by them and by the assesses.

- The CBDT has issued Circular No.4 of 2012 in which the burden is put on the assessee to approach the Assessing Officers to get their records updated and corrected by filing Section 154 applications. It should not be a ground for the Assessing Officers not to suo motu correct his records and upload correct data.

- Each assessee has a right and can demand that correct and true data relating to the past demands should be uploaded. Asking the assessee to file section 154 applications entails substantial expenses and defeats the main purpose behind computerisation. Further, the Assessing Officers do not adhere to the time limit prescribed for disposal of the section 154 applications.

- To ensure transparency (and accountability), a register must be maintained with details and particulars of each application made u/s 154, the date on which it was made, date of disposal and its fate. The Section 154 application has to be disposed of by a speaking order and communicated to the assessee. There must be full compliance of the said requirements. **[Unreported]**

TRIBUNAL DECISIONS

SECTION 14A AND RULE 8D: IF ASSESSING OFFICER DOES NOT DEAL WITH ASSESSEE'S ARGUMENTS, IT MEANS THAT HE HAD NOT REACHED OBJECTIVE SATISFACTION THAT ASSESSEE'S METHOD IS INCORRECT AND CANNOT INVOKE RULE 8D

In the case of Kalyani Steels Ltd vs. ACIT, Pune Tribunal held that invoking of Rule 8D to compute the disallowance u/s 14A is neither automatic and nor is triggered merely because assessee has earned an exempt income. The invoking of Rule 8D of the Rules is permissible only when the Assessing Officer records the satisfaction in regard to the incorrectness of the claim of the assessee, having regard to the accounts of the assessee. **[Unreported]**

SECTION32: ROAD CONSTRUCTED ON BUILD-OPERATE-TRANSFER ("BOT") TERMS IS ELIGIBLE FOR DEPRECIATION EVEN THOUGH ASSESSEE IS NOT THE LEGAL OWNER OF THE ROAD

In the case of DCIT Vs. Swarna Tollway Pvt. Ltd, the assessee constructed a road on BUILD-OPERATE-TRANSFER ("BOT") terms. NHAI remains legal owner of the site with full powers, the assessee had been granted not merely possession but also right to enjoyment of the site.

Hyderabad Tribunal held that benefit depreciation u/s 32 will be available in the case based on observation as under:

- Though the NHAI remains legal owner of the site with full powers to hold, dispose of and deal with the site consistent with the provisions of the agreement, the assessee had been granted not merely possession but also right to enjoyment of the site and NHAI was obliged to defend this right and the assessee has the power to exclude others.
- The very concept of depreciation suggests that the tax benefit on account of depreciation belongs to one who has invested in the capital asset, is utilizing the capital asset and thereby loosing gradually investment cost by wear and tear and would need to replace the same by having lost its value fully over a period of time.
- The term "owned" as occurring in Section 32 (1) of the Act must be assigned a wider meaning. Anyone in possession of property in his own title exercising such dominion over the property as would enable others being excluded there from and having the right to use and occupy the property and/or to enjoy its usufruct in his own right would be the owner of the buildings, though a formal deed of title may not have been executed and registered. **[2014] 43 taxmann.com 252 (Hyderabad - Trib)**

SECTION 32: DEPRECIATION NOT ALLOWED ON NON COMPETE FEES:

In the case of Gujarat Glass Private Limited vs. ACIT, the assessee has paid non-compete fees which were claimed as intangible asset whereas AO was of the opinion that it was capital expenditure.

Mumbai Tribunal observed as under:

- The expression, "*any other business or commercial rights of similar nature*" in the definition of "*intangible asset*" in Section 32(1)(i) shows that the initial part, i.e. know how, patents, copyrights, trademarks, license, franchises, has been disjointed by the conjunction 'or. The use of the disjunction 'or' has a very relevant role, because, the legislature accepts the difference and distinction of intangibles and rights. The legislature has used 'or' in the provision for explaining the distinction of application of like nature with that of the unlike nature, which is an accepted principle i.e. doctrine of ejusdem generis.

- Taking note of the word 'or', used as a disjunction is essential to carve out a meaningful genus. The argument whether non compete rights constitute is a *right in rem* or a *right in personam* is a matter to be decided by an appropriate higher judicial forum.

Tribunal held that non-compete fee does not fall within the ambit of any other commercial or business rights. Since the payment is a capital expenditure, it cannot be allowed as an expense and also cannot be amortized. **[Unreported]**

SECTION 32(1) (ii): ANY RIGHT (INCLUDING LEASEHOLD RIGHTS) WHICH ENABLES CARRYING ON BUSINESS EFFECTIVELY AND PROFITABLY IS AN "INTANGIBLE ASSET" AND ELIGIBLE FOR DEPRECIATION

In the case of Tirumala Music Centre (P) Ltd vs. ACIT, assessee has got right to carry business effectively and profitably. Assessee was of the opinion that right including leasehold rights which enables carrying on business effectively is covered under "business or commercial rights" and hence classified as Intangible Asset under section 32.

Hyderabad Tribunal held that:

- Section 32(1) (ii) allows depreciation on "business or commercial rights" which means rights obtained for effectively carrying on business or commerce.

- Commerce is a wider term which encompasses business in its fold. Therefore, any right which is obtained for carrying on business effectively and profitably has to fall within the meaning of the term "intangible asset" **[2013] 39 taxmann.com 196 (Hyderabad - Tribunal)**

Explanation to Section 37: If the purpose of the expenditure is not an offence/ prohibited by law, fact that prior approval of the Government was not obtained cannot be basis of disallowance

In the case of Jai Surgicals Ltd vs. ACIT, Delhi Tribunal held that the Explanation to Section 37(1) is a deeming provision and disallows expenditure incurred by an assessee for 'any purpose' which is either an offence or prohibited by law. The inquiry to determine the applicability or otherwise of the Explanation is restricted to ascertaining the purpose of the expenditure. The investigation should be carried out to see the object and consideration for the expenditure incurred. If the purpose of the expenditure is neither to commit an offence nor is prohibited by any law,

then there can be no question of disallowance. It means that the offence or prohibition under law should be judged with the 'purpose' of the expenditure on a standalone basis divorced from the fulfillment or otherwise of the procedural formalities attached with and necessary for the incurring of such expenditure. If the expenditure is otherwise lawful and neither amounts to offence nor is prohibited by law, but the procedural provisions attached for incurring it are not complied with, no doubt irregularity will creep in, but such irregularity would not make the expenditure itself as unlawful so as to be brought within the scope of the Explanation. On facts, the payment of job work charges is not an offence or prohibited by law. The fact that there was no prior approval from the Central Government u/s 297 of the Companies Act does not make the expenditure of job work charges disallowable. **[Unreported]**

SECTION 41(1): LIABILITY OUTSTANDING FOR LONG PERIOD OF TIME IS ASSESSABLE AS INCOME (DESPITE NO WRITE-BACK IN ACCOUNTS) IF ASSESSEE UNABLE TO PROVE GENUINENESS OF LIABILITY

In the case of ITO vs. Shailesh D Shah/Yusuf R Tanwar vs. ITO, the assessee was having some old liability which is unpaid from long time.

Mumbai Tribunal observed that:

- ☐ It is very improbable that payments to labour can remain outstanding for more than three years. The assessee has not been able to produce the records relating to the name, addresses and bills of the labour etc to prove that the liability continues to exist. It is accordingly a case of cessation of liability.

- ☐ The assessee has just continued the entry of the same in his books of account without any intention to pay back the same. The view that such sums shown as liability is assessable to tax was taken by courts earlier and was observed that it would be illogical to say that a debtor or an employer, holding on to unpaid dues, should be given the benefit of his showing the amount as a liability, even though he would be entitled in law to say that a claim for its recovery is time barred, and continue to enjoy the amount. However, contrary views by courts are also taken.

- ☐ If both views are read in harmony, it can be observed that the assessee cannot be allowed to show an amount as a liability even though he has no intention to pay it back but to enjoy the same for an unlimited period without being added to his income only on the excuse that he has not written off the same in his books of accounts.

- ☐ If the facts of the case establish that the liability has been genuinely shown by the assessee and his subsequent conduct shows that he has paid back the said credits and his intention was not to enjoy the amount for unlimited period without any intention to pay back the same, then it cannot be said to be a case of cessation of liability.

- ☐ On facts, not only is the existence of outstanding liability of labour charges for so many years improbable in the normal course of business but the assessee has also failed to give any evidence regarding the identity and genuineness of the creditors.

Tribunal held that it was a case of cessation of liability and Section 41(1) was applicable. **[Unreported]**

SECTION 50B: TRANSFER OF ASSETS VIA AMALGAMATION WITHOUT MONETARY CONSIDERATION IS NOT A "SLUMP SALE"

In the case of ITO vs. Zinger Investments (P) Ltd, the assessee had transferred its manufacturing division to Novapan Industries Limited (NIL) under a scheme of amalgamation. As per scheme under section 391/394 of the Companies Act, all the assets and liabilities of the assessee were vested with NIL against which, the assessee was given investments valued at Rs 25,24,00,000 held by NIL besides allotment of 68,12,000 equity shares of Rs. 10 each of the face value to Rs. 6,81,00,000 to the shareholders of the assessee. The Assessing Officer held that the transfer of the manufacturing division to NIL tantamount to a 'slump sale' within the meaning of Section 50B attracting liability of capital gains therein.

Hyderabad Tribunal held that:

- ☐ To qualify as a slump sale, there must be transfer of one or more undertakings as a result of sale and the sale should be for a lump sum consideration without values being assigned to the individual assets and liabilities.

- ☐ The presence of money consideration is an essential element to a transaction of sale. If the consideration is not money but some other valuable consideration it may be an exchange or barter but not a sale.

In the present case, as no monetary consideration was received by the assessee for transfer of the assets and liabilities of the manufacturing division to Novapan Industries Ltd, the transaction is not a "slump sale" and does not attract Section 50B. **[2013] 38 taxmann.com 388 (Hyderabad - Trib)**

SECTION 54E, 54EA, 54EB AND 54EC: THE TERM "MONTH" IN SECTION 54E, 54EA, 54EB AND 54EC DOES NOT MEAN "30 DAYS" BUT THE "CALENDAR MONTH". SO, THE EXPRESSION "WITHIN A MONTH" MEANS "BEFORE THE END OF THE CALENDAR MONTH"

In the case of Alkaben B Patel vs. ITO, the assessee had for, for the purpose of re-investment under Section 54E, 54EA and 54EB, taken the month as calendar month, however Assessing Officer was of the opinion that month should be read as 30 days period.

The Special Bench of Ahemdabad Tribunal held that:

- ☐ Sections 54E, 54EA and 54EB require the investment to be made "*within a period of six months after the date of such transfer*". The word "month" refers in this section a period of 30 days or it refers to the month only. The term 'month' is not defined in the Income-tax Act. Therefore, its meaning has to be understood as per the General Clauses Act, 1897 which defines the word "month" to mean a month reckoned according to the British calendar.

- ☐ On some occasions, the Legislature had not used the term "Month" but has used the number of days to prescribe a specific period. For example, the First Proviso to Section 254(2A) provides that the Tribunal may pass an order granting stay but for a period not exceeding 180 days. This is an important distinction made in the statute while subscribing the limitation/ period. This distinction thus resolves the present controversy by itself. **[2014] 43 taxmann.com 333 (Ahmedabad - Trib) (SB)**

SECTION 56(2)(vii) DOES NOT APPLY TO BONUS AND RIGHTS SHARES OFFERED ON A PROPORTIONATE BASIS EVEN IF THE OFFER PRICE IS LESS THAN THE FMV OF THE SHARES

In the case of Sudhir Menon HUF vs. ACIT, Mumbai Tribunal observed as under:

- ☐ Where an individual or a HUF receives any property for a consideration which is less than the FMV of the property, the difference shall be assessed as income of the recipient. However Section 56(2) (vii) does not apply to the issue of bonus shares because there is a mere capitalization of profit by the issuing-company and there is neither any increase nor decrease in the wealth of the shareholder as his per centage holding remains constant.

- ☐ The same argument applies pari material to the issue of additional shares to the extent it is proportional to the existing shareholding because to the extent the value of the property in the additional shares is derived from that of the existing shareholding, on the basis of which the same are allotted, no additional property can be said to have been received by the shareholder.

- ☐ The fall in the value of the existing holding has to be taken into account as long as there is no disproportionate allotment, i.e., shares are allotted pro-rata to the shareholders, based on their existing holdings, there is no scope for any property being received by them on the said allotment of shares; there being only an apportionment of the value of their existing holding over a larger number of shares.

Mumbai Tribunal held that there is, accordingly, no question of Section 56(2)(vii)(c) getting attracted in such a case. A higher than proportionate or a non-uniform allotment though would attract the rigor of the provision to the extent of the disproportionate allotment and by suitably factoring in the decline in the value of the existing holding. **[2014] 45 taxmann.com 176 (Mumbai - Trib)**

SECTION 80-IA(5): "INITIAL YEAR" IN THE SECTION ANALYSED

In the case of M/s. Shevie Exports vs. JCIT, Mumbai Tribunal analysed that the fiction created by Section 80-IA(5) is that the eligible business is the only source of income and the deduction would be allowed from the initial assessment year or any subsequent assessment year.

Tribunal observed as under:

- ☐ It is nowhere defined as to what is the "*initial assessment year*". Prior to 1.4.2000, Section 80-IA (12) defined the "*initial assessment year*" for various types of eligible assessees. However, after the amendment by the Finance Act, 1999, the definition of "*initial assessment year*" has been specifically taken away.

- ☐ Now, when the assessee exercises the option of choosing the initial assessment year as culled out in Section 80-IA(2) from which it chooses its 10 years of deduction out of 15 years, then only the losses of the years starting from the initial assessment year alone are to be brought forward as stipulated in Section 80IA(5).

- ☐ The loss prior to the initial assessment year which has already been set-off cannot be brought forward and adjusted into the period of ten years from the initial assessment year as contemplated or chosen by the assessee. It is only when the loss have been incurred from the initial assessment year, then the assessee has to adjust loss in the subsequent assessment years and it has to be computed as if the eligible business is the only source of income and then only deduction u/s 80-IA can be determined.

Tribunal observed that this is the true import of Section 80-IA(5) **[2013] 33 taxmann.com 446 (Mumbai - Trib)**

SECTION 80IA(4): THE ASSESSEE IS ELIGIBLE FOR BENEFIT U/S 80-IA EVEN IF ONLY PART OF THE INFRASTRUCTURAL PROJECT WORK IS EXECUTED BY IT

In the case of B.T. Patil and Sons Belgum Constructions Pvt. Ltd vs. ACIT, assessee was a developer, claimed deduction under section 80IA during the year. Normally each project takes more than one year to get completed. Assessee executes the work by shouldering Investment and technical risk by employing team of technically and administratively qualified persons, however all the liability for work done lies on the part of the assessee and if any default is found on the any area assessee is liable for all types of damages.

Mumbai Tribunal observed as under:

- The view of the Larger Bench that the assessee had to be directly engaged in developing, maintaining and operating the facility and that there had to be a complete development of the facility and not just a part of it is contrary to the law laid down in **ABG Heavy Industries** (Bom).

- The High Court held that the effect of the amendment by the Finance Act of 1999 is that the benefit of Section 80IA(4) is available to any enterprise carrying on the business of (i) developing, (ii) maintaining and operating, or (iii) developing, maintaining and operating an infrastructure facility.

- It was also held that the assessee did not have to develop the entire project in order to qualify for deduction u/s 80-IA and that Parliament did not legislate a condition impossible of compliance. The Explanation below 80-IA (13) inserted by Finance Act 2007 and 2009 w.e.f 1.4.2000 which provides that section 80-IA(4) shall not apply to a person executing a "*works contract*" does not apply to a case where the assessee executes the work by shouldering Investment and technical risk by employing team of technically and administratively qualified persons and it is liable for liquidated damages if failed to fulfill the obligation laid down in the agreement and also securing by Bank guarantee.

- On facts, the assessee had shouldered the investment and technical risk in respect of the work executed and it was liable for liquidated damages if failed to fulfill the obligation laid down in the agreement. The liability which had been assumed by the assessee was obligations involving the development of an infrastructure facility.

Mumbai Tribunal held that it is not correct to say that the assessee is merely a contractor and not a developer. The assessee is eligible for benefit u/s 80-1A even if only part of the Infrastructural Project work is executed by it. **[2013] 34 taxmann.com 97 (Pune - Trib)**

SECTION 80-IB (10): LIMIT ON EXTENT OF COMMERCIAL AREA IMPOSED BY CLAUSE (D) OF SECTION 80IB (10) INSERTED W.E.F. 1.4.2005 DOES NOT APPLY TO PROJECTS APPROVED BEFORE THAT DATE

In the case of ITO vs. M/S Yash Developers, Mumbai Tribunal held that:

- In the assessee's own case for the same project relating to Assessment Years 2005 - 2006 and 2006 - 2007, which falls after the insertion of clause (d) to Section 80IB(10), the Tribunal held that the assessee is eligible for deduction u/s 80IB(10) in respect of the housing project.

- The condition of limiting commercial establishment/shops to 2000 sq.ft, which has come into force w.e.f. 1.4.2005 would be applicable for projects approved on or after 1.4.2005 and where the approval of the project was prior to 31.3.2005, the amended provision would have no application for those projects.**[Unreported]**

SECTION 147: FAILURE TO COMPUTE CAPITAL GAINS U/S 50C DOES NOT LEAD TO ESCAPEMENT OF INCOME

In the case ITO vs. Haresh Chand Agarwal HUF, Agra Tribunal held that Section 50C is not a final determination to prove that it is a case of escapement of income. The report of the approved valuer may give estimated figure on the basis of facts of each case. The Assessing Officer at the original assessment stage considered all the documents and material produced before him and has accepted the cost of property as was declared by the assessee. The reassessment is on change of opinion is not justified. **[Unreported]**

SECTION 147/ 151: MERELY WRITING "APPROVED" IN THE SANCTION FORM WITHOUT RECORDING SATISFACTION RENDERS THE REOPENING VOID

In the case of Amarlal Bajaj vs. ACIT, the Assessing Officer issued on the assessee a notice under Section 148 after four years from the end of the relevant assessment year seeking to reopen the aforesaid assessment which the assessee challenged.

Mumbai Tribunal observed as under:

- Section 147 and 148 are a charter to the Revenue to reopen earlier assessments and are, therefore protected by safeguards against unnecessary harassment of the assessee.

- Section 151 guards that Section 147 may not be used unless a superior officer is satisfied that the Assessing Officer has good and adequate reasons to invoke the provisions of Section 147. The superior authority has to examine the reasons, material or grounds and to judge whether they are sufficient and adequate to the formation of the necessary belief on the part of the assessing officer.

- If, after applying his mind and also recording his reasons, howsoever briefly, the Commissioner is of the opinion that the Assessing Officer's belief is well reasoned and bona fide, he is to accord his sanction to the issue of notice u/s 148 of the Act.

Tribunal held that in this case, from the perusal of the order sheet on record it was observed that, the Commissioner has simply put "approved" and signed the report thereby giving sanction to the Assessing Officer. Nowhere the Commissioner has recorded a satisfaction note not even in brief. Therefore, it cannot be said that the Commissioner has accorded sanction after applying his mind and after recording his satisfaction. **[2013] 37 taxmann.com 7 (Mumbai - Trib)**

SECTION 153A: IN CASE OF COMPLETED ASSESSMENTS, ADDITION CAN BE MADE ONLY IF INCRIMINATING DOCUMENT FOUND DURING SEARCH

In the case of MGF Automobiles Ltd vs. ACIT, Delhi Tribunal held that addition in assessment order can be made only if incremental income document found during search under progress.

It was observed by Tribunal there are three possible circumstances that emerge on the date of initiation of search u/s 132 (1):

- ☐ Proceedings are pending;
- ☐ Proceedings are not pending but some incriminating material found in the course of search indicating undisclosed income and/or assets and
- ☐ Proceedings are not pending and no incriminating material has been found.
- ☐ In circumstance where the proceedings are pending, they are abated and the Assessing Officer gets a free hand to make the assessment. In circumstance where proceedings are not pending but some incrimating material is found during search, there is no question of abatement and the Assessing Officer has to pass an assessment order u/s 153A to assess the undisclosed income. In circumstance where proceedings are not pending and no incriminating material is found the Assessing Officer has to pass an assessment order though as there is no incriminating material no income can be assessed.
- ☐ On facts, as the assessments were completed and there was no incriminating material found during the search. Hence, the Assessing Officer was not entitled to make any addition. **[Unreported]**

SECTION 201(1A) AND SECTION 40(a)(ia): ENTIRE EXPENDITURE CANNOT DISALLOWED IN CASE OF SHORT OR LESSER DEDUCTION OF TDS

In the case of Apollo Tyres Ltd vs. DCIT, assessee has short deducted TDS. Assessee has contended that entire expenditure should not be disallowed.

Cochin Tribunal held as under:

- ☐ A combined reading of Section 201(1A) and Section 40(a)(ia) shows that while a case of short-deduction of TDS is covered by Section 201(1A), it is not covered by Section 40(a)(ia). There is an obvious omission to include short deduction / lesser deduction in Section 40(a)(ia).

Therefore, in case of short /lesser deduction of tax, the entire expenditure whose genuineness was not doubted by the Assessing Officer cannot be disallowed. **[2013] 35 taxmann.com 593 (Cochin - Trib.)**

SECTION 271(1)(C): MISTAKE IN CLAIM IN RETURN OF INCOME IS NOT CONCEALMENT OR FURNISHING OF INACCURATE PARTICULARS OF INCOME

In the case of Amruta Organics Pvt. Ltd vs. DCIT, assessee mistakenly calculated depreciation; resultant income of the assessee remains a loss. The assessee had been incurring losses since the year 2003 due to the market forces.

Pune Tribunal held that:

- ☐ A mere mistake in making of a claim in the return of income would not ipso facto reflect concealment or furnishing of inaccurate particulars of income in terms of Section 271(1) (c).

- ☐ The wrong claim of depreciation cannot be said to be made with an intention to evade taxes in as much as even after the disallowance of depreciation, the resultant income of the assessee remains a loss. The assessee had been incurring losses since the year 2003 due to the market forces. Considering the entirety of circumstances, the claim on account of depreciation was a mistake, and did not invite the provisions of Section 271(1) (c). **[Unreported]**

EXPLANATION 5 TO SECTION 271(1)(C): UNDISCLOSED INCOME OFFERED IN BELATED RETURN FILED U/S 139(4) ELIGIBLE FOR IMMUNITY FROM PENALTY

In the case of ITO vs. Gope M. Rochlani, assessee has filed belated return and disclosed some of the income which were not previously disclosed in return filed. Assessee contended that "Due Date" for filing of the return as used in Section 271(1)(c) would include due date for filing belated return.

Mumbai Tribunal observed as under:

- ☐ Explanation 5A to Section 271(1)(c) provides that if during the course of search, the assessee is found to be the owner of any asset or income which has not been shown in the return of income which has been furnished before the date of search and the "*due date*" for filing the return of income has expired, the assessee is deemed to have concealed the particulars of his income or furnish inaccurate particulars of income and liable for penalty u/s 271(1)(c).

- ☐ In other words, if the income is offered in the return is filed by the "*due date*", no penalty can be imposed.

- ☐ The "*due date*" can be very well inferred as due date of filing of return of income u/s 139(4) because wherever the legislature has provided the consequences of filing of the return of income u/s 139(4), then the same has also been specifically provided like Section 139(3) which denies the benefit of carry forward of losses u/s 72 to 74A if the return of income is not filed within the time limit provided u/s 139(1).

Tribunal held that in absence of such a restriction, the limitation of time of "due date" cannot be strictly reckoned with Section 139(1). Even a belated return filed u/s 139(4) will be entitled to the benefit of immunity from penalty.

ASSESSEE CANNOT BE DENIED CREDIT FOR TDS ON THE GROUND OF DISCREPANCY IN FORM 26AS FILED BY THE DEDUCTOR

In case of Lsg Sky Chef (India) Pvt. Ltd vs. DCIT, the assessee had furnished the TDS certificate bearing the full detail of tax deducted; however form 26AS did not reflect the said amount credit. The assessee in its return of income claimed credit of tax deducted at source. However, the same was not allowed fully.

Mumbai Tribunal held that:

- ☐ Though Form 26AS (read with Rule 31AB and Sub Section 203AA and 206C (5)) represents a part of a wholesome procedure designed by the Revenue for accounting of TDS (and TCS), the burden of proving as to why the said Form (Statement) does not reflect the details of the entire tax deducted at source for and on behalf of a deductee cannot be placed on an assessee-deductee.

- ☐ The assessee, by furnishing the TDS certificate/s bearing the full details of the tax deducted at source, credit for which is being claimed, has discharged the primary onus on it toward claiming credit in its respect.

- ☐ The Revenue is fully entitled to conduct proper verification in the matter and satisfy itself with regard to the veracity of the assessee's claim/s, but cannot deny the assessee credit in respect of TDS without specifying any infirmity in its claim/s. Form 26AS is a statement generated at the end of the Revenue, and the assessee cannot be in any manner held responsible for any discrepancy therein or for the non-matching of TDS reflected therein with the assessee's claim/s.

- ☐ The plea that the deductor may have specified a wrong TAN, so that the TDS may stand reflected in the account of another deductee, is no reason or ground for not allowing credit for the TDS in the hands of the proper deductee. The onus for the purpose lies squarely on the Revenue. **[2014] 45 taxmann.com 256 (Mumbai - Trib)**

LAW OF JURISDICTIONAL HIGH COURT IS NOT BINDING IF THERE IS A LATER CONTRARY JUDGEMENT OF NON-JURISDICTIONAL HIGH COURT. SECTION 22: PROPERTY USED BY FIRM IN WHICH ASSESSEE-OWNER IS PARTNER IS NOT USED FOR ASSESSEE'S BUSINESS AND NOT ENTITLED FOR EXEMPTION

In the case of Prakash Vasanthbhai Golwala vs. ACIT, the assessee was owner of a property which was used by the partnership firm where assessee is partner.

Ahmedabad Tribunal observed that:

- ☐ Though the jurisdictional High Court in **Rasiklal Balabhai** held that the annual letting value of house property owned by the assessee and used for the business carried on by him in partnership was not liable to be included in his total income u/s 22, the Calcutta High Court has dissented from this view in **Prodip Kumar Bothra** and held that the exemption in respect of house property cannot be allowed to assessee if the property is used by the partnership firm because the owner of the house property and the occupier of the property must be the same person.

- ☐ The Karnataka High Court in **K.N. Guruswamy** and the Allahabad High Court in **Shiv Mohan Lal** and **Mustafa Khan** (All) has taken the same view as the Calcutta High Court that user by a partnership firm/ HUF is not user by the assessee-owner for business purposes.

- ☐ In view of the divergent views expressed by the High Courts, the thumb rule that the latest decision of the High Court is required to be followed to maintain judicial discipline.

Tribunal held that as the judgement of the (*jurisdictional*) Gujarat High Court is earlier in point of time and the judgement of the (*non-jurisdictional*) Calcutta and other High Courts is later in point of time, the view expressed by the Revenue Authorities has to be affirmed and the assessee's ground dismissed. **[2014] 41 taxmann.com 122 (Ahmedabad - Trib)**

LOSS ON FORWARD FOREIGN EXCHANGE CONTRACTS IS INCIDENTAL TO THE EXPORTS BUSINESS AND NOT *A "*SPECULATION LOSS*".* HOWEVER, IF THE CONTRACT IS PREMATURELY CANCELLED, THE ASSESSEE HAS TO JUSTIFY THE LOSS

In the case of London Star Diamond Company (I) P. Ltd vs. DCIT, assessee used to normally enter into forward contract in order to hedge the consideration receivable against export sale.

Mumbai Tribunal observed that a forward contract, entered into with banks for hedging losses due to foreign exchange fluctuations on the export proceeds, is in the nature of a "*hedging contract*" and is integral or incidental to the export activity of the assessee and cannot be considered as an independent business activity.

Tribunal held that:

- The losses or gains constitute business loss or gains and do not arise from speculation activities. The fact that there is a premature cancellation of the forward contract does not alter the nature of the transaction.

- There is also no requirement in the law that there should be a 1:1 correlation between the forward contracts and the export invoices. So long as the total value of the forward contracts does not exceed the value of the invoices, the loss has to be treated as a business loss. **[2013] 38 taxmann.com 338 (Mumbai - Trib)**

A CO-OPERATIVE HOUSING SOCIETY IS NOT A MUTUAL ASSOCIATION BECAUSE ITS MEMBERS CAN EARN INCOME FROM ITS PROPERTY. THE TRANSFER FEE AND TDR PREMIUM CHARGED BY THE SOCIETY FROM ITS MEMBERS IS A COMMERCIAL TRANSACTION AND NOT ELIGIBLE FOR EXEMPTION ON GROUNDS OF MUTUALITY

In the case of Hatkesh Co-op Housing Society Ltd vs. ACIT, assessee claimed that transfer fee and premium charged by society from its members is not income of society as it is mutual association of its members only. Assessing Officer was of the opinion that since society can earn profit out of the money received from its members so it cannot be said to be a mutual concern.

Mumbai Tribunal held that the transfer fee and TDR premium charged by the society from its members is not eligible for exemption and observed as under:

- There are three objections to treating a Co-op Housing Society as a mutual concern.

- The first objection is that while a mutual concern cannot lead to any profit for the members, a member of a co-op housing society can earn income from the property such as by letting. The contributors, by virtue of their membership, obtain a valuable capital asset in their own hands, i.e., the leasehold right in the plots allotted to them, as well as the interest in the super structure. They may encash or capitalize on or even trade on the property. Such valuable rights that inure to the members are separate and distinct from the right that vest in them as a part of the class of contributors and militates against the very notion of mutuality, which in its concept and operation cannot yield any income to them in their individual capacity.

- The second objection is that the assessee's activities of charging premium at one half the amount of the premium received by the transferor-member from the transferee-member are commercial transaction. As such, not only does the arrangement lead to creation and holding of wealth / property by the individual-members, it allows them to encash or otherwise exploit it, paying the society its share. That is, the society also partakes of the profit arising on the subsequent transfer by a member, to the extent of 50 per cent thereof.

- The third objection is that the policy of allowing the individual members to purchase TDRs from outside and load them on to their existing structures and of allowing non-members residing in the flats built by the members on their plots to have access to and enjoy the common facilities means that there is a break-down in the identity between the contributors and participants and violates another basic condition of mutuality that there must be no dealings with the non-members. .**[Unreported]**

ESOP TO EXPATRIATE EMPLOYEE OF FOREIGN COMPANY NOT CHARGEABLE FOR PERIOD HE WAS OUTSIDE INDIA EVEN IF ESOP WAS VESTED AND EXERCISED IN INDIA

In the case of ACIT vs. Robert Arthur Keltz, the assessee was an employee of 'M' USA. He exercised employee's stock option plan granted to him while on his assignment in India. He therefore, offered to tax the amount of proportionate ESOP perquisites earned in India, i.e. proportionate to the number of days of his assignment in India. However, the Assessing Officer while framing the assessment brought to tax the entire amount of perquisite on account of stock options.

Delhi Tribunal held that if a part of the activity done by the assessee-employee has no relation to any India specific job or activity it is not chargeable to tax in India. On facts, the assessee was in India only for a short period. Prior to that, he has not done any service connected with any activity in India. As the assessee had not rendered service in India for the whole grant period, only such proportion of the ESOP perquisite as is relatable to the service rendered by the assessee in India is taxable in India. **[2013] 35 taxmann.com 424 (Delhi - Trib)**

CONDONATION OF DELAY SHOULD BE CONSIDERED LENIENTLY:

In the case of Y.P. Trivedi vs. JCIT, assessee has filed application for appeal with a delay of 496 days. The reasons explained by the assessee showed that the delay in filing appeal was due to bonafide mistake and inadvertence.

Mumbai Tribunal condoned the delay and observed as under:

- The facts do not suggest that the assessee has acted in a malafide manner or that the reasons explained are only a device to cover an ulterior purpose.

- It is a settled proposition of law that Courts should take a lenient view on the matter of condonation of delay provided the explanation and the reason for delay is bonafide and not merely a device to cover an ulterior purpose or an attempt to save limitation in an underhand way.

- The Court should be liberal in construing sufficient cause and should lean in favour of such party. Whenever substantial Justice and technical considerations are opposed to each other, cause of substantial Justice has to be preferred. .**[Unreported]**

INCOME TAX

INETRNATIONAL TAXATION

CIRCULARS/ NOTIFICATIONS/PRESS RELEASE

Furnishing of additional information along with TRC to claim tax treaty benefits by CBDT:

The CBDT has issued a notification amending Rule 21AB of the Income-tax Rules, 1962 prescribing the additional information required to be furnished by Non-Residents along with the Tax Residency Certificate (TRC). The details are required to be furnished in Form 10F.

The details required to be furnished are as follows:

- Status (individual, company, firm etc.) of the Assessee;
- Permanent Account Number (PAN) of the taxpayer if allotted
- Nationality (in case of an individual) or country or specified territory of incorporation or
- registration (in case of others)
- Taxpayer's tax identification number in the country or specified territory of residence and in case there is no such number, then, a unique number on the basis of which the person is identified by the Government of the country or the specified territory of which the taxpayer claims to be a resident
- Period for which the residential status, as mentioned in the TRC, is applicable; and
- Address of the taxpayer outside India during the period for which the certificate is applicable

[Notification NO. 57/2013, dated 01-08-2013]

SAFE HARBOUR RULE (SHR)

In exercise of power confirmed under section 92CB of the Income tax Act, 1961, the CBDT has issued the Safe Harbour Rules. The definition of safe harbour rule provided in section 92CB means circumstances in which the Income-tax Authority shall accept the transfer price declared by the assessee. The draft safe harbour rules were placed in public domain along with CBDT Press Release on 14.08.2013 seeking comments of various stake holders. The comments received from various stake holders have been considered and necessary modifications have been made and the final rules are provided under Rule 10TA to rule 10TG.

- ☐ Safe harbours for various sectors, shall be as under–

Sr. No.	Eligible International Transaction	Safe Harbour ratios
1.	Software development services (IT services) and Information Technology Enabled services (ITES), with insignificant risks ▪ where the aggregate value of such transactions < Rs 500 crores ▪ where the aggregate value of such transactions > Rs 500 crores	Operating profit margin to operating expense ▪ ≥ 20 per cent ▪ ≥ 22 per cent
2.	Knowledge processes outsourcing services (KPO services), with insignificant risks	Operating profit margin to operating expense ≥ 25 per cent
3.	Intra-group loan to wholly owned subsidiary (WOS) where the amount of loan: ▪ < Rs 50 crores ▪ > Rs 50 crores	Interest rate equal to or greater than the base rate of State Bank of India (SBI) as on 30th June of the relevant previous year: ▪ plus 150 basis points ▪ plus 300 basis points
4.	Explicit corporate guarantee to WOS where the amount guaranteed ▪ < Rs 100 crores ▪ Rs 100 crores, and the credit rating of the borrower, by a Securities and Exchange Board of India (SEBI) registered agency is of the adequate to highest safety (explicit corporate guarantee does not include letter of comfort, implicit corporate guarantee, performance guarantee or any other guarantee of similar nature)	▪ Commission or fee of 2 per cent or more per annum ▪ Commission or fee of 1.75 per cent or more per annum
5.	Specified contract research and development services (Contract R&D services), with insignificant risks, wholly or partly relating to software development	Operating profit margin to operating expense ≥ 30 per cent
6.	Contract R&D services, with insignificant risks, wholly or partly relating to generic pharmaceutical drugs	Operating profit margin to operating expense ≥ 29 per cent

Sr. No.	Eligible International Transaction	Safe Harbour ratios
7.	Manufacture and export of: ▪ core auto components ▪ non-core auto components where 90 per cent or more of total turnover relates to Original Equipment Manufacturer sales	Operating profit margin to operating expense: ▪ ≥ 12 per cent ▪ ≥ 8.5 per cent

☐ Validity for five years

The SHRs are applicable for a period of 5 years starting with Assessment Year (AY) 2013-2014 for the prescribed sectors. The option of being governed by SHRs shall continue to remain in force for the period specified by the taxpayer in the prescribed form (Form No. 3CEFA) or a period of five years whichever is less.

☐ No threshold for eligibility to SHR

There are no thresholds/upper ceilings of transaction amount for eligibility to SHR. The threshold of Rs 100 crores for IT, ITES and KPO sector as proposed by the draft SHR has been done away with. However, different safe harbour ratios are provided for transactions above and below Rs 500 crores in the cases of IT and ITES services. Further, corporate guarantee transactions above Rs 100 crores are now eligible for applicability of SHRs, provided the credit rating of the borrower (i.e. associated enterprise) done by a SEBI registered agency is of the adequate to highest safety.

☐ Categorization of services and safe harbours

The definitions of various eligible international transactions, including that of the IT, ITES, KPO and contract R&D services relating to software development, are largely retained same as those provided in the draft SHRs. To provide distinction from routine business process outsourcing services, the definition of KPO services has been modified to include only those services that require “application of knowledge and advanced analytical and technical skills”. The SHRs have also provided the definition of generic pharmaceutical drugs as “a drug that is comparable to a drug already approved by regulatory authority is dosage form, strength, route of administration, quality and performance characteristics, and intended use”. Further there is no reduction in the safe harbour ratios from those prescribed in the draft SHRs, except in case of KPO services where it has been reduced from 30 per cent to 25 per cent. On the contrary, the safe harbour ratio for the IT and ITES services for the over Rs 500 crores category is specified at a marginally higher rate of 22 per cent.

☐ Continued applicability of SHR

The taxpayer can opt-out of the safe harbour regime from the second year onwards, by filing a declaration to that effect with the AO. Further, the option exercised by the taxpayer can be held invalid by the Transfer Pricing Officer (relating to the eligibility of the taxpayer or of the international transaction or both), if there is any change in the facts and circumstances on the basis of which the option exercised by the taxpayer was initially held to be valid. However, such withdrawal cannot be done without providing the taxpayer an opportunity of being heard. In such case, the taxpayer has a right to file his objection with the Commissioner.

- ☐ Timelines prescribed and taxpayers granted right to object against adverse order

The Rules provide for a time bound procedure for determination of the eligibility of the taxpayer and of the international transactions for SHR. In case action is not taken by AO/TPO within the following time lines, the option exercised by the taxpayer shall be treated as valid:-

- reference by the AO to the TPO shall be made (for determination of the eligibility of the assessee or eligibility of the international transactions or both) of an assessee within a period of two months from the end of the month in which Form No. 3CEFA is received by him;

- TPO shall pass an order determining the validity of the option exercised by the taxpayer within a period of two months from the end of the month in which reference received from the AO;

Further, the taxpayer shall have a right to file an objection with the Commissioner against adverse order regarding the eligibility of taxpayer/international transaction. Here again, if the Commissioner does not passes an order within a period of two months from the end of the month in which the objection has been received by him from the taxpayer, the option exercised by the taxpayer shall be treated as valid.

- ☐ Procedural requirements

To exercise their option to be governed by the SHRs, the taxpayer is required to file specified form (Form No 3CEFA) with the AO on or before the due date for furnishing the return of income for –

- the relevant assessment year, in case the option is exercised only for that assessment year; or

- the first of the assessment years, in case the option is exercised for more than one assessment years.

The Form No. 3CEF requires information on the nature of business or activities of the taxpayer as well as details of the eligible international transactions opted for the SHRs. The return of income needs to be furnished before the date of furnishing of Form 3CEFA.

In case SHRs are opted at once for more than one assessment years, the taxpayer for each assessment years following the initial assessment year, needs to furnish a statement to the AO providing details of eligible transactions, their quantum and details of the profit margins or the rate of interest or commission, before furnishing return of income of that year.

- Even where the taxpayer opts to be governed by the SHRs, they will be required to comply with the regulations regarding mandatory documentation and filing the Accountant’s report for each AY under consideration, like any other taxpayer

- Safe harbour rules shall not apply if an AE is located in any country or territory notified under Section 94A of the Act, or low tax (less than 15 per cent tax rate) country or territory.

[Notification NO. 73/2013, dated 18-09-2013]

Application of General Anti Avoidance Rule (GAAR):

CBDT has introduced GAAR under chapter X-A of Income Tax Act, 1961. They shall come into force on the 1st day of April, 2016 i.e. in respect of the tax benefit obtained from the arrangement on or after the 1st. day of April, 2015, irrespective of the date on which it has been entered into.

Chapter X-A does not apply to:

- An arrangement where the tax benefit in the relevant A.Y. arising, in aggregate, to all the parties to the arrangement does not exceed a sum of Rs. 3Crore

- A Foreign Institutional Investor(FII)

  {Being an Assessee who has taken benefit of an agreement referred to in sec 90 or 90A & has invested in listed securities or unlisted securities with the prior permission of the competent authority.}

- A non-resident person who has investment by way of offshore derivative instruments or otherwise, directly or indirectly, in a FII

- Any income accruing or arising to, or deemed to accrue or arise to, or received or deemed to be received by, any person from transfer of investment made before the 30 August 2010.

Determination of consequences of impermissible avoidance arrangement.

Where a part of an arrangement is declared to be an impermissible avoidance arrangement, the consequences in relation to tax shall be determined with reference to such part only.

Notice, Forms for reference by AO to the commissioner

- ☐ The Assessing Officer (AO) shall, before making a reference to the Commissioner, issue a notice in writing to the taxpayer. The notice shall contain the following:

  - Details of the arrangement to which GAAR provisions are proposed to be applied

  - The tax benefit arising under the arrangement

  - The basis and reason for considering that the main purpose of the identified arrangement is to obtain tax benefit

  - The basis and reasons why the arrangement satisfies the condition to consider such arrangement as an IAA &

  - The list of documents and evidence relied upon in respect of forming basis and reasons as stated above.

- The AO shall make a reference to the Commissioner in Form 3CEG which contains the following:
    - Name and address of the taxpayer;
    - PAN of taxpayer;
    - Constitution (status) of the taxpayer;
    - Residential status of the taxpayer;
    - AY in respect of which the proceedings relating to GAAR are proposed to be invoked;
    - Factual matrix of the arrangement and details of other parties to the arrangement;
    - Details of tax benefit to the taxpayer and all parties to the arrangement;
    - Brief facts in respect of computation of tax benefit;
    - Whether obtaining the tax benefit is the main purpose of the arrangement or part of the arrangement;
    - Whether a notice has been served on the taxpayer;
    - Indicate which of the prescribed conditions is satisfied by the arrangement;
    - Brief reasons for seeking declaration of arrangement as IAA;
    - Tax consequence likely to arise if arrangement is declared as IAA; and
    - The last date of completion of assessment/ re-assessment proceedings.
- The Commissioner, if satisfied that provisions of GAAR are not required to be invoked with reference to an arrangement, after considering reference received from AO or reply of the taxpayer in response to notice issued, shall issue directions to AO in form 3CEH mentioning, inter -alia, basis of finding that GAAR provisions are not applicable.
- The Commissioner for the purpose of further reference, shall record his satisfaction regarding the applicability of the provisions of GAAR in Form No. 3CEI containing the prescribed particulars (similar to the ones as required to be made by the AO as mentioned above along with certain other prescribed details) and enclose the same along with the reference being made to the Approving Panel.

Time limits

- No directions shall be issued by the Commissioner after the expiry of one month from the end of the month in which the date of compliance of the notice (notice providing an opportunity of being heard) expires.

- ☐ No reference shall be made by the Commissioner to the Approving Panel after the expiry of two months from the end of the month in which the final submission is received from the taxpayer in response to the notice issued to him.

- ☐ The Commissioner shall issue directions to the AO in Form No.3CEH, -

  - When reference is received from AO - within a period of one month from the end of month in which the reference is received by him; and

  - When reply of the taxpayer is received in response to the notice issued - within a period of two months from the end of month in which the final submission of the taxpayer in response to the notice issued by the Commissioner is received.

[Notification NO. 75/2013, dated 23-09-2013]

DTAAs/Protocols Signed and Notified

India-Australia: Protocol to the DTAA

The salient features of the Protocol are outlined below:

- ☐ The Protocol has introduced a definition of the term National under Article 3 of the Convention.

- ☐ The threshold for the furnishing of services, including consultancy services through employees, which creates Service PE in the Source State, has been increased to 183 days in 12 months period.

- ☐ A threshold of 90 days in any 12 month period has been prescribed for constituting the PE arising out of carrying on of activities in connection with the exploration for or exploitation of natural resources.

- ☐ A threshold of 183 days in any 12-month period has been prescribed to constitute a PE arising due to carrying on of activities of operation of the substantial equipment.

- ☐ The Protocol has also eliminated the Force of Attraction rule under Article 7 -Business Profits of the Convention. Thus, profits arising on the sale of goods or other business activities as attributable to the PE may be subject to tax in the PE state.

- ☐ A new Article 24A on Non-discrimination has been inserted in line with the international practices and was applicable to all kinds of taxes notwithstanding Article 2 - Taxes Covered and persons, whether or not resident of both or either of the contracting states. Furthermore, this Article shall not apply to any domestic law provisions of the contracting states, which are enshrined to prevent the avoidance or evasion of taxes, to address thin capitalization and to ensure collection of taxes or to provide tax incentives to eligible taxpayers in respect of research and development expenditure.

- ☐ Article 26 on Exchange of information in the Convention has been amended by the protocol in line with the treaties entered into by India with countries including Singapore, Norway, the Netherlands and Nepal. This Article was applicable notwithstanding Article 1 and Article 2 of the Convention and would help the

Revenue Authorities of two contracting states to exchange taxpayer information on a wider range of taxes.

- A new Article 26A on Assistance in Collection of Taxes has been inserted to lend assistance to the contracting states in the collection of revenue claims, subject to certain conditions and procedures. This Article was in line with the tax treaties entered into by India with Norway, Nepal, Finland, Luxemburg, Ethiopia and Armenia, among others.

- The protocol shall be effective as given below.

  - In the case of Articles on General Definitions, Permanent Establishments, and Business Profits in the Convention, from Financial Year 2014-15 onwards.

  - In the case of Articles on Non-Discrimination and Exchange of Information in the Convention, from April 2, 2013.

  - In the case of the Article on Assistance in the Collection of Taxes in the Convention, from July 18, 2013.

[Notification NO. 74/2013, dated 20-09-2013]

DTAA between Albania and India

The Union Government of India and Government of Albania on 8 July 2013 signed an Agreement for Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to the Taxes on Income and on Capital (DTAA). The agreement was signed to provide tax stability for the residents of both the nations. It would also facilitate mutual economic cooperation between the two countries. The signed agreement would also stimulate the flow of investment, technology and services between India and Albania.

The agreement incorporates provisions for effective exchange of information between tax authorities of the two countries, which also includes exchange of banking information and supply of information without recourse to domestic interest.

Major Points of the Agreement Signed

- According to the provisions of the treaty, taxes on profits from business activities will be paid only in the country where the business is resident, as long as it has a permanent office. In any case, the business can be taxed in the other country, only for the profits realized at the permanent office (establishment).

- Taxes on dividends, interests, licenses and royalties, will be paid at the country where they are earned or obtained, but if the beneficial owner of these revenues is resident in the other country, the tax imposed on him/her, shall not exceed 10 per cent of the gross amount, of the dividends, interests, licenses or royalties.

- When a person in Albania generates income or owns capital that in accordance with the provisions of the agreement can be taxed in India, Albania will allow a deduction from the Albanian income and capital tax,

equal to the income tax paid in India. However, this deduction, in any case shall not exceed that part of the income or capital tax as calculated, before the deduction is given accordingly.

- Para 2 of Article 9 of the agreement incorporates concerns related to Associated Enterprises and thus involves recourse to Mutual Agreement Procedures for relieving double taxation in cases that involves transfer pricing adjustments.

- An article on the Assistance in Collection of Taxes is also mentioned under the Article and includes provisions to take measures on conservancy. It includes anti-abuse (limitation of benefits) provisions to ensure that the benefits of the Agreement are availed of by the genuine residents of the two countries.

[Notification NO. 2/2014, dated 07-01-2014]

INTERNATIONAL TAXATIONCASE LAWS

HIGH COURT DECISION

Samsung Heavy Industries Co. Ltd. vs. DIT (Uttarakhand High Court)[1]

Article 7 of DTAA: Even in a composite contract, Dept cannot assess off-shore profits without showing how it is attributable to the permanent establishment

Facts of the case:

- The assessee, a foreign company, having a Project Office in India, entered into a consortium contract with ONGC and L&T. It was claimed that the assessee had suffered a loss on the work done inside India and that income on the work done outside India was not assessable to tax in India. The assessee filed return of income for the loss incurred

- The Assessing Officer (AO) held that 25 per cent of the work done outside India had to be assessed in India, and also the AO refused to accept the deduction claimed by assessee.

- Income tax Appellate Tribunal confirmed the order of the AO. It was held that the said project office constituted a “permanent establishment” under Article 5(1).

Held:

- Being a foreign company, the assessee is governed by the Income-tax laws as prevalent in home country. In terms of Article 7(1), profits of an enterprise of a Contracting State shall be taxable only in that state unless the enterprise carries on business in the other Contracting State through a Permanent Established (PE). The said paragraph also provides that the profits of the enterprise may be taxed in the other State only so much of the same as is attributable to that Permanent Established (PE).

[1] Appeal No. 01 of 2012

- In terms of the DTAA, if an enterprise does not have a tax identity in India in the form of a permanent establishment, it has no obligation to either submit any tax return with, or pay any tax to India.

- There was no finding recorded by tax authority that 25 per cent of the gross revenue of the assessee was attributable to the business carried out by the said Project Office. Neither the AO nor the Tribunal has made any effort to bring on record any evidence to justify the same.

Accordingly, the High Court held that tax liability could not be fastened without establishing that the same is attributable to the tax identity or permanent establishment of the enterprise situate in India.

Cairn UK Holdings Ltd vs. DIT (Delhi High Court)[2]

Non-residents are eligible for the benefit of 10per cent tax rate on long-term capital gains under the Proviso to s. 112. The AAR should avoid giving conflicting rulings

Facts of the case:

- The assessee, a foreign company registered in Scotland, held equity shares in Cairn India Limited (CIL) which is listed company. During the financial year 2009-10, the assessee transferred its equity shares in CIL to another foreign company through an off-market transaction. This transfer resulted in LTCG which the taxpayer offered to tax at a beneficial rate of 10 per cent under the Indian Income-tax Act, 1961.

- According Authority for Advance Ruling (AAR), the benefit of the lower tax rate on transfer of shares of a listed company was available only to taxpayers who were eligible for indexation benefit under Section 48 of the Act.

- A non-resident could not take the benefit of indexation provisions in computing capital gains. If the non-resident was given the benefit of 10 per cent tax rate on sale of listed company shares in an off-market transaction, the 20 per cent rate on LTCG would become redundant, which could not have been the intent of the statute.

High Court's Ruling

- The benefit could not be denied only because the indexation benefit was not applicable to a non-resident assessee. If the legislature intended to deny the benefit of reduced tax rate to taxpayers who had taken benefit of neutralization of exchange risk, this would have been explicitly provided for in the statute. Merely because grant of benefit of lower tax rate to non-residents on sale of shares of a listed company would result in the same benefit becoming available to all non-resident taxpayers could not justify reading Section 112 (1) of the Act differently.

- Relying on the SC's observation in case of Vodafone International Holding, the Court held that certainty and stability formed the basic foundation of any fiscal law. The AAR's taking a diametrically reverse view in this case had brought about uncertainty in understanding the impact and effect of the tax laws.

---

[2] 337 ITR 131

- The decisions in Timken France SAS had been followed by the AAR in several cases in the past. The AAR should follow its earlier view, unless there were strong grounds and reasons to take a contrary view. In this case, there was no compelling justification or reason to override and disturb the earlier view.

DIT vs. Alcatel Lucent USA Inc (Delhi High Court)[3]

S. 234B: A non-resident assessee which does not admit income chargeable to tax must be inferred to have induced the Indian payer not to deduct TDS and so it is liable for advance-tax interest

Facts of the case:

- The assessee, a USA company, supplied telecom equipments to customers in India. The assessee claimed that it did not have a PE in India and that the income was not chargeable to tax.

- The Income tax authority conducted a survey in the premises of the assessee of Indian subsidiary and Assessing Officers concluded that the assessee was having Permanent Establishment (PE) in India and attributed 2.5 per cent of the sale proceeds of the hardware as profit attributable to the PE in India.

- The AO also levied interest u/s 234B for failure to pay advance-tax. Before the CIT (A), the assessee accepted that the income was chargeable to tax but argued, relying on Jacabs Civil Incorporated **330 ITR 578 (Del), that as it was a foreign company and the income was liable for TDS, it was not liable to pay advance-tax.**

- The CIT (A) and Income-tax Appellate Tribunal ruled in the favour of the assessee.

High Court Ruling:

- In case of Jacabs, the assessee admitted the taxable income in the income-tax return. However in this case the assessee did not admitted the taxable income in the income-tax return. Accordingly the facts of the case were different from that the facts in case of Jacabs.

- The argument that the Indian parties are not liable to deduct tax u/s 195 despite the presumed request of the assessee is one of convenience and not acceptable because in a practical view of the matter, the Indian payers could not have resisted the assessee's request given future business prospects and the need to keep the assessee in good humour.

- Also, having denied its tax liability and leading the Indian payers to believe that no tax was deductible it is inequitable & unfair on the assessee's part to shift the responsibility to the Indian payers & expect them to deduct tax from the remittances. The assessee must take responsibility for its volte face. Once liability to tax is accepted, all consequences follow; they cannot be avoided

- The High Court observed that it would be equitable that the assessee, who accepted the tax liability after initially denying it, should be permitted to shift the responsibility to the Indian payers. Once the liability to tax is accepted by the assessee, all the consequences follow.

---

[3] I.T.A 327 to 330; 336 to 340 / 2012

- Accordingly, the High Court held that the taxpayer was liable to pay interest under Section 234B of the Act.

Platinum Asset Management Ltd vs. DDIT.[4]

Section 115AD of the Act – loss arising to a FII from index derivative transactions, is a capital loss and can be set-off against capital gains from sale of shares:

Facts of the case:

- The taxpayer was a Foreign Institutional Investor ("FII"). In respect of its two sub-accounts, the taxpayer had furnished the return of income declaring short-term capital loss. The loss had arisen from index derivative transactions. Hence, the AO concluded that it was a business loss assessable under the head 'income from business and profession' and not short-term capital loss as claimed by the taxpayer. The set off was denied as the taxpayer had no PE in India. In appeal, CIT(A) confirmed the order.

☐ The issues before the Tribunal were:

- Whether the loss arising from index derivative\ transactions was business loss or capital loss? Whether the loss arising from index derivative transaction can be set-off against capital gains arising from sale of shares?

Held:

- In terms of section 115AD of the Act, a FII is an 'investor' and further, income from transfer of securities is chargeable under the head 'capital gains' (long-term or short-term) and not business loss, and eligible for set off against capital gains.

- SEBI (FII) Regulations and section 115 AD of the Act show that in case of FIIs the government has not contemplated that the tax authority should distinguish between the securities as those constituting capital asset or stock-in-trade. If a FII receives income in respect of securities or from transfer of securities, such income should be considered only u/s. 115AD (1).

- Though in common parlance, shares and debentures are distinct from derivatives, such distinction is obliterated by mentioning the term 'securities' as defined in section 2(h) of Securities Contract (Regulation) Act, 1956 .

AUTHORITY FOR ADVANCE RULINGS

Endemol India (P.)Ltd.[5]

Section 9(1)(vii) of the Act; Article 12 of India- Netherlands DTAA – while in terms of the Act, the consideration paid for the services was FTS, since the recipient was not enabled to independently apply the technology, knowledge or expertise, the payment was not FTS under India-Netherlands DTAA, which in absence of PE in India, was not taxable in India.

---

[4] 2013-ITRV-ITAT-MUM-074

[5] A.A.R. Nos. 1075 of 2011

Facts of the case:

- The Applicant was an Indian tax resident company and a member of an international group of companies. The Applicant was engaged in the business of providing and distributing tele vision programmes. Dutch Co (DCo) was also a member company of the Group. The Applicant entered into Consultancy Agreement with DCo under which DCo was to provide certain services such as, General Management, International Operations, Legal and Tax Advisory, Controlling and Accounting, Corporate Communications, Human Resources, Corporate Development, Mergers & Acquisitions, etc. These services were provided by DCo outside India. According to the Applicant these were administrative services.

☐ The Applicant approached the AAR for its ruling on the following issues.

- Whether the payments made by the Applicant to DCo for administrative services would be in the nature of FTS under Article 12 of India- Netherlands DTAA?
- If the payments were not FTS, would they be Business Income, which in absence of PE of DCo in India, would not be chargeable to tax in India?
- If the payments were not FTS, would they be subject to withholding under section 195 of the Act?

Held:

☐ As regards the Act

- The services rendered by DCo require technical knowledge, experience, skill, know-how or processes and hence, cannot be termed merely as administrative and support services as tried to be made out by the Applicant.
- As per The consultancy agreement, DCo was to render its 'considerable experience, knowledge and expertise' and the payments were to be made therefore.
- The definition of FTS in Explanation 2 to section 9(1)(vii) of the Act, includes managerial, technical or consultancy services. Hence, the consideration paid for the services rendered by DCo were covered by the said definition of FTS.

☐ As regards India-Netherlands DTAA

- Definition of FTS in Article 12(5) of India-Netherlands DTAA, contains 'make available' clause, which would require that the Applicant should be enabled to independently apply the technology, knowledge or expertise. The Applicant merely took assistance of DCo in its business activities and there was nothing to suggest that it was enabled to independently apply the technology, knowledge or expertise and thus, 'make available' requirement was not satisfied.
- DCo did not have any PE in India. Hence, the consideration paid for the services rendered was not taxable in India.

Eruditus Education (P.) Ltd., In re[6]

Section 9, Article 12, 5 of India Singapore DTAA. Provision of high quality education FTS - However exemption under Article 12 available to Singapore educational institution - on facts no PE and sum not chargeable to tax in India.

Facts of the case:

- The applicant was an Indian company in the business of providing high quality executive education programs. The applicant entered into agreement with a Singapore company ("SingCo"), which was in the business of providing management education programmes globally. As per the Agreement, SingCo was to conduct teaching intervention at SingCo's global campuses in Singapore/France/India and through telepresence in Singapore, while the applicant was to assist in marketing, organizing, managing and facilitating. The programme was to be for 11 months and teaching intervention by SingCo was to be for 30 days comprising in-class teaching at Singapore and at French campuses of SingCo (16 days), in-class teaching by SingCo faculty in India (6 days) and teaching through tele-presence in Singapore (8 days). The applicant was to compensate SingCo for the cost and other incidental expenses.

Held:

- The services to be rendered by SingCo involved expertise in, or possession of, special technical skill or knowledge. Hence, the payment will be FTS, both under the Act and under India - Singapore DTAA. However, since there is no dispute that SingCo is an educational institution, the payment will be covered by the exclusion in Article 12(5)(c) of India-Singapore DTAA.

- On facts, SingCo will not have PE in India under Article 5(1) or 5(8) of India-Singapore DTAA.

- Accordingly the amount is not chargeable to tax in India.

Booz & Company (Australia) Pvt. Ltd.[7]

Provision of Technical and professional employees to the Indian affiliate company (ICo) results in a Permanent establishment (PE) in India; Factors such as interdependency and nature of services rendered considered in arriving at the conclusion.

Facts:

- The Booz & Co. Group (Group entities) is a global network of group companies. With the intention of optimizing its global business network and expertise, entities within the Group provided as well as availed services from each other.

- Accordingly, the Group entities received payments from ICo (Indian affiliate of Group) for provision of technical and professional personnel.

---

[6] A.A.R. No. 1037 of 2011

[7] TS-76-AAR-2014

- Features of the arrangement between the Group entities and ICo as appearing in the application and also emphasized by the tax authorities are as follows:

  - All projects won by the Group were catered to by a common pool of personnel.

  - ICo executed its projects through its own employees and to the extent required, procured the services of personnel of the relevant Group entity.

  - The personnel were under the control and supervision of ICo in respect of ICo's project. However they were bound by the employment agreement entered with, and overall control of, the relevant Group entity. Thus the relevant Group entity had the power to recall and replace its personnel.

  - The relevant Group entity provided on-the-job training to such personnel, was answerable to third party claims for infringement of any rights by such personnel.

  - The expertise of the relevant Group entities in giving consultancy in the fields that the Group operates, the brand equity the Group enjoys, the capabilities the Group has developed across the globe and services from the Group professionals and experts is needed for ICo to optimally function.

  - The Group's business is manpower-centric in which the only important asset is human resource. The Group entities contended that in the absence of a Permanent Establishment (PE) of the relevant Group entity in India, the fee received from ICo cannot be taxed as business income in India but should be taxed as Fee for technical services (FTS).

  - The Tax Authorities contended that ICo is exclusively dependent on Group entities in getting the services of capable personnel as well as their on-the-job training, in order to achieve optimal efficiency. This dependency of ICo on the Group entities blurs the identity of individual entities and thus, ICo constitutes a dependent agent of the Group entities. Additionally, the number and high level of qualification of personnel deployed by the Group entities to ICo clearly establishes that ICo constitutes a service PE. The access given by ICo's client/ICo to the personnel deployed to ICo in a given space also renders that place a fixed place PE of the relevant Group entities.

Held:

- **On Fixed Place PE:**

  - Under a Double Tax Avoidance Agreement (DTAA), one of the sine qua non of a fixed place PE is that, the fixed place of business through which the business is carried on should be 'at the disposal' of the relevant Group entity.

  - Conducting trading operations generally requires a fixed place which the taxpayer uses on a continuous basis. However, taxpayers rendering service usually do not require a place to be at their constant disposal and therefore application of 'disposal test' is generally more complex in such cases.

  - Various factors have to be taken into account to decide a fixed place PE which, inter alia, includes a right of disposal over the premises. Generally, the establishment must belong to the foreign enterprise and involve an element of ownership, management and authority over the establishment.

- **On Service PE:**

  - In terms of the DTAA a service PE is triggered if services are provided in a source State and such services are provided through employees or other personnel. In case of deputation of employees, if the lien over such employees is retained by the deputing company and the employees continue to be on the payroll of the deputing company, a Service PE emerges.

  - Where a business of a group cannot be carried on exclusively without intervention of another entity, normally that entity must be deemed to be the establishment of the group in that particular country.

- **On Agency PE:**

  On the issue of Agency PE, the relevant question is ‘business connection’.

  The essential features of ‘business connection’ are as follows:

  - A real and intimate relation must exist between the activities carried out outside India by nonresident (NR) and activities within India;

  - Such relation must contribute directly or indirectly to earning of income by the NR in his business;

  - A course of dealing or continuity of relationship and not a mere isolated or stray nexus between the business of the NR outside India and the activity in India, would furnish a strong indication of ‘business connection’ in India.

  - Apart from the fact that the requirements of agency are satisfied, the facts fulfill the above essential features of ‘business connection’.

  - **On the basis of the above, the AAR ruled that the fact pattern of the Group entities and ICo, a PE of the Group entities does exist in India. Therefore, incomes received by them from ICo are taxable as business profit under Article 7 of the respective DTAAs. Where there is no DTAA, it is taxable under the provisions of the Act.**

INOME TAX APPELLATE TRIBUNAL DECISIONS

POSCO Engineering & Construction Co Ltd vs. ADIT (ITAT Delhi)[8]

Entire law on taxability of “composite” contracts for supply of offshore & onshore supply & services under Act & DTAA explained

Facts of the case:

- The assessee was a company incorporated in Korea engaged in construction, design and service work for steel mill facilities with general civil engineering, electricity and housing projects. During the year under

[8] ITA No. 5787/Del/2013

consideration, the taxpayer undertook a turnkey project in India from Steel Authority of India Limited (SAIL),involving offshore supplies, and offshore design and engineering, onshore supplies and onshore supervision of the installation work.

- During the same year, the assessee received an advance against the first milestone towards offshore supply, onshore supply and onshore supervision. The taxpayer did not offer a tax advance in respect of offshore supplies on the premise that the title in the supplies was transferred outside India, and for the onshore portion, the advance was not offered to tax in the year under consideration but was offered in subsequent years in which the actual activities took place.

Tribunal's Rulings:

☐ **Income from Offshore supplies**

- Opposing the AO's contention, the Tribunal held that the contract with SAIL was not a composite contract, since all components were separately identifiable and only the income related to activities in India were taxable in India and further the tribunal held that the title transfer in the offshore supplies took place outside India, nothing could be taxed as attributable to the PE in India

- The Tribunal observed that certain onshore services, i.e. training, testing, defect liability, liquidated damages, for which no consideration had been separately identified in the contract, formed part of the consideration for the offshore supplies. Thus, the Tribunal held that the consideration for such services needed to be apportioned from the consideration for offshore supplies, and should be taxed in India as attributable to the PE in India. Having held that, the Tribunal directed the AO to verify and determine the value of onshore services in the nature of training, etc.

☐ **Income from the onshore portion (supplies and services)**

There was no dispute as to the taxability of the onshore portion, and the limited issue before the Tribunal was in the year of receipt of advance or in the year of actual supplies/services. The Tribunal accepted the taxpayer's contention and held that the onshore portion was taxable in the year of actual supply/service rendered. Though, the Tribunal directed the AO to verify the actual dates of supplies and the services rendered.

☐ **Income from design and engineering**

The Tribunal held that income from design and engineering was taxable as Fees technical Services under the Act as well as under the tax treaty. The Tribunal dismissed the taxpayer's contention that design and engineering was an inseparable part of the supplies. The Tribunal also disapproved the AO's action of taxing design and engineering as attributable to the PE. The Tribunal held that since design and engineering was not attributable to the PE, it would be taxable on a gross basis.

London Star Diamond Company (I) P. Ltd vs. DCIT (ITAT Mumbai)[9]

Loss on forward foreign exchange contracts is incidental to the exports business and not a "speculation loss".

[9] I.T.A. No.6169/M/2012

However, if the contract is prematurely cancelled, the assessee has to justify the loss

Facts of the case:

- Assessee was engaged in the business of trading and manufacturing rough and polished diamonds, in respect of which it had outstanding receivable in foreign currency. To hedge the possible foreign exchange loss on exports, the Company had entered into forward contracts (FCs) with banks. Before the Assessing Officer (AO), the Company submitted that the net loss, being an integral part of the export business, constituted a business loss and not a speculative loss, but this claim was disallowed by AO. The Commissioner of Income-tax (Appeals) upheld the AO's order. Aggrieved by this order, the Company appealed to the Tribunal.

Tribunal Ruling:

- FCs when entered with banks for hedging losses with respect to foreign exchange fluctuations of the export proceeds had to be considered integral or incidental to the assessee's export activity. Such losses and gains are constituted business loss or gains and not speculation loss or gains. The fact that forward contracts were prematurely cancelled could not alter the nature of the transaction. FCs were a commodity

- The law does not require one-to-one correlation between the FCs and export invoices. Where total value of the FC does not exceed the total outstanding receivable in foreign exchange, the claim is sustainable as a business loss. Considering the analysis of transactions put forth by the company, FCs were an integral part, or incidental to, the core business of exporting diamonds. Therefore, FCs constituted 'hedging transactions' and not 'speculative contracts'.

- Losses arising on cancellation of matured FCs, being integral or incidental to business of export of diamonds, was allowable as a business loss. Loss on premature cancellation of FCs, occurred as the maturity date of some such FCs fell during week-end days. This being an acceptable explanation, suchloss is allowable as a business loss, subject to verification of facts by the AO.

ADIT vs. Valentine Maritime (Gulf) LLC (ITAT Mumbai)[10]

If the contract falls u/s 44BB, incidental technical services are not assessable as "fees for technical services" u/s 9(1)(vii).

Facts of the case:

- The contract was a composite one and its main purpose was to install offshore pipelines, etc. The activities undertaken were incidental to the main job and were an integral part of the contract to ensure that all activities related to pipelines are successfully complied with the contract.

Held:

- According to department the activities relating to providing technical services, assessed as "fees for technical services" u/s 9(1)(vii) was not acceptable. When a contract consists of a number of terms and conditions, each condition does not form a separate contract. The entire consideration is assessable only u/s 44BB and no part of it is assessable as fees for technical services u/s 9(1)(vii).

- The argument of department based on Alcatel Lucent USA (Del) that even a foreign company is liable to pay advance tax and consequential interest u/s 234B is not acceptable in view of the contrary decision of the jurisdictional High Court in NGC Network 313 ITR 187 (Bom).

[10] I.T.A. No.700/Mum/2009

Tesco International Sourcing Ltd. vs. DDIT.[11]

Section 9(1)(i) of the Act – no income arises to a LO of non-resident whose activities are confined to sourcing of goods for export

Facts of the case:

- HKCo was a company incorporated in Hong Kong and a member of an international Group of companies. HKCo acted as a sourcing channel for the entire Group. It sourced products internationally at competitive prices and of quality standard prescribed by the Group and resold goods to the affiliates. HKCo had established a Liaison Office ("LO") in India for acting as a communication channel between HKCo and apparels manufacturers in India. Indian suppliers raised invoice on HKCo and HKCo, in turn, raised invoice on the buyer entities without any mark up. HKCo charged 5per cent commission to the buyer on the invoice value. LO also monitored the progress, quality, etc., at the manufacturing facilities and also the time schedule.

- The AO concluded that the activities of LO pertained to supply chain management activities of HKCo. Hence, the exclusion in Explanation 1(b) to section 9(1)(i) of the Act did not apply and passed draft assessment order accordingly. Relying on the decision in Columbia Sportswear Company, the DRP accepted the conclusion of the AO and directed him to make the assessment.

Held:

- The LO was engaged in (i) identification of the vendors in India; (ii) communication of the requirements with regard to design and specifications to the vendors; (iii) receipt of the prototype from the vendor; (iv) quality check for the products before production of goods; and (v) tracking the production and delivery including forecasting and scheduling of the order.

- Considering the activities carried on by the LO of HKCo, the activities squarely fall within the ambit of explanation 1(b) to section 9(1)(i) of the Act. Further, there is no evidence to suggest that LO had indulged in commercial activities. In arriving at the conclusion of non taxability, strong reliance is placed on the decision of the Karnataka High Court in Nike Inc.

Antwerp Diamond Bank NV vs. ADIT[12]

Article 7,11 of India- Belgium DTAA – (i) interest paid by Indian branch of foreign bank deductible for computing profit attributable to PE; (ii) interest paid by branch to HO being payment to self, no taxable income in hands of HO

Facts of the case:

- The taxpayer was Indian branch of a Belgian bank. During the relevant assessment year, the taxpayer had made payments to its Head Office ("HO") towards interest on subordinate debts and term borrowing and had claimed the interest as an expense of the branch. The said interest was offered for taxation in the hands of the HO in terms of Article 11 of India-Belgium DTTA.

---

[11] I.T.A Nos.1323 to 1327

[12] TS-150-ITAT-2014(Mum)

- Relying on the decision in ABN AMRO Bank NV vs. ADIT [2005] 97 ITD 89, the AO disallowed interest paid to the HO. CIT(A) confirmed the order of the AO.

Held:

- The decision relied on by the AO and CIT(A) has been reversed in Sumitomo Mitsui Banking Corp. vs. DDIT [2012], which was in the context of India-Japan DTAA. The Tribunal in Sumitomo case held that although interest paid to the HO by Indian branch (which constitutes PE in India) is not deductible as expenditure under the domestic law being payment to self, the same is deductible while determining the taxable profit attributable to the PE in India in terms of DTAA. As per the domestic law, the said interest, being payment to self, cannot give rise to taxable income in India in the hands of HO. The same position also applies to payment of Interest by Indian branch of a foreign bank to its sister branch offices abroad.

US Technology Resources Pvt Ltd vs. ACIT[13]

Article 12(4), India-USA DTAA – Provision of advisory services in relation to assisting in management and decision making are technical in nature and satisfies the test of 'make available' as stipulated under the India-US DTAA. Accordingly it is taxable as fees for included services (FIS):

Facts of the case:

- The Taxpayer is an Indian company (ICo) engaged in providing software development services to the customers based in India.

- ICo had engaged an American company (FCo) to provide assistance, advice and support to ICo in management, decision making, sales and business development, financial decision making, legal matters and public relations activities, treasury service, risk management service and any other management support as may be mutually agreed between the parties.

- For the above services, ICo made certain payments to FCo without deducting taxes and claimed the deduction for the same. ICo contended that the services rendered by FCo are mainly in the form of assistance in decision making; therefore, such services are clearly in the nature of management services, which is outside the ambit of definition of "FIS" under India USA DTAA. Further, it was argued that these services do not 'make available' any technical knowledge or expertise such that the person acquiring the service is enabled to apply the technology.

- However the Tax Authority disallowed the payments on the grounds that such payments to non-residents were in the nature of consultancy fees on which tax was required to be withheld u/s. 195 of the Act. Also as soon as the advice or support is received, the same is available to ICo for using them in the decision making process of the management. Therefore, it may not be correct to say that the technical services were not 'made available' to ICo.

- In terms of Article 12(4) of India-USA DTAA, FIS means payments of any kind to any person in consideration for rendering of any technical or consultancy services (including through the provision of services of technical or other personnel), if such services made available technical knowledge, etc.

[13] TS-511-ITAT-2013(Coch)

Held:

- Memorandum of Understanding between India and USA makes it clear that only services which are technical in nature can be considered for included services. Even consultancy services should be technical in nature.

- The services rendered by FCo were used by ICo for making various management decisions. Tribunal also referred to the definitions of terms “management” and “decision making” from various management authors and observed that “Decision making is an act of selecting the suitable solution to the problems from various available alternative solutions to guide actions towards achievement of desired objectives”.

- The knowledge accumulated by FCo through study, experience and experimentation with regard to management, finance, risk, etc. of a particular business is nothing but technical knowledge. In the era of technology transformation, the information/ experience gathered by FCo relating to financial risk management of business is technical knowledge. The knowledge and expertise of FCo would be used to support ICo in selecting suitable solution after considering all the alternatives available. Further FCo was giving training to the employees of ICo in making use of the inputs, experience, experimentation, etc. for taking better decision in order to achieve the desired objectives/goals.

- The information and expertise made available to ICo was very much available with them and it could be used in future whenever the occasion arises.

- Thus the management services provided by FCo were in the nature of FIS as per India-USA DTAA and subject to withholding tax in India.

English Indian Clays Ltd vs. ACIT (IT)[14]

Section 9(1)(vii) – Providing report on market survey and identifying potential customers are consultancy services taxable as FTS under the Act.

Facts of the case:

- The Taxpayer, an Indian company, had entered into an agreement with a Foreign Company (FCo) to study the market situation in South East Asia for the product manufactured by the Taxpayer. The agreement referred to these services as ‘consultancy services’.

- The Tax Authority observed that the services are in the nature of consultancy charges under the Act and liable for withholding taxes as FCo did not carry out marketing services but was required to conduct market survey and identify potential customers.

- However, the Taxpayer argued that FCo was engaged only for the purpose of marketing the Taxpayer’s product in South East Asian countries. The nature of the transaction is required to be determined on the basis of the substance and not by the nomenclature. Hence the payments cannot be considered as consultancy charges.

[14] ITA No.72/Coch/2012

Held:

- The work of FCo is to identify the potential customers and file a report regarding the market strategy and developmental studies. The Agreement does not enable FCo to market the products of Taxpayer in South East Asian countries. FCo had to provide a market survey report based on which the Taxpayer could market its product. Hence the payments were in the nature of consultancy charges taxable under the provisions of the Act.

United Helicharters Pvt. Ltd. vs. ACIT[15]

Article 12, Indo U.S. DTAA, section 9-Training to pilots does not make available technical knowledge - Payment for training not taxable in India.

Facts of the case:

- The taxpayer was engaged in the business of charter hire of helicopters. During the year under consideration, a US company provided training to pilots and other staff of the taxpayer in consideration of which the taxpayer made payments to a US company.
- The taxpayer contended that the receipt of the US Company were business profits, which, in absence of PE of US company in India, were not chargeable to tax in India. However, the AO treated the payments as FTS in terms of Explanation 2 to section 9(1)(vii) of the Act and hence, chargeable to tax.
- The issue before the Tribunal was, whether expenditure on training of pilots was in the nature of FTS under Article 12(4) of India-USA DTAA?

Held:

- In terms of Article 12(4)(b) of India-USA DTAA, to constitute FTS the services should have 'made available' technical knowledge, experience, skill, know-how or processes or consist of the development and transfer of a technical plan or technical design.
- The training given to the pilots and other staff was as per the requirement of the regulator and was necessary for eligibility of the pilots and other staff working in aviation industry. Such training does not fall under the term 'make available' under India-USA DTAA. Since the training expenses were not taxable in India in hands of non-resident company, the taxpayer was not required to deduct tax at source while making payment.
- The ITAT ruled that such training does not make available technical skills etc. without considering education institution exclusion.

Sargent & Lundy, LLC, USA vs. ADCIT (IT)[16]

Provision of blueprints i.e., technical designs and plans, without recourse and capable of being used in the future satisfies the test of 'make available' as stipulated under the India-US DTAA; taxable as fees for included services

---

[15] 44 SOT 652 (Ahd)

[16] TS-341-ITAT-2013(Mum)

Facts of the case:

- The Taxpayer, a US tax resident (US Co.), was a consulting firm engaged in providing services to the power industry. The US Co. provided services in the nature of operating power plants, decommissioning, consulting, project solutions and other engineering based services.

- The US Co. entered into an agreement with an Indian Company (I Co.) for rendering consulting and engineering services in relation to ultra-mega power projects in India as per which, the US Co. was required to prepare necessary designs and documents.

- The Tax Authority observed that the services were technical in nature and accordingly, taxable as fees for technical services (FTS) under the Act. Further, the services rendered by the US Co. satisfied the test of 'make available' under the India-US DTAA and, thus, were taxable as fees for included services (FIS).

- Aggrieved, the Taxpayer appealed before the Tribunal on the issue whether the services rendered can be regarded as 'making available' technical knowledge, skill etc. under the India-US DTAA.

Held:

- The expression 'make available', in the context of FIS, contemplates that the services are of such a nature that the payer of the services comes to possess the technical knowledge so provided, which enables the payer to utilize the same in the future.

- Reliance was placed on the decision of the Karnataka High Court (HC) in De Beers India Minerals Pvt. Ltd [346 ITR 467] wherein the HC had observed that technical knowledge is 'made available' if the person acquiring such knowledge is possessed of the same and enabling the person to apply it in the future, on its own.

- In the facts, the US Co. renders technical services in the form of technical plans, designs, projects etc. which are nothing but blueprints of the technical side of the projects. Such services were rendered at a pre-bid stage and is quite natural, that such technical plans etc. are meant for use in the future, if and when, I Co. takes up the bid for installation of the projects.

- When the technical services provided by the US Co. are of such nature, which are capable of use in the future, the same satisfies the test of 'make available' as envisaged under the India-US DTAA. Accordingly, the services rendered by the US Co qualify as FIS and are, therefore, taxable in India.

ITO vs. M/s. Pubmatic India Pvt. Ltd[17]

Section 195 - Purchase of online advertisement space and its sale being independent business transactions, cannot be considered as conducting business on behalf of Seller Company. There is no dependent agent permanent establishment (DAPE) for principal to principal dealings; Payments in the nature of business income not taxable in absence of PE and not liable to withholding tax in India.

---

[17] I.T.A. No. 7044/Mum/2011

Facts of the case:

- The Taxpayer, an Indian company (I Co.), and its parent company, a resident of the US (US Co.), are engaged in the business of providing services of internet advertising and marketing services. I Co. cater to Indian clients whereas the US Co. caters solely to clients outside India and generally in the US. In case of advertisements on foreign websites, the US Co. purchases the advertisement space from foreign website owners and sells them to I Co. at cost plus mark-up and I Co. in turn, sells to I Co.'s clients. In India, a similar procedure, in reverse, is followed when foreign clients of the US Co. want to place advertisements on Indian websites.

- I Co. made payments to US Co. towards purchase of online advertising space without deducting taxes.

- The Tax Authority disallowed the payments made by the I Co. for failure to deduct taxes and contended that the I Co. constituted a DAPE for US Co. as I Co. was habitually conducting business on behalf of the US Co. in India and the activities of the I Co. were devoted wholly or almost wholly on behalf of US Co.

- On appeal, the CIT(A) ruled in favour of I Co. by holding that the I Co. and US Co. are independent parties transacting on arm's length and therefore I Co. did not constitute DAPE.

Held:

- ☐ On appeal by the tax authority, the Tribunal based on the following reasons held that I Co. was an independent party and did not constitute a DAPE of US Co. Further, purchase of advertisement space on a foreign website by I Co. from US Co. constituted a trading receipt of US Co., not taxable in India in the absence of a PE.

    - The advertisement space from US Co. was purchased for I Co.'s customers and was not a transaction which was carried out on behalf of US Co. Further the same was sold at cost plus mark-up being an arm's length price to I Co on a principal-to-principal basis. All risks and rewards of the business were borne by I Co.

    - The advertisement space was in turn 'sold' by I Co. to customers at a different price and the same income has been offered as business income of I Co.

    - The similarity of business activity does not, by itself, indicate that I Co is acting or doing business on behalf of US Co.

Further, neither I Co. nor US Co. was providing services or goods to the clients of the other party or dealing with the clients of the other party.

Accordingly, remittance was towards business income which was not taxable in absence of PE.

M/s. Credit Lyonnais (through their successors: Calyon Bank) vs. ADIT[18]

Sub-arranger fee paid to non-resident does not amount to FTS under the Act as such services do not require technical knowledge, expertise or qualification. Doing small parts of overall activity cannot be regarded as rendering managerial services.

---

[18] ITA No.9596/Mum/2004

Facts of the case:

- The Taxpayer was appointed as arranger by an Indian bank for mobilizing deposits from NRI customers and to act as a collecting bank for receiving and handling application forms under "India Millennium Deposit" (IMD) scheme. The services included; canvassing potential investors; printing marketing material and distributing them; assisting customers in filing the application and obtaining necessary documents; ensuring compliance with local laws; ensuring that payment instruments and applications are correct; issuing acknowledgements; preparing daily remittance schedules and consolidated statements etc.

- The Taxpayer in turn appointed sub-arrangers for mobilizing IMDs both in and outside India. The sub-arrangers work was in the nature of soliciting NRI customers for IMD of Indian banks and then to remit the amount received by them to the designated banks.

- The Tax Authority disallowed the payments of sub arranger fees on the grounds that such payments to non-residents were in the nature of FTS on which tax was required to be withheld under the Act.

Held:

- From the nature and scope of services rendered by the sub-arrangers, it was clear that no technical knowledge, expertise or qualification was required. Convincing potential customers and helping them to fill requisite forms and coordinating transfer of funds, cannot be considered as a "technical service".

- The services rendered by the sub-arrangers were only a small part of the management of the IMD issue. Sub-arrangers were not involved in the "management" of IMD issue. The Taxpayer was simply acting as commission agent or broker for which it was entitled to a particular rate of commission. Sub-arranger obligation was a part of overall obligation of IMDs and hence services cannot be regarded as fees for managerial services.

St. Jude Medical (Hongkong) Limited[19]

Profits of branch office (BO) established after closure of liaison office cannot be attributed to the liaison office; Attribution should be done only after BO comes into existence and profits of holding company cannot be attributed on BO of its subsidiary.

Facts of the case:

- The Taxpayer, a Hong Kong Company, was a Wholly Owned Subsidiary (WOS) of an US Company (USCo), and was engaged in the business of selling heart valves, a life saving medical produce. Further USCo was also engaged in the same line of business in the Asian region including India.

- The Taxpayer had set up a Liaison Office (LO) in India with the permission of the Reserve Bank of India (RBI).

- Role of LO was limited to coordinate for market survey; support services to the new clients; etc. It was a common ground that the Taxpayer as also parent USCo conducted sale through independent distributors.

---

[19] ITA Nos.4626 & 4627/Mum/2005

- At a later date, the Taxpayer set up a Branch Office (BO) and closed it's LO.

- For the period up to the closure of LO, NIL return of income was filed on the ground that LO's operations in India were restricted to RBI permitted activities and LO did not earn any income in India.

- The Tax Authority, based on documents impounded in the course of survey on BO , held that the Taxpayer was involved in business activity in India and was liable in respect of profits earned by HO as also USCo,

Held:

- The procedure adopted by the Tax Authority, to attribute income of USCo in the hands of the Taxpayer, was not correct since there should be separate proceedings for two separate companies established in different countries. It is legally not possible to consider the profits attributable to USCo in the hands of the Taxpayer and therefore, profit of USCo was excluded from the income of the Taxpayer

- There was a clear distinction between the liaison activities and the branch activity and the Taxpayer was not involved in business activity when they were only permitted to do liaison activity by the RBI and accordingly the profit attributable to the liaison period was deleted.

DDIT vs. Marriott International Licensing Company BV[20]

Payment can be characterized as "royalties" only if it is consideration for use or right to use any defined property in existence at the time of use—since the payment made was not for pre-existing defined property, it could not be characterized as "royalties". Contribution linked to per centage of turnover is unlikely to be regarded as reimbursement of expenses.

Facts of the case:

- The taxpayer was a company incorporated in, and tax resident of, the Netherlands. The taxpayer had entered into a Franchise Agreement with a hotel in India for providing sales, marketing publicity and promotion services outside India. The Indian hotel was also to participate in the hotel system of the taxpayer. Clause 3.2 of the agreement provided that the hotel was to pay certain proportion of its gross revenue for international marketing activities which were in the nature of advertising and printed media, marketing, promotional, public relations and sales campaigns etc.

- The issue before the Tribunal was, whether the payment made under clause 3.2 of the agreement was purely reimbursement of expenses on sales promotion and marketing and hence was not "royalties"?

Held:

- To cover any amount within the purview of Article 12(4) of India-Netherlands DTAA, the payment should be received as consideration 'for the use of or right to use' any defined property (i.e. copyright, patent, trademark, etc). Thus, a payment would be "royalties" if it is made for defined property existing at the time of use and not for creation of defined property. Even if the payment contributed towards brand building, it would not be for use of the brand and hence cannot be characterized as "royalties".

---

[20] ITA No.416/Mum/2008

- The contribution, being a per centage of gross revenue, was not reimbursement of actual expenses on itemized basis and no material was placed on record to demonstrate that actual expenses were equal to the reimbursed amount. Therefore, the AO should decide on the taxability of the amounts under Article 7 of India-Netherlands DTAA.

ITO vs. Kendle India Pvt. Ltd.[21]

S/s. 9, 195 - Procurement of information on clinical trials not used by the taxpayer for its own technical knowhow, but for onward transmission is not royalty.

Facts of the case:

- The Taxpayer, an Indian Company (I Co.), entered into a master clinical services agreement (MCSA) with an overseas drug manufacturing company (FCo.) for clinical trials.

- In pursuance thereto, I Co. entered into an arrangement with a Sri Lankan Company (SCo.) to undertake clinical trials in Sri Lanka. SCo. in turn had a tie-up with a clinical trial unit (CTU) of a Sri Lankan university for the conduct of clinical trials. The reports received from SCo. were passed on to FCo. by the Taxpayer.

- I Co. applied for a nil withholding tax order on its payments to SCo. on the basis that the remittance was a business profit, not taxable in the absence of SCo.'s permanent establishment (PE) in India under the India-Sri Lanka DTAA. This DTAA does not have an article on technical services unlike many of the DTAAs signed by India.

- The Tax Authority held that the payment was for imparting commercial experience to FCo. through the Taxpayer and hence constituted royalty under Article 12(3) of the India-Sri Lanka DTAA.

- On appeal, the CIT(A) ruled in favour of I Co. The CIT(A) held that the nature of services rendered by SCo and CTU does not qualify as "royalty" either in terms of the Act or the India-Sri Lanka DTAA. The services may be characterized as fees for technical or professional services (FTS) or business profits. In the absence of the FTS article, these services are to be treated as business profits which can only be taxed in India if SCo. has a PE in India.

- Aggrieved, the Tax Authority appealed before the Tribunal.

- I Co. argued that the information provided is akin to providing study report or book which is general in nature. The payment is in fact for availing services from SCo. pursuant to which SCo. follows a standard protocol to generate data consistently with the practice adopted worldwide. SCo. is thus only compiling the data of a routine nature which cannot be called technical information which determines the decision to commercially manufacture the drug or not.

Held:

- After considering the facts, the Tribunal upheld the reasoning of CIT(A) and ruled that, though, the payment is for procuring commercial information, it is not royalty because:

[21] ITA No. 3879/Del/2011

- The services rendered by SCo. are for supply of information which the I Co. is not using for any technical knowhow.
- The I Co. is acting as a conduit. The remittance is for procurement of commercial information for onward transmission to FCo.

Brown & Sharpe Inc. vs. DCIT.[22]

Income attributable to the Liaison office (LO) engaged in promoting sales in India on behalf of its head office is taxable in India.

Facts of the case:

- The Taxpayer, a US company, has set up an LO in India with the RBI approval. The RBI approval was granted on the condition that the LO will not render any services, directly or indirectly, in India.
- The Tax Authority contended that the LO was not merely a communication channel but it was also promoting the Taxpayer's product brands in India, which was evident from the fact that the performance incentive of LO's employees was calculated on the basis of number of orders received by the Taxpayer.
- The Taxpayer contended that LO was established only as a communication channel between the Taxpayer and its customers or prospective customers in India. The LO did not render any service for the procurement of order or sale of the product in India. Hence, there was no income earned in India. In this regard, the Taxpayer referred to various decisions like Angel Garment Ltd. [287 ITR 341 (AAR)], U.A.E. Exchange Centre Ltd. [313 ITR 94], and K. T. Corporation etc.
- Furthermore, the payments made to the LO were merely reimbursement of expenses incurred by the LO on behalf of the Taxpayer. Hence, it cannot be liable to tax in India.
- Aggrieved, the Taxpayer appealed before the Tribunal.

Held:

- The LO was engaged in promoting the Taxpayer's product and brands in India. Other than the Chief Representative Officer, the LO had also appointed a Technical Support Manager. The employees of the LO were offered sales incentive plan as per which they were to be provided with remuneration, based on the achievement of the sales target of the Taxpayer in India.
- The Taxpayer was registered with the Registrar of Companies for carrying on business in India. It had also, on its own volition, filed a return of income declaring loss under the head 'Profits and gains of business or profession.' Thus, the Taxpayer itself has taken a stand that it derives income from business in India.
- The decisions relied on by the Taxpayer involved, the activities of preparatory and auxiliary nature. Such as:

[22] ITA Nos Nos.2015/Del/2008, 2435/Del/2010 & 5026/Del/2011

- LO downloading information contained in the main server located in the UAE; (UAE Exchange Centre (supra))

- LO collecting information and sample of garments and textiles which was passed on to its HO and LO acted as a communication channel between the HO and its customers; (Angel Garment Ltd. (supra))

- LO was merely holding seminars, conferences, receiving trade enquiries, collecting feedbacks and advertising the technology used by its HO (K.T. Corporation (supra)). However, in the present case, the employees were promoting the sale of the Taxpayer's goods in India.

Thus, income attributable to LO is taxable in India. Though reimbursement of expenses cannot be treated as income, the receipt, in excess of expenses actually incurred has to be treated as income.

IBM India Private Limited vs. DIT.[23]

S/s. 9(1)(vii), 195 – Absence of Fee for technical services (FTS) article in the DTAA, does not result in the income being taxed as per the domestic laws in terms of Article 24 of India-Philippines DTAA; Services provided in the course of business covered by business income article; Not taxable in absence of a PE in India; other Income article does not cover such income.

Facts of the case:

- The Taxpayer is an Indian Company (ICo) engaged in the business of providing information technology services. The Taxpayer made certain payments to a Philippines Co. (FCo) for certain business information services, work force management, web content management and human resource accounting services without withholding tax at source.

- The Taxpayer contended that in absence of FTS Article in India- Philippines DTAA, Article 7 on 'business profits' should be applicable, and payment made to FCo is not chargeable to tax in absence of PE in India.

- However, the Tax Authorities contended that in the absence of an FTS article in the DTAA, the same should be taxable as per the domestic laws by virtue of Article 24(1) of the DTAA, which provides that the laws of the contracting states shall continue to govern the taxation of income except where provisions to the contrary are made in the DTAA.

Held:

- ☐ On Applicability of Article 24:

    - If Article 24(1) is interpreted as conferring right to tax 'FTS' in accordance with the domestic laws of a contracting state, then Article 23 dealing with other income and granting exclusive right of taxation to country of residence would become redundant as Article 23 will then cease to be an omnibus clause covering the residuary income.

---

[23] In ITA No.598/Bang/2011

- It is a well settled principle that a clash is to be avoided while interpreting the provisions of a treaty. Hence the scope, context and setting of the articles have to be understood in their proper perspective.
- Article 24(1) does not confer a right to invoke the provisions of domestic laws for classification or taxability of income covered by other articles of the DTAA. Article 24 is limited to elimination of double taxation and operates in the field of computation of doubly taxed income and tax thereon in accordance with the domestic laws and is not part of treaty Articles which deal with the classification of income.
- On interplay between Article 7 and Article 23:
- The services rendered by FCo are in the course of its business and hence covered under Article 7 of the DTAA and not other income Article. Further in the absence of PE in India of FCo, the amount paid is not chargeable to tax in India.
- Even assuming that the payments made to FCo are covered by Article 23, the same should also not be taxable in India, by virtue of exclusive taxation rights being provided to the country of residence.

DDIT vs. DQ Entertainment (International) P. Ltd[24]

Section 9, 195 of the Act – on facts, as the source of income was outside India, exception carved in section 9(1)(vii)(b) of the Act applied and the payments made for services was not chargeable.

Facts of the case:

- The taxpayer was engaged in the production of 2D and 3D animation films for various clients. During the relevant years, the taxpayer entered into 'Outsourcing Facilities Agreement' for outsourcing some episodes or part of episodes to two sub-contractors – a Hong Kong entity and a Chinese entity. Under the agreement, both the entities were to provide production work/Production material to taxpayer by availing the necessary production premises, facilities, personnel, materials, services and expertise.
- According to the taxpayer: the payment was made to the sub-contractors in the course of business; the subcontractors did not have any 'business connection' or PE in India; the income did not arise under the deeming provision of section 9(1)(vii) of the Act; and hence the payments were not taxable in India.
- According to the AO since the production material was specifically created by sub-contractors for the taxpayer, the substance of contract was not supply of goods but was provisioning of services. Hence, the payments were FTS u/s. 9(1)(vii) of the Act and therefore, the taxpayer should have withheld the tax.

Held:

- The production of animation films or part of certain episodes did not have any element of technical services. Delhi Tribunal3 as also Delhi HC4 held that utilization of knowledge, information and expertise of party undertaking a job of another party is no reason to treat the services rendered as technical or consultancy services

---

[24] ITA Nos. 276 & 277/Hyd/2010

- Section 9(1)(vii)(b) of the Act carves out an exception in case of resident utilizing services in business carried on outside India or earning income from a source outside India. As per decision of Supreme Court5, contract is to be considered the source of income and since, as per the contract with the overseas clients, the jurisdiction was of the courts/arbitration at the place where overseas client was located (subjecting the taxpayer to foreign laws), 'source of income' was outside India. The viewership of the animation films was also located outside India.

- Thus, there was a direct nexus between the payments and earning of income from source outside India. Therefore, exception in section 9(1)(vii)(b) will be applicable and there was no liability to withhold tax u/s. 195.

Reliance Infocom Ltd. & others.vs.DDIT(IT)[25]

S/s. 9, 195 - Payment for Software License under a standalone agreement, and not an integral part of purchase of equipment (embedded software) is consideration for transfer or use of copyright and is taxable as royalty, both under the Act and various DTAAs. Purchase of embedded software amounts to purchase of copyrighted article, not taxable as royalty.

Facts of the case:

- The Taxpayer, an Indian telecom company, wanted to establish a wireless telecommunications network in India. It entered into a contract with an Indian company (ICo.) for supply of hardware, software and services for establishing the network. The software supply contract was thereafter assigned by ICo. to its Foreign Group Company (FCo.) under a tripartite agreement between the Taxpayer, FCo. and ICo. FCo. Supplied software under this agreement. Various other shrink-wrap/off-the-shelf software were acquired from third parties. All software was meant for use in operation of network equipments.

- The Tax Authority considered the payments made to FCo. to be in the nature of royalty and rejected the nil withholding application made by the Taxpayer.

- On appeal, the CIT(A) observed that the Taxpayer was forbidden to decompile, reverse engineer, disassemble, decode, modify or sub-license the software, as per the agreements and hence as the Taxpayer only had a "copy of software" without any part of "copyright of the software", the payments did not amount to royalty.

Aggrieved, the Tax Authority appealed before the Tribunal.

Held:

- The Tribunal, based on facts distinguished the decisions in the case of Motorola Inc. [270 ITR (AT) 62 (SB)], Delhi High Court in Erickson [343 ITR 370] and Nokia Networks. The Tribunal noted that in the above decisions there was purchase of software along with hardware and the same was purchase of "copyrighted article" and no "copyright" was involved. Software was an integral part of the supply of equipment for telecommunications, generally called embedded software and there was no separate sale of software.

---

[25] [TS-433-ITAT-2013(Mum)]

- In the present case, the Taxpayer purchased the software by virtue of a standalone “software license agreement”. The software was neither an integral part of purchase of equipment nor was it embedded software. The delivery was separate, in the form of CDs, mostly abroad and was installed in India separately.

- The Tribunal also concluded as follows:

- FCo. Transferred a license to use its copyright to the Taxpayer where FCo. Continued to be the owner of the copyright and all other IPRs. The license granted for making use of the “copyright” in respect of shrink-wrapped software/off-the-shelf software, authorizing the end user to make use of its own network equipment, would also amount to transfer of part of the copyright. Consequently, this would amount to transfer of “right to use the copyright” for internal business.

- The Karnataka HC decisions in the cases of Samsung [345 ITR 494 (Kar)] and Synopsis International dealt with facts similar to the facts in the present case. The Karnataka HC held that the end users of the computer program are granted use of a “copyright” when a license to make copies of the computer program for back-up or archival purposes is given.

- In another Karnataka HC decision in the case of Lucent Technologies [348 ITR 196 (Kar)], wherein, on similar facts, it was held that payment for purchase of copy of a computer program that was supplied as a bundled contract, along with hardware on which the computer program was to be installed, was taxable as royalty.

- Based on the above, the Tribunal ruled that payment made by the Taxpayer to FCo. and various other suppliers was taxable as royalty.

ITO V/S RIGHT FLORISTS PVT.LTD.[26]

The assessee, Right Florists, an Indian company, is engaged in the business of online florist and in the course of its business, it had paid a sum of Rs 30, 44,000 to Google Ireland Limited and Yahoo USA for online advertising without deducting tax at source. The assessing officer held that the assessee ought to have deducted TDS and since there was a failure, the expenditure was disallowed u/s 40(a) (i). On appeal, CIT (A) deleted the disallowance made by the assessing officer on the ground that no tax shall be deductible at source as the income of both Google and Yahoo is not chargeable to tax in India in absence of any permanent establishment in India.

On appeal by the department, the tribunal observed that a website does not constitute a ‘permanent establishment’ unless the servers on which websites are hosted are also located in the same jurisdiction. As the servers of Google and Yahoo are not located in India, there is no PE in India. The tribunal further placed reliance on the decision of Yahoo India (P) Ltd. (2011) 140 TTJ 195 (Mum) and Pinstorm Technologies (P) Ltd (2012) 54 SOT 78 (Mum), and held that the advertising revenues are not assessable as “royalty”. Tribunal observed that fees for said services is not in the nature of the ‘Fees for Technical Services’ since no human intervention is involved.

ROMER LABS SINGAPORE PTE. LTD. V/S ADIT [27]

Assessee a Singapore company provided services to an Indian company rendering services relating to testing solutions, sample analytical testing of food and feed samples. It claimed that receipt there-from was taxable as

[26] ITO .v. Right Florists Pvt. Ltd.(2013) 86 DTR 165/154 TTJ 142 /143 ITD 445 /25 ITR 639(Kol.)(Trib.)
[27] Romer Labs Singapore Pte. Ltd. v. ADIT (2013) 141 ITD 50 (Delhi)(Trib.)

business income and thus not taxable in India. During the year under consideration, the assessee provided services to Indian companies for testing of dog feeds and similar products. The Assessing Officer held that the amount received was taxable as technical services as per article 12(4) between India and Singapore. The assessing officer made an assessment where it is held that assessee has made available technical knowledge, skill or know-how to Indian customer and as such, the payments made to it were to the nature of fee for technical services as defined under Article 12(4) of the DTAA between India and Singapore. On appeal, CIT(A) upheld the view of the assessing officer.

On further appeal by the assessee, tribunal held that services provided by assessee could not be said to have 'make available' any technical knowledge, experience, skill, know-how or processes to assessee. Thus, the receipts of the assessee would not amount to be fees for technical services and hence shall not be taxable in India.

ACIT V/S. ROBERT ARTHUR KELTZ [28]

The assessee, an employee of M/s UTIO, USA, was granted "employee stock options" of 34,000 shares on 09.01.2004 when he was outside India. The assessee was deputed to the India liaison office on 01.04.2006 and the stock options vested on 09.01.2007 when he was in India. The assessee exercised the stock options on 01.02.2007, when he was still in India. The assessing officer held that as the assessee was in India on the date of vesting and exercise of the stock options, the entire benefit thereof was assessable as a perquisite in his hands. However, the CIT(A) held that since the employee has been in India only for a part of the vesting period, only a proportionate stock option benefit, which is attributable to the period spent in India accrued to the employee and was chargeable to tax in India.

The Tribunal observed that if a part of the activity done by the assessee has no relation to any India specific job or activity it is not chargeable to tax in India. On facts, the assessee was in India only for a short period i.e. 01.04.2006 onwards. Prior to that, he has not rendered any service connected with any activity in India. Accordingly, as the assessee has not rendered service in India for the entire vesting period, only such proportion of the ESOP perquisite as is relatable to the service rendered by the assessee in India is taxable in India.

The Tribunal applied the ratio laid down in the case of DCIT vs. Eric Moroux and Ghorayeb Emile (ITA no. 1174 and 1175/Del/2005) and held that only such proportion of the perquisite as is relatable to the service rendered by the assessee in India is taxable in India.

PT MCKINSEY INDONESIA V/S DDIT[29]

Assessee is a foreign company which is engaged in business of providing strategic consultancy services to clients. It provided information to its Indian group company based on their requirement. Assessee claimed that the charge received from Indian group company was to be assessed as business profits. The assessing officer held that the fees received by the assessee would be categorized as 'Royalty' in terms of Article 12 of the India-Indonesia DTAA. On application before the Dispute Resolution Panel, it was held that provisions of article 22(3) of DTAA i.e. of "other income" would be applicable and the income receipt in question was to be taxed as income from other sources.

On appeal, Tribunal observed that the assessing officer could nowhere establish that information supplied in question was arising out of exploitation of know-how generated by skills or innovation of person who possessed such talent. The information received was in the nature of data and consideration for the same cannot constitute royalty. Thus, the Tribunal held that payment should be treated as business profits as per Article 7. ITAT further held that the residuary head (Article 22- other income) was analogous to sections 56-57 of the Income Tax Act (income from other sources) and such further observed that "If a certain receipt cannot be taxed under any other head, only then the sections dealing with 'Income from Other Sources', come into play in domestic taxation matters" and likewise is applicable for DTAA.

---

[28] ACIT .v. Robert Arthur Keltz(2013) 59 SOT 203(Delhi)(Trib.)

[29] P.T.McKinsey Indonesia v Dy.CIT (2013) 141 ITD 357/88 DTR 324/25 ITR 52 (Mum.)(Trib.)

It should be noted that existing India-Indonesia DTAA does not have an FTS clause. However, the new treaty signed in 2012 which is not yet in force has FTS clause in Article 12.

DCIT V/S VIROLA INTERNATIONAL[30]

The assessee is an exporter of leather footwear and footwear uppers. During the year under consideration, the assessee had made payments to various non-residents, without deducting any taxes at source, towards 'design and development expenses'. The AO held the amounts so paid to the non-residents were in the nature of 'fees for technical services' under the Act, as also under the applicable tax treaties, held that the assessee was, under section 195, had an obligation to withhold tax at source from these payments, and, accordingly, proceeded to make the disallowance under section 40(a)(i).

Learned CIT(A) deleted the disallowance on the ground that no tax was deductible from these amounts and further held that " even if, by any stretch of imagination, such payments are considered as FTS, no TDS was required to be made at the time of credit/ payment as per the law existing at that time because services were not rendered in India…". The disallowance was thus deleted.

On appeal to ITAT, it was observed that in accordance with the law laid down in Ishikawajma-Harima Heavy Industries, which was good law at the time of the remittance, unless the services are rendered in India, the same cannot be brought to tax as 'fees for technical services' u/s 9. Though the law was amended retrospectively, so far as tax withholding liability is concerned, it depends on the law as it existed at the point of time when payments, from which taxes ought to have been withheld, were made. Tribunal further held that the tax deductor cannot be expected to have clairvoyance of knowing how the law would change in future and that a retrospective amendment in law does change the tax liability in respect of an income, with retrospective effect, but it cannot change the tax withholding liability, with retrospective effect. Therefore, ITAT held that the assessee did not have any liability under section 195 r.w.s. 9(1)(vii) to deduct tax at source from these payments and hence the assessee no disallowance can be made in respect of these payments

QUALCOMM INCORPORATED V/S ADIT[31]

The assessee had licensed certain intellectual property (IP) with respect to the manufactures of Code Division Multiple Access (CDMA) mobile handsets and network equipment to non-resident (NR) Original Equipment Managers (OEMs). OEMs used the IP to manufacture CDMA handsets and wireless equipment outside India and sold them to customers, who, in turn, sold the handsets to end-users of telecom services in India.

The Tax Authority assessed a part of royalty, to the extent it related to equipment sold to customers in India by suggesting that part was taxable in India as the IP that was licensed was utilized in business carried on in India or for earning income from India sources (the secondary source rule) under the Income-tax Act, 1961.

The Tribunal ruled that the royalty payment by OEMs was not taxable in India since the secondary source rule was not applicable to the facts of the case as OEMs did not carry on business in India nor did the customers who purchased the equipment constitute a source of income. Further, the onus of proof is on the Tax Authority to establish that OEMs were carrying on business in India.

---

[30] DCIT .v. Virola International(2014) 162 TTJ 112/147 ITD 519(Agra)(Trib.)

[31] Qualcomm Incorporated v. ADIT WNS (Delhi Tribunal)

ADIT(IT) .V. CLIFFORD CHANCE[32]

The assessee, a UK based partnership firm of Solicitors, provided legal consultancy services in connection with different projects in India and claimed that the taxability of the income arising there from had to be processed under Article 15-Independent Professional Service of the India-UK DTAA. The AO rejected the claim regarding applicability of Article 15 and held that as the assessee had a PE in India as per Article 5 and as the services had been rendered in India, the entire income was chargeable to tax in India under Article 7. In AY 1996-97, the Tribunal {Clifford chance, United Kingdom v. Dy. CIT (2002) 82 ITD 106 (Mum)} accepted the claim of the assessee that if the aggregate period of stay of the employees/ partners did not exceed 90 days, the income was not taxable under Article 15 of the DTAA and if it exceeded that period, only the Indian activity was taxable u/s 9(i). The said verdict was affirmed by the Bombay High Court in 176 Taxman 485. Later, another Bench in Linklaters LLP vs. ITO (2010) 40 SOT 51 (Mum) held that as the aforesaid verdicts of the Tribunal & High Court in Clifford Chance turned on the basis that fees for technical services rendered outside India were not chargeable to tax u/s 9(1)(vii) and that they were not good law in view of the retrospective amendment to s. 9(1) by the Finance Act, 2010 w.e.f. 1.6.1976 which provided that "fees for technical services" would be taxable in India even if they were rendered outside India. In Linklaters LLP it was also held that the expression "directly or indirectly attributable" in Article 7(1) triggered the "force of attraction" rule and that the entire earnings relatable to the projects in India would be chargeable to tax in India. As there was doubt as to the correctness of the view in Linklaters, the Special Bench was constituted to consider two issues (i) whether the verdict of the High Court in Clifford Chance was good law after the retrospective amendment to s. 9 & (ii) whether the expression "directly or indirectly attributable to the PE" in Article 7(1) meant that the consideration attributable to the services rendered in the State of residence is taxable in the source State.

The view taken by the Tribunal and the High Court in Clifford Chance was that if Article 15 of the

India-UK Treaty is not applicable because the stay of the partner exceeded 90 days, then the taxability of the income would be determined by s. 9(1)(i) of the Act. It was held that for determination of income u/s 9(1)(i), the territorial nexus doctrine plays an important part and if the income arises out of operations in more than one jurisdiction, it would not be correct to contend that the entire income accrues or arises in each of the jurisdictions. The High Court applied the law laid down by the Supreme Court in the context of s. 9(1) (i) that if all the operations are not carried out in the taxable territories, the profits and gains of business deemed to accrue in India through and from business connection in India shall be only such profits and gains as are reasonably attributable to the operations carried out in the taxable territories. Accordingly, the view expressed in Linklaters LLP that the judgment of the Bombay High Court is based on the premise of s. 9(1)(vii) and that the said premise no longer holds good in view of the retrospective amendment is not correct. The law laid down by the High Court continues to be good law ;(ii) As regards the rule of "force of attraction", Article 7(1) provides that the profits of the UK enterprise "directly or indirectly attributable to the PE" may be assessed in India. The connotation of what is "directly attributable to the PE" is set out in Article 7(2) while the connotation of what is "indirectly attributable to the PE" is set out in Article 7(3). When the connotation of "profits indirectly attributable" to the PE is defined specifically in Article 7(3), one cannot refer to Article 7(1) of the UN Model Convention which is materially different from Article 7(1) & 7(3) of the India-UK DTAA. The reliance placed in Linklater on the UN Model Convention to come to the conclusion that the connotation of "profits indirectly attributable to PE" in Article 7(1) incorporates the "force of attraction" rule thereby bringing an enterprise having a PE in another country within the fiscal jurisdiction of that another country to such a degree that such another country can properly tax all profits that the enterprise derives from that country, whether the transactions are routed and performed through their PE or not, is clearly misplaced and not acceptable. (AY. 1998-99 to 2003 -04)

SC ENVIRO AGRO INDIA LTD. V/S DY. CIT[33]

---

[32] ADIT(IT) .v. Clifford Chance (2013)143 ITD 1/ 24 ITR 1 / 87 DTR 210/154 TTJ 537 (SB) (Mum.)(Trib.)

[33] SC Enviro Agro India Ltd. v. Dy.CIT (2013) 143 ITD 195/58 SOT 22(URO) (Mum.)(Trib.)

Assessee is manufacturer of household insecticides and pesticides. It entered into a license agreement with SCCL for commercial production of specified products and paid royalty to SCCL for utilizing know-how and license. SCCL acquired 90 per cent of equity share capital of Assessee Company. Assessee sold most of its products to SCI a 100 per cent subsidiary of SCCL. TPO held that it was a contract manufacturing agreement and there was no justification for payment of royalty and hence, determined arm's length price at NIL. The Assessing Officer made similar disallowance in the assessment order passed 'having regard to' the TPO's order. Commissioner (Appeals) held that assessee was contract manufacturer so allowed royalty payment on the sales made to outside parties and therefore, partly allowed the claim of the assessee.

On appeal to Tribunal it was held that transfer pricing rules do not authorize TPO to disallow any

expenditure on ground that it was not necessary or prudent for assessee to have incurred same. Since royalty was paid for allowing assessee in utilizing technical knowhow and license which was independent of fact as to whether assessee was a manufacturer, payment of royalty was wholly and exclusively for purpose of business. The TPO has to examine whether the price paid or amount paid was at arm's length or not under the provisions of Transfer Pricing and its rules. The rule does not authorize the TPO to disallow any expenditure on the ground that it was not necessary or prudent for assessee to have incurred the same. On that principle alone the TPO has exceeded the jurisdiction. Ratio in CIT v.EKL Appliances (2012) 206 Taxman 97(Mag.) (Delhi) (HC) followed. (AY.2003-04, 2004-05)

The assessee paid commission to AEs at 12.5per cent compared to 5per cent paid to non-AE foreign agents, this was due to the additional obligations undertaken by the AEs, being bearing of market development, advertising and sales promotion expenses as well as market risks, which were absent in case of agreement with non-AE foreign agents. The TPO rejected assessee's comparison and compared the average non-AE export price with the price charged to AEs. He also took 5per cent as the arm's length rate of commission based on the commission paid to non-AE foreign agents. On appeal, the CIT (A) admitted that there were no direct comparable uncontrolled transactions for computing arm's length price, and therefore, after analyzing the profit ratio and operating expenses of the AEs, he held that the AEs were running at losses and no third party would carry on such business at loss. Thus, he accepted the operating margin of the AEs. On the issue of commission paid to AEs at 12.5per cent, observing the relevant obligations carried out by

The AEs, which were not there in the case of non-AE foreign agents, the CIT (A) took 10per cent per cent as the arm's length rate of commission. Benefit of arm's length range of +/- 5per cent, in terms of the proviso to section 92C was also given on the premise that it was a standard deduction.

HIGH COURT RULINGS

DIT (INTERNATIONAL TAXATION) VS. E FUNDS IT SOLUTIONS & ORS. [34]

While under Article 5(6), a holding or a subsidiary company by themselves would not become PE of each other, a subsidiary can become a PE of the holding company if it satisfies the requirements of Article 5. Accordingly, any premises belonging to the subsidiary that is at the disposal of the parent (the "right-to-use test") and that constitutes a fixed place of business (the "location test" and the "duration test") through which the parent carries on its own business (the "business activity test"), gives rise to a PE of the parent under Art. 5(1).

[34] CIT .v.eFunds IT Solution(2014) 99 DTR 257 (Delhi)(HC)

The word “permanent” refers to some degree of permanency and not a mere transitory nature of the business in the other State. The expression “fixed place of business” refers not only to physical location in the form of immovable property or premises but in certain instances can mean machinery and equipment. The word “fixed” refers to a distinct place with some or certain degree of permanence. The carrying on of “business” should be “through” the fixed place of business. Re. What constitutes a “Service PE” under Article 5(2) (l) of the DTAA: Article 5(2) (l) and (k) defines what can be called service PE. Sub-clause (l) requires furnishing of services within the second contracting State by a foreign enterprise through its employees or other personnel. But a PE is created only if activities of that nature continue for a period or periods aggregating more than 90 days in 12 months period or under clause (ii) services are performed within that State for a related enterprise as defined in Article 9 paragraph 1.

Article 5 (3) contains a list of negative activities which are deemed not to create PE. First and foremost, Article 5(1)/(2) should be applicable but then if the activities fall within parameters of paragraph 3, PE is not created for imposing tax in the second state. It does not follow that if activities are not covered in the negative or exclusions set out in paragraph 3, a PE is established or deemed to be established under paragraphs 1 or 2 of Article 5;

A dependent agency is one which is bound to follow instructions and is personally dependent on the enterprise he represents. Such dependency must not be isolated or once in a while transaction but should be of comprehensive nature.

The MAP procedure and agreement is no doubt relevant but cannot be determinative or the primary basis to decide whether the assessee had PE in India. (ITA No. 735/2011, dt. 5/02/2014.)(AY. 2000- 01 to 2007-08)

DIT (IT) V/S. WIZCRAFT INTERNATIONAL ENTERTAINMENT PVT.LTD.[35]

The assessee, Wizcraft International Entertainment Pvt. Ltd., is an event management company. The assessee had engaged the services of an agent, Mr. Colin Davie, to bring artists to India. The assessee paid remuneration to the artists, to the agent and reimbursed expenses in connection with the visit and performance of artists in India. AO was of the view that any payment made to the artists or their agent should be treated as consideration payable to the artist only. Further, according to the AO, the income of the artist had to be taxed in the State in which activities were organized which, in present case, was India. While it was noted that tax had been deducted on the amounts paid to the artists, no tax was deducted on payments made to the agent or for expenses. The AO proceeded to treat the assessee as a defaulter for neither deducting tax nor filing return of income as a representative assessee.

CIT (A) held that AO had completely misdirected himself and noted that it was a common practice to remit money in advance to incur expenses. Expenses in connection with artists’ performance in India and their reimbursement did not constitute income derived by artists from their personal activities so as to be taxable under Article 18 of India-UK DTAA, held CIT (A). Thus, it was held that the reimbursement of expenses were not taxable in India.

Article 18 of India-UK DTAA provides for taxation of income of artists and athletes and states that income derived from their personal activities may be taxed in the Contracting State in which the activities are exercised. Article 18(2) states that where income arising from personal activities are such exercised in a Contracting State by an entertainer or athlete accrues not to that entertainer or athlete himself but to another person, that income may be taxed in that Contracting State.

---

[35] DIT .v. Wizcraft International Entertainment Pvt. Ltd(2014) 364 ITR 227/223 Taxman 250 /104 DTRJ 68(Bom.)(HC)

Tribunal also held that AO, unjustifiably and without material on record, held that the payment for reimbursement of expenses were liable for tax deduction at source and in absence of certificate u/s 195(2), tax was required to be deducted and paid on the gross amount.

High Court upheld the Tribunal's and CIT(A) decision and held that commission income to the agent is not liable to tax in India and there was no obligation on the part of the assessee to deduct the tax at source at the time of making of payment. In so far as payment or reimbursement of expenses in connection with the visit and performance of the artists in India, the amount reimbursed to them was towards air travel and was supported by documents. On that tax need not be deducted.

DIT V/S. INFRASOFT LTD [36]

The assessee, an international software marketing and development company developed customized software which was licensed to an Indian customer and the branch office of the assessee in India. In the course of assessment, the AO taxed the receipts on licensing the software as 'royalty' as per article 12 of Indo-US DTAA. The CIT (A) upheld the order of AO. The Tribunal, however, held that the amount received by the assessee under the license agreement for allowing the use of the software was not royalty either under the Act or under the DTAA.

On appeal to High Court the following ruling was made that in order to qualify as royalty payment, it is necessary to establish that there is transfer of all or any rights (including the granting of any license) in respect of copyright of a literary, artistic or scientific work. In order to treat the consideration paid by the Licensee as royalty, it is to be established that the licensee, by making such payment, obtains all or any of the copyright rights of such literary work. Distinction has to be made between the acquisition of a "copyright right" and a "copyrighted article". Copyright is distinct from the material object, copyrighted. Just because one has the copyrighted article, it does not follow that one has also the copyright in it. Viewed from this angle, a non-exclusive and non-transferable license enabling the use of a copyrighted product cannot be construed as an authority to enjoy any or all of the enumerated rights ingrained in Article 12 of DTAA. There is no transfer of any right in respect of copyright by the assessee and it is a case of mere transfer of a copyrighted article. The payment is for a copyrighted article and represents the purchase price of an article and cannot be considered as royalty either under the Act or under the DTAA.

Further the High Court observed that it was not necessary to examine the effect of subsequent amendment to section 9(1)(vi) and also whether amount received for use of software would be royalty in terms thereof for the reason that the assessee was covered by the DTAA, the provisions of which are more beneficial. In view of the above the appeal was dismissed.

DIT V/S NISSO LWAI CORPORATION, JAPAN[37]

The assessee company provided design and engineering services, manufacture, delivery, technical assistance through supervision of erection and commissioning etc to establish compressor house-I for RINL. The payments were made by RINL separately for each of the services/equipments provided/supplied by the assessee. It, inter alia, included payment made towards supply of design and engineering drawings. The assessee company claimed the said payment is not taxable under the Income Tax Act as it was a transaction of sale of goods that has taken place outside India. In our view the decision of Delhi ITAT Bench in the case of Mannesmann Demag Sack AG v. Add. CIT reported in (2008), 119 TTJ 543 (Del), on which reliance was placed by Ld DR, is not applicable to the facts of the

[36] DIT .v. Infrasoft Ltd. (2014) 220 Taxman 273 (Delhi)(HC)

[37] DIT .v. NissoLwai Corporation, Japan (AP)(HC),www.itatonline.org

instant case. In the case of Mannesmann Demag Sack, supra, the decision was rendered on the basis of the terms of the contract which provided that technical services shall include supply of design and drawings. Hence on the facts of the case, the Tribunal held that design and drawing charges are in the nature of fee for technical services. However, it may be pertinent to note that the Tribunal in that case, accepted the alternative contention of the assessee that the said fee cannot be assessed in India, unless it is shown that some part of work has emanated from Indian territories. Hence on a conspectus of the matter, we are of the view that the amount received by the assessee for supply of design and engineering drawings is in the nature of plant and since the preparation and delivery has taken place outside Indian territories, the same cannot be subjected to tax in India.

Sanofi Pasteur Holding SA v/s Department of Revenue[38]

Two French companies named “Murieux Alliance” (‘MA’) and “Grouped Industrial Marcel Dassault” (“GIMD”) held shares in another French company named “Shahn”. MA & GIMD acquired shares in an Indian company named “Shantha Biotechnics Ltd” (“Shantha”). In 2006, shares in Shantha were transferred to Shahn. MA and GIMD subsequently sold the shares in Shahn to another French company named “Sanofi Pasteur Holding”. The assessee filed an application for advance ruling claiming that as the two French companies had sold the shares of another French company to a third French company, the gains were not chargeable to tax in India. The department opposed the application on the ground that Shahn was formed with no purpose other than to hold the shares of the Indian company and that the transaction was taxable in India. The AAR upheld the department’s plea on the ground that the French company’s (Shahn) only asset were the shares in the Indian company & so when its shares were sold, what really passes were the underlying assets and the control of the Indian company thus becoming a case for tax avoidance.

The High Court held that the corporate veil of Shahn cannot be pierced. According to the High Court, Shahn was an independent corporate entity that had commercial substance and business purpose and was not a device for avoiding Indian tax. As the Assessees had transferred shares of Shahn, being a French resident company, taxation of capital gains arising as consequence of the transaction is allocated exclusively to France under the India- France DTAA and, therefore, not taxable in India. The HC also held that the retrospective amendments to the ITA will not impact the allocation of taxing rights under a DTAA.

POOMPUHAR SHIPPING CORPORATION V/S ITO[39]

Poompuhar Shipping Corporation is a state owned company engaged in the business of transporting coal from various parts in India to Tamil Nadu for Tamil Nadu Electricity Board, Chennai. For this purpose, the asseesee entered into agreements in standard time charter form with foreign shipping companies having their vessels registered in different countries. The assessee made charter payment to the foreign shipping companies without deducting tax at source.

The High Court observed that the term equipment has neither been defined under the Act nor in DTAA. However, ‘plant’ has been defined under the Act to embrace within its fold, ‘ships’ along with ‘vehicles, books, scientific apparatus and surgical equipment used for the purposes of the business of profession’. Thus, a ship is equipment forming part of a ship-owner’s business. When the use or right to use the ship for an economic benefit is provided, the consideration for use of industrial, commercial and scientific equipment is royalty under the Act. The presence or absence of possession, effective/general control and custody with the assessee, even though may be matters of

[38] Sanofi Pasteur Holding SA .v. Dept of Revenue, Ministry of Finance (2013) 354 ITR 316/257 CTR 401/84 DTR 185/213 Taxman 504 (AP.) (HC).

[39] Poompuhar Shipping Corporation Ltd. v. ITO (2013) 38 Taxmann.com 158/95 DTR 161 (Mad.)(HC). West Asia Martime Ltd v.ITO (2013) 95 DTR 161(Mad)(HC)

agreement, are not of any relevance to decide the character of payment.

Thus, Hon'ble High Court held that payment under the time charter being for use of the ship is, therefore, covered within the meaning of royalty under the Act

Further , the High court found that as per Article 8 of the India-Cyprus DTAA, only payments to foreign shipping companies that operates in international traffic is taxable in the country in which foreign shipping companies have a 'place of effective management'. In this case, the ships operated only along the coastline of India. Hence the test of international traffic is not met. Therefore, in the view of the high court, article 8 could not be invoked to determine withholding tax on payments to foreign shipping companies.

The ship has a place of business at the place where the ship is docked. Since the ship moves from one point to another due to the nature of business contract, and the movement is integrated having business and geographical coherence, it could be inferred that the foreign enterprise has a PE in India. However, the payment is made for hire charges, which are not attributable to the PE but to the use of the ship. Therefore, the High court held that the payment is taxable as royalty and not as business profits.

TRANSFER PRICING DECISIONS

TRIBUNAL RULINGS

MAERSK GLOBAL CENTRES (INDIA) PRIVATE LIMITED V/S ACIT (SB)[40]

The Assessee is a provider of information technology enabled services (ITeS) including process support/ optimization and technical support services to its Associated Enterprises (AEs). The assessee's transfer pricing documentation revealed that its international transactions were at arm's length using Transactional Net Margin Method (TNMM). The TPO rejected the transfer pricing documentation and made an adjustment by treating the activities of the assessee to be in the nature of KPO services instead of BPO services.

The Special Bench, while approving TNMM as the most appropriate method, and considering the gamut of services provided by companies in the ITeS sector, ruled that there is no requirement to further segregate ITeS into BPO and KPO activities. The SB also held that comparable companies having abnormally high profits need not be eliminated, but there should further investigation to ascertain whether such trends reflect normal business conditions or not. Where a high profit margin making entity does not satisfy comparability criteria or the same does not reflect normal business conditions, then such entity needs to be excluded from the comparability analysis.

MISSIONPHARMA LOGISTICS (INDIA) PVT.LTD VS. ACIT[41]

The assessee, Missionpharma Logistics (India) Pvt. Ltd, is engaged in procuring of medicines and other hospital disposables from Indian manufacturers as per the specifications of its Danish AE. The assessee packs these materials into medical kits of the size and lots as ordered by its AE and dispatches them to the AE's final customers. Bills are raised for the same on the AE. The assessee adopted TNMM and identified comparables to compute ALP of its transactions. During transfer pricing proceedings, the TPO selected the AE as the 'tested party'.

ITAT held that the assessee, not the AE, should be considered as the tested party. ITAT held that having no export

[40] Maersk Global Center (India) Pvt. Ltd. .v. ACIT(SB)(2014) 101 DTR 1/161 TTJ 137/31 ITR 1(Mum.) (Trib.)
[41] Missionpharma Logistics (India) Pvt. Ltd(TS-82-ITAT-2013(Ahd)-TP)

sales was not sufficient criteria to reject comparables. ITAT observed that the assessee did not carry any type of risk – inventory, timely delivery, foreign exchange fluctuations, quality, standard etc.

ITAT held that even if the AE was taken as the tested party, no addition could be made if the margin for the aggregate transactions was considered.

M/S BHARTI AIRTEL LIMITED V/S ACIT[42]

The assessee issued a corporate guarantee to Deutsche Bank on behalf of its associated enterprise, Bharti Airtel (Sri Lanka) whereby it guaranteed repayment for working capital facility. The assessee claimed that since it had not incurred any cost on account of issue of such guarantee, and the guarantee was issued as a part of the shareholder activity, no transfer pricing adjustment could be made. However, the TPO held that as the AE had benefited, the ALP had to be computed on CUP method at a commission income of 2.68per cent plus a mark-up of 200 bps. This was upheld by the DRP by relying on the retrospective amendment to s. 92B which specifically included guarantees in the definition of “international transaction”.

The Tribunal, on facts, held that the guarantee provided by the assessee, does not have a real bearing on profits, incomes, losses or assets of the assessee and hence the transaction does not fall within the definition of “international transaction” as per section 92B of the Income Tax Act, 1961. Further the Tribunal held that the onus is on the revenue to demonstrate that the transaction has a bearing on profits, income, losses or assets of the enterprise. The said impact has to be on real basis i.e. not on contingent or hypothetical basis. There has to be some material on record to indicate that an intra AE international transaction has some impact on profits, income, losses or assets. When an assessee extends assistance to the AE, which does not cost anything to the assessee and particularly for which the assessee could not have realized money by giving it to someone else during the course of its normal business, such an assistance or accommodation does not have any bearing on its profits, income, losses or assets, and, therefore, it is outside the ambit of international transaction u/s 92B (1).

CAPGEMINI INDIA PRIVATE LIMITED V/S ACIT[43]

The Tribunal had to consider the following important transfer pricing issues: (i) whether a one-time and extraordinary item of expenditure (ESOP cost) debited to the assessee’s P&L A/c has to be excluded while comparing the margins, (ii) whether for the purpose of comparison of margins, the consolidated results of comparables having profit from different overseas markets can be considered? (iii) Whether extreme profit and loss cases should be excluded or in case extreme profit cases are included, the case of losses should also be included? (iv) whether a turnover filter can be adopted to exclude companies with extremely high turnover? (v) whether the assessee can seek to exclude its own comparables? (vi) whether an adjustment for working capital is permissible? (vii) whether if the assessee can show that because the AE is in a high tax jurisdiction and that there is no transfer of profit to a low tax jurisdiction, a transfer pricing adjustment need not be made?

- ☐ The Tribunal held:

- ▪ A comparison of margin between the assessee and the comparables has to be made under identical conditions. As the comparables had not claimed any extraordinary item of expenditure on account of ESOP cost, for the purpose of making proper comparison of the margin, onetime ESOP cost incurred by the

[42] BhartiAirtel Limited. .v. ACIT(2014)101 DTR 154/161 TTJ 428(Delhi)(Trib.)

[43] Capgemini India Private Limited .v. ACIT(2013) 27 ITR 74(Mum) (Trib).

assessee has to be excluded. There is nothing in the Rules that prohibits adjustment in the margin of the assessee to remove impact of any extraordinary factors (Skoda Auto India(P) Ltd. v. ACIT (2009) 30 SOT 319 (Pune), Demag Cranes & Components (India) (P) Ltd. (2012) 49 SOT 610 (Pune), Transwitch, Toyota Kirloskar Motors followed);

- Under Rule 10B(2) (d), the comparability of transactions has to be considered after taking into account the prevailing market conditions including geographical locations, size of market and cost of capital and labour etc. Therefore, consolidated results which include profit from different overseas jurisdictions having different geographical and marketing conditions will not be comparable. Only standalone results should be adopted for the purpose of comparison of margins (American Express followed);

- Comparable cases cannot be rejected only on the ground of extremely high profit or loss. In case the companies satisfy the comparability criteria, and do not involve any abnormal business conditions, the same cannot be rejected only on the ground of loss or high profit. The OECD guidelines also provide that loss making uncontrolled transactions should be further investigated and it should be rejected only when the loss does not reflect the normal business conditions;

- In certain Tribunal decisions, various reasons have been given for applying the turnover filter for comparison of margins such as economy of scale, greater bargaining power, more skilled employees and higher risk taking capabilities in cases of high turnover companies, which increase the margins with rise in turnover. However, in these decisions, no detailed examination has been made as to how these factors increase the profitability with rising turnover. The concept of economy of scale is relevant to manufacturing concerns, which have high fixed assets and, therefore, with the rise in volume, cost per unit of the product decreases, which is the reason of increase in margin as scale of operations goes up because with the same fixed cost there is more output when the turnover is high. The same is not true in case of service companies, which do not require high fixed assets. In these cases employees are the main assets, who in the case of the assessee are software engineers, who are recruited from project to project depending upon the requirement. The revenue in these cases is directly related to manpower utilized. With rise in volume cost goes up proportionately. Therefore, the concept of economy of scale cannot be applied to service oriented companies. On facts, it is shown by the department that in the case of the comparables selected by the assessee, there is no linear relationship between margin and turnover and that that the margin has come down with the rise in turnover in some cases. Such detailed study was not available before the various Benches of the Tribunal which have applied the turnover filter and consequently those decisions cannot be followed;

- Under Rule 10B (2), comparability of international transactions with uncontrolled transactions has to be judged with reference to functions performed, asset employed and risk assumed. The functions performed by all comparable companies are same as it is because of same functions they have been selected by the assessee as comparables. The asset employed has two dimensions i.e. quantity and quality.

  More employees would mean more turnovers, but there is no linear relationship between margin and turnover. As regards quality of employees, this will depend upon the nature of projects and since the comparables are operating in the same field having similar nature of work, and employee cost being morecin case of more skilled manpower; it will not have much impact on the margins. As for the bargaining power, the assessee is part of a multinational group and well established in the field and, therefore, it cannot be accepted that it has less bargaining power than any of the Indian Companies, however big it may be. Therefore, it would not be appropriate to apply turnover filter for the purpose of comparison of margins. However, for the purpose of comparison, the turnover would be relevant only from the limited purpose to ensure that the comparable

selected is an established player capable of executing all types of work relating to software development as the assessee is also an established company in the field (GenesiscIntegrating System not followed);

- The assessee had selected Infosys and Wipro as comparables on the basis of its own transfer pricing study after being fully aware of its work profile. The assessee raised no plea either before the TPO or DRP for excluding these comparables though it had added some more comparables. The assessee, therefore, cannot raise any grievance before the Tribunal to exclude these comparables, without giving any cogent and convincing reason. The reasons given by the assessee (turnover filter) are not found convincing and so it cannot be permitted to exclude Infosys and Wipro (Kansai Nerolac Paint followed) (vi) Working capital adjustments are required to be made because these do impact the profitability of the company. Rule 10B(2)(d) also provides that the comparability has to be judged with respect to various factors including the market conditions, geographical conditions, cost of labour and capital in the market. Accounts receivable/payable effect the cost of working capital. A company which has a substantial amount blocked with the debtors for a long period cannot be fully comparable to the case which is able to recover the debt promptly. The average of opening and closing balance in the account receivable/payable for the relevant year may be adopted which may broadly give the representative level of working capital over the year. Even if there is some difference with respect to the representative level, it will not affect the comparability as the same method will be applied to all cases. Working capital adjustment cannot be denied to the assessee only on the ground that the assessee had not made any claim in the TP study if it is possible to make such adjustment. Working capital adjustment will improve the comparability.

- The argument that no adjustment need be made because the parent company is situated in US where tax rate is high and that there was no reason for the assessee to transfer profit to the parent company is not acceptable. The arm's length price of an international transaction has to be calculated with respect to similar transaction with an unrelated party as per the method prescribed and the revenue is not required to prove tax avoidance due to transfer of profit to lower tax jurisdiction. Arguments such as that the parent company was incurring loss or had shown lower margin are not relevant. (AY. 2007-08)

ONWARD TECHNOLOGIES LTD. V/S DY. CIT[44]

The Tribunal had to consider the following important transfer pricing issues: (i) whether the foreign AE can be taken as the tested party & if the sale price received by the foreign AEs from the services ultimately sold to customers is equal to that charged by the assessee from its AEs, it would show that the international transaction between the assessee and the AEs is at ALP? (ii) whether the transfer pricing additions can result in the overall profit of the group of AEs being breached? & (iii) whether if the assessee has consistently followed a method for determination of the ALP and the same has been accepted by the TPO in the past, he cannot reject that method for the current year?

☐ The Tribunal held that:

- The argument that the foreign AE should be selected as the tested party and the profit earned by the foreign AE from outside comparables should be compared with the price charged by the assessee from the AE to determine whether they are at ALP is not acceptable because under the scheme of s. 92C, the profit actually realized by the Indian assessee from the transaction with its foreign AE has to be compared with that of the comparables. There is no question of substituting the profit realized by the Indian enterprise from its foreign AE with the profit realized by the foreign AE from the ultimate customers for the purposes of determining the ALP of the international transaction of the Indian enterprise with its foreign AE. The scope of TP adjustment

[44] Onward Technologies Ltd .v.Dy.CIT(2013) 89 DTR 311/155 TTJ 439 /26 ITR 734(Mum.)(Trib.).

under the Indian taxation law is limited to transaction between the assessee and its foreign AE. The contention that the profit earned by the foreign AE should be substituted for the profit of the comparables is patently unacceptable. The fact that this may be permissible under the US and UK transfer pricing regulations is irrelevant;

- The contention of the assessee that the authorities cannot go beyond the overall profit of the group of AEs in determining the ALP of the international transaction is also not acceptable because it willconstitute a new method/ yardstick for determining the ALP. The transfer pricing adjustments made in India may result in the overall profit earned by all the AEs taken as one unit being breached; (iii) The contention that as the assessee consistently followed the same method for determination of the ALP and it was accepted by the TPO in the past, he cannot take a different view is not acceptable. A delicate balance needs to be maintained between the principle of consistency and the rule of res judicata. There is no estoppel against the provisions of the Act. As the method employed by the assessee for determining the ALP is contrary to the statutory provisions, the inadvertent acceptance of the wrong method by the TPO in an earlier year does not grant a license to the assessee to continue calculating the ALP in the grossly erroneous manner in perpetuity. It needs to be discontinued forthwith. (AY. 2006-07)

AURIONPRO SOLUTIONS LTD V/S ADDL. CIT[45]

The assessee, an Indian company, gave loans of Rs. 15.65 crores to its AEs in USA, Singapore and Bahrain. It claimed that the said loans were "working capital advances" given for commercial consideration to secure business and that no interest was recoverable on it. The TPO applied the CUP method and determined the ALP of the advances at LIBOR plus 3per cent mark up. The DRP held that only inbound loans (ECBs) taken by the Indian entities from outside India could be benchmarked with LIBOR and that outbound loans had to be benchmarked on the interest rate prevailing in India on corporate bonds. It treated the advance as an unrated bond having very high risk and enhanced the assessment by directing the TPO to adopt 14per cent as the ALP rate.

The Tribunal reversed the DRP's decision and held that The assessee's argument that the non-charging of interest on the working capital advances to AEs from whom the assessee was getting good business was justified by commercial considerations and that no transfer pricing adjustment is warranted is not acceptable because the existence or non-existence of commercial consideration between the assessee and the AEs is not a required condition for applicability of the TP regulations Further, the advance was not the credit period extended to the AEs in respect of business transactions but was a transaction of advancing loans to the AEs which falls under the ambit of "international transaction" u/s 92B. In principle, the DRP is justified in its view that the ALP should be determined on the basis of the interest rate that would have been earned by the assessee by advancing loans to an unrelated third party (in India) such as a Fixed Deposit with the Bank. However, since LIBOR has been accepted by the Tribunal in other cases, the ALP should be determined on the basis of LIBOR + 2per cent

DCIT V/S GE BE PVT. LTD.[46]

GE BE Pvt Ltd is a joint venture between GE Mauritius Ltd. and Bharat Electronics Ltd. ('BEL'). The assessee manufactures X-ray and CT tubes, HV Tanks, detectors, parts and accessories for medical diagnostic imaging equipments on contract basis for its AE. During AY 2004-05, it entered into various international transactions including sale of finished goods, import of raw materials, provision of engineering services, purchase of fixed assets etc. The

---

[45] Aurionpro Solutions Ltd .v. ACIT(2013) 33 Taxmann.com 187/27 ITR 276 (Mum). (Trib.)

[46] GE BE Pvt. Ltd. (TS-364-ITAT-2013(Bang)-TP)

assessee selected Cost Plus Method ('CPM') as the most appropriate method to determine the arm's length price ('ALP') of the international transactions. During TP proceedings, the TPO rejected the assessee's comparables and identified comparable companies and accordingly made an adjustment of Rs. 432.78 crores to the income of the assessee. The CIT (A) upheld the adjustment made by the TPO.

ITAT observed that, as a general rule, UN Practical TP manual advocates use of CPM in the case of Contract manufacturers. However, in the Indian context, determination of most appropriate method is subject to the satisfaction of the parameters laid down in Rule 10C (1) & (2) of the Rules. ITAT examined the parameters laid down in Rule 10C (1) and observed that, on the basis of facts and UN TP Manual Guidelines, Rule 10C (1) was satisfied. Thus, ITAT held that, in case of contract manufacturers like the assessee, CPM was the most appropriate method.

ASIAN PAINTS LTD V/S ACIT[47]

Asian Paints Ltd is a company engaged in the business of manufacturing and sales of paints and enamels. The assessee filed its return for AY 07-08 declaring total income of Rs. 405.67 Cr. The assessee had given a guarantee to Bank of Singapore and to a Bank in Australia, so as to enable the Banks to provide loan to assessee's the AEs. Commission/fees for guarantees at 0.20per centwas offered by the assessee. The TPO determined the rate of commission at 3per cent and made a TP adjustment of Rs. 2.44 Cr. The CIT (A) deleted the addition observing that TPO had adopted a 'naked quote' without factoring in the qualitative factors which determined the fees. CIT (A) stated that quotation given by third party e.g. a Banker did not constitute a CUP since it was quotation and not an actual 'uncontrolled transaction'.

ITAT observed that the instant issue was covered in assessee's favour by co-ordinate bench ruling in assessee's own case for AY 2006-07. The co-ordinate bench had observed that charging of guarantee commission was dependent on the transaction and mutual understanding between the bank and the parties. There could be instances, where on the evaluation of various parameters, of financial credibility and stakes of the client, the bank may not charge any guarantee commission which completely depended upon its evaluation. ITAT stated that TPO's application of guarantee commission rate by simply relying upon certain market data without carrying-out any comparability analysis of the actual transaction was incorrect.

GLENMARK PHARMACEUTICALS LTD. VS. ADDL. CIT[48]

Glenmark Pharmaceuticals Ltd. is engaged in the business of manufacturing and marketing pharmaceutical products and related R&D activities. During AY 2008-09, the assessee extended guarantee in respect of bank loan and L/C facility obtained by its AEs, viz. Glenmark Holding SA Switzerland and Glenmark Generic SA Argentina. The assessee charged guarantee fee @0.53per cent in respect of guarantee for bank loan and @1.47per cent in respect of guarantee for L/C facility.

During the TP proceedings, TPO benchmarked guarantee commission considering the guarantees commission rate charged by banks @ 3per cent. The CIT (A) confirmed the adjustment and aggrieved, the assessee was in appeal before ITAT.

ITAT observed that CUP was the most appropriate method for benchmarking guarantee commission. ITAT further observed that in case of Reliance Industries, corporate guarantee rate of 0.5per cent was approved by the Tribunal. Further in case of Nimbus Communication [TS-167-ITAT-2013(Mum)-TP] and Everest Kanto Cylinders [TS-714-

---

[47] Asian Paints Ltd. (TS-353-ITAT-2013(Mum)-TP)

[48] Glenmark Pharmaceuticals Ltd. (TS-329-ITAT-2013(Mum)-TP)

ITAT-2012(Mum)-TP], rate of 0.25per cent was accepted to be at ALP. Therefore, ITAT decided that Bank guarantee rates adopted by TPO are Incomparable Uncontrolled Prices and cannot be used to benchmark corporate guarantee prices. ITAT also observed that bank guarantee and corporate guarantee are conceptually different and held that the TPO cannot pick up the naked quotes of the bank guarantee rates as given in the websites for public as CUP unless they are adjusted to the various controlling factors under Rule 10B. ITAT thereby approved guarantee commission fee @ 0.53per cent and 1.47per cent charged by assessee.

CREDIT LYONNAIS VS. ADIT [49]

The assessee, Credit Lyonnais, facilitated foreign currency loan to its clients from it's HO/overseas branch but did not show any income in its return for AY 2002-03. The assessee had helped foreign currency loan syndication in respect of two loans to Reliance Petroleum Ltd. and Reliance Industries Ltd. to the tune of USD 50 million and USD 11 million respectively. Credit Agricole Indosuez (Asia), Singapore (CAI) worked as an agent and Credit Lyonnais worked as lead arrangers/co-arrangers. ANZ Investment Bank, BA Asia Ltd. as well as ABN Amro Bank were also the co-arrangers. The role of the assessee for these transactions was to provide financial analysis of the borrowers, general market conditions and regulatory environment.

During TP proceedings, the TPO held that 25per cent of the total amount comprising interest and fee received by the offshore branches of the bank should have been received by the assessee. Therefore, TPO proposed addition of Rs. 70.99 lakhs. The assessee had contended that all negotiations with clients were done by desks in HK and assessee had no role in decision of granting loan. The transactions were completed outside India since all documents were signed outside India. The assessee did not provide any service as an agent/arranger and the fee or interest received by the foreign branches on this account was not attributable to the assessee. On appeal, CIT (A) reduced the adjustment from 25per cent to 20per cent.

ITAT held that since the assessee's role in providing services was the core basis of taking the decision of granting loan, such services would not fall under the terms of facilitation of conclusion of loan agreement or signing of such agreement for the purpose of Para 4 of the Protocol. Therefore, ITAT held that income was attributable to Indian PE.

However, as assessee had not contributed to the loan amount which was provided by the syndicate, interest income could not be attributed to the assessee. But since the assessee had provided services, arm's length consideration was required to be determined under TP provisions. ITAT also held that estimation made by the CIT(A) at the rate of 20per cent was just and proper. However, ITAT directed that it should be restricted to fees received by foreign branches and interest should not be considered for benchmarking.

GLOBAL TURBINE SERVICES INC V/S ADIT[50]

The assessee, Global Turbine Services Inc was set-up as an Indian Branch of its parent company . During AY 2005-06, the assessee was engaged in the business of manpower sourcing and support services to its AEs. These AEs identified their personnel requirements including skills, experience, and other qualifications and the assessee were required to provide such personal staff for specific project and duration. The assessee submitted that AY 2005-06 was its first year of commencement of operations and during this gestation period, it had suffered a loss of Rs.732, 795 on account of inadequate volumes of work.

---

[49] Credit Lyonnais (TS-283-ITAT-2013(Mum)-TP)

[50] Global Turbine Services Inc.(TS-259-ITAT-2013(DEL)-TP)

The TPO made a transfer pricing adjustment of Rs.85.65 Lakhs with respect to the sourcing and support services provided by the assessee to its AE's, on various grounds. The TPO contended that the assessee was working as a man power sourcing and support services provider and assumed all the operational/ business risks like market risks, foreign exchange risks, and capacity risks.

On appeal by the assessee, the CIT (A) confirmed the order of the TPO and rejected the assessee's plea about capacity under utilization. The CIT(A) held that business loss was least expected as the appellant was engaged in recruiting highly technical and skilled employees, thus the loss due to the transfer price of the international transactions pertaining to the services.

The Tribunal held that the assessee argued that it was entitled to adjustments on account of capacity utilization and start-up costs on a reasonable basis. The assessee submitted that creation of capacity was a business investment for the assessee and such an investment was necessary during the gestation period and would be borne by any independent company in its initial years. Therefore, being the first year of its operation, it had incurred certain start-up expenditure and its capacity utilization was also not satisfactory which had abnormally affected the profit margin. Assessee also relied on various judicial preceding including the case of Amdocs Business Services Pvt. Ltd. [TS-537-ITAT-2012(PUN)] where it was observed that "The plea set-up by the assessee for economic adjustments on account of under capacity utilization and being in start up phase, is not something which is unreasonable and neither it is otiose to the mechanism of transfer pricing assessments." The assessee also requested for the acceptance of additional evidence which elaborated the effect of capacity non utilization on the assessee's profitability.

Relying on the case of Amdocs Business Services Pvt. Ltd. [TS-537-ITAT-2012(PUN)], ITAT accepted assessee's plea for capacity under utilization adjustment. ITAT held that suitable adjustment for non-utilization of capacity was to be taken in to account after considering the ALP while working out TP adjustment, which was not done by the lower authorities. Accordingly ITAT restored the matter of under capacity utilization back to the file of the TPO to decide the same afresh, vide a speaking order, after considering the additional evidence submitted by the assessee.

BMW INDIA PVT.LTD. VS. ACIT[51]

The assessee BMW India Pvt. Ltd. is engaged in import and sale of premium segment cars in India and operates as a normal risk distributor in India. It imports completely built units (CBU) of various models of BMW cars from BMW Group for resale in India. It also carries out low value adding assembly of completely knocked down (CKD) kits for certain BMW models in its assembly facility in Chennai. During AY 2008-09, the assessee entered into various international transactions with its AE, such as purchase of raw material, trade vehicles, spare parts, receipt of technical support services, etc. The assessee had applied Resale Price Method (RPM) as primary method for TP analysis, supported TNMM as secondary method. Under RPM, the assessee's GP margin was 27.36per cent as against margin for comparables 13.65per cent. Under TNMM, the assessee net margin was 13.52per cent, as against comparables margin of 2.11per cent.

During transfer pricing proceedings, the TPO accepted the assessee's declared international transactions to be at arm's length. However, he noted that the assessee had incurred heavy advertising, marketing and promotion expenditure (AMP expenditure) and ratio of AMP expenses to sales was at 7.09per cent, as against 1.99per cent for comparables. The TPO held that the assessee's brand promotion activity has resulted in creation of marketing intangible for its AE, BMW AG. Since the ownership of brand vested with the AE, the TPO held that the assessee should have been compensated for its services of brand promotion. Applying bright line test, TPO determined non-routine expenditure of Rs. 42.31 Cr and proposed addition of Rs. 48.65 Cr considering mark-up of 15per cent.

[51] BMW India Pvt. Ltd.(TS-230-ITAT-2013(DEL)-TP)

DRP granted partial relief and directed the TPO to exclude from the AMP calculation, the amounts pertaining to the after sales support costs and salesman bonus etc. However, TPO kept the amount of adjustment unchanged in the final order.

ITAT accepted the assessee's claim that its request for withdrawing as intervener was accepted by Special Bench in LG case. ITAT also held that the assessee was not precluded from advancing arguments on facts and law which were not addressed before the Special Bench by the intervener/parties and not considered consequently by the Special Bench. ITAT also clarified that it would not necessarily follow that the ruling of the Special Bench would not apply to the assessee wherever facts and law so demand.

ITAT also accepted additional ground raised by the assessee that the TPO erred in not following DRP's direction regarding exclusion of certain cost components while working out AMP adjustment. ITAT noted that all the relevant facts for additional ground were already on record. ITAT held that TPO's action of not following DRP directions was not acceptable. ITAT observed, "It is not open and should not be open to anyone to thumb his nose on the statutorily supported directions of a higher forum and it is for the CBDT to look into this malaise which appears to have crept in the functioning of the department."

Referring to the clauses of importation agreement between the assessee and AE, ITAT noted that all the intangibles are owned by the AE and responsibility of sales promotion and full utilization of market potential rest with the assessee. The assessee was also responsible for providing customer service and establishing efficient distribution network. It was also responsible to perform adequate advertisement and sales promotion and establish public and media relations. Referring to TP study and contract with AE, ITAT concluded that the assessee had agreed to perform the functions of advertising and sales promotion and thus, the functions of the assessee far exceeded the functions performed by a routine distributor and it was also in confirmation with terms of contracts. Therefore, the assessee had rightly characterized itself as distributor with greater intensity of functions.

ITAT rejected the assessee's argument that incurring of AMP expenditure as a function of distributor is not an international transaction. ITAT relied on LG ruling in this context. ITAT observed that it was an international transaction, which benefitted AE. ITAT also held that since SB had upheld use of bright line test for determining non-routine expenditure and this principle was applicable to assessee, even though it was not an intervener in LG ruling.

ITAT noted from the assessee's submission that the AMP expenditure of Rs. 58.79 Cr was required to be reduced for certain costs for after-sale service, bonus to salesman, etc. and the resultant AMP figure would only be around Rs. 33 cr, which would work out to 3.62per cent of the turnover. As compared to the ratio for comparables at 1.99per cent, the excess AMP expenses would be to the tune of 1.63per cent of the turnover. In contrast to this, the assessee's GP margin is 27.36per cent and NP margin is 13.52per cent, while the gross profit and net profit margins for comparables are 13.65per cent and 2.11per centrespectively. ITAT observed that excess of assessee's margins over that of comparables, viz. 13.71per cent (27.36per cent- 13.65per cent) and 11.41per cent (13.52per cent- 2.11per cent) is to be compared with excess of AMP expenditure of 5.10per cent, without giving effect to DRP's direction (7.09per cent -1.99per cent) and 1.63per cent (3.62per cent - 1.99per cent), after giving effect to DRP directions. Thus, the assessee was already sufficiently compensated for excess AMP expenditure in terms of higher profit margin. ITAT noted that none of the above figures were disputed by the Department. Therefore, ITAT held that no further adjustment was required in respect of excess AMP expenditure.

ITAT observed the rewarding the distributor by way of price adjustment is well recognized and well accepted remuneration model. Reliance was placed on OECD TP Guidelines and Australian Tax Guidance in this respect. ITAT also noted that the AE had provided the assessee a loan at a rate better than external benchmark rate based on average PLR.

HIGH COURT RULINGS

VODAFONE INDIA SERVICE PVT. LTD V. UOI[52]

The assessee, Vodafone India Service Pvt. Ltd, an Indian company, issued equity shares at the premium of Rs.8591 per share aggregating Rs.246.38 crores to its holding company. Though the transaction was reported as an "international transaction" in Form 3 CEB, the assessee claimed that the transfer pricing provisions did not apply as there was no income arising to it. The AO referred the issue to the TPO without dealing with the preliminary objection. He held that the assessee ought to have charged the NAV of the share (Rs. 53,775) and that the difference between the NAV and the issue price was a deemed loan from the assessee to the holding company for which the assessee ought to have received 13.5per cent interest. He accordingly computed the adjustment for the shares premium at Rs. 1308 crore and the interest thereon at Rs. 88 crore. The AO passed a draft assessment order u/s 144C (1) in which he held that he was bound u/s 92-CA (4) with the TPO's determination and could not consider the contention whether the transfer pricing provisions applied. The assessee filed a Writ Petition challenging the jurisdiction of the TPO/AO to make the adjustment.

The High Court held that it is clear from s. 92(1) that there must be income arising/ potentially arising by an international transaction for the application of the transfer pricing provisions. This is a jurisdictional requirement and has to be dealt with by the AO when specifically raised by the assessee before making reference to the AO. Grant of personal hearing before referring the matter to the TPO has to be read into s. 92CA (1) in cases where the very jurisdiction to tax under Chapter X is challenged by the assessee (Veer Gems v. Asst. CIT (2013) 351 ITR 35 (Guj) disagreed with to the extent it holds that no hearing is required at the stage of reference to the TPO even on jurisdictional issues). If, after the hearing the assessee, the AO holds that there is an international transaction, that would be binding on the TPO;(iii) The department's contention, based on CBDT Instruction No.3 dated 20.05.2003, that the action of the AO in referring the international transaction is a mere administrative act is not acceptable. The AO is bound to hear the assessee in respect of jurisdictional issues before making the reference. The failure to do so is an illegality;(iv) The assessee's contention that the DRP would not give a fair hearing as one of its members is the DIT (TP) is not acceptable because it overlooks the fact that these are not appeal proceedings but to finalize the draft assessment order. Also, the DIT (TP) who approved the TPO's order is not on the panel;

(v) The Revenue should keep in mind the sage advice of Nani Palkhivala that the department should not cause misery and harassment to the assessee and the gnawing feeling that he is made the victim of palpable injustice. In this case it would be natural for the assessee to feel harassed as neither the AO nor the TPO gave a hearing or dealt with the preliminary objection. It is hoped that the revenue will be more sensitive to the just demands of the assessee and not treat the assessee as an adversary who has to be taxed, no matter what;(vi) The DRP should decide the assessee's objection regarding chargeability of alleged shortfall in share premium as a preliminary issue. In case the DRP's decision on the preliminary issue is adverse, the assessee shall be entitled to challenge it in a writ petition if it can show that the DRP's decision on the preliminary issue is patently illegal notwithstanding the availability of alternate remedy before the ITAT. (W.P. No. 1877 of 2013, Dt. 29.11.2013.)

---

[52] Vodafone India services Pvt. Ltd. (No.2) .v. UOI (2013) 96 DTR 193 / (2014) 264 CTR 30 (Bom.)(HC).

INBOUND INVESTMENT AND OUTBOUND INVESTMENT

RECENT CHANGES IN FDI

CHANGES IN SECTOR WISE CAP

SR. NO	SECTOR	ACTIVITY	2014 REVISED POLICY		FDI PREVIOUS POLICY	
			INVESTMENT CAP	APPROVAL ROUTE	INVESTMENT CAP	APPROVAL ROUTE
1	Petroleum & Natural Gas	Petroleum refining by PSU, without any disinvestment or dilution of domestic equity in the existing PSUs.	49 per cent	Automatic	49 per cent	Government
2	Defense	-	26 per cent	Government	26 per cent	Government
			Above 26 per cent	Cabinet Committee on Security (CCS) on case to case basis, wherever it is likely to result in access to modern and 'state-of-art' technology in the country.		
3	Telecom	-	100 per cent	Automatic up to 49 per cent Government route beyond 49 per cent	74 per cent	Automatic up to 49 per cent Government route beyond 49 per cent and up to 74 per cent
4	Single Brand Product Retail Trading	-	100 per cent	Automatic up to 49 per cent Government route beyond 49 per cent	100 per cent	Government

5	Financial Services	1) Asset Construction Company	100 per cent of paid-up capital of ARC (FDI+FII/FPI)	Automatic up to 49 per cent Government route beyond 49 per cent	74 per cent of paid-up capital of ARC (FDI+FII)	Government
		2) Banking- Private Sector	74 per cent including investment by FIIs/ FPIs	Automatic up to 49 per cent Government route beyond 49 per cent upto 74 per cent	74 per cent including investment by FIIs	Automatic up to 49 per cent Government route beyond 49 per cent upto 74 per cent
		3) Commodity Exchange	49 per cent (FDI + FII/FPI) [Investment by Registered FII / FPI under Portfolio Investment Scheme (PIS) will be limited to 23 per cent and Investment under FDI Scheme limited to 26 per cent]	Automatic	49 per cent (FDI & FII) investment by Registered FII under Portfolio Investment Scheme (PIS) will be limited to 23 per cent and Investment under FDI Scheme limited to 26 per cent]	Government (For FDI)
		4) Credit Information Companies CIC	74 per cent (FDI+FII/FPI)	Automatic	49 per cent (FDI & FII)	Government
		5) Infrastructure Company in the Securities Market	49 per cent (FDI + FII/FPI) [FDI limit of 26 per cent and FII/FPI limit of 23 per cent of the paid-up capital]	Automatic	49 per cent (FDI & FII) [FDI limit of 26 per cent and an FII limit of 23 per cent of the paid-up capital]	Government (For FDI)
		6) Insurance	26 per cent (FDI+FII/FPI+NRI)	Automatic	26 per cent	Automatic
6	Power Exchanges	-	49 per cent FDI+FII/FPI)	Automatic	49 per cent (FDI &FII)	Government (for FDI)

- Micro and Small Enterprises (MSE) (earlier Small Scale Industries) in terms of MSMED Act, 2006 not engaged in any activity/sector mentioned in Annex A to schedule 1 to the Notification No. FEMA. 20/2000-RB dated 3rd May 2000, may issue shares or convertible debentures to a person resident outside India, subject to the limits prescribed in Annex B to schedule 1 of the aforementioned notification, in accordance with the entry routes specified and the provision of Foreign Direct Investment Policy, from time to time.

- Any Industrial undertaking, with or without FDI, not an MSE, having an industrial license under the Industries (Development & Regulation) Act, 1951 for manufacturing items reserved for manufacture in the MSE sector may issue shares in excess of 24 per cent of its paid up capital with prior approval of the Foreign Investment Promotion Board of the Government of India.

  Further, in terms of the provisions of MSMED Act, meaning of Micro & Small is as follows-

  - In the case of the enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the first schedule to the Industries (Development and Regulation) Act, 1951, a micro enterprise means where the investment in plant and machinery does not exceed twenty five lakh rupees; a small enterprise means where the investment in plant and machinery is more than twenty five lakh rupees but does not exceed five crore rupees;

  - In the case of the enterprises engaged in providing or rendering services, a micro enterprise means where the investment in equipment does not exceed ten lakh rupees; a small enterprise means where the investment in equipment is more than ten lakh rupees but does not exceed two crore rupees.

  [A.P. (DIR Series) Circular No.107 dated 20-02-2014]

FOREIGN DIRECT INVESTMENT (FDI) IN LIMITED LIABILITY PARTNERSHIP (LLP)

In terms of Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000, only a Company incorporated under the Companies Act, 1956 or a Venture Capital Fund is eligible to accept FDI.

It has now been decided that a Limited Liability Partnership (LLP) formed and registered under the Limited Liability Partnership Act, 2008 shall be eligible to accept Foreign Direct Investment (FDI) subject to the conditions prescribed in Annex I of the Notification No. FEMA 20/2000-RB dated May 3, 2000.

[Circular No. 123, dated 16-4-2014]

FDI REPORTING MECHANISM FOR TRANSFER OF EQUITY SHARES, FULLY AND MANDATORILY CONVERTIBLE PREFERENCE SHARES AND DEBENTURES

- To rationalize the existing procedure, in cases where the NR investor including an NRI acquires shares on the stock exchanges in terms of the A.P. (DIR Series) Circular No. 38 dated September. 6, 2013, the investee company would have to file form FC-TRS with the AD Category-I bank.

- In order to facilitate operational convenience it has been decided that the AD Category-I bank may approach Regional Office concerned of Reserve Bank of India, Foreign Exchange Department to regularize the delay in submission of form FC-TRS, beyond the prescribed period of 60 days and in all other cases, form FC-TRS shall continue to be scrutinized at AD bank level as per extant practice.

- The AD banks shall continue to comply with the consolidated reporting requirement as stipulated in terms of Para 6.4 of A.P. (DIR Series) Circular No. 16 dated October 4, 2004.

[A.P. (DIR Series) Circular No.127 dated 02-05-2014]

REVISED FORMAT OF ANNUAL RETURN ON FOREIGN LIABILITIES & ASSETS

All Indian Companies who have made and/or received FDI are required to file the Annual Return on Foreign Liabilities and Assets (FLA) in the soft form to the Reserve Bank by July 15 every year. With effect from F.Y.2013-2014, the Annual Return form for FLA has been modified. The revised format is available at RBI website.

[A.P. (DIR Series)Circular No. 145, dated 18-6-2014]

RECENT CHANGES IN FII:

MAINTENANCE OF COLLATERAL BY FOREIGN INSTITUTIONAL INVESTORS (FII'S) FOR TRANSACTIONS IN THE CASH AND F & O SEGMENTS

Earlier, FII had to offer Domestic Government Securities (acquired by the FIIs in accordance with the relevant provisions) and Foreign Sovereign Securities with AAA rating as collateral to the recognized Stock Exchanges in India for their transactions in derivatives segment, in addition to cash, for their transactions in the cash segment of the market.

It has been now decided to permit FIIs to use, in addition to already permitted collaterals as mentioned above, their investments in corporate bonds as collateral in the cash segment and government securities and corporate bonds as collaterals in the F & O segment.

[A.P. (DIR Series) Circular No. 90 dated 14-3-2013]

FOREIGN INVESTMENT IN INDIA - PARTICIPATION BY SEBI REGISTERED FIIS, QFIS AND SEBI REGISTERED LONG TERM INVESTORS IN CREDIT ENHANCED BONDS

Earlier in terms of A.P. (DIR Series) Circular no. 120 dated June 26, 2013, credit enhancement can be provided by eligible non-resident entities to the domestic debt raised through issue of INR bonds/ debentures by all borrowers eligible to raise ECB under the automatic route.

As per new circular, SEBI registered Foreign Institutional Investors (FIIs), Qualified Foreign Investors (QFIs) and long term investors registered with SEBI – Sovereign Wealth Funds (SWFs), Multilateral Agencies, Pension/ Insurance/ Endowment Funds, foreign Central Banks are now permitted to invest in the credit enhanced bonds, as per paragraph 3 and 4 of A.P. (DIR Series) Circular No. 120 dated June 26, 2013, up to a limit of USD 50,00,00,000 within the overall limit of USD 5,10,00,00,000 earmarked for corporate debt.

[A.P. (DIR Series) Circular No. 74 dated 11-11-2013]

FOREIGN INVESTMENT IN INDIA BY SEBI REGISTERED FII, QFI AND LONG TERM INVESTORS IN CORPORATE DEBT- REVISED LIMITS FOR CP

The present limit for investment by SEBI registered FIIs, QFIs and long term investors in corporate debt stands at USD 5,10,00,00,000. Out of the above limit of USD 5,10,00,00,000 a sub-limit of USD 35,00,00,000 is available for investment by eligible investors in Commercial Paper (CP).

This sub-limit is being presently utilized only to the extent of around 58 per cent of the limit put in place by SEBI

With a view to encourage long term investors, it has now been decided, to reduce, with immediate effect, the existing Commercial Paper sub-limit of USD 35,00,00,000 by USD 15,00,00,000 to USD 20,00,00,000. The balance USD 15,00,00,000 shall, however, continue to be part of the total corporate debt limit of USD 5,10,00,00,000 and will be available to eligible foreign investors for investment in corporate debt.

[A.P. (DIR Series) Circular No. 104 dated 14-02-2014]

FOREIGN INVESTMENT IN INDIA BY SEBI REGISTERED LONG TERM INVESTORS IN GOVERNMENT DATED SECURITIES

The Present Limit for investments by FIIs, QFIs and long term investors in Government securities stands at USD 3,00,00,00,000 out of which a sub-limit of USD 50,00,00,000 is available for investment by long term investors in Government dated securities.

As per A.P. (DIR Series) Circular No.99 dated 29th January, 2014, with immediate effect, the existing sub-limit of USD 50,00,00,000 available to long term investors registered with SEBI – Sovereign Wealth Funds (SWFs), Multilateral Agencies, Pension/ Insurance/ Endowment Funds and Foreign Central Banks for investment in Government dated securities increased to USD 1,00,00,00,000 within the total limit of USD 3,00,00,00,000 available for foreign investments in Government securities.

[A.P. (DIR Series) Circular No. 11 dated 07-04-2014]

FOREIGN INVESTMENT IN INDIA: PARTICIPATION BY REGISTERED FPIS, SEBI REGISTERED LONG TERM INVESTORS AND NRIS IN NON-CONVERTIBLE /REDEEMABLE PREFERENCE SHARES OR DEBENTURES OF INDIAN COMPANIES

As per circular, registered Foreign Institutional Investors (FIIs), Qualified Foreign Investors (QFIs) deemed as registered Foreign Portfolio investors, registered Foreign Portfolio Investors (FPIs), long term investors registered with SEBI – Sovereign Wealth Funds (SWFs), Multilateral Agencies, Pension/ Insurance/ Endowment Funds, foreign Central Banks are allowed to invest on repatriation basis, in non-convertible/ redeemable preference shares or debentures issued by an Indian company in terms of A.P. (DIR Series) Circular No. 84 dated January 6, 2014 and listed on recognized stock exchanges in India, within the overall limit of USD 5,10,00,00,000 earmarked for corporate debt.

[A.P. (DIR Series) Circular No. 140 dated 06-06-2014]

RECENT DEVELOPMENTS IN OVERSEAS DIRECT INVESTMENT (ODI)

- The RBI has now issued circular whereby the said limit has been restated to 400 per cent of the net worth as per the last audited balance sheet of the Indian entity. however, the same comes with a caveat i.e., any ODI or financial commitment of more than USD 10,00,00,000 in a particular financial year will require prior approval of the RBI, even if such ODI or financial commitment is within the eligible ODI limit of 400 per cent.

- Now even LLP's are notified as Indian Party and hence can accordingly undertake financial commitment (investment) to/on behalf of a Joint Venture or Wholly Owned Subsidiary abroad.

- Given the fact that currently Indian Rupee is not fully convertible and financial products linked to Indian Rupee such as (e.g. non-deliverable trades involving foreign currency, rupee exchange rates, stock indices linked to Indian market, etc.) could have implications for the exchange rate management of the country, it has been clarified by RBI that Overseas entity having equity participation directly / indirectly shall not offer such products without the specific approval of the Reserve Bank of India.

[A.P. (DIR Series) Circular No. 1 dated 03-07-2014]

ROLLOVER OF GUARANTEES

It has been decided not to treat / reckon the renewal / rollover of an existing / original guarantee, which is part of the total financial commitment of the Indian party in terms of Regulation 6 of the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) (Amendment) Regulations, 2004, as a fresh financial commitment, provided that:

- The existing / original guarantee was issued in terms of the then extant / prevailing FEMA guidelines;

- There is no change in the end use of the guarantee, i.e. the facilities availed by the JV / WOS / Step Down Subsidiary;

- There is no change in any of the terms & conditions, including the amount of the guarantee except the validity period;

- The reporting of the rolled over guarantee would be done as a fresh financial commitment in Part II of Form ODI, as hitherto; and

- If the Indian party is under investigation by any investigation / enforcement agency or regulatory body, the concerned agency / body shall be kept informed about the same.

In case, however, the above conditions are not met, the Indian party shall obtain prior approval of the Reserve Bank for rollover / renewal of the existing guarantee through the designated AD bank.

RECENT DEVELOPMENT IN ECB

SIMPLIFICATION OF PROCEDURE FOR ELONGATION / ROLLOVER IN THE REPAYMENT PERMISSION AFTER EXPIRY OF ORIGINAL MATURITY

Earlier any elongation / rollover in the repayment on expiry of the original maturity of the ECB requires the prior approval of the Reserve Bank however now RBI has delegated the power to the designated AD Category– I bank to allow re-schedule of ECB due to changes in draw-down schedule and / or repayment schedule with the certain conditions.

Conditions to be satisfied for approval from designated bank-

- Changes, if any, in all-in-cost (AIC) is only on account of the change in average maturity period (AMP) due to re-schedulement of ECB and post re-schedulement, the AIC and the AMP are in conformity with applicable guidelines. There should not be any increase in the rate of interest and no additional cost (in foreign currency / Indian Rupees) should be involved.
- The re-schedulement is allowed only once, before the maturity of the ECB.
- If the lender is an overseas branch of a domestic bank, the prudential norms applicable on account of re-schedulement should be complied with.
- The changes on account of re-schedulement should be reported to DSIM through revised Form 83.
- The ECB should be in compliance with all applicable guidelines related to eligible borrower, recognized lender, AIC, AMP, end-uses, etc.
- The borrower should not be in the default / caution list of RBI and should not be under the investigation of Directorate of Enforcement.

The facility will be available for ECBs raised both under the automatic and approval routes. Provisions of this Circular do not apply to FCCBs.

[A.P. (DIR Series) Circular No. 128 dated 09-05-2014]

SIMPLIFICATION OF PROCEDURE FOR ECBS FROM DIRECT / INDIRECT FOREIGN EQUITY

As per the extant ECB policy, ECBs from direct foreign equity holders (FEHs) are considered both under the automatic and the approval routes, as the case may be. ECBs from indirect equity holders and group companies and ECBs from direct FEH for general corporate purpose are, however, considered under the approval route. Any request for change of the ECB lender in case of FEH requires RBI's approval.

As a measure of simplification of the existing procedure, it has been decided to delegate powers to AD banks to approve the following cases under the automatic route:

- Proposals for raising ECB by companies belonging to manufacturing, infrastructure, hotels, hospitals and software sectors from indirect equity holders and group companies.

- Proposals for raising ECB for companies in miscellaneous services from direct / indirect equity holders and group companies. Miscellaneous services mean companies engaged in training activities (but not educational institutes), research and development activities and companies supporting infrastructure sector. Companies doing trading business, companies providing logistics services, financial services and consultancy services are, however, not covered under the facility.

- Proposals for raising ECB by companies belonging to manufacturing, infrastructure, hotels, hospitals and software sectors for general corporate purpose.ECB for general corporate purpose (which includes working capital financing) are, however, permitted only from direct equity holder.

- Proposals involving change of lender when the ECB is from FEH – direct / indirect equity holders and Group Company.

[A.P. (DIR Series) Circular No. 128 dated 09-05-2014]

RESTRICTION ON RAISING ECB BY OVERSEAS BRANCH OF DOMESTIC BANK FOR REPAYMENT OF RUPEE LOAN FROM DOMESTIC BANK

It has been determined that eligible Indian companies will not be permitted to raise ECB from overseas branches / subsidiaries of Indian banks for the purpose of refinance / repayment of the Rupee loans raised from the domestic banking system in respect of the following:

- Scheme of take-out financing

- Repayment of existing Rupee loans for companies in infrastructure sector

- Spectrum allocation

- Repayment of Rupee loans

[A.P. (DIR Series) Circular No. 129 dated 09-05-2014]

EXTENSION OF TIME LIMIT TO RAISE ECB FOR WORKING CAPITAL AS PERMISSIBLE END USE BY CIVIL AVIATION SECTOR

In terms of Circular no. 113 of 2012, ECB can be raised by airline companies for working capital as a permissible end-use, under the approval route, subject to the conditions stipulated in the said Circular. The scheme was extended till December 31, 2013 vide Circular No. 116 dated June 25, 2013. On a review, it has been decided that this scheme of raising ECB for working capital for Civil Aviation Sector will continue till March 31, 2015.

CHANGE IN REPORTING ARRANGEMENT OF ECB

In order to capture details of the financial hedges contracted by corporate, of their foreign currency exposure relating to ECB and their foreign currency earnings and expenditure, the format of ECB-2 Return has been modified and the same has been given in the Annex to Circular No. 105 dated Feb 17, 2014). The reporting in the modified ECB-2 Return will be applicable from the return of the month April 2014 onwards.

RECENT CHANGES IN EXPORT OF GOODS AND SERVICES

CHANGE IN TIME LIMIT FOR SUBMISSION OF FORM

Exporter undertaking Project Exports and Service contracts abroad are now required to submit form DPX1, PEX-1 and TCS-1 to the Approving Authority (AA) i.e. AD Bank/ Exim Bank/ Working Group, within 30 days of entering into contract for grant of post-award approval, instead of earlier 15 days.

TIME LIMIT FOR REALIZATION & REPATRIATION VALUE OF GOODS/SOFTWARES/SERVICES BY SEZ EXPORTS

Earlier there was no time limit for realization and repatriation of export proceeds for the exports made by SEZ however vide Circular A.P. (DIR Series) Circular No. 108, 11 June, 2013 SEZs shall realize and repatriate, full value of goods/software/services, to India within a period of twelve months from the date of export.

COMMON FORM FOR DECLARATION OF EXPORTS OF GOODS/SOFTWARES FROM NON-EDI PORTS

In order to simplify the existing form used for declaration of exports of Goods/ Software's a common form called "Export Declaration Form" (EDF) has been devised to declare all types of export of goods from Non-EDI ports and a common "SOFTEX Form" to declare single as well as bulk software exports. The EDF will replace the existing GR/PP form used for declaration of export of Goods. The procedure relating to the exports of goods through EDI ports will remain the same and SDF FORM WILL BE APPLICABLE AS HITHERTO.

WRITE OFF

Subject to the stipulations regarding surrender of incentives prior to "write-off" adduced in the A.P. (DIR Series) Circular No. 03 dated 22 July 2010, the following liberalization in the limits of "write-offs" of unrealized export bills:

- Self "write-off" by an exporter

  (Other than Status Holder Exporter) ---05 per cent*

- Self "write-off" by Status Holder Exporters --10 per cent*

- 'Write-off" by Authorized Dealer bank ---10 per cent*

*of the total export proceeds realized during the previous calendar year

The above limits will be related to total export proceeds realized during the previous calendar year and will be cumulatively available in a year.

The above “write-off” will be subject to the following conditions:

- The relevant amount has remained outstanding for more than one year;

- Satisfactory documentary evidence is furnished in support of the exporter having made all efforts to realize the dues;

- The case under any of the categories specified in clause 4(c) of the Circular No. 88 dated March 12, 2013.

The exporter has surrendered proportionate export incentives (for the cases not covered under A. P. (DIR. Series) Circular No.03 dated July 22, 2010), if any, availed of in respect of the relative shipments. The AD Category – I banks should obtain documents evidencing surrender of export incentives availed of before permitting the relevant bills to be written off.

In case of self write-off, the exporter should submit to the concerned AD bank, a Chartered Accountant’s certificate, indicating the export realization in the preceding calendar year and also the amount of write-off already availed of during the year, if any, the relevant GR / SDF Nos. to be written off, Bill No., invoice value, commodity exported, country of export. The CA certificate may also indicate that the export benefits, if any, availed of by the exporter have been surrendered.

RECENT CHANGES IN COMPOUNDING

DELEGATION OF FURTHER POWERS TO REGIONAL OFFICES OF THE RBI TO COMPOUND THE CONTRAVENTIONS OF FEMA

RBI has more straightened regional offices As per A.P. (DIR Series) Circular No.117, dated April 04, 2014; the powers to compound the following contraventions will now be vested with the Regional Offices:

S.NO.	FEMA REGULATION	BRIEF DESCRIPTION OF CONTRAVENTION
1	Paragraph 9(1)(A) of Schedule I to FEMA 20/2000-RB dated May 3, 2000	Delay in reporting inward remittance received for issue of shares.
2	Paragraph 9(1)(B) of Schedule I to FEMA 20/2000-RB dated May 3, 2000	Delay in filing form FC (GPR) after issue of shares.
3	Paragraph 8 of Schedule I to FEMA 20/2000-RB dated May 3, 2000	Delay in issue of shares/refund of share application money beyond 180 days, mode of receipt of funds, etc.
4	Paragraph 5 of Schedule I to FEMA 20/2000-RB dated May 3, 2000	Violation of pricing guidelines for issue of shares.

5	Regulation 2(ii) read with Regulation 5(1) of FEMA 20/2000-RB dated May 3, 2000	Issue of ineligible instruments such as non-convertible debentures, partly paid shares, shares with optionality clause, etc.
6	Paragraph 2 or 3 of Schedule I to FEMA 20/2000-RB dated May 3, 2000	Issue of shares without approval of RBI or FIPB respectively

The above contraventions can be compounded by all Regional Offices (except Kochi and Panaji) without any limit on the amount of contravention. Kochi and Panaji Regional offices can compound the above contraventions for amount of contravention below Rupees one hundred lakh (Rs 1,00,00,000). The contraventions above Rupees one hundred lakhs (Rs 1,00,00,000/-) under the jurisdiction of Panaji and Kochi Regional Offices and all other contraventions of FEMA will continue to be compounded at Cell for Effective Implementation of FEMA (CEFA), Mumbai, as hitherto.

RECENT CHANGES IN LIAISON OFFICE

CLARIFICATION ON ESTABLISHMENT OF LIAISON OFFICE/ BRANCH OFFICE/ PROJECT OFFICE IN INDIA BY FOREIGN ENTITIES

As per Regulation 4 of the Notification No.FEMA.22/2000-RB dated May 3, 2000, viz., Foreign Exchange Management (Establishment in India of Branch or Office or other Place of Business) Regulations, 2000, no entity or person, being a citizen of Pakistan, Bangladesh, Sri Lanka, Afghanistan, Iran or China shall establish in India, a branch office or a liaison office or a project office or any other place of business by whatever name called, without the prior permission of the Reserve Bank.

It is clarified that the provisions of the above said regulation along with their specified conditions shall apply for all entities from Hong Kong and Macau. Accordingly, applications from entities registered in / resident of Hong Kong and Macau, for establishment of Liaison/ Branch/ Project Offices or any other place of business by whatever name called shall require prior approval from Reserve Bank of India.

[A.P. (DIR Series) Circular No.93 dated 15-1-2014]

DELEGATION OF POWERS TO AD BANKS IN RELATION TO TRANSFER OF ASSETS OF LO / BO / PO OF A FOREIGN ENTITY EITHER TO ITS WOS / JV / OTHERS IN INDIA

Earlier, ADs were delegated with powers to allow closure of the accounts of LO/BO and repatriate the surplus balances subject to submission of prescribed closure documents.

In order to smoothen the entire process of closure of LO/BO, the powers have been delegated to AD Category-1 banks subject to fulfillment of certain conditions.

[A.P. (DIR Series) Circular No.142 dated 12-6-2014]

RECENT CHANGES IN EXPORT OF CURRENCY

Any person resident in India:

- May take outside India (other than to Nepal and Bhutan) currency notes of Government of India and Reserve Bank of India notes up to an amount not exceeding Rs 25,000 (Rupees twenty five thousand only); and

- Who had gone out of India on a temporary visit, may bring into India at the time of his return from any place outside India (other than from Nepal and Bhutan), currency notes of Government of India and Reserve Bank of India notes up to an amount not exceeding Rs 25,000 (Rupees twenty five thousand only).

  Any person resident outside India, not being a citizen of Pakistan and Bangladesh and also not a traveler coming from and going to Pakistan and Bangladesh, and visiting India:

- may take outside India currency notes of Government of India and Reserve Bank of India notes up to an amount not exceeding Rs 25,000 (Rupees twenty five thousand only) while exiting only through an airport.

- may bring into India currency notes of Government of India and Reserve Bank of India notes up to an amount not exceeding Rs 25,000 (Rupees twenty five thousand only) while entering only through an airport.

REMITTANCES TO NON-RESIDENT- PROCEDURE TO BE FOLLOWED IN RESPECT OF DEDUCTION OF TAX AT SOURCE FOR REMITTANCES TO THE NON-RESIDENTS

With effect from June 30, 2014 vide Circular no. RBI/2013-14/669, RBI has reviewed policy relating to issue of instruction under FEMA act with corresponding instruction to be followed for remittance to non-resident under Income tax act. So has now been decided that Reserve Bank of India will not issue any instructions under the FEMA, in this regard. It shall be mandatory on the part of Authorised Dealers to comply with the requirement of the tax laws, as applicable.

LIBERALIZATION OF RESIDENT BANK ACCOUNT MAINTAINED BY RESIDENTS IN INDIA – JOINT HOLDER WITH NON-RESIDENT: (W.E.F JAN 9, 2014)

Earlier individuals resident in India were permitted to include non-resident close relative(s) (relatives as defined in Section 6 of the Companies Act, 1956) as a joint holder(s) in their resident savings bank accounts on “former or survivor” basis. Such non-resident Indian close relatives are however not eligible to operate the account during the life time of the resident account holder in terms of said instructions. However now RBI has decided that AD banks may include an NRI close relative (relatives as defined in Section 6 of the Companies Act, 1956) in existing / new resident bank accounts as joint holder with the resident account holder on “Either or Survivor” basis subject to the following conditions-

- Such account will be treated as resident bank account for all purposes and all regulations applicable to a resident bank account shall be applicable.

- Cheques, instruments, remittances, cash, card or any other proceeds belonging to the NRI close relative shall not be eligible for credit to this account.

- The NRI close relative shall operate such account only for and on behalf of the resident for domestic payment and not for creating any beneficial interest for himself.

Where the NRI close relative becomes a joint holder with more than one resident in such account, such NRI close relative should be the close relative of all the resident bank account holders.

- Where due to any eventuality, the non-resident account holder becomes the survivor of such an account, it shall be categorized as Non-Resident Ordinary Rupee (NRO) account as per the extant regulations.
- Onus will be on the non-resident account holder to keep AD bank informed to get the account categorized as NRO account and all such regulations as applicable to NRO account shall be applicable.
- The above joint account holder facility may be extended to all types of resident accounts including savings bank account.

RECENT CHANGES IN LIBERALISED REMITTANCE SCHEME

INCREASE IN THE LIMIT FROM USD 75,000 TO USD 125,000

As per circular, it has now been decided to enhance the existing limit of USD 75,000 per financial year (April-March) to USD 1,25,000 with immediate effect.

With effect from 5th August 2013, Resident Individuals will be allowed to set-up Joint Venture (JV) / Wholly Owned Subsidiary (WOS) outside India for bonafide business activities outside India within the specified limit of US Dollars.

Earlier banks were required to furnish information on the number of applications received and the total amount remitted under the Liberalized Remittance Scheme (the Scheme), on a monthly basis, in the prescribed format in both hard copy as well as soft copy in Excel format.

As per A. P. (DIR Series) Circular No. 106 dated May 23, 2013, it has been decided, to collect the data in soft form only and to dispense with the submission of hard copies of the monthly statements by the AD banks. (w.e.f. July 01. 2013).

[A.P. (DIR Series) Circular No.138 dated 03-6-2014]

ACCOUNTS, AUDIT AND INVESTMENTS

CIRCULAR/NOTIFICATIONS ISSUED BY STATUTORY BODIES UNDER VARIOUS ACT

NEW COMPANIES ACT 2013

Background:-

The long-awaited Companies Bill 2013 got its assent in the Lok Sabha on 18 December 2012 and in the Rajya Sabha on 8 August 2013. After having obtained the assent of the President of India on 29 August 2013, it has now become the much awaited Companies Act, 2013 (2013 Act). 98 sections have been made applicable from September 2013 & the others from April 2014.

The 2013 Act introduces significant changes in the provisions related to governance, e-management, compliance and enforcement, disclosure norms, auditors and mergers and acquisitions. Also, new concepts such as one-person company, small companies, dormant company, class action suits, registered valuers and corporate social responsibility have been included.

New concepts – at a glance:

Dormant Company

- Where Company is formed and registered under this Act for future project or to hold an assets or intellectual property and has no significant accounting transactions.

- These are new Class of Companies to be formed for future projects / hold an assets/ intellectual property rights.

One Person Company

- **"**One Person Company" (hereinafter OPC) is the new concept introduced in the Companies Act, 2013. The concept provides you with a golden opportunity to incorporate your own legal company without taking second person as a member.

- The best suited for start ups, proprietary business etc.

Small Company

Means a company, other than a public company-

- Paid up share capital which does not exceed Rs 50 Lakhs rupees or such higher amount as may be prescribed (shall not be more than five crores)

- Turnover of which, as per its last profit loss account, does not exceed Rs 2 Crore or such higher amount as may be prescribed (shall not be more than twenty crores)

Resident Director

- As per provisions of sub section 3 of section 149 of the Act, every company shall have at least one Director who has stayed in India for a total period of not less than 182 days in previous calendar year.

- These provisions are to be complied with, within one year from commencement of the Act

Women Director

- ☐ Following type of Companies shall appoint at least one Woman Director:

    - Every listed Company

    - Every other public company having Paid up share capital of Rs 100 Crore or more or Turnover of Rs 300 Crore or more

- ☐ Transition Period for compliance of provisions:

    - For Existing Companies – within one year from commencement of the Act.

    - For newly incorporated Company – within 6 months from date of incorporation.

Class Action Suits

The provisions of section 245 of the Act provides for Class Action Suit whereby such number of members, depositors or any class of them, if they are of opinion that management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interest of the company or its members or depositors, may file an application before the National Company Law Tribunal on behalf of the members or depositors.

Revision of Accounts

If it appears to the Directors of the Company that the financial statements or report of the Board do not comply with provisions of section 129 (True & Fair view) or section 134 (financial statements, Board Report), they may prepare revised financial statement or revised Report of Board in respect of any of the three preceding financial years after taking approval of National Company Law Tribunal

Rotation of Auditors

- A period of 5 years is prescribed before re appointment of same auditor.

- No audit firm having common partner or partners to the other audit firm, whose tenure has expired immediately preceding financial year, shall be appointed as auditor of the same company for a period 5 years.

- Transition period of 3 years has been prescribed to comply with provisions of rotation of auditors from the date of commencement of this section.

Private Placements

- Private Placement means any offer of securities or invitation to subscribe securities to a select group of person by a company, other than by way of public offer, through issue of a private placement offer letter and which satisfies the conditions specified in section 42 of the Act.
- Company can make private placement through issue of private placement offer letter and complying with the provisions of Part II of Chapter III of the Act.
- Private placement can be made to such number of persons not exceeding fifty

Key highlights:-

Types of companies

- Maximum number of members in a private company increased from 50 to 200
- Limit of number of members in an association or partnership (without incorporation) to be increased up to 100
- One Person Company (OPC) - a new vehicle for individuals for carrying on business with limited liability

Share capital

- For defined infrastructural projects, preference shares can be issued for a period exceeding 20 years
- Provisions relating to further issue of capital made applicable to all companies
- The terms for offer of securities, form and manner of 'private placement' to be as prescribed
- Shares cannot be issued at a discount except sweat equity shares
- Time gap between 2 buy-backs shall be minimum 1 Year

Deposits

- Stringent norms provided for acceptance of fresh deposits from members and public
- Any deposit accepted before the commencement of 2013 Act or any interest due thereon to be repaid within 1 year from the commencement of 2013 Act or from the date on which such payments are due, whichever is earlier.
- Credit rating made mandatory for acceptance of public deposits

Corporate Social Responsibility (CSR)

2 per cent of average net profits of last 3 years to be mandatorily spent on CSR by companies having

- net worth of ` 5 billion or more; or
- turnover of ` 10 billion or more; or
- net profit of ` 50 million or more

Financial Statements & Accounts

- Financial Statement to include following additional information/ statements:
- Cash flow statement for the financial year
- A statement of change in equity, if applicable
- Any explanatory note annexed to it.
- Maintenance of Books of Accounts & other relevant papers in Electronic Mode is permitted.
- Act does not contain provisions which correspond to provisions of section 212 of the Companies Act, 1956 and it appears that details required to be given in respect of subsidiary companies u/s.212 of the Companies Act, 1956 are dispensed with.
- New section which prescribes for re opening of accounts of the company by order of competent Court or Tribunal, on an application by Central Government or IT or SEBI or any other authority, to the effect that:
- The relevant earlier accounts were prepared in a fraudulent manner or
- The affairs of the company were mismanaged during the relevant period, casting doubt on the reliability of financial statements.
- New section which allows directors to prepare revised financial statement or revised Board of Directors Report if it appears to them that do not comply with provisions of section 129 or 135 of the Act.
- Revision of financial statements or Boards' Report can be sought for any of three preceding financial years.
- Application has to be made to Tribunal and upon its approval the voluntary revision can be under taken.
- Voluntary revised Financial Statement or Board's Report shall not be prepared or filed more than once in financial year.
- A Report of Board of Directors' will include following new/ additional disclosures:
    - Extract of Annual Return

- Number of meetings of Board of Directors
- A statement on declaration given by independent directors
- Company's policy on directors' appointment and remuneration, criteria for determining qualification, positive attributes, independence etc.
- Explanation or comment on every qualification, reservation or adverse remark or disclaimer made by
- The auditors in their report Or Company Secretary in Practice in his secretarial audit report
- Particulars of loans, guarantee or investment
- Particulars of contracts, arrangements with related parties
- State of the company's affairs
- Material changes and commitments, if any, affecting the financial statements which have occurred between the end of financial year and date of report

☐ Listed company to place their financial statements and all other documents required to be attached to financial statements, on its website

Audit and Accounting

- To align with the provisions of the Income tax Act, companies to have a uniform financial year – ending on 31 March each year
- Consolidation of financials for a company having a subsidiary, associate or a joint venture made mandatory
- National Financial Reporting Authority (NFRA) to be constituted by Central Government to provide for dealing with matters relating to accounting and auditing policies and standards to be followed by companies and their auditors
- Mandatory audit rotation for listed and prescribed classes of companies
- Restriction placed on provision of specified non-audit services by an auditor to ensure independence and accountability of the auditor
- Mandatory internal audit for prescribed classes of Companies.

Internal Audit function

- Such class or classes of companies as may be prescribed shall be required to appoint an internal auditor, who shall either be chartered Accountant or Cost Accountant or such other professional as may be decided by Board to conduct internal audit.

- For the first time provision of Internal Auditor is brought within the ambit of Act, unlike previous Acts where it was recommended through CARO.

Management, administration and corporate governance

- ☐ At least 1 director of a company shall be a person who has stayed in India for 182 days or more in the previous calendar year. Existing companies to comply with this provision within 1 year from the date of commencement of the 2013 Act.
- ☐ Listed and prescribed class of companies to have at least 1 woman director. Existing companies to comply with this provision within 1 year from the date of commencement of the 2013 Act.
- ☐ Prescribed class of companies to have whole-time Key Managerial Personnel (KMP) – Chief Finance Officer to be a whole time KMP for prescribed classes of companies – Whole time Director included in definition of KMP
- ☐ Electronic voting for Board and shareholders meetings introduced
- ☐ Following committees of the Board made mandatory for listed and prescribed classes of companies:
    - Audit committee
    - Stakeholder relationship committee
    - Nomination and Remuneration committee
    - Corporate Social Responsibility committee
- ☐ Director to vacate office on remaining absent from all the meetings of the Board of Directors held during 12 months with or without obtaining leave of absence
- ☐ Contents of Directors' Report elaborated. Directors to annually report on the existence and effective operations of systems on compliance with all applicable laws
- ☐ Secretarial audit mandatory for listed and prescribed classes of companies
- ☐ Approval of Central Government required for certain managerial remuneration

Meetings of Board:

- Not more than 120 days to elapse between two Board meetings
- Delivery of notice of 7 days for meetings of Boards through electronic means is recognized.
- Presence of Independent Director is mandatory in case of meetings called at shorter notice

- In absence of independent directors from meeting called on shorter notice, the decisions needs to be ratified by at least one independent director.

- Meetings through Audio Video conferencing and Audio Video means capable of storing the proceedings of meetings with date and time are now recognized mode of holding a meeting

- Central Government may specify such matters which shall not be dealt with in a meeting through video conferencing or other audio video means.

Related Party transactions

- Requirement of obtaining Central Government approval for related party transactions not required

- Approval of related party transactions by Board of Directors at Board meeting made mandatory

- Related party transactions to also require prior shareholder's approval by special resolution for companies having prescribed paid up capital or transactions exceeding prescribed amounts.

- Related party transactions to be disclosed in the Director's Report along with justification thereof

Inter corporate loans / investments

- Loans, guarantee and security made to any person (the 1956 Act dealt only with body corporate) will attract the 2013 Act compliance requirement

- Rate of interest on loan granted cannot be lower than the prevailing yield of 1 year, 3 year, 5 year or 10 year Government Security closest to the tenure of the loan

- The list of exemptions has been curtailed

Loan to Directors

- No company shall directly or indirectly advance any loan (including loan represented by a book debt) or give guarantee or provide security in connection with such loan to any director / related persons – An exception to the above rule is made for MD or a whole time director (WTD) if such loan is in accordance with the terms of services extended to all employees or is approved by shareholders by special resolution

- Provisions for loan to directors applicable to private Companies

Charge Matters:

- ☐ The duty of filing of particulars of creation, modification or satisfaction of charge will be of the Company.

- ☐ Time limit for filing of particulars of creation of charge has been increased to 300 days upon application being made to Registrar, the Registrar may allow filing of particulars of creation or modification of charge up to 300 days upon payment of additional fees

- ☐ After 300 days the Order of Central Government extending the time for filing of particulars of creation or modification of charge, will be required.

- ☐ If company fails to register a charge, the charge holder has a right to register the charge by applying to Registrar.

- ☐ Punishment for contravention:

    - For Company = fine not less than Rs 1 Lakh but may extend to Rs 10 Lakhs

    - Every officer in default may face imprisonment which may extend to 6 months Or Fine not less than Rs 25 Thousand but may extend to Rs 1 Lakh or both.

Mergers & Acquisitions

- Restriction placed on multi-layer investment subsidiaries

- Merger of Indian company with a foreign company allowed

- Fast track merger for small companies and between holding company and its wholly owned subsidiary introduced

- Person / group of persons holding 90 per cent or more equity shares by virtue of amalgamation etc. can purchase the remaining equity shares of the company from minority shareholders

- Any valuation of shares / assets etc. required under 2013 Act to be performed by a Registered Valuer

Measures for investor protection

- Provisions relating class action suits introduced

- Exit options for minority holders on reorganization

National Company Law Tribunal (NCLT)

2013 Act replaces the High Court with a Tribunal to be known as National Company Law Tribunal, which will consists of Judicial and Technical members, as Central Government may deem necessary, to exercise and discharge the powers and functions conferred including approval of merger, corporate reorganization, capital reduction, extension of financial year etc.

Miscellaneous

- Mandatory transfer of profits to reserves for dividend declaration dispensed

- Inability to pay debts will be considered as criteria for determining a sick company

- Provisions of revival and rehabilitation of sick companies to apply to all companies and not only to an "industrial company"

- Central Government to establish Serious Fraud Investigation Office for investigation of frauds relating to a company

- Any person representing the company is made liable for punishment for fraudulently obtaining credit facilities from any bank or financial institutions for making any false, deceptive or misleading statement, promise or forecast

Corporate Law

CIRCULAR / NOTIFICATION

USE OF WORD 'NATIONAL' IN THE NAMES OF COMPANIES OR LIMITED LIABILITY PARTNERSHIPS (LLPS)

The MCA has directed that no company should be allowed to be registered with the word 'National' as part of its title unless it is a government company and the Central/State government(s) has a stake in it. Similarly, the word 'Bank' may be allowed in the name of an entity only when such entity produces a 'No Objection Certificate' from the RBI in this regard. By the same analogy the word "stock Exchange" or "Exchange" should be allowed in name of a company only where 'No Objection Certificate' from SEBI in this regard is produced by the promoters.

[MCA General Circular No. 02/ 2014, dated 11-2-2014]

Clarification with regard to Section 185 of the Companies Act, 2013

Section 372A of the Companies Act, 1956 specifically exempts any loans made, any guarantee given or security provided or any investment made by a holding company to its wholly owned subsidiary. Whereas, Section 185 of the Act prohibits guarantee given or any security provided by a holding company in respect of any loan taken by its subsidiary company except in ordinary course of business. In order to maintain harmony with regard to applicability of Section 372A and Section 185, the MCA has clarified that any guarantee given or security provided by a holding company in respect of loans made by a bank or financial institution to its subsidiary company, exemption as provided in clause (d) of sub section (8) of Section 372A shall be applicable till Section 186 of the Act is notified. This clarification shall be applicable only in cases where the loans so obtained are utilised for the principal business activities.

[MCA General Circular No. 03/ 2014, dated 14-2-2014]

Clarification with regard to Section 180 of the Companies Act, 2013

MCA had received many representations regarding various difficulties arising out of implementation of section 180 of the Companies Act, 2013 with reference to borrowings and/or creation of security, based on the basis of ordinary resolution. After examination of the matter, the Ministry clarified that the resolution passed under section 293 of the Companies Act, 1956 prior to 12/9/2013 with reference to borrowings (subject to the limits prescribed) and / or creation of security on assets of the company will be regarded as sufficient compliance of the requirements of section 180 of the Companies Act, 2013 for a period of one year from the date of notification of section 180 of the Act. Therefore a relief has been granted to the companies to comply with the requirements.

[MCA General Circular No. 04/ 2014, dated 25-3-2014]

Commencement of provisions of Companies Act, 2013 w.r.t maintenance of books of accounts, etc.

A number of provisions of the Companies Act, 2013 including those relating to maintenance of books of account, preparation, adoption & filing of financial statements (and documents required to be attached thereto), Auditors reports and the Board of Directors report (Board's report) have been brought into force with effect from 1st April, 2014. MCA had received numerous requests for clarification w.r.t the financial year from which these provisions will be effective. The MCA has clarified that the financial statements (and documents required to be attached thereto), auditor's report and Board's report in respect of financial years that commenced earlier than 1st April, 2014 shall be governed by the relevant provisions/ Schedules/ rules of the Companies Act, 1956 and that in respect of financial years commencing on or after 1st April, 2014, the provisions of the new Act shall apply. Therefore for the financial statements of F.Y. 2013-14 or calendar year 2014, the provisions of Companies Act 1956 will continue to apply.

Availability of E-forms on MCA portal and Table of fees for various forms to be filed with ROC

MCA has clarified that instead of staggered roll out of e-forms as notified earlier; there would be a single roll out for all e-forms. Accordingly, it is clarified that all E-forms will be available for upload with effect from 28th April, 2014. A schedule showing the mapping of e-forms under Companies Act, 2013 with the corresponding e-forms under Companies Act, 1956 is also provided and the same is available at the link: http://www.mca.gov.in/Ministry/pdf/eformsMapping.pdf.

MCA has also released a schedule of fees applicable for filing of various forms with the ROC pursuant to Rule 12 of the Companies (Registration of Offices and Fees) Rules, 2014. The schedule can be referred to at the link: http://www.mca.gov.in/Ministry/pdf/tableoffee_01042014.pdf.

Amendment of Schedule II of Companies Act, 2013

The MCA has amended Schedule II of the Companies Act, 2013 dealing with rates of depreciation. The amendment relates to rates of depreciation in respect of intangible assets (Toll Roads) created under Build, Own, Operate, Transfer or any other form of public private partnership route in case of toll roads. The actual amendment and the detailed methodology of amortization can be referred on the MCA website at the link: http://www.mca.gov.in/Ministry/pdf/Amendment_Schedule2.pdf.

[MCA General Circular No. 08/2014, dated 04-04-2014]

Certification of E-forms/non e-forms under the Companies Act, 2013 by the Practicing Professionals

Under the Companies Act, 2013, professionals i.e. members of ICAI, ICSI and ICOAI have been allowed to authenticate various e-forms required to be filed with ROC. MCA has clarified in this circular the manner in which instances of filing of documents, applications containing false or misleading information or omission of material fact etc. shall be handled.

[MCA General Circular No. 10/ 2014, dated 07-05-2014]

Applicability of PAN requirements for Foreign Nationals

MCA has clarified that the PAN details are mandatory only for those foreign nationals who are required to possess "PAN" in terms of provisions of the Income-tax Act, 1961 on the date of application for incorporation Where the intending Director who is a Foreign National is not required to compulsorily possess PAN, it will be sufficient for such a person to furnish his/her passport number, along with undertaking stating that provisions of mandatory applicability of PAN are not applicable to the person concerned.

[MCA General Circular No. 12/ 2014, dated 22-05-2014]

Clarification regarding maintaining register in new format u/s 186 (9)

MCA has clarified that registers maintained by Companies pursuant to 372A (5) of Companies Act, 1956 may continue as per requirement under these provisions and new format prescribed vide Form MBP2 shall be used for particulars entered in such registers on and from 1.4.2014.

[MCA General Circular No. 15/ 2014, dated 09-06-2014]

Applicability of PAN requirements for Foreign Nationals

In continuation of the General Circular No. 12/2014 dated 22.05.2014 regards the above subject, it is clarified that the provisions of the said Circular are applicable to a Foreign National who is a subscriber /promoter at the time of incorporation of the Company. In case said subscriber/promoter, does not possess Permanent Account Number (PAN), he/she shall furnish a declaration in the prescribed proforma, as an attachment to the Incorporation Form (INC – 7). Further, it is clarified that, in case of a Resident Director of the proposed company he/she shall be required to submit PAN details at the time of incorporation.

[MCA General Circular No. 16/ 2014, dated 10-06-2014]

Clarification for filing of form no INC- 27 for conversion of company from public to private under the provision of companies Act, 2013

The relevant section 14(2) (1) of Companies Act, 2013 have not be notified. In this view, Application for conversion from pubic company to private have to be filed and disposed as per section 31(2A) (1) of companies act, 1956 till the corresponding provision of Companies Act, 2013 are notified.

[MCA General Circular No. 18/ 2014, dated 11-06-2014]

Clarification on rules prescribed under companies act, 2013 – Matters relating to share capital and Debentures

In regards to Share Transfer Forms executed before 1st April 2014, MCA has clarified that since transaction relating to transfer of shares is a contract between two or more persons/shareholders, any share transfer form executed before and submitted to the company concerned within the period prescribed under relevant section of Companies Act, 1956 needs to be accepted by the companies for registration of transfers. In case any such shares transfer form, executed prior to 1st April 2014, is not submitted within the prescribed period under the companies Act 1956, the concerned company may get itself satisfied suitably with regard to justification of delay in submission etc. In case a company decides not to accept the share transfer form, it shall convey the reasons for such non- acceptance within time provided under section 56(4)(c) of the Act.

Also MCA has clarified that powers of the Board provided under rule 6(2)(a) of Companies (Share Capital and Debentures) Rules , 2014 with regard to issue of duplicate share certificates can be exercised by a Committee of Directors subject to any regulations imposed by the Board in this regard.

[MCA General Circular No. 19/ 2014, dated 12-06-2014]

Rule 3(5) of Companies (Declaration and Payment of Dividend) Rules, 2014

Above mentioned rule has been substituted and thus No company shall declare dividend unless carried over previous losses and depreciation not provided in previous year or years are set off against profit of the Company of the current year.

[MCA Notification 1/31/2013, dated 12-06-2014]

Clarification with regard to voting through electronic means

Section 108 of the Companies Act, 2013 read with rule 20 of the Companies (Management and Administration) Rules 2014 deal with the exercise of right to vote by members by electronic means (e-means). Due to practical difficulties in compliance with procedural requirement, the relevant provisions are not mandatory till 31st December 2014. The relevant notification in this regards is being issued separately.

[MCA General Circular No. 20/ 2014, dated 17-06-2014]

Clarification regarding filing of DPT4 Under Companies Act, 2013

MCA has grant extension of time for the period of 2 months i.e. up to 31/08/2014 without any additional fees for filing of form DPT4 under the provisions of the Companies Act, 2013. As per section 74(1)(a) of the Companies Act, 2013 and the Companies (Acceptance of Deposits) Rules 2014 made there under, Companies are required to file as statement regarding deposits existing as on date of commencement of the Act within a period of 3 months from such commencement.

[MCA General Circular No. 27/ 2014, dated 30-06-2014]

SEBI

Circular / Notification

SEBI (Issue of Capital and Disclosure Requirements) (Amendment) Regulations, 2014

SEBI has notified the aforesaid regulation w.e.f 4th February 2014 wherein certain amendments made in regulation 26, sub-regulation (7) stated that an issuer making an IPO may obtain grading for such offer from one or more credit rating agencies registered with the Board. The SEBI has also notified certain changes to the Illustrative format of Statement of Assets and Liabilities in sub-para (IX), clause (B), and sub-clause (9), item (f).

[SEBI Notification No. LAD-NRO/GN/2013-14/44/226, dated 04-02-2013]

Enhancing disclosures for mutual fund products, etc.

SEBI has framed a Long Term Policy for Mutual Funds in India which inter alia includes enhancing the reach of Mutual Fund products, promoting financial inclusion, tax treatment, obligation of various stakeholders, increasing transparency, etc. This policy issued as per the aforesaid circular would be applicable since 1st April, 2014. The circular includes requirements pertaining to disclosures of Assets Under Management, votes cast by Mutual Funds, financial inclusion, development of alternative distribution channels etc.

[SEBI Circular No. – CIR/IMD/DF/05/2014, dated 24-03-2013]

Format for Auditors' Certificate required under Clause 24(i) of the Equity Listing Agreement

Clause 24(i) of the Listing Agreement requires that the company, while filing for approval of any draft Scheme of amalgamation / merger / reconstruction, etc. with the stock exchange under Clause 24(f), shall also file an auditors' certificate to the effect that the accounting treatment contained in the scheme is in compliance with all the Accounting Standards specified by the Central Government. SEBI observed that there is no standardization in the format of the Auditor's Certificate. Therefore standard format for Auditors' Certificate is formalized and made applicable for companies.

[SEBI Circular No. – CIR/CFD/DIL/1/2014, dated 25-03-2013]

Corporate Governance in listed entities – Amendments to Clauses 35B and 49 of the Equity Listing Agreement

The Companies Act, 2013 was enacted on August 30, 2013 which provides for a major overhaul in the Corporate Governance norms for all companies. The rules pertaining to Corporate Governance were notified on March 27, 2014. In light of the stricter provisions of the Companies Act, 2013, SEBI has decided to review the provisions of the Listing Agreement in this regard with the objectives to align with the provisions of the Companies Act, 2013, adopt best practices on corporate governance and to make the corporate governance framework more effective.

[SEBI Circular No. – CIR/CFD/POLICY CELL/2/2014, dated 17-04-2013]

Issue of SEBI (Mutual Funds) (Amendment) Regulations, 2014.

SEBI has made certain changes to the SEBI (Mutual Funds) Regulations 1996 vide the aforesaid notification. The amendments mainly deal with investment by the sponsor or asset management company of not less than 1 per cent of the amount raised in the new fund offer or Rs 50 Lakh, whichever is less, in the growth option of the scheme and such investment shall not be redeemed unless the scheme is wound up.

[SEBI Notification No. – LAD-NRO/GN/2014-15/01, dated 06-05-2013]

INDIRECT TAX

CENTRAL EXCISE

NOTIFICATIONS:

Removal of Capital Goods

- Sub Rule 5A of Rule 3 of the Cenvat Credit Rules, 2004 has been amended to provide to provide the rates in case of Capital goods on which Cenvat credit has been taken are removed after being used, the manufacturer or provider of output services shall pay an amount equal to the CENVAT Credit taken on the said capital goods reduced by the percentage points calculated by straight line method as specified below for each quarter of a year or part thereof from the date of taking the CENVAT Credit, namely:-

    - for computers and computer peripherals:

Year	Rate (per cent) per quarter
1	10
2	8
3	5
4 and 5	1

    - for capital goods, other than computers and computer peripherals @ 2.5 per cent for each quarter.

  Provided that if the amount so calculated is less than the amount equal to the duty leviable on transaction value, the amount to be paid shall be equal to the duty leviable on transaction value.

- Further if the capital goods are cleared as waste and scrap, the manufacturer shall pay an amount equal to the duty leviable on transaction value.

[Notification NO. 12/2013-CE (NT)]

Threshold limit lowered to Rs 1 lakh during previous year w.e.f. 1 January 2014 for mandatory e-payment.

Rule 8(1) of the Central Excise Rules, 2002 had been amended w.e.f. from 1stJanuary, 2014, to reduce the threshold limit for e-payment of central excise to Rs1 Lakhs from existing limit of Rs 10 lakhs.

A similar amendment to the third proviso to Rule 6(2) of the Service Tax Rules has been made vide notification no. 16/2013-ST.

[Notification NO. 15/2013-CE (NT)]

Addition of Importer as category

- ☐ Vide above mentioned Notification the category of Importer is added under Rule 9(1) of Central Excise Rules, 2002 for the purpose of Registration. Thus the Registration criteria under Central Excise now also cover the category of Importer.
- ☐ With the inclusion of Importer category in the definition of First stage Dealer the first provison under Rule 11(7) has been omitted.
- ☐ The above amendment shall be effective from 1st day of March 2014.

[Notification NO. 17/2013-CE (NT)]

CIRCULARS:

Levy of Education Cess and the Secondary and Higher Education Cess on other cesses

It has been reiterated that the Education Cess and the Secondary and Higher Education Cess are not to be calculated on cesses which are levied under Acts administered by Department/Ministries other than Ministry of Finance (Department of Revenue) but are only collected by the Department of Revenue in terms of those Acts.

[Circular No.978/2/2014-CX]

Implementation of decision of Hon’ble Supreme Court in case of M/s Fiat India ltd

CBEC based on references received from trade and field formations seeking clarification on implementation of the Fiat judgment wherein the revenue could reject the transaction value declared under section 4 and invoke the provisions of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 to assess Central Excise duty have clarified on the following aspects:

- ☐ Transaction Value below manufacturing cost and profit

  The Hon’ble Supreme Court had cited two instances wherein a manufacturer may sell goods at a price lower than the cost of manufacture and profit and yet the declared value can be considered as normal price. These instances are when the company wants to switch over its business or where a manufacturer has goods which could not be sold within a reasonable time. The Hon’ble Court had further held that these examples are not exhaustive. Therefore, mere sale of goods below the manufacturing cost and profit should not be taken as the sole basis for rejecting the transaction value.

- ☐ Verification of payment of duty

  - Under the self-assessment procedure, there is a legal obligation on the assessee to correctly assess and pay the duty. During the audit by the central excise officers aspects such as the percentage of loss at which sale has taken place, the period for which such loss making price has prevailed, reasons for sale at such loss making price, whether such sales are contrary to the standard and accepted business practices, and whether such sale is leading to erosion of capital of the company, may be looked into.

- Calculations of manufacturing cost may be carried out using CAS-4 standards based on the information submitted by the manufacturer, duly certified by a Chartered or Cost Accountant should normally be accepted. Only where a decision to investigate a case has been taken at the level of the Commissioner and it is considered necessary in the interest of investigation, steps such as ordering Cost Audit of the Unit or summoning of the Costing data should be undertaken.

☐ Period of application

- On issue of whether invoking of the extended period of limitation can be applied for periods prior to the date of judgment, in a case where price is not the sole consideration for the sale, whether money value of any additional consideration flowing directly or indirectly from the buyer to the assessee is added to the transaction value, CBEC clarified that in cases where a show cause notice has been issued on the grounds of the FIAT judgment alone , there may not be a case for invoking the extended period of limitation . In such cases, only the normal period of limitation will apply.

- For the period after the date of the judgment, i.e. from 29/08/2012 onwards, if there is a sale in the circumstances similar to the case of M/s FIAT and yet transaction value of goods is declared as the correct assessable value, then such declaration would amount to wilful mis-statement of the assessable value.

  [Circular No. 979/03/2014-CX]

SERVICE TAX

NOTIFICATIONS:

Amendment in Abetment for Construction of Residential Flats

Notification 26/2012-ST has been amended and other conditions remaining same, 75 per cent abatement would be applicable for a residential unit in case of:–

- the carpet area of the unit is less than 2000 square feet; and

- the amount charged for the unit is less than Rs One Crore;

  [Notification NO. 09/2013]

Exemption on services provided to SEZ authorized operations

In supersession of Notification 40/2012-ST, a new set of procedures has been prescribed in order to claim exemption/ refund by SEZ w.e.f. 01/07/2013.

[Notification NO. 12/2013]

Amendment in Mega Exemption for services provided by Canteen

New entry 19A has been inserted wherein services provided in relation to serving of food or beverages by a canteen maintained in a factory covered under the Factories Act, 1948 (63 of 1948), having the facility of air-conditioning or central air-heating at any time during the year has been exempted from the purview of service tax.

[Notification NO. 14/2013]

Amendment to extend the scope of exemption of Sponsorship services

W. e. f. 1st January 2014, Entry No 11(a) of Mega Exemption Notification No. 25/2012-ST dated 20th June 2012 has been amended to extend the scope of exemption of sponsorship to those sporting events which are organized by national sports federation or its affiliated federations, where the participating teams or individuals represent not only any district, state or zone but also country.

[Notification NO. 01/2014]

Relaxation from service tax

Central Government hereby directs that the service tax payable on the services provided by an authorized person or sub-broker to the member of a recognized association or a registered association, in relation to a forward contract, shall not be required to be paid in respect of such taxable service on which the service tax was not being levied during the period of 10th September 2004 to 30th June 2012 in accordance with the said practice.

[Notification NO. 03/2014]

CIRCULARS:

Clarification regarding Education Services.

CBEC on representations received from various educational institutions has issued clarification regarding applicability of service tax on various issues raised by those institutions

Additionally under the said circular it has been clarified that hostels, housekeeping, security services, canteen, etc. would also be covered under the term 'auxiliary education services' provided to educational institutions in addition to other services as mentioned in the definition.

[Circular No 172/7/2013]

Clarification on Restaurant Services.

CBEC based on the representations received towards amendment made in restaurant service vide Notification 03/2013-ST have issued the following clarification:

- In a complex where both Air conditioned and Non air Conditioned restaurant are functioning which are clearly demarcated and separately named but the food is served from a single common kitchen, the service tax liability will be only on the service provided in the air conditioned restaurant while service provided in the non air-conditioned / non-centrally air-heated restaurant will be treated as exempted service and credit entitlement would be as per the Cenvat Credit Rules.

- Any service provided by hotel having air conditioned or centrally air heating services and providing restaurant services in other areas like swimming pool or an open area attached to the restaurant would be liable for service tax.

- Goods sold on MRP (fixed under the legal Metrology Act) would be excluded for the determination of value of service portion by the restaurants.

[Circular No 173/7/2013]

Circular No 175: Clarification regarding levy of service tax on services provided by a Resident Welfare Association (RWA) to its owner.

The above circular clarifies various issues related to the scope of exemption granted to Resident Welfare Associations under the negative list approach as provided under Entry No. 28(c) of Mega Exemption No 25/2012 dated 20th June 2012.

- If per month contribution of any member of RWA does not exceed Rs 5,000 the entire contribution of such member would be eligible for the exemption under the said notification.

- Threshold exemption limit of Rs 10 Lakhs under Notification No 33/2012-ST is applicable to RWA, subject to conditions prescribed in the notification. As per explanation B to the notification, the definition of “aggregate value does not include the value of services which are exempt from service tax.

- Where the payment for a electricity bill raised by an electricity transmission or distribution utility in the name of owner of apartment is collected and paid by the RWA to the utility, without charging any commission or a consideration on the same, the RWA is acting as a pure agent and hence exclusion from the value of taxable service would be available.

- However, in the case of electricity bills issued in the name of RWA, in respect of electricity consumed for common use of lifts, motor pumps for water supply, lights in common area, etc., since there is no agent involved in these transactions, hence the exclusions from the value of service tax will not be available.

- RWA may avail CENVAT Credit and use the same for payment of service tax, in accordance with the CENVAT Credit Rules.

[Circular No 173/7/2013]

CASE LAWS (INDIRECT TAX)

HIGH COURT DECISIONS

Cenvat credit on items used in fabrication and erection of various sections in existing plants - capital goods

UOI.Versus M/s. Hindustan Zinc Ltd. & Anr.[53][RAJ.]

- The Hon'ble Rajasthan High Court while deciding on the availment of Cenvat credit on items such as M.S. Plate, SS Plate, Beams, Hr Coils, plain Plates, Channels, Angles Joist etc, used in fabrication and erection of various sections in existing plants, which are capital goods, held that such goods which are necessary for running of plant and upkeeping of the machinery directly involved in the manufacturing and products were held to be eligible to avail Modvat credit, relying on the decision of Union of India vs. Aditya Cement.

CENVAT credit on stockbroker's service

United Telecoms Ltd. Vs CCE., BANGALORE-I[54] [KAR.]

- The Karnataka High Court while deciding on the eligibility of availing CENVAT credit on stockbroker's service used for the purpose of disposal of the shares held in another company held that, on a perusal of the main objects and objects incidental or ancillary to the attainment of main objects of the appellant, it is not that the assessee is carrying only the main objects and not the incidental objects as in sub-para 8 of Part B. The questions whether the incidental objects of investing and dealing in shares would in any way relate to and form part of the main business of the assessee has been answered by the authorities in the negative. The court further observed that the fact remains that the incidental business which finds mention in para 8 is not being actually carried on and a categorical finding is given by all the authorities in that regard. Therefore, the court opined that the claim for input service credit is not against any liability arising out of the business activity of the assessee and not relatable to the business activity of the assessee and therefore, they found that there is no scope for interfering with the order of the Tribunal.

---

[53] [2013 (6) TMI 144 – RAJ. HC]
[54] [2014 (5) TMI 218 – Kar. HC]

CESTAT

CENVAT Credit on duty paying documents

CASTROL (I) LTD vs. CCE, RAIGAD[55] [MUM.]

- Hon'ble Tribunal while deciding on the issue of whether the appellant is entitled to the credit availed on the ground that the registration number of the service provider was not indicated on the invoices held that it is the fact on record that during the adjudication proceedings, the appellant had provided to the department, registration number of the service providers. Therefore, the adjudicating authority could have easily verified whether these service providers were registered with the department at the relevant time and whether they had discharged the service tax liability in accordance with the law instead of raising the level of litigation by denying the credit as if it was Tribunal's job to get verification done and the matter was remanded back to the adjudicating authority for verification of the registration numbers declared by the appellant in respect of the service providers and also for verifying whether the service tax indicated in the invoices was paid to the exchequer or not.

CENVAT credit of Service Tax paid for premises taken on rent for job worker

M/s New Allenberry Works Vs CCE, Delhi-IV[56] [DEL.]

- Hon'ble Tribunal while deciding the case on the eligibility of Cenvat credit towards Service Tax paid for premises taken on rent for job worker can be considered to be an input service held that the expression 'in relation to business' as appearing under the definition of 'input service' cannot be extended to such an extent so as to include the activities at the end of an independent person. While deciding the case the court held that if the activities at the job worker's end are considered to be activities related to the appellants business, there would be no end to the stretching of the said expression and the links in the chain would keep on increasing and hence the said credit cannot be considered to be an input service.

- Further the Hon'ble Tribunal also held that as the appellant was reflecting the credits taken in their statutory records as also seen in the returns filed with the department, the issue involved is also a bona fide dispute on interpretation of law and does not involve any clandestine activities and, therefore, no suppression, misstatement or mala fide intention can be attributed to the appellant so as to justifiably invoke longer period of limitation and penalty.

Goods Transport Agency Service - Availment of CENVAT Credit

Rucha Engineers P Ltd vs CCE[57] [MUM.]

- While deciding on the availment of CENVAT Credit on Goods Transport Agency Service, the Hon'ble Tribunal held it is immaterial who has paid the service tax. The court observed that the lower authorities have failed to appreciate the fact that the service has suffered service tax and any payment towards duty or service is entitled for input service credit/input credit. Therefore, the finding of the lower authorities that in the case of Goods Transport Agency Service, service tax is required to be paid by the service recipient only is not tenable.

---

[55] [2014 (7) TMI 70 - CESTAT MUM.]

[56] [2014-TIOL-732-CESTAT-DEL]

[57] [2014 (1) TMI 1566 - CESTAT MUM.]

OVERVIEW OF ECONOMIC SURVEY

In the Financial Year 2013-2014, the Indian economy registered a 5 per cent growth. The GDP growth in the Financial Year 2014-15 is projected to remain under 6 per cent. Economic growth during financial Year 2013-2014 was due to agriculture on account of favourable monsoon. Sustained economic growth can be ensured if issues like structural constraints due to low manufacturing base, delay in project approvals and insufficient complementary investments, agricultural production's high dependence on the monsoon and high food inflation are tackled.

The services sector accounted for about 60 per cent of GDP in Financial Year 2013-2014 and it grew at 6.8 per cent, as compared to about 7 per cent in Financial Year 2012-13 due to less growth in transportation and communication. There is a high growth recorded in the financial services and real estate sectors. Industry was the worst performing sector with a meager growth of 0.4 per cent, as compared to about 1 per cent in the earlier year. This was on account of contraction in manufacturing, partially due to less investment, considering high interest costs. Mining is a challenge due to stagnation in crude petroleum and coal, partially due to regulatory issues. Inflation eased, industrial production was dismal due to a contractionary monetary policy. The easing of the Wholesale Price Index (WPI) based inflation to 6 per cent in Financial Year 2013-2014, as compared to 7.4 per cent in Financial Year 2012-13, partially contributed to improved economic growth in the Financial Year. Increased food prices continue upside risks. High interest rates and tight liquidity, more than 6 per cent inflation, affected business sentiment and political uncertainty prior to the general elections affected investment. Consumption was low on account of reduction in government spending.

Slow recovery, uncertainty over the next government in India (prior to the 2014 general elections) and expectations on the withdrawal of quantitative easing in the U.S. resulted in volatility in Foreign Institutional investor inflow and domestic currency. Improved net exports growth led to the narrowing of trade and Current Account Deficit**.** Trade deficit narrowed due to RBI restrictions and a depreciated rupee though exports were high due to improved global demand and imports were reduced. The pace of economic recovery during Financial Year 2015-2016 is expected to be better than the pace during Financial Year 2014-2015 which will depend on various factors with the performance of agriculture and industry, inflation rate and policy support being of critical importance. The Economic Survey of India, 2013–2014, gives a few priority areas for the Government of India such as reviving investments, strengthening macro-economic stability, creating non-agricultural jobs, and developing infrastructure and agriculture.

Fiscal deficit of 4.5 per cent of GDP in Financial Year 2014-2015 is lower than the budgeted target of 4.8 per cent of GDP. The Government of India announced a fiscal consolidation roadmap that aims to reduce India's fiscal deficit to 4.8 per cent in Financial Year 2014-2015, 4.2 per cent in Financial Year 2015-2016, 3.6 per cent in Financial Year 2016-2017 and to 3 per cent by Financial Year 2017-2018. To comply with this, the government has reduced its allocation of expenditure for the Financial Year 2014-2015, which would translate into lower fiscal deficit for the year.

KEY BUDGET PROPOSALS

INCOME TAX RATES

PERSONAL TAX

The proposals in the Finance Bill shall become applicable from Assessment year 2015 -2016 (i.e. the financial year to end on March 31, 2015), unless otherwise specifically stated.

Tax Slab

There is change in the tax slabs of Personal Income Tax for the A.Y. 2015-16.

Income Tax Rates are tabulated below:

Individuals (including women assessee below the age of 60 years), Hindu Undivided Family, Association of Persons, Body of Individuals, Artificial Judicial Person

Income	Existing Rates (%)			Proposed Rates (%)		
	Tax	Education Cess	Total	Tax	Education Cess	Total
Rs. NIL to Rs. 2,00,000						
Rs. 200,001 to Rs. 2,50,000	10	0.30	10.30	-	-	-
Rs.2,50,001 to Rs.5,00,000	10	0.30	10.30	10	0.30	10.30
Rs.5,00,001 to Rs.10,00,000	20	0.60	20.60	20	0.60	20.60
Rs. 10,00,001 and above	30	0.90	30.90	30	0.90	30.90

- In the case of a resident individual of the age of sixty years or above but less than eighty years, the basic exemption limit has changed to Rs. 3,00,000/-. For income upto Rs. 5,00,000 tax @ 10 per cent shall be applicable.
- In the case of a resident individual of the age of eighty years or above, the basic exemption limit remains same i.e. Rs. 5,00,000/-. For income upto Rs 10,00,000 tax @ 20 per cent shall be applicable.
- In case of individuals whose total income exceeds one crore rupees, the amount of income-tax shall be increased by a surcharge at the rate of ten percent of such income-tax.

CO-OPERATIVE SOCIETIES

Income	Tax Rates
Up to Rs. 10,000	10 percent
Rs. 10,001 to 20,000	20 percent
Rs. 20,001 and above	30 percent

The amount of income-tax shall be increased by a surcharge at the rate of ten percent of such income-tax in case of a co-operative society having a total income exceeding one crore rupees.

LOCAL AUTHORITIES

Local Authorities are taxable at the rate of 30 per cent.

PARTNERSHIP FIRMS

Partnership Firms are taxable at the rate of 30 per cent.

COMPANIES

In the Case of Domestic Companies:

The tax rate continues to remain same as prevailing for A.Y. 2014-2015 i.e. @ 30 percent.

The existing surcharge of five per cent shall continue to be levied if the total income of the domestic company exceeds one crore rupees but does not exceed ten crore rupees.

The surcharge at the rate of ten percent shall continue to be levied if the total income of the exceeds ten crore rupees.

In the Case of Foreign Companies:

The existing surcharge of two per cent shall continue to be levied if the total income exceeds one crore rupees but does not exceed ten crore rupees.

The surcharge at the rate of five percent shall continue to be levied if the total income exceeds ten crore rupees.

Education Cess:

There is no change to the rate of Education Cess. It continues to remain the same @3 percent.

FOREIGN POLICY ANNOUNCEMENTS

- Foreign Exchange Regulations

The applicable cap/ restriction on Foreign Direct Investment (F.D.I.) in few key identifiable sectors were proposed to be further liberalized

Sector	Liberalization
Defence	Increased from 26 percent to 49 percent through FIPB route with full management and control.
Insurance	Increased from 26 percent to 49 percent through FIPB route with full management and control.
Manufacturing companies	Allowed to sell its product through retail including e-commerce
Real Estate	Requirement of minimum built up area of capital conditions is reduced from 50,000sq. mt. to 20,000sq. mt. Investment reduced from USD 10 million to USD 5 million with 3 year post completion lock in. Projects which expend minimum 30 per cent in low cost affordable houses will be exempted from minimum built up area with condition of 3 year post completion lock in.

- Real Estate Investment Trust (REIT) & Infrastructure Investment Trusts (InvITs)

Real Estate Investment Trusts (REIT) have been successfully used as instruments for pooling of investment in several countries. Taking cue from the same, Government of India has announced the intention to introduce the same for Indian Markets.

REIT would be given a tax pass-through status to avoid double taxation. A 'pass-through' status means that the income generated would be taxed in the hands of the investor, and that the fund itself would not have to pay taxes on the same.

A modified REIT type structure for infrastructure projects has also been announced as Infrastructure Investment Trusts (InvITs), which would have a similar tax efficient pass through status, for PPP and other infrastructure projects. These two instruments would be a lucrative investment option for foreign investors including the NRIs.

- Foreign Portfolio Investors (FPIs)

In an attempt to boost confidence of FPIs & bring about desired tax certainty, several amendments have been introduced in the finance bill to provide clarity on the characterization of income of FPI from portfolio investments in Indian stock market. Foreign Portfolio Investors (FPIs) have currently invested more than Rs 8 Lakh crore (about 130 billion USD) in India.

DIRECT TAX PROPOSALS

DOMESTIC TAXATION

Section 44AE - Presumptive Taxation for business of heavy vehicles

Section 44AE provides for presumptive basis of taxation for person's engaged in the business of plying, hiring or leasing of goods carriage. The section provided different presumptive rates for the two categories of goods carriage namely heavy vehicles and other than heavy vehicles.

It is now proposed to amend the definition of the term "goods carriage" to mean all goods carriage as defined in section 2 of the Motor Vehicles Act, 1988. Further, the presumptive rate has been changed to Rs. 7500 per month per vehicle for all types of goods carriage. These provisions shall become effective from 1st April, 2015.

Section 116 – Additions in Income Tax Authority

It is proposed to amend section 116 to introduce new positions under the category of Income Tax Authority. Accordingly, clause (aa) has been inserted after clause (a) to introduce Principal Directors General of Income Tax or Principal Chief Commissioners of Income-tax, and another clause (ba) after clause (b) to introduce Principal Directors of Income-tax or Principal Commissioners of Income-tax. Further for the purpose of appointment of additional income tax authorities as defined under section 116 of the Act, appropriate amendments shall be made to section 117 of the Act. This amendment is brought retrospectively with effect from 1st June, 2013.

Further, following amendments have been made under various clauses of section 2 of the Act to define various income tax authorities:

Section	Amendment	Terms	Definition
2 (15A)	Substituted	"Chief Commissioner"	means a person appointed to be a Chief Commissioner of Income-tax or a Principal Chief Commissioner of Income-tax under sub-section (1) of section 117
2(16)	Substituted	"Commissioner"	means a person appointed to be a Commissioner of Income-tax or a Director of Income Tax or a Principal Director of Income-tax under sub-section (1) of section 117
2(21)	Substituted	"Director General or Director"	means a person appointed to be a Director General of Income-tax or a Principal Director General of Income-tax or, as the case may be, a Director of Income-tax or a Principal Director of Income-tax, under sub-section (1) of section 117, and includes a person appointed under that sub-section to be an Additional Director of Income-tax or a Joint Director of Income-tax or an Assistant Director or Deputy Director of Income-tax.
2(34A)	Newly inserted	"Principal Chief Commissioner of Income-tax"	means a person appointed to be a Principal Chief Commissioner of Income-tax under sub-section (1) of section 117;

Section	Amendment	Terms	Definition
2(34B)	Newly inserted	"Principal Commissioner of Income-tax"	means a person appointed to be a Principal Commissioner of Income-tax under sub-section (1) of section 117;
2(34C) -	Newly inserted	"Principal Director of Income-tax"	means a person appointed to be a Principal Director of Income-tax under sub-section (1) of section 117;
2(34D)	Newly inserted	"Principal Director General of Income-tax"	means a person appointed to be a Principal Director General of Income-tax under sub-section (1) of section 117;

TRANSFER PRICING

Section 92B - Rationalization of meaning of Deemed International transaction

Sub-section (2) of the Section 92B extends the scope of the definition of international transaction by providing that a transaction entered into with an unrelated person shall be deemed to be a transaction with an associated enterprise, if there exists a prior agreement in relation to the transaction between such other person and the associated enterprise, or the terms of the relevant transaction are determined in substance between the other person and the associated enterprise.

The sub-section as presently worded has led to a doubt that if the person determining the terms or having prior agreement is resident then whether it amounts to International transaction or not. In light of the ambiguity on interpretation, it is now proposed to clarify that irrespective of whether such other person is resident or not the said transaction will amount to international transactions, if such other person has prior agreement with associated enterprise or relevant terms of agreement between an enterprise and such other person are determined by associated enterprise. Accordingly, sub-section 2 of section 92B shall be amended with effect from 1st April 2015.

Section 92CC - Applicability of Advance Pricing Agreement ('APA') for past 4 years (Roll-back)

The existing section 92CC of the Act provides that APA for determining the Arm's Length Price (ALP) or specifying the manner, in which ALP is to be determined in relation to an international transaction, can be entered between the assessee and the CBDT for the subsequent period of 5 years.

It is now proposed to amend section 92CC of the Act by insertion of clause (9A) after clause (9) to give effect to the APA entered into by the assessee with CBDT for preceding 4 years. This amendment shall be effective from 1st October 2014. It has been stated that such a roll-back will be subject to the prescribed conditions, procedure and manner and thus, it implies that the relevant Rules will be issued in this respect.

This amendment is seen positive move by the government to align the Indian APA practices in line with that of various other countries and to reduce the large scale litigation which is currently pending or may arise in further matters.

Section 271G - Transfer Pricing Officer ('TPO') can now levy penalty for failure to furnish information or documentation

Existing provisions of Section 271G authorizes Assessing officer and Commissioner (Appeals) to levy penalty of 2%

of the value of international transactions, if any person fails to furnish the information or documents to be maintained as prescribed under Rule 10D read with Section 92D of the Act. It is now proposed to widen the power of application of penalty by enabling Transfer Pricing Officer to levy the said penalty under section 271G on the assessee for failure to furnish information and documents. This amendment shall be effective from 1st October 2014.

Section 115-O Dividend Distribution Tax

Under the existing provisions of section 115-O of the Act, dividend distribution tax is payable at the rate of 15% on the amounts paid as dividend after reduction of distribution tax by the company. Thus, the tax is computed with reference to the net amount.

It is proposed to amend section 115-O by insertion of sub section (1B) below explanation to sub-section (1A), to provide that for the purposes of determining the tax on distributed profits payable in accordance with the said section, amount of distributable income which are actually received by the shareholders of the domestic company shall be grossed up by applicable rate specified in sub-section (1).

For the sake of better understanding, the aforesaid amendment is explained by way of example as under:

Particulars	Reference	Amount Rs.
Amount of Dividend distributed		85
Increased by amount of tax	[(85*0.15)/(1-0.15)]	15
Amount on which DDT computed	(85 + 15)	100
DDT @ 15% on aforesaid	(100* 15 %)	15
Tax payable under section 115 –O		15
Dividend distributed to shareholders	(100-15)	85

The aforesaid amendment is proposed with a view to ensure that tax is levied on proper base and shall be effective from 1st October, 2014.

Similarly, it is also proposed to amend section 115R to provide effect of grossing up on the income distributed by the Mutual Funds with effect from 1stOctober, 2014.

Long-term Capital Gains on debt oriented Mutual Fund and its qualification as Short-term capital asset

Under the existing provisions of clause (42A) of section 2 of the Act, in the case of a share held in a company or any other security listed in a recognized stock exchange in India or a unit of the Unit Trust of India or a unit of a Mutual Fund or a zero coupon bond, the period of holding for qualifying it as short-term capital asset is not more than twelve months.

It is proposed to amend the aforesaid clause so as to provide that an unlisted security and a unit of a mutual fund (other than an equity oriented mutual fund) shall be a short-term capital asset if it is held for not more than thirty-six months.

The amendment will be effective from 1st April, 2015 and will accordingly apply, in relation to the assessment year

2015-16 and subsequent assessment years.

Section 153C - Assessment of income of a person other than the person who has been searched

Under the existing provisions of section 153C of the Act, if the Assessing Officer is satisfied that any money, bullion, jewellery or other valuable article or thing or books of account or documents seized or requisitioned belongs or belong to any person, other than the person referred to in section 153A, then books of account or documents or assets seized or requisitioned shall be handed over to the Assessing Officer having jurisdiction over such other person and that Assessing Officer shall proceed against each such other person and issue such other person notice and assess or reassess income of such other person in accordance with the provisions of section 153A.

It is proposed to insert a condition for such an act of the assessing officer. He can do so if he is satisfied that the books of account or documents or assets seized or requisitioned have a bearing on the determination of the total income of such other person for the relevant assessment year or years referred to in sub-section (1) of section 153A.The amendment will be effective from 1st October, 2014.

Section 12A: Applicability of the registration granted to a trust or institution to earlier years

The provisions of section 12A(2) provides exemption under section 11 and 12 of the Act to a trust/institution prospectively i.e. from the assessment year immediately following the financial year in which application for registration under section 12AA is made.

It is proposed to amend section 12A(2) to provide the following:

- Exemption under section 11 and 12 for any earlier assessment year which is pending before the assessing officer as on the date of registration under section 12AA, if the objects and activities of the trust/institution are the same as those on the basis of which such registration has been granted.

- No action for reopening of an assessment of trust/institution under section 147 shall be taken by the assessing officer for any assessment year preceeding the first assessment year for which registration applies, merely for the reason that registration under section 12AA was not obtained for that assessment year.

- Both the aforesaid benefits would not be available if at anytime the Trust/institution had applied for registration and the same was refused under section 12AA or such registration was cancelled.

This amendment shall be effective from 1st October 2014,

Section 115BBC - Anonymous donations under

The provision of section 115BBC provides an aggregation mechanism for levy of tax on certain assessee being university, hospital, charitable organization etc. receiving anonymous donations. The income tax payable in such cases was aggregate of-

(i) Tax calculated at 30% on the aggregate anonymous donations received in excess of higher of-

A. 5% of total donations received or

B. one lakh rupees

(ii) Tax with which assessee would have been chargeable had his total income been reduced ***by the aggregate of anonymous donations received***.

W.e.f. 1st April, 2015 (Assessment year 2015-16), it is proposed to amend the aforesaid mechanism in respect of (ii) above to be the amount of income tax which would have been chargeable had his total income been reduced ***by the amount which is taxed at the rate of 30% in (i) above***.

Section 10(23C): Rationalization of taxation regime in case of charitable trust, institutions

It is proposed to insert sub-section 6 to section 11 and an explanation to section 10(23C) to provide that income required to be applied/accumulated or set apart for application shall be determined without any deduction /allowance by way of depreciation in respect of any asset, acquisition of which has been claimed as an application under these sections in same or any previous year. This amendment shall become effective from 1st April, 2015 i.e. Assessment year 2015-16.

It is further proposed to insert sub-section 7 to section 11 to provide that where a trust/institution has been granted registration for exemption under section 11 and such registration is in force for a previous year, then such trust/ institution would not be entitled to claim any exemption under section 10[other than 10(1) and 10(23C)]. This amendment shall become effective from 1st April, 2015 i.e. Assessment year 2015-16.

Similarly, entities which have been approved/notified for claiming exemption under section 10(23C) would not be entitled to claim exemption under other provisions of section 10[other than 10(1)]

Section 10(23C) provides exemption to certain educational institutions, universities and hospitals, subject to various conditions, which exist solely for education/philanthropic purposes but not for purposes of profit and which are wholly or substantially financed by the Government. It is proposed to insert an explanation to clarify that if the government grant received by such assessee during relevant previous year exceeds a percentage (which is yet to be prescribed) of the total receipts (including voluntary contributions) then such assessee shall be constituted as being substantially financed by the Government for that previous year. This amendment shall become effective from 1st April, 2015 i.e. Assessment year 2015-16.

Section 12AA: Cancellation of registration of trust/institution in certain cases

It is proposed to amend section 12AA to provide that where a trust /institution has been granted registration under section 12A and subsequently it is noticed that activities of the trust/institution are being carried out in a manner that provisions of section 11 and 12 do not apply then the Principal commissioner may by an order in writing cancel the registration to such trust/institution, if such trust /institution does not prove that there was a reasonable cause for the activities carried out in such manner. This amendment shall become effective from 1stOctober, 2014.

Section 220: Interest payable by the assessee

It is proposed to insert Sub-section (1A) in section 220 to provide that where any appeal is filed or initiated in respect of the any notice of demand served upon an assessee then the amount specified in the notice shall be deemed to be valid till the disposal of the appeal or any proceedings and any such notice shall have the effect as specified in section 3 of the Taxation Laws (Continuation and Validation of Recovery Proceedings) Act,1964. This amendment shall become effective from the 1stOctober, 2014

It is proposed to insert sub-section (2)in section 220 to provide that where as a result of an order under sections

specified in the first proviso, the amount on which interest was payable had been reduced and subsequently as a result of an order, the amount on which interest was payable is increased, the assessee shall be liable to pay interest on the amount payable as a result of such order from the day immediately following the end of the period mentioned in the first notice of demand referred to in sub section (1) of the said section and ending with the day on which the amount is paid. This amendment shall become effective from the 1st October, 2014

Section 285BA: Obligation to furnish statement of Information

It is proposed to amend section 285BA of the Act which provide for filing of an annual information return by specified persons in respect of specified financial transactions which are registered or recorded by them and which are relevant and required for the purposes of the Act. It is proposed to provide that where any person furnishing a statement of information under sub-section (1), or in pursuance of a notice issued under sub-section (5), comes to know or discovers any inaccuracy in the information provided in the statement, then, he shall, within ten days, inform the relevant authority about the inaccuracy in such statement and furnish the correct information in the manner as may be prescribed.

It is also proposed that the Central Government may specify- (a) the persons referred to in sub-section (1) of section 285BA to be registered with the prescribed income-tax authority; (b) the nature of information and the manner in which such information shall be maintained and (c) the due diligence to be carried for the purpose of identification of any reportable account referred to in sub-section (1) of section 285BA.

Correspondingly, It is also proposed to insert a new section 271FAA so as to provide that if a person who is required to furnish a "statement of financial transaction or reportable account", provides inaccurate information in the statement due to (a) failure to comply with the due diligence or deliberately or (b) the person knows of the inaccuracy at the time of furnishing the statement, but does not inform the prescribed income-tax authority (c) the person discovers the inaccuracy after the statement is furnished and fails to inform and furnish correct information within the time specified then, the prescribed income-tax authority may levy a penalty of sum of fifty thousand rupees.

These amendments will effective from 1st April, 2015.

Section 133A: Power of Survey

Section 133A of the Act enables the Income-tax authority to enter any premises in which business or profession is carried out for the purposes of survey. An income-tax authority may impound and retain in his custody any books of account or documents inspected by him during the course of survey.

It is proposed to insert a new sub section (2A) to section 133A to provide that an income-tax authority may for the purpose of verifying TDS enter any office, or a place where business or profession is carried on, within the limits of the area assigned to him, or any such place in respect of which he is authorized.

It has been further provided to alter the number of days for which the Income tax authority can retain the books of account or document under proviso to sub section (3) to section 133A up to 15 days. This amendment shall be effective from 1st October, 2014.

Section 133C: Inquiry by prescribed income-tax authority

It is proposed to insert a new section 133C in the Act for the purpose of verification of information in possession of an income tax authority relating to any person and issue a notice to such person requiring him, on or before a date to be therein specified, to furnish information or documents, verified in the manner specified therein which may be useful for, or relevant to, any enquiry or proceeding under this Act.This amendment shall be effective from 1st October, 2014.

Mutual Funds, Securitisation Trusts and Venture Capital Companies or Venture Capital Funds to file return of income

Clause (23D) of section 10 exempts the income of a Mutual Fund; clause (23DA) of section 10 exempts the income of a securitisation trust from the activity of securitisation; and clause (23FB) of section 10 exempts the income of a venture capital company (VCC) or venture capital fund (VCF) from investment in a venture capital undertaking.

Under the current scenario, these entities/funds are not obligated to furnish their return of income under section 139 of the Act instead they were required to furnish a statement giving details of the nature of the income paid or credited during the previous year and such other relevant details as may be prescribed.

It is now proposed that if the total income in respect of which fund, trust or company is assessable, without giving effect to the provisions of section 10, exceeds the maximum amount which is not chargeable to income-tax, shall furnish a return of such income of the previous year as if it were a return required to be furnished under sub-section (1) of section 139. Further, requirement of filing of statements before an income-tax authority is proposed to be dispensed with by omitting sub-section (3A) of section 115R and sub-section (3) of section 115TA.

This amendment shall become effective from 1stApril, 2015.

Section 32AC: Investment Allowance to a Manufacturing Company

By Finance Act, 2013, new section 32AC was inserted w.e.f 1st April, 2014 (Assessment year 2014-15) for the assessee company engaged in the business of manufacture of an article or things and invests a sum exceeds Rs.100 crore in new assets during the period beginning from 1stApril, 2013 and ending on 31stMarch, 2015, then the assessee can claim a deduction of 15% of cost of new assets acquired and installed for assessment year 2014-15 and 2015-16.

It is proposed to insert new sub-section (1A) to section 32AC w.e.f 1stApril, 2015 (Assessment year 2015-16) to provide a deduction of 15% of new assets acquired and installed during the previous year, to the assessee company engaged in the business of manufacture or production of any article or things and invests a sum exceeds Rs. 25 crore in new assets during that previous year. However, it is also proposed that no deduction under sub-section (1A) shall be allowed for the assessment year 2015-16 to the assessee, which is eligible to claim deduction under sub-section (1) for the said assessment year.

It is also proposed that the assessee who is eligible to claim deduction under the existing combined threshold limit of Rs.100 crore for investment made in previous years 2013-14 and 2014-15 shall continue to be eligible to claim deduction under the existing provisions contained in sub-section (1) of section 32AC even if its investment in the year 2014-15 is below the proposed new threshold limit of investment of Rs. 25 crore during the previous year. However, no deduction under sub-section (1A) shall be allowed for any assessment year commencing on or after the 1st April, 2018 (Assessment year 2018-19).

Extension of sunset date for tax holiday for power sector

It is proposed to amend section 80-IA (4) (iv) to extend the terminal date for a further period of three year, i.e., up to 31st March, 2017. The aforesaid amendment will take effect from 1st April, 2015 (i.e. AY 2015-16).

Alternate Minimum Tax

It is proposed to insert new clause (iii) to section 115JC(2) w.e.f. 1st April, 2015 (Assessment year 2015-16), to provide that total income shall be increased by the deduction claimed under section 35AD (i.e. deduction claimed in respect of capital expenditure incurred for specified business carried by assessee) for purpose of computing the adjusted total income.

The amount of depreciation allowance in accordance with the provisions of section 32 shall be reduced in computing the adjusted total income, in respect of the assets on which the deduction under section 35AD is claimed.

Sec 115JEE – Applicability of Alternative Minimum Tax (AMT)

It is proposed to insert a new clause (c) in sub-section (1) so as to include a person who has claimed deduction under section 35AD within the ambit of chapter XII-BA of the Act. Further, it is proposed to insert a new sub-section (3) in section 115JEE to provide that notwithstanding anything contained in sub-section (1) or sub-section (2), the credit for taxes paid under section 115JC shall be allowed in accordance with the provisions of section 115JD.The aforesaid amendment shall become effective from 1stApril, 2015.

Estimate of value of assets by Valuation Officer

Under the existing provisions contained in section 142A, the Assessing Officer may, for the purpose of making an assessment or reassessment, require the Valuation Officer to make an estimate of the value of any investment, any bullion, jewellery or fair market value of any property. On receipt of the report of the Valuation Officer, the Assessing Officer may after giving the assessee an opportunity of being heard take into account such report for the purposes of assessment or reassessment.

It is proposed to substitute the section 142A so as to provide that the Assessing Officer may, for the purposes of assessment or reassessment, require the assistance of a Valuation Officer to estimate the value, including fair market value, of any asset, property or investment and submit the report to him. The Assessing Officer may make a reference whether or not he is satisfied about the correctness or completeness of the accounts of the assessee.

The Valuation Officer is required to estimate the value of the asset, property or investment after taking into account the evidence produced by the assessee and any other evidence in his possession gathered, after giving an opportunity of being heard to the assessee. If the assessee does not co-operate or comply with the directions of the Valuation Officer he may, estimate the value of the asset, property or investment to the best of his judgment.

The Valuation Officer shall send a copy of his estimate to the Assessing Officer and the assessee within a period of six months from the end of the month in which the reference is made by the Assessing officer. The Assessing Officer on receipt of the report from the Valuation Officer may, after giving the assessee an opportunity of being heard, take into account such report in making the assessment or reassessment.

These amendments shall become effective from 1stOctober, 2014.

Exclusion of time in computing the period of limitation for completion of assessments and reassessments

It is proposed to insert clause (iv) to Explanation 1 of section 153, w.e.f. 1st October, 2014, to provide for the exclusion of the period, commencing from the date on which Assessing officer has made reference to the Valuation officer under section 142A (1) and ending with the date on which the Valuation report is received by the Assessing officer, in computing the period of limitation for completion of assessments and reassessments.

Exclusion of time in computing the period of limitation for completion of assessments in case of search

It is proposed to insert clause (iia) to Explanation of section 153A, w.e.f. 1st October, 2014, to provide for the exclusion of the period, commencing from the date on which Assessing officer has made reference to the Valuation officer under section 142A (1) and ending with the date on which the Valuation report is received by the Assessing officer, in computing the period of limitation for completion of assessments and reassessments.

Insertion of Explanation 2 to Sec 37 -Disallowability of expenditure incurred for Corporate Social Responsibility Activities

Section 37(1) of the Act provide that deduction for any expenditure, which is not mentioned specifically in section 30 to section 36 of the Act, shall be allowed if the same is incurred wholly and exclusively for the purposes of carrying on business or profession.

It is proposed to insert a new explanation in sub-section (1) of section 37, namely explanation 2, to clarify that for the purposes of sub-section (1) of the said section, any expenditure incurred by an assessee on the activities relating to corporate social responsibility ('CSR') referred to in section 135 of the Companies Act, 2013 shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession.

Thus, CSR expenditure which is of the nature described in section 30 to section 36 of the Act will be allowed as deduction under those sections subject to fulfillment of conditions specified therein and any other CSR expenditure would be considered as application of income not allowable as deduction in computing taxable income. The explanation will be effective from 1stApril, 2015.

Sec 276D – Consequences of failure to furnish accounts and documents or comply with directions u/s 142

It is proposed to amend section 276D to provide that in case a person willfully fails to produce accounts and documents as required in any notice issued under sub-section (1) of section 142 or wilfully fails to comply with a direction issued to him under sub-section (2A) of section 142, he shall be punishable with rigorous imprisonment for a term which may extend to one year and with fine. This amendment shall be effective from 1st October, 2014.

Extension of time limit for provisional attachment u/s 281B

It is proposed to amend the proviso to sub-section (2) so as to provide that the Chief Commissioner, Commissioner, Director General or Director may extend the period of provisional attachment so that the total period of extension does not exceed two years or upto sixty days after the date of assessment or reassessment, whichever is later. This amendment shall be effective from 1stOctober, 2014.

Sec 140 – No signing but only verification of Return of Income

It is proposed to amend section 140 of the Act to do away with the requirement of signing the return of income and accordingly to omit the statutory requirement of signing such return. The income tax return shall now be required to be only verified by the persons in the manner prescribed u/s 139 of the Act. The above amendment shall become effective from 1stApril, 2015.

Sec 35AD – Deduction in respect of expenditure on specified business

Section 35AD provides investment linked tax incentive by way of allowing a deduction in respect of the whole of any expenditure of capital nature (other than expenditure on land, goodwill and financial instrument) incurred wholly and exclusively, for the purposes of the "specified business" during the previous year in which such expenditure is incurred.

It is proposed to include two new businesses as "specified business" for the purposes of the investment-linked deduction under sub-section 5 to section 35AD so as to promote investment in these sectors, which are :-

(a) laying and operating a slurry pipeline for the transportation of iron ore;

(b) Setting up and operating a semiconductor wafer fabrication manufacturing unit, if such unit is notified by the Board in accordance with the prescribed guidelines.

The date of commencement of operations for availing investment linked deduction in respect of the above two new specified businesses shall be on or after 1st April, 2014.

Further, sub-section (7A) has been inserted in section 35AD to provide that any asset in respect of which deduction is claimed under section 35AD shall be used only for the specified business for a period of eight years beginning with the previous year in which such asset is acquired or constructed. If such asset is used for any purpose other than the specified business, the total amount of deduction so claimed and allowed in any previous year in respect of such

asset, as reduced by the amount of depreciation allowable in accordance with the provisions of section 32 as if no deduction had been allowed under section 35AD, shall be deemed to be income of the assessee chargeable under the head “Profits and gains of business or profession” of the previous year in which the asset is so used as per newly inserted sub-section (7B).

Where any deduction has been availed of by the assessee on account of capital expenditure incurred for the purposes of specified business in any assessment year u/s 35AD, no deduction under section 10AA shall be available to the assessee in the same or any other assessment year in respect of such specified business.

Section 80C: Increase in limit of deduction from gross total income

It is proposed to increase maximum amount of deduction allowed under section 80C to individuals and HUF from Rs. 1,00,000to Rs.1,50,000 w.e.f. 1st April, 2015 i.e. assessment year 2015-16, to encourage house hold savings. It is also proposed to make consequential amendment in sections 80CCE and 80CCD, which provides the ceiling for aggregate deduction allowed u/s 80C, 80CCCand 80CCD.

Deduction from income from house property

It is proposed to amend the second proviso to clause (b) of section 24 w.e.f. 1st April, 2015 i.e. assessment year 2015-16 so as to increase the amount of interest on capital borrowed for acquisition or construction of self occupied house property, from Rs. 1,50,000 to Rs.2,00,000.

Section 54 and 54F: Capital gains exemption in case of investment in a residential house property restricted to one residential house situated in India

The existing provisions contained in sub-section (1) of section 54, *inter alia*, provide that where capital gain arises from the transfer of a long-term capital asset, being buildings or lands appurtenant thereto, and being a residential house, and the assessee within a period of one year before or two years after the date of transfer, purchases, or within a period of three years after the date of transfer constructs, a residential house then the amount of capital gains to the extent invested in the new residential house is not chargeable to tax under section 45 of the Act.

The existing provisions contained in sub-section (1) of section 54F, *inter alia*, provide that where capital gains arises from transfer of a long-term capital asset, not being a residential house, and the assessee within a period of one year before or two years after the date of transfer, purchases, or within a period of three years after the date of transfer constructs, a residential house then the portion of capital gains in the ratio of cost of new asset to the net consideration received on transfer is not chargeable to tax.

The Finance Bill now proposes to amend the aforesaid sub-section (1) of section 54 and sub-section (1) Section 54F so as to provide that such rollover relief under the said sections shall be available only if the investment is made in one residential house situated in India.

The above amendment plugs two loopholes which exist in the current provision namely: a) tax payers can claim exemption even if they purchase/construct more than one new residential property; b) tax payers can claim exemption for investing in a residential house whether situated in or outside India. In order to plug the said loopholes, post the amendment the exemption shall only be available if the investments made in one residential house and the same should be situated in India.

These amendments are effective from assessment year 2015-16 onwards.

Section 54EC: Total exemption cannot exceed 50 lakhs irrespective of financial years in which investment is made

The existing provisions of section 54EC(1) of the Act provide for exemption from capital gains arising from transfer of a long-term capital asset if the assessee has, within a period of six months, invested the whole or part of capital gains in the long-term specified asset. The said exemption is subject to a maximum amount of fifty lakh rupees.

However, the taxpayers claimed double exemption on same transaction(s) of transfer of long-term capital asset(s) by splitting the investment of fifty lakh rupees each in two years thereby resulting in the claim for relief of one crore rupees as against the intended limit for relief of fifty lakh rupees. In this regard, there are contradictory ITAT rulings. In the case of *ShriAspiGinwala, Shree Ram Engg.& Mfg. Industries vs. ACIT [ITA No.- 3226/Ahd/2011]* and *ShriVivekJairazbhoy vs. DCIT [ITA No.-236/Bang/2012]* whereby the Hon'ble Ahmedabad Tribunal and Hon'ble Bangalore Tribunal respectively ruled that the taxpayer is eligible to claim double deduction. However, the Hon'ble Jaipur Tribunal gave a contrary view, in case of *ACIT vs. Shri Raj Kumar Jain & Sons (HUF) [ITA No.- 648/JP/2011]*, holding that the exemption shall be limited to fifty lakh rupees.

Therefore, to bring this controversy to rest and to restrict the relief to fifty lakh rupees, it is proposed to insert a proviso which states that any investment in the long-term specified asset, out of capital gains from transfer of original asset(s), made during year of transfer or in the subsequent year, shall not exceed fifty lakh rupees.

This amendment is effective from assessment year 2015-16 onwards.

Section 45: Trading in commodity derivatives is not a Speculative transaction only if it is chargeable to Commodity transaction tax

Finance Act 2013, inserted clause (e) to Sub-Section 5 of Section 45 to exclude eligible transactions in respect of trading in commodity derivatives carried in a recognized association. It was clarified vide Circular No. 3 dated 24.01.2014 that the eligible transaction shall include only those transactions in commodity derivatives which are liable to commodities transaction tax.

To incorporate the clarification made by said circular, it is proposed to amend clause (e) of the proviso to the clause (5) of section 43 effective from 1stApril, 2014, to clarify that the eligible transaction in respect of trading in commodity derivatives carried out in a recognised association and chargeable to commodities transaction tax shall not be considered to be a speculative transaction.

In case of transfer of an asset by way of compulsory acquisition, Capital gains to arise only after final order of the court

Provisions of section 45(5) of the Act provide for charging of any profits or gains arising from transfer of a capital asset by way of compulsory acquisition where the compensation is enhanced or further enhanced by the court, Tribunal or any other authority. The said enhanced compensation as per Clause (b) of the said sub-section was deemed to be the income chargeable of the previous year in which such amount is received by the assessee.

As there is uncertainty about the year in which the amount of compensation is received in pursuance of interim order of the court, it is proposed to provide that the amount of compensation received in pursuance of an interim order of the court, Tribunal or other authority shall be deemed to be income chargeable under the head 'Capital gains' in

the previous year in which the final order of such court, Tribunal or other authority is made. This amendment shall become effective from 1st April, 2015.

Section 73: Trading in Shares shall not be Speculation Business

It is proposed that the Explanation to section 73 of the Act with regards to losses incurred in respect of a speculation business shall not be applicable to a company whose principal business is business of trading in shares. Thus, any loss incurred by a company engaged in business of trading in shares shall not be treated as any losses incurred in respect of speculation business.This amendment shall become effective from 1st April, 2015.

Cost Inflation Index

The existing definition of Cost Inflation Index (CII) in relation to previous years were notified by the Government having regard to seventy-five percent of average rise in the Consumer Price Index (CPI) for urban non-manual employees (UNME) for the immediately preceding previous year to such previous year.

The release of CPI for UNME has been discontinued. Therefore, it is proposed to amend the clause (v) of the Explanation to section 48 to provide that CII in relation to a previous year means such index as may be notified by the Central Government having regard to seventy-five percent of average rise in the Consumer Price Index (Urban) for the immediately preceding previous year to such previous year.This amendment shall become effective from 1st April, 2016.

INTERNATIONAL TAXATION

Characterization of Income in case of Foreign Institutional Investors

Under the existing provisions of sub-section (14) of section 2 of the Act, the term “capital asset” is defined to include property of any kind held by an assessee, whether or not connected with his business or profession, but does not include any stock-in-trade or personal assets as provided in the definition.

It is proposed to amend sub-section (14) of section 2 of the Act to provide that any security held by Foreign Institutional Investor which has invested in such security in accordance with the regulations made under the Securities and Exchange Board of India Act, 1992 would be treated as capital asset only so that any income arising from transfer of such security by a Foreign Portfolio Investor (FPI) would be in the nature of capital gain. This amendment shall become effective from 1st April, 2015 and will, accordingly, apply in relation to the assessment year 2015-16 and subsequent assessment years.

The aforesaid amendment is proposed in order to end uncertainty faced by the FPI (referred as foreign institutional investors in the Act) in characterization of their income arising from transaction in securities.

Special Provisions Relating To Business Trusts – Real Estate Investment Trust (REIT) and Infrastructure Investment Trust (Invits)

In order to promote socio-economic growth, the Finance Bill proposes to amend the Act to put in place a specific taxation regime for providing the way the income in the hands of such trusts is to be taxed and the taxability of the income distributed by such business trusts in the hands of the unit holders of such trusts. Such regime has the following main features:–

- Section 2 (13A) shall be inserted with effect from the 1st October, 2014 to define “business trust” which shall mean to be a trust registered as an Infrastructure Investment Trust or a Real Estate Investment Trust, the units of which are required to be listed on a recognized stock exchange, in accordance with the regulations made under the Securities Exchange Board of India Act, 1992 and notified by the Central Government in this behalf.
- Section 10(23FC) shall be inserted to provide that in computing the total income of a previous year of a business trust, any income by way of interest received or receivable from a special purpose vehicle shall not be included and hence no withholding tax at the level of SPV. Hence, the Finance Bill proposes to create a pass through regime for interest income of the business trust.
- Further an explanation shall be added to Section 10(23FC) to define the term “special purpose vehicle” to mean an Indian company in which the business trust holds controlling interest and any specific percentage of shareholding or interest, as may be required by the regulations under which such trust is granted registration.
- Further, if any interest income referred to in Section 10(23FC) is distributed by a business trust to its non-resident unit holders, withholding tax at the rate of 5 per cent shall apply and where the distribution is to a resident unit holder withholding tax at the rate of 10 per cent shall be effected by the trust.
- Section 10 (23FD) shall be inserted to provide that in computing the total income of a previous year any distributed income received by a unit holder from the business trust, not being that proportion of the income which is of the same nature as the income referred to in clause (23FC) shall not be included.

- Any long term capital gains arising from trading of the listed units of a business trust on a recognised stock exchange shall be exempt from tax on payment of securities transaction tax (STT). Further any short term capital gains from such trading would be taxable at the rate of 15%.
- However, the above benefits shall not apply in respect of any income arising from transfer of units of a business trust which were acquired in consideration of a transfer of share of a special purpose vehicle to a business trust in exchange of units allotted by that trust to the transferor.
- Any capital gains arising to the sponsor at the time of exchange of shares in SPVs with units of the business trust, the taxation of gains shall be deferred and taxed at the time of disposal of units by the sponsor. Further, for the purpose of computing capital gain, the cost of these units shall be considered as cost of the shares to the sponsor. The holding period of shares shall also be included in the holding period of such units.
- In case of overseas borrowings in foreign currency by the business trust, the benefit of reduced rate of 5 per cent tax on interest payments to non-resident lenders shall be available on similar conditions, for such period as is provided in section 194LC of the Act.
- The dividend received by the trust shall be subject to dividend distribution tax at the level of SPV but will be exempt in the hands of the trust and the dividend component of the income distributed by the trust to unit holders will also be exempt.
- The income by way of capital gains on disposal of assets by the trust shall be taxable in the hands of the trust at the applicable rate. However, if such capital gains are distributed, then the component of distributed income attributable to capital gains would be exempt in the hands of the unit holder. Any other income of the trust shall be taxable at the maximum marginal rate.
- The business trust is required to furnish its return of income.
- The necessary forms to be filed and other reporting requirements to be met by the trust shall be prescribed to implement the above scheme.

These amendments will take effect from 1st October, 2014.

Section 115BBD: Reduced tax rates on certain dividends received from foreign companies extended without sunset clause

The existing provisions of Section 115BBD of the Act provide that where the total income of an assessee, being an Indian company, included any income by way of dividends declared, distributed or paid by a foreign company in which Indian Company holds 26% or more in nominal value of equity share capital, the income-tax payable shall be the aggregate of-

(*a*) the amount of income-tax calculated on the income by way of such dividends, at the rate of 15%; and

(*b*) the amount of income-tax with which the assessee would have been chargeable had its total income been reduced by the aforesaid income by way of dividends.

With a view to encourage Indian companies to repatriate foreign dividends into the country, it is proposed to extend the benefit of reduced rate of tax of 15% on foreign dividends received in financial year 2014-15 and subsequent financial years. This amendment will become effective from 1stApril, 2015 and will, accordingly, apply in relation to the assessment year 2015-16 and subsequent assessment years.

Section 194LC: Concessional rate of interest on overseas borrowing

The existing provisions of section 194LC of the Act provide for lower withholding tax rate of 5 per cent on interest paid by an Indian company to non-residents on monies borrowed by it in foreign currency from a source outside India under a loan agreement or through issue of long-term infrastructure bonds at any time on or after the 1st July, 2012 but before the 1st July, 2015 subject to certain conditions.

In order to further boost such low cost long-term foreign borrowings by Indian companies, it is proposed to amend section 194LC to extend the benefit of this concessional rate of withholding tax to borrowings by way of issue of any long-term bond, and not limited to a long term infrastructure bond.

It is proposed to extend the said concessional rate of withholding tax for borrowings made before 1st July, 2017 i.e. additional two years as compared to existing provisions. Further, it is proposed that the higher rates of withholding tax as per 206AA shall not applicable to reduced withholding tax on interest on such long term bonds and therefore proposes consequential amendment in Section 206AA.

This amendment will be effective from 1st October, 2014.

SERVICE TAX

Effective date to be notified by Central Government:

Section 65B: Proposed changes in Interpretations:

- "Radio taxi" has been specifically excluded from the definition of "metered cab".
- "Print media" has been now defined under section 65B(39a).

Section. 66D: Proposed changes in Negative List:

- Only selling of space for advertisement in print media to be covered under clause (g) of negative list.
- "radio taxis" omitted from sub-clause (vi) of clause (o) so as to provide for levy of service tax on services by radio taxis,

New rules are proposed to be prescribed for meaning of "rate of Exchange" as appearing under explanation to section 67A which currently means the "customs rate".

Time limit for adjudication has been specified under section 73, as either six months or one year, depending on the nature of case, to be adhered to where it is possible.

Central Excise officer may be authorized to search for and seize or such documents or books or things as may be useful for or relevant to any proceedings.

Provisions of sub-section (2A) of section 5A, section, 15A and section 15B of the Central Excise Act are proposed to be made applicable under service tax.

Section 94: Proposes power to make rules with regard to-

- Imposition, on persons liable to pay service tax, for the proper levy and collection of duty.
- provisions for withdrawal of facilities or imposition of restrictions
- issue incidental or supplemental matters
- any other matters

Retrospective exemption proposed in case of taxable services provided by the Employees' State Insurance Corporation, prior to the 1st day of July, 2012.

Clarification has been issued with regard to rule 7 of the Cenvat Credit Rules, 2004 to allow distribution of input service credit to all units (which are operational in the current year) in the ratio of their turnover of the previous year/ previous quarter as the case may be.

NOTIFICATIONS

Notification No. 06/2014-ST: Amendments in mega exemption notification (with immediate effect)

- Transport of passenger by air-conditioned contract carriage would be liable to service tax on abated value.
- Exemption available to services by way of technical testing or analysis of newly developed drugs, including

vaccines and herbal remedies on human participants by a clinical research organization approved by the Drug Controller General of India has been withdrawn.

- Deletion of concept of 'auxiliary educational services'. Specific services received by eligible educational institution exempted such as transport facility to students or faculty, catering service, security or cleaning service, service relation to admission. Further renting of immovable property to such institution is also taxable.
- Services such as consultancy, designing, etc., not directly connected with the specified services to Government or local authority or governmental authority is now taxable.
- Scope of Hotels, inn, guest house to include dharmashalas or ashram or such other entities.
- Services by way of loading, unloading, packing, storage or warehousing, transport by vessel, rail or road (GTA), of cotton, ginned or baled, is being exempted.
- Services received by RBI from outside India in relation to management of foreign exchange reserves.
- Services provided by the Indian tour operators to foreign tourists in relation to tours wholly conducted outside India are being exempted.
- All life micro-insurance schemes approved by the Insurance Regulatory Development Authority (IRDA), where sum assured does not exceed Fifty Thousand Rupees are being exempted from service tax.
- Services provided by Common Bio-medical Waste Treatment Facility operators by way of treatment, disposal of bio medical waste or processes incidental to such treatment or disposal are being exempted.

Notification No.07/2014-ST: Simplification in procedural aspect for SEZ

Procedural changes are being made in Notification No 12/2013-ST in case of SEZ or developer with immediate effect.

Notification No. 08/2014-ST: Amendment in Abatement Notification

- Condition for availing abatement in GTA sevices has been amended
- Abatement provided to air conditioned contract carriage for transportation of passenger at 60 per cent.
- Cenvat credit on rent a cab and tour operator service available subject to certain conditions from 1 October 2014).
- Abatement increased on transport of goods by vessel to 60 per cent.

Notification No. 09/2014-ST: Amending the Service tax Rules

- Service provided by recovery agents to banks, NBFC etc. is covered under reverse charge mechanism.
- Mandatory e-payment by all assesses.

Notification No.11/2014-ST: Service tax on service portion in Works Contracts

- Category 'B' and 'C' of works contracts are proposed to be merged into one single category with rationalized percentage of service portion as 70 per cent under Rule 2A of the Service Tax (Determination of Value) Rules, 2006 w.e.f. 1 October, 2014.

Notification No.12/2014-ST: Change in Interest rate

Period of Delay	Interest rate for other than small service provider	Interest rate for small service provider
Up to six months	18 per cent	15 per cent
More than six months and up to one year	18 per cent for the first six months of delay and 24 per cent for the delay beyond six months.	15 per cent for the first six months of delay and 21 per cent for the delay beyond six months.
More than one year	18 per cent for the first six months of delay; 24 per cent for the period beyond six months up to one year and 30 per cent for any delay beyond one year.	15 per cent for the first six months of delay; 21 per cent for the period beyond six months up to one year and 27 per cent for any delay beyond one year.

Notification No.13/2014-ST: Point of Taxation Rules:

The first Proviso to rule 7 of the Point of Taxation Rules (POTR) is being amended to provide that point of taxation in respect of reverse charge will be the payment date or the first day that occurs immediately after a period of three months (earlier six months) from the date of invoice, whichever is earlier. This amendment will apply only to invoices issued after 1st October, 2014. A transition rule is being prescribed under new rule 10 of POTR.

Notification 14/2014-ST: Place of Provision of Services Rules (Effective 1 October 2014):

- Provision for prescribing conditions for determination of place of provision of repair service carried out on temporarily imported goods is being modified.
- The definition of intermediary is being amended to include the intermediary of goods in its scope. Accordingly an intermediary of goods, such as a commission agent or consignment agent shall be covered under rule 9(c) of the Place of Supply of Services Rules.
- Service consisting of hiring of Vessels (excluding yachts) and Aircraft is being excluded from rule 9(d) will be covered by the general rule.

Notification No.15/2014-ST: Advance Ruling:

Resident private limited company is eligible to make application under Advance Ruling in service tax with immediate effect.

CUSTOMS

Section 129A: Admission of Appeal to Tribunal

Right of refusal to admit an appeal by the Tribunal has been proposed to be raised from Rupees fifty thousand to Rupees two lakhs. (Similar changes made in Central Excise)

Section 129E of the Customs Act is substituted to by new section so as to provide for deposit of certain percentage of duty demanded or penalty imposed or both before filing an appeal (Similar changes made under Central Excise)

Tariff

Section 8B: Safeguard Duty

Proposed amendment has been sought under sub-section (2A) of section 8B of the Customs Tariff Act relating to levy of Safeguard Duty so as to align the provisions with sub-section (2A) of section 9A of the Customs Tariff Act relating to Anti-dumping duty.

First Schedule to the Customs Tariff Act is proposed to be amended in the manner specified in the Third Schedule of the finance bill so as to,–

- omit a tariff item;
- revise the rate of customs duty on certain tariff items; and
- amend units specified in column 3 in respect of certain goods.

NOTIFICATIONS

Changes in BCD rates

Description	New Rate	Old Rate
Pre-forms of precious and semi-precious stones.	Nil	2%
Half-cut or broken diamonds	2.5%	Nil
Cut & polished diamonds including lab-grown diamonds and colored gemstones	2.5%	2%
Ethane and other goods under sub-heading 2901 10 00, ethylene, propylene and butadiene	2.5%	5%
Raw materials for manufacture of spandex yarn viz. Diphenylmethane 4,4 di-isocyanate (MDI) and Polytetramethylene ether glycol (PT MEG)	Nil	5%
LCD and LED TV panels of below 19 inches	Nil	10%
Colour picture tubes for manufacture of cathode ray TV	Nil	10%
E-Book readers	Nil	7.5%

CVD on Anthracite coal, Coking coal and other Coal is being reduced from 6% to 2%

Baggage rules have been amended to provide as follows:

- Raise the free baggage allowance from Rs.35,000 to Rs.45,000.
- Reduce the duty free allowance of cigarettes from 200 to 100, of cigars from 50 to 25 and of tobacco from 250 gms to 125 gms.

The duty free entitlement for import of trimmings & embellishments and other goods used by the readymade textile garment sector for manufacture of garments for export is being increased from 3% to 5%.

Specified goods imported for use in the manufacture of textile garments for export are fully exempt from BCD and CVD subject to the condition.

Special Additional Duty (SAD) on all inputs/components used in the manufacture of Personal Computers (laptops/desktops) and tablet computers is being exempted, subject to actual user condition.

CENTRAL EXCISE

LEGISLATIVE CHANGES

Section 15A & 15B: Furnishing of Information return

A new section 15A in the Central Excise Act is proposed to be inserted so as to empower the Central Government to prescribe an authority or agency to whom the information return shall be filed by the specified persons such as Income-tax authorities, State Electricity Boards, VAT or Sales Tax authorities, Registrar of Companies, banking companies etc. Information can be collected for the purposes of the Act, such as, to identify tax evaders or recover confirmed dues. It also seeks to insert new section 15B which provides for imposition of penalty on failure to furnish information return.

Section 35L:

A new sub-section (2) in section 35L of the Central Excise Act so as to clarify that determination of disputes relating to taxability or excisability is covered under the expression “determination of any question having a relation to rate of duty”.

Others

Retrospective amendment has been proposed as provided under Fifth Schedule of the finance bill

- with effect from 29th June, 2010 to 16th March, 2012 so as to exempt duty of excise–
- on polyester staple fibre/polyester filament yarn manufactured from plastic waste or scrap or plastic waste including waste polyethylene terephthalate bottles;
- on tow manufactured and captively consumed within the factory of its production for the manufacture of goods above;
- with effect from 1st March, 2011 to 16th March, 2012 so as to exempt duty of excise on unbranded articles of precious metals.

Retrospective amendment has been proposed as provided under Sixth Schedule of the finance bill-

- with effect from 8th February, 2013 to 10th July, 2014 so as to exempt duty of excise on liquefied propane and butane mixture, liquefied butane and liquefied petroleum gases (LPG) for supply to non-domestic exempted category (NDEC) customers by the Indian Oil Corporation Limited, Hindustan Petroleum Corporation Limited or Bharat Petroleum Corporation Limited;
- with effect from 17th March, 2012 to 7th May, 2012 so as to exempt duty of excise on polyester staple fibre/polyester filament yarn manufactured from plastic waste or scrap or plastic waste including waste polyethylene terephthalate bottles;
- with effect from 17th March, 2012 to 10th July, 2014 so as to exempt duty of excise on tow manufactured and consumed within the factory of production for the manufacture of goods at above.

Clause 104 of the Bill seeks to amend the Third Schedule to the Central Excise Act in the manner specified in the Seventh Schedule so as to insert and amend certain entries therein.

Tariff

Clause 105 of the Bill seeks to amend the First Schedule to the Central Excise Tariff Act in the manner specified in the Eighth Schedule so as to,–

- revise the rate of excise duty on certain tariff items;
- omit a tariff item;
- incorporate changes in a tariff item; and
- amend units specified in column (3) in respect of certain goods.

Notification No. 21/2014-CE(N.T): Change in Cenvat Credit Rules, 2004

Definition of “Place of removal” has been inserted under CCR, 2004.

With effect from 1st September 2014, manufacturer or the provider of output service shall not be eligible to avail CENVAT credit after six months of the date of issue of any of the documents specified in sub- rule (1) of rule 9 of CCR, 2004.

E-payment made mandatory to all class of assesses.

Notification no 20/2014-CE(N.T): Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000

In the above rules, a proviso has been inserted whereby it is stated that if the goods are sold at a price which is not the sole consideration for sale of such excisable goods and sold at a price less than manufacturing cost and profit and if no additional consideration is flowing directly or indirectly from the buyer to such assessee the value of such goods shall be deemed to be the transaction value.”

INDUSTRY SPECIFIC ANALYSIS

FINANCE SECTOR

INTRODUCTION

Rising incomes are driving the demand for financial services across income brackets. Product innovation is leading to healthy growth in insurance and NBFCs. India benefits from a large cross-utilisation of channels to expand the reach of financial services. The financial inclusion drive from the RBI has expanded the target market to semi-urban and rural areas. In the last one decade, Banking, Financial services and Insurance (BFSI) has turned out as amongst the most preferred sectors for foreign investment in India.

The financial services segment has been a major contributor in service sector and as per Economic Survey 2014, the services sector has been a great stimulus to the Indian economy accounting for 57 per cent of the gross domestic product (GDP). The growth of the financial sector in India at present is nearly 8.5 per cent per year.

This sector is dominated by commercial banks which have over 60 per cent share of the total assets, India's financial sector comprises commercial banks, insurance firms, non-banking institutions, mutual funds, cooperatives and pension funds, among other financial entities.

The last two decades have seen the sector developing a more contemporary outlook. The Government of India has helped in this development, introducing reforms to liberalise, regulate and enhance the country's financial services. Today, India is recognised as one of the world's most vibrant capital markets. Notwithstanding challenges, the sector's future seems to be in good hands.

BANKS

Indian banks operating overseas saw higher credit growth in comparison to their foreign counterparts operating in India, according to Reserve Bank of India's (RBI) survey on international trade in banking services. The survey for 2012–13 showed growth of credit extended by Indian banks' branches operating overseas to have increased by 31.7 per cent to Rs 585,570 crore (US$ 98.18 billion).

Increased growth in agriculture and services sectors as well as in the personal loans segment, helped bank credit grow during the April–November period of 2013 by 7.2 per cent; during the same period of 2012, bank credit growth stood at 6.6 per cent. “Higher growth in credit to agriculture may be attributed to the expected better kharif crop which has been announced by the Ministry of Agriculture,” stated the report by credit rating agency CARE Ratings.

As per Economic Survey 2014, growth rate of aggregate deposits marginally moderated to 14.1 per cent in 2013-14 from 14.2 per cent in the previous year. During financial year 2013-14, public-sector banks and foreign banks registered acceleration in bank credit, while there was a deceleration for private-sector banks. Commercial banks' investment in government and other approved securities was low at 26.9 per cent at end March 2014 compared to 28.0 per cent a year ago. Consequently, the investment-deposit ratio declined from 29.7 per cent at end March 2013 to 28.7 per cent at end March 2014.

NON-BANKING FINANCIAL INSTITUTIONS (NBFIS)

NBFCs have served the unbanked customers by pioneering into retail asset-backed lending, lending against securities and microfinance. NBFCs aspire to emerge as a one-stop shop for all financial services.

The sector has witnessed moderate consolidation activities in recent years, a trend expected to continue in the near future. New banking licence-related guidelines issued by RBI in early 2013 place NBFCs ahead in competition for licenses owing largely to their rural network.

As per Economic Survey 2014, the total number of NBFCs registered with the RBI declined from 12,385 as at the end of June 2012 to 12,225 as on 30 June 2013. The number of NBFC-Ds declined from 271 to 254 during the same period.

FOREIGN INSTITUTIONAL INVESTORS (FIIS) IN INDIA

Non-resident Indians (NRIs) and FIIs will now be allowed to invest in the insurance sector, within the overall 26 per cent cap on foreign direct investment (FDI). The department of industrial policy and promotion (DIPP) in a press note confirmed that apart from insurance companies, the relaxation would also cover insurance brokers, third-party administrators (TPAs), surveyors and loss assessors.

According to data released by the Securities and Exchange Board of India (SEBI), FIIs were gross buyers of debt securities valued at Rs 30,266 crore (US$ 5.07 billion) and sellers of bonds worth Rs 11,450 crore (US$ 1.91 billion) in the period January 1–24, 2014, which resulted in a net inflow of Rs 18,816 crore (US$ 3.15 billion). Also, during the same period, FIIs invested Rs 3,473 crore (US$ 582.21 million) into the equity market, making their total investment in debt and stocks to be around Rs 22,289 crore (US$ 3.73 billion).

Foreign investors invested about Rs 371,342 crore (US$ 62.25 billion) into India's stock market in the four years ended December 2013. This figure surpasses the investments in the boom years of 2005–08.

As far as the financial sector of India is concerned, Mauritius has contributed the largest share (43%) of FDI investment among all the countries. USA, UK, Cyprus and Singapore are some other countries in the list of top five. The overall FDI equity inflows in India is estimated to be US$5 billion during last 10 years.

Investments by FIIs in the Indian stock market crossed the Rs 1 trillion (US$ 16.77 billion) mark in December 2013 – the third time this has been achieved since FIIs' entry into the capital market in 1992–93.

CAPITAL MARKET

The Government of India has taken various steps for deepening the reforms in the capital markets, including simplification of initial public offering (IPO) process and allowing qualified foreign investors (QFIs) to access the Indian bond markets. The government has also proposed simplification of procedures and prescribing uniform registration and other norms for the entry for foreign portfolio investors.

Indian benchmark indices, i.e. the BSE and NSE closed at 25413.78 and 7611.35 (as on 30 June 2014), gaining 31.03 per cent and 30.28 per cent respectively over the closing value of 19395.81 (Sensex) and 5842.20 (Nifty) on 30 June 2013.

ROAD AHEAD

As per a report, India is one of the top 10 economies in the world, helped in no small part by its strong banking and insurance sectors. It is expected to become the fifth largest banking sector in the world by 2020 and the third largest by 2025, according to a joint report by KPMG–CII. The report expects bank credit to grow at a compound annual growth rate (CAGR) of 17 per cent in the medium term leading to better credit penetration.

The insurance sector also has bright times ahead. Life Insurance Council, the industry body of life insurers in India, has estimated a CAGR of 12–15 per cent over the next few years for the segment, with the country's insurable population projected to touch 750 million by FY 2020.

DIRECT TAX PROPOSALS

- Increase in Section 80C investment limit and deduction for interest housing loan raised to Rs 2 lakh from Rs 1.5 lakh may increase funds / revenue for this industry.

INDIRECT TAX PROPOSALS

New exemptions from Service Tax

- Life micro-insurance schemes for the poor, approved by IRDA, where sum assured does not exceed Rupees Fifty Thousand.
- Specialized financial services received by RBI from global financial institutions in the course of management of foreign exchange reserves, e.g., external asset management, custodial services, securities lending services, etc

OTHER PROPOSALS

- ☐ **Capital Market**
  - Government and RBI to put in place a modern monetary policy framework to meet the challenge of an increasing complex economy.
  - **Following measures will be taken to energize Capital markets:**

    Uniform KYC norms.

    Single operating demat account

    Uniform tax treatment for pension fund and mutual fund linked retirement plan
- ☐ **Banking**
  - Banks to be permitted to raise long term funds for lending to infrastructure sector with minimum regulatory pre-emption such as CRR, SLR and Priority Sector Lending (PSL).
  - RBI to create a framework for licensing small banks and other differentiated banks.
  - Six new Debt Recovery Tribunals to be set up.
  - Rs2,40,000 crore to be infuse as equity by 2018 in banks to be in line with Basel-III norms
- ☐ **Insurance Sector**
  - The pending insurance laws (amendment) Bill to be immediately brought for consideration of the Parliament.
  - The regulatory gap under the Prize Chits and Money Circulation Scheme (Banking) Act, 1978 will be bridged.
  - Increasing FDI/FII cap for insurances companies current FDI cap at 26% to 49% and listing to LIC.
- ☐ **Small Savings**
  - Kissan Vikas Patra (KVP) to be reintroduced.
  - A National Savings Certificate with insurance cover to provide additional benefits for the small saver.

- PPF Scheme, annual ceiling will be enhanced to Rs.1.5 lakh p.a.

Information technology in India

Information Technology (IT) has made possible information access at gigabit speeds. It has created a level playing field among nations and has created a positive impact on the lives of millions.

India's IT potential today, is paramount for its march towards global competitiveness, healthy gross domestic product (GDP) and meeting up the energy and environmental challenges.

The Indian IT and Information Technology enabled Services (ITeS) sectors go hand-in-hand in every aspect. The industry has not only transformed India's image on the global platform, but also fuelled economic growth by energising the higher education sector (especially in engineering and computer science). The industry has employed almost 10 million Indians and, hence, has contributed significantly to social transformation in the country.

India is one of the fastest-growing IT services markets in the world. It is also the world's largest sourcing destination, accounting for approximately 52 per cent of the US$ 124–130 billion market. The country's cost competitiveness in providing IT services continues to be its USP in the global sourcing market.

India has the potential to build a US$ 100 billion software product industry by 2025, according to Indian Software Product Industry Roundtable (iSPIRT). The software products market in India, which includes accounting software and cloud computing-based telephony services, is expected to grow at 14 per cent in 2014.

The Department of Electronics and Information Technology is coordinating strategic activities, promoting skill development programmes, enhancing infrastructure capabilities and supporting research and development (R&D) for India's leadership position in IT and ITeS.

Market Size

Indian IT and ITeS industry is divided into four major segments – IT services, business process management (BPM), software products and engineering services, and hardware. The IT services sector accounted for the largest share of the IT and ITeS industry, with a total market size of US$ 56.3 billion during FY13, followed by BPM sector (US$ 20.9 billion), and software products and engineering services (US$ 17.9 billion); the market size for hardware was US$ 13.3 billion during FY12.

The Indian IT-BPM industry is expected to add revenues of US$ 13–14 billion to the existing revenues by FY15, according to National Association of Software and Services Companies (NASSCOM).

The industry grew at a compound annual growth rate (CAGR) of 13.1 per cent during FY08–13.Total exports from the IT-BPM sector (excluding hardware) were estimated at US$ 76 billion during FY13, Export of IT services has been the major contributor, accounting for 57.9 per cent of total IT exports (excluding hardware) in FY13. BPM accounted for 23.5 per cent of total IT exports during the same fiscal. The IT outsourcing sector is expected to see exports growing by 13–15 per cent during FY15.

According to 'Marketing, Disrupted: Opportunities for the Indian technology industry' report by NASSCOM and Sapient Nitro Investments, the technology industry of India will have a US$ 37 billion of CMO opportunity by 2020,

Indian IT's core competencies and strengths have placed it on the international canvas, attracting investments from major countries.

According to data released by the Department of Industrial Policy and Promotion (DIPP), the computer software and hardware sector attracted foreign direct investment (FDI) worth Rs 59,381.64 crore (US$ 9.89 billion) between April

2000 and February 2014.

Major players in Indian IT and ITeS sector are planning huge investments in their existing business in India as well as their foreign operations.

Government Initiatives

The Government of India played a key role with public funding of a large, well trained pool of engineers and management personnel who could forge the Indian IT industry.

According to a study by Gartner, the Central Government and the respective State Governments are expected to collectively spend US$ 6.4 billion on IT products and services in 2014, an increase of 4.3 per cent over 2013, as the more and more state governments and local authorities are now moving their data and record system in digital mode and almost all administrative functions are planned to be linked to electronic systems which will provide continuous support to the IT and ITEs Industry in India.

The Government of India has given an in-principle approval for setting up of the first electronic system design and manufacturing (ESDM) cluster development in Electronics City, Bengaluru. The ESDM project will come up on a 1.16 acre of land at an investment of approximately Rs 85 crore (US$ 14.16 million).

The Union Railway Budget 2014 as introduced on 8th2014, provides host of opportunities for Indian IT industry.

According to Indian Industry experts the IT initiatives outlined in the railway budget would bring in greater efficiency and transparency in the system, and open up several opportunities for Indian information technology companies, industry R Chandrashekhar, president of software industry body National Association of Software and Services Companies (Nasscom) has expressed his views in following words "The thrust on technology initiatives in the railway budget are a welcome step to improve efficiency, modernisation, customer satisfaction and access. Providing Wi-Fi services, nextgen eticketing system, GIS mapping and digitisation of records will enable the Indian Railways in its overall growth objectives," and added that "Leveraging technology for transformation in India is a key priority for Nasscom and we look forward to work with the ministry of railways in enabling the private sector to collaborate on these initiatives," .

Proposals announced by Railway minister D V Sadananda Gowda like paperless offices in the next five years, real-time tracking of trains and rolling stock, mobile-based alerts for wakeup calls and destination arrival, station navigation information system, improving the e-ticketing system to support 7,200 tickets per minute compared with 2,000 tickets per minute and increasing the number of simultaneous users at any point to 1,20,000 requires an increased involvement of IT Industry and thereby providing a much needed financial support as well as will help generate employment.

The IT industry believes the thrust on public-private partnerships is a potential business opportunity for Indian IT companies. Abhaya Agarwal, partner-infrastructure practice at Ernst & Young LLP, said, "All the computerisation including hospital management information system which he (the minister) has talked about will ultimately bring lot of efficiency."

Road Ahead

India is the most preferred location for engineering offshoring, according to a customer poll conducted by Booz and Co. Companies are now offshoring complete product responsibility. Increased focus on R&D by IT firms in India has resulted in rising number of patents filed by them.

India's IT sector is gradually moving from linear models (rising headcount to increase revenue) to non-linear ones.

In line with this, IT companies in the country are focusing on new models such as platform-based BPM services and creation of intellectual property.

Tier II and III cities are increasingly gaining traction among IT companies aiming to establish business in India.

Skilled Cheap labour, affordable real estate, favourable government regulations, tax breaks and special economic zone (SEZ) schemes are facilitating their emergence as new IT destinations.

Indian insurance companies also plan to spend Rs 12,100 crore (US$ 2.01 billion) on IT products and services in 2014, a 12 per cent rise over 2013, according to Gartner. This forecast includes spending by insurers on internal IT (including personnel), software, hardware, external IT services and telecommunications.

In the next 5-10 years, railways will be able to carry more cargo compared with the present over billion tonnes without the addition of too much manpower, thereby bringing in more efficiency and transparency into the system, Agarwal added.

INDIRECT TAX PROPOSAL

- Relief from applicability of both service tax and VAT on software licenses.
- Colour picture tubes exempted from basic customs duty to make cathode ray TVs cheaper.
- Exempt special additional duty (SAD) from 4 percent on all inputs/components used in the manufacture of personal computers;
- Impose education cess on imported electronic products.

OTHER PROPOSALS

- Rs 100 crore for development of Technology Development Fund.
- Rs 500 crore for National Rural Internet and Technology Mission.
- E-Visa to facilitates will be introduce in a phase manner at 9 airport in India.
- Launch "Digital India" programme for ensuring Broadband connectivity at Village Level.
- A National Rural Internet and Technology Mission proposed for services in villages and schools, training in IT skills and E-Kranti.
- Rs 100 crore for support of about 600 new and existing Community Radio Stations.

INFRASTRUCTURE

Introduction

India's Planning Commission has projected an investment of US$ 1 trillion for the infrastructure sector during the 12th Five-Year Plan (2012–17), with 40 per cent of the funds coming from the country's private sector. India's focus on infrastructure since the turn of the millennium has helped make it the second fastest growing economy in the world. The country's constant growth gives investors, domestic and foreign, a tremendous opportunity for investment in its infrastructure sector.

While the role of foreign investment in the sector cannot be overstated, domestic companies too are making a mark abroad, as attested by Larsen & Toubro's (L&T) contract for the Doha Metro project and GMR Infrastructure's contract to upgrade the Philippines' Mactan–Cebu International Airport.

A strong infrastructure sector is vital to the development of a country's economy. Here, the Indian government has played an important role. Just recently, it allowed 100 per cent foreign direct investment (FDI) under the automatic route for port development projects. The government has also, this year, decided to convert roads into national highways, and has sought collaboration with Sudan in the field of renewable energy.

As per Economic Survey 2013-14, according to the Ministry of Statistics and Programme Implementation (MOSPI) Flash Report for February 2014, of 239 central-sector infrastructure projects costing ` 1000 crore and above, 99 are delayed with respect to the latest schedule and 11 have reported additional delays with respect to the date of completion reported in the previous month.

The current industrial downturn presents an opportunity to push ahead with critical reforms and remove infrastructure bottlenecks. The reform momentum needs to be accelerated to create a favourable climate for stronger growth in the medium and long terms. From the infrastructure-sector perspective, augmenting coal production, permitting commercial coal mining, restructuring power distribution, upgrading road and rail networks, reducing delays in regulatory approvals, land acquisition and rehabilitation, and solving financing constraints are some of the issues that require urgent attention. Steps are needed to upscale projects under public-private partnership (PPP) mode in order to attract private-sector investment in infrastructure.

Market Size

As per a study, the value of total roads and bridges infrastructure in the country is projected to grow at a compound annual growth rate (CAGR) of 17.4 per cent over FY 12–17. India's roads and bridges infrastructure, which was valued at US$ 6.9 billion in 2009, is expected to reach US$ 19.2 billion by 2017.

The total approximate earnings of the Indian Railways on originating basis during FY 13–14 were Rs 140,485.02 crore (US$ 23.34 billion) as against Rs 121,831.65 crore (US$ 20.25 billion) during FY 12–13.

The capacity of ports in India by the end of the 12th Five-Year Plan is targeted to touch 2,493.10 million tonnes per annum (MTPA) as compared to 1,245.30 MTPA at the end of the 11th Five-Year Plan (2007–12).

Investments

The FDI inflows in construction (infrastructure) activities during the period April 2000 – March 2014 stood at US$ 2,575.79 million, as per the data released by Department of Industrial Policy and Promotion (DIPP).

Government Initiatives

Some of the Indian government's recent initiatives in the infrastructure sector are summarised below:

The Union Cabinet in February 2014 gave its approval for declaration of around 7,200 km of State Roads as new national highways. Other road development projects in the pipeline include existing national highways network totalling 21,271 km, which are not covered under any programmes/schemes as of now.

Also, in a move to enhance energy efficiency of the Indian Railways, a web-based Electrical Energy Management System, RAILSAVER, was inaugurated by Mr. Kul Bhushan, Member Electrical, Railway Board, in April 2014. The portal will be used for tackling the challenges of global warming and sustainability of the environment.

In another development, the Indian government has facilitated 100 per cent FDI under the automatic route for port development projects. A 10-year tax holiday has been accorded to enterprises that are engaged in the business of developing, maintaining and operating ports, inland waterways and inland ports.

The country is also looking to collaborate with foreign partners. India and Sudan have good potential for enhancing cooperation in promoting renewable energy, as per Dr Farooq Abdullah, Union Minister of New and Renewable Energy, Government of India. The Minister has also offered Indian assistance for developing renewable energy resources in Sudan.

Recent Railway budget proposal to allow FDI in sectors other than railway operations and undertaking projects on PPP basis will provide much needed capital infusion and will lead to acceleratory growth in infrastructure and ancillary industries in long run.

ROAD AHEAD

The Planning Commission estimates total infrastructure spending to be about 10 per cent of gross domestic product (GDP) during the 12th Five-Year Plan (2012–17), up from 7.6 per cent during the previous plan (2007–12).

DIRECT TAX PROPOSAL

- 10 year tax holiday extended to the undertakings which begin generation, distribution and transmission of power by 31.03.2017.
- The eligible date of borrowing in foreign currency extended from 30.06.2015 to 30.06.2017 for a concessional tax rate of 5 percent on interest payments.
- Tax incentive extended to all types of bonds instead of only infrastructure bonds it may reduce fund flow to the sector.

OTHER PROPOSALS

- Bank will be encouraged to give long term funds & loans to the infrastructure sector.
- Rs 1000 crore for rail connectivity in northeastern region
- Scheme for development of new airports at tier II and III cities through PPP mode.
- Rs 100 crore for metro scheme in Ahmedabad and Lucknow.
- The requirement of certification by Ministry of Road Transport (or NHAI) for availing of customs duty exemption on specified goods required for construction of roads is being done away with.
- Take up Ultra Mega Solar Power Projects in Rajasthan, Gujarat, Tamil Nadu, and Laddakh in J&K.
- Implementation of the Green Energy Corridor Project will be accelerated to facilitate evacuation of renewable energy across the country.
- Rs.14,389 crore for Pradhan Mantri Gram Sadak Yojana.
- Committed to revive the Special Economic Zones (SEZs).
- Rs. 100 crore for National Industrial Corridor Authority, to coordinate the development of the industrial corridors, with smart cities linked to transport connectivity.

- Corpus of Rs500 crores to support mainstreaming PPPs.
- Rs. 500 crore for Deendayal Upadhyaya Gram Jyoti Yojana
- Sixteen new port projects are proposed to be awarded this year with a focus on port connectivity. Rs 1,635 crore will be allocated for the development of Outer Harbour Project in Tuticorin for phase I.
- A project on the river Ganga called 'Jal Marg Vikas' (National Waterways-I) will be developed between Allahabad and Haldia to cover a distance of 1620 kms, which will enable commercial navigation of at least 1500 tonne vessels.
- Rs. 37,880 crores for investment in National Highways Authority of India and State Roads includes Rs. 3,000 crores for the North East.
- Rs. 500 crore by NHAI for work on select expressways.

REAL ESTATE

INTRODUCTION

The Indian real estate sector continues to be a favoured destination for global investors. The urban population will surge in the coming years, which, coupled with growth in employment, education and health care, will push the demand for residential and commercial space.

Urbanisation has been rapid in the past few years, with 'upwardly-mobile' buyers keen to invest and reap dividends from the real estate market growth. Increasing migration to the cities will drive this demand. Also anticipate a rise in sales of housing property following the recent stock market rally and a slew of optimistic RBI rules to allow foreign banks into the country's protected banking ecosystem. Steady housing demand will be a big constant for the Indian economy this year, and the industry will focus on meeting this demand.

However, the real estate sector is burdened with high costs because of which there is little possibility of reduction in home prices in most micromarkets. Construction cost has increased by 40% in two years, while government taxes and premiums have also gone up substantially. This eliminates any scope for reduced prices, despite the weak market. Banks' reluctance to lend to real estate companies has led to increased cost of borrowing, adding to the overall cost. In fact, these factors will also result in an increase in prices in improved market conditions. The housing industry will revive at a faster pace if a stable government is formed after the general elections in 2014.

The recent move to introduce Reits, or Real Estate Investment Trusts, is a progressive one as well. Reits are a great instrument to tap cash flow into the Indian economy, and help smaller investors access income-generating real estate assets. It will help both developers and investors, through better financing and investment options. This will give the Indian real estate market more depth. Providing tax incentives to REITs for investment in housing, especially the affordable housing sector, will increase chances of its success.

According to Economic Survey 2014, Real Estate and ownership of dwellings with a share of 5.9 per cent in India's GDP, grew by 5.6 per cent in 2012-13. Real estate in particular, grew by 26.1 per cent. Housing activities have both forward and backward linkages which not only contribute to capital formation, generation of employment, and income opportunities but also to economic growth. Estimates show that every rupee invested in housing and construction adds 78 paise to the GDP.

As per Economic Survey 2014, a major policy concern for India is the widening gap between demand and supply of housing units and inadequate housing finance solutions. Nearly 30 per cent of the country's population lives in cities and urban areas and this figure is projected to reach 50 per cent in 2030. The present urban housing shortage is 18.78 million units of which 95.6 per cent is in economically weaker sections (EWS) / low income group (LIG) segments and requires huge financial investment. A number of incentives/ initiatives are being taken for promoting affordable housing such as allowing external commercial borrowing (ECB) for low cost affordable housing projects.

Growing infrastructure requirement in diverse sectors such as tourism, education, healthcare, etc., are offering several investment opportunities for both domestic as well as foreign investors. Total investment by private equity (PE) funds in the real estate sector from January–March 2014 was approximately Rs 28 billion (US$ 465.19 million). This is a substantial increase of 28 per cent compared to the previous quarter and close to 2.5 times the investments during January–March 2013.

The role of the Government of India has been instrumental in the development of the sector. With the government trying to introduce developer and buyer friendly policies, the outlook for the real estate sector in 2014 does look promising.

MARKET SIZE

The market size of the Indian real estate sector is expected to touch approximately to US$ 180 billion by 2020 as compared to US$ 55.6 billion in 2010–11. The Confederation of Real Estate Developers' Associations of India (CREDAI) has identified demand from tier-II and tier-III cities as an impetus for better real estate solutions. With rapid land and infrastructure development in smaller cities and towns, assisted by bank loans, higher earnings and improved standards of living, housing and construction demand will increase here.

The net office space absorption across the top eight cities – Delhi-NCR, Mumbai, Bengaluru, Chennai, Hyderabad, Pune, Kolkata and Ahmedabad – was up 58 per cent during January–March 2014 as compared to the corresponding period last year, according to real estate consultancy Cushman & Wakefield. Among the eight cities, Ahmedabad and Delhi-NCR recorded a threefold increase in net absorption during the period over January–March 2013.

As per the report of Cushman & Wakefield, the number of new launches in the residential segment during the first quarter of 2014 has increased by 43 per cent at 55,000 units across eight major cities. Bengaluru recorded the largest number of units launched at an increase of 22 per cent at 16,838 units, followed by Mumbai and Chennai.

INVESTMENTS OPPORTUNITIES

According to global real estate consultant DTZ, The Corporates look to expand businesses, India is expected to witness major demand for office space in 2014. Office space absorption across the country's seven major cities – Delhi-NCR, Mumbai, Bengaluru, Chennai, Pune, Hyderabad and Kolkata – is likely to increase seven per cent this year to 29 million square feet (sq ft),.

According to a report by Jones Lang LaSalle, new supply of retail space in shopping malls in India's top seven cities is expected to more than double to 11.7 million sq ft in 2014. This will take up the mall stock across India's metropolitan cities to 87.7 million sq ft by the end of the year.

According to the Department of Industrial Policy and Promotion (DIPP), the construction development sector, including townships, housing, built-up infrastructure and construction-development projects garnered total foreign direct

investment (FDI) worth US$ 23,131.64 million in the period April 2000–February 2014. Construction (infrastructure) activities during the period received FDI worth US$ 2,462.60 million.

The following are some of the major investments and developments in the Indian real estate sector:

- Larsen & Toubro (L&T) has bagged a major residential order to build 271 villas and 24 towers in Bengaluru. "One of our key focus areas has been the growing potential in the residential sector and by winning these prestigious orders we have made significant inroads into this space," said Mr. S N Subrahmanyan, Senior Executive Vice-President (Infrastructure and Construction), L&T.

- As per Mr. Abhinandan Lodha, Deputy Managing Director, Lodha Group, Lodha Developers has acquired Clariant Chemicals' 87-acre plot of land in Thane, Mumbai, a rapidly developing part of the Mumbai Metropolitan Region for Rs 1,154 crore (US$ 191.76 million).

GOVERNMENT INITIATIVES

The Government of India has allowed FDI up to 100 per cent in development projects for townships and settlements. Hundred per cent FDI is also permitted in the hotel and tourism sector through the automatic route.

The Real Estate (Regulation and Development) Bill, 2013, as approved by the Union Cabinet is a pioneering initiative aimed at delivering a uniform regulatory environment to protect the consumer, help in quick verdicts of disputes and ensure systematic growth of the sector.

ROAD AHEAD

The Indian construction and real estate sector continues to be a favoured destination for global investors. Several large global investors, including a number of sovereign funds, have taken the first move by partnering with successful local investors and developers for investing in the Indian real estate market. This is expected to result in high transaction activity, especially in income yielding commercial office assets during 2014.

Mr. Sanjay Dutt, Executive Managing Director – South Asia, Cushman & Wakefield said, the residential asset class looks to have great potential for growth. "With housing requirements growing across cities and funds investing in the asset class primarily in the form of NCDs providing fixed returns, investments in the right project have the potential to yield healthy returns,".

Further, demand for space from sectors such as education and healthcare has opened up ample opportunities in the real estate sector. The country still needs to add three million hospital beds to meet the global average of three for every 1,000 people.

Real estate contributes about 5 per cent to India's GDP. The market size of this sector is expected to increase at a compound annual growth rate (CAGR) of 11.2 per cent during FY 2008–2020.

There is vast opportunity for the real estate sector to grow. The healthcare sector is estimated to touch US$ 100 billion by 2015. Also, emergence of nuclear families and growing urbanisation has given rise to several townships that are developed to take care of the elderly. Further, growth in the number of tourists has resulted in demand for service apartments.

IMPACT OF RAIL BUDGET

The proposed 5.79 percent increase in rail freight may impact the margin of Real Estate Industry because 30-40 demand of cement industry is from this sector.

DIRECT TAX PROPOSAL

- Tax exemption on interest on housing loan raised to Rs 2 lakh from Rs 1.5 lakh.
- Conducive tax regime to Infrastructure Investment Trusts and Real Estate Investment Trusts to be set up in accordance with regulations of the Securities and Exchange Board of India.

OTHER PROPOSAL

- Rs 7060 crore for the projects of developing one hundred Smart Cities
- A modified REITS type structure for infrastructure projects as the Infrastructure Investment Trusts (INVITS), these two instruments to attract long term finance from foreign and domestic sources including the NRIs.
- Rs. 4000 crores for National Housing Bank to increase credit for affordable housing to the urban poor/EWS/ LIG segment.
- Rs 8,000 crore for National Housing Bank (NHB) to support Rural Housing Scheme in the country.
- Slum development to be included in the list of Corporate Social Responsibility (CSR) activities to encourage the private sector to contribute more.
- Requirement of the built up area and capital conditions for FDI is being reduced from 50,000 square metres to 20,000 square metres and from USD 10 million to USD 5 million respectively with a three year post completion lock in.

ENGINEERING

INTRODUCTION

Engineering is by far the largest segment in the Indian industry. It is a diverse industry with a number of segments, and can be broadly categorised into two segments, namely, heavy engineering and light engineering. Powered by significant investments in power projects and infrastructure development, the sector has witnessed tremendous growth in recent years. It employs approximately four million skilled and semi-skilled workers and accounts for 27 per cent of the total factories in the industrial sector.

During FY 2013 order inflows were weak due to delays in project awards, land acquisition problems and environmental issues. Even the operating margins came under pressure due to commodity price inflation. Thus, rising commodity prices and slowdown in order inflows proved to be a double whammy for the engineering companies.

The engineering sector is among the top contributors to the total Indian export basket. Engineering exports from the country include transport equipment, capital goods, other machinery/equipment and light engineering products such as castings, forgings and fasteners. The sector accounts for about 20 per cent of India's total exports and is the largest foreign exchange earner for the country in terms of merchandised goods. The Engineering Export Promotion Council (EEPC) is the apex body in charge of promotion of engineering goods, products and services from India.

Continued growth of manufacturing sector and favourable regulatory policies will further propel the sector's growth. With 100 per cent foreign direct investment (FDI) allowed through the automatic route, major international players such as Cummins, ABB and Alfa Laval have entered the Indian engineering sector and have raised the industry's competitiveness.

MARKET SIZE

As per *Press Release (Media Reports, Department of Industrial Policy and Promotion (DIPP) statistic, Engineering Export Promotion Council, The Union Budget 2014-15).* Engineering research & design (ER&D) revenues are projected to increase to US$ 45 billion in 2020 from US$ 11.2 billion in 2012. The turnover of engineering services firms is also likely to touch US$ 37 billion by 2020.

Engineering exports from the country stood at US$ 61.61 billion in 2013–14, registering a growth of 8.49 per cent compared to the previous year. During April 2014, the overseas sales of engineering products rose 21.3 per cent to US$ 5.7 billion.

Engineering exports to India's Free Trade Agreement (FTA) partners such as South Korea, Japan, Sri Lanka and the Association of Southeast Asian Nations (ASEAN) bloc have witnessed robust growth. Shipments to South Korea rose by over 60 per cent and to Japan by 16 per cent during February 2014.

Of the country's total engineering exports, the United States (US) and Europe account for over 60 per cent. Transport equipment is the leading contributor to engineering exports, accounting for 32.5 per cent of the total exports during FY 13.

INVESTMENTS

As per data released recently by Department of Industrial Policy and Promotion (DIPP).The foreign direct investment (FDI) inflows in miscellaneous mechanical and engineering industries during April 2000 to March 2014 stood at US$ 2,606.83 million.

GOVERNMENT INITIATIVES

The government in its interim budget 2014-15 has announced cut in excise duty, or factory gate tax, on capital goods, consumer durables and vehicles. It would also provide 15 per cent exemption on tax to manufacturing companies that invest more than US$ 18.4 million in plant and machinery over FY 15. Further, the National Manufacturing Policy has set the goal of increasing the share of manufacturing in gross domestic product (GDP) to 25 per cent and to create 100 million jobs over the next decade. It is expected to get further boost by favourable provision in the existing budget 2014.

ROAD AHEAD

As per *Press Release (Media Reports, Department of Industrial Policy and Promotion (DIPP) statistic, Engineering Export Promotion Council, The Union Budget 2014-15).* India is fast moving from exporting low-value goods to developing countries to exporting high-value goods to developed countries. With development in associated sectors such as automotive, industrial goods and infrastructure, coupled with a well-developed technical human resources pool, engineering exports are expected to touch US$ 120 billion by 2015. "Engineering exports are likely to grow in India with the new government set to take bold decisions that will boost the sector," as per EEPC.

As per a report, India's share of global engineering process outsourcing is expected to reach US$ 40 billion by 2020, which will be 30 per cent of the total global market. The Indian electrical machinery industry is likely to double its sales to US$ 100 billion between 2012 and 2022.

The industry can also look forward to deriving revenues from newer services and from newer geographies with Big Data, Cloud, M2M and Internet of Things, becoming a reality.

Engineering Services Outsourcing (ESO) is a huge opportunity for India over the next few years. By 2020, the ESO market in India is expected to reach US$ 40–50 billion, driven by the increasing onshore to offshore movement of services.

The next couple of years may remain challenging for the engineering companies. While execution pace is slowing down due to various internal as well as macro issues, margins have also come under pressure due to rising input cost and competition.

DIRECT TAX PROPOSAL

- Investment allowance at the rate of 15 percent to a manufacturing company. This benefit to be available for three years i.e. upto 31.03.2017.

- Investment linked deduction extended to two new sectors, slurry pipelines for the transportation of iron ore, and semi-conductor wafer fabrication manufacturing units.

INDIRECT TAX PROPOSAL

- Exemption from excise duty on machinery, equipments, etc. required for setting up of compressed biogas plant (Bio-CNG) and solar energy production projects

- Export duty on bauxite increased from 10 percent to 20 percent

- Increase in basic customs duty on imported flat-rolled products of stainless steel from 5 percent to 7.5 percent.

OTHER PROPOSAL

- Production and exploitation of Coal Bed Methane reserves will be accelerated.

AGRICULTURE

Introduction

At 179.9 million hectares, India holds the second largest agricultural land in the world. A majority of the Indian population relies on agriculture for employment and livelihood. Steady investments in technology development, irrigation infrastructure, emphasis on modern agricultural practices and provision of agricultural credit and subsidies are the major factors contributing to agriculture growth.

The country has today emerged as a major player in the global agriculture market. As per Economic Survey 2014, as a concomitant of growth, the share of agriculture and allied sector in gross domestic product (GDP) declined to 15.2 per

cent during the Eleventh Plan and further to 13.9 per cent in 2013-14 (provisional estimates). Agriculture accounts for about 11 per cent of India's total exports; it is also an essential link in the supply chain of the manufacturing sector and at the same time constitutes a big market for industrial products. Currently, India is the world's largest rice exporter and second in terms of wheat exports. Horticulture exports have also seen good growth. India's agro exports during 2013–14 touched US$ 45 billion as against US$ 25 billion in 2011–12.

The Department of Agriculture and Cooperation under the Ministry of Agriculture is the nodal organisation responsible for development of the agriculture sector in India. The organisation is responsible for formulation and implementation of national policies and programmes aimed at achieving rapid agricultural growth through optimum utilisation of land, water, soil and plant resources of the country.

Market Size

As per Economic Survey 2014, substantial progress in acreage and production are recorded for 2013-14. As per the 3rd Advance Estimates (3rd AE) the acreage under foodgrains has increased to about 126.2 million ha; and to 28.2 million ha under oilseeds.

As per a study report, the agriculture sector in India is likely to grow in the range of 5.2–5.7 per cent in the 2013–14 agriculture year (July-June), nearly three times as compared to the previous year. In FY 12, total food grains production in India reached an all-time high of 259.3 million tonnes (MT). Rice and wheat production stood at 105.3 MT and 94.9 MT respectively.

Total exports of Indian agri and processed food products in the period April–February 2013–14 stood at US$ 20,331.05 million as compared to US$ 19,144.45 million during the corresponding period of the previous year, according to the Agricultural and Processed Food Products Export Development Authority (APEDA).

In 2012–13, the share of exports of 'agricultural and processed food products' in total exports rose to 13.53 per cent from 10.5 per cent share in 2010–11. Guar gum has emerged as India's largest item of farm exports with a share of 9.58 per cent during the period, followed by basmati rice and marine products.

On account of higher output in Assam and West Bengal, tea production in India in April–February, 2013–14 rose by 7 per cent to 1,152.91 million kg. The production was 1,073.93 million kg during the corresponding period of the previous year, according to data from the Tea Board.

INVESTMENTS

The foreign direct investment (FDI) inflows in agricultural services and machinery sector during April 2000–February 2014 stood at US$ 338.65 million and US$ 1,696.98 million respectively, as per data released by Department of Industrial Policy and Promotion (DIPP).

Government Initiatives

The Government of India is implementing many programmes for raising investments in agriculture. Notable among them are Rashtriya Krishi Vikas Yojana (RKVY); National Food Security Mission (NFSM); National Horticulture Mission (NHM); Gramin Bhandaran Yojana; Integrated Scheme of Oilseeds, Pulses, Oil palm, and Maize (ISOPOM), etc. The following are some of the major initiatives taken by the Government of India:

The government has allowed 100 per cent FDI under automatic route in storage and warehousing, including cold storages. Hundred per cent FDI is also permitted for development of seeds under the automatic route.

The government is promoting production of various organic inputs in the country, including bio-fertilisers under

the National Project on Organic Farming (NPOF). The project provides financial assistance up to 25 per cent of total financial outlay up to a ceiling of Rs 40 lakhs as credit linked back-ended subsidy for setting up bio-fertilisers production units.

The credit target for 2013–14 was Rs 7 trillion (US$ 116.06 billion). Further, the government on January 31, 2014 released Rs 180.22 crore (US$ 29.89 million) as grant-in-aid to states under the scheme to develop infrastructure facilities for production and distribution of quality seeds.

The Cabinet Committee on Economic Affairs (CCEA) has approved the implementation of the National Mission on Agricultural Extension and Technology (NMAET) during the 12th Five Year Plan with a total outlay of Rs 13,073.08 crore (US$ 2.17 billion). The mission aims to restructure and strengthen agricultural extension to enable delivery of appropriate technology and improved agronomic practices to farmers.

Further, in 2013–14, a pilot scheme on Nutri Farms was launched with an outlay of Rs 200 crore (US$ 33.18 million) to promote cultivation of bio-fortified food crops enriched with critical micro nutrients such as iron-rich bajra, protein-rich maize and zinc-rich wheat, etc., to improve the nutrition status of the most vulnerable sections of the country's population.

Road Ahead

With a population of about 1.2 billion, India requires a robust, modernised agriculture sector to ensure food security. The 12th Five Year Plan estimated a potential storage capacity expansion of 35 MT. Cold storage capacity also needs to grow rapidly from the current level of 24 MT. The government has targeted an overall growth rate of 4 per cent for the farm sector under the 12th Plan.

Indian agriculture is still heavily dependent on monsoon, due to inadequate irrigation; the performance of Agriculture Sector is prom to peril of weather condition.

The government proposed to link rivers will provide a much needed boost to the Agriculture Sector and will also reduce the dependency of the sector on weather condition especially monsoon in longer run.

BUDGET PROPOSALS

- Short term crop loan: Farmers to get further incentive of 3% for farmers who pay on time. Was already getting loan at 7%.
- Rs. 100 crore to provide to every farmer a soil health card and additional Rs. 56 crores to set up 100 Mobile Soil Testing Laboratories across the country.
- Rs. 100 crore to establish a "National Adaptation Fund" for climate change.
- Provide finance to 5 lakh joint farming groups of "Bhoomi Heen Kisan" through NABARD.
- Rs. 500 crore for establishing a Price Stabilization Fund, for mitigating Price volatility.
- Rs. 50 crores for the development of indigenous cattle breeds and an equal amount for starting a blue revolution in inland fisheries.
- Banks target of Rs. 8 lakh crore has been set for agriculture credit.
- NABARD operated the Rural Infrastructure Development Fund (RIDF): proposal to raise the corpus of RIDF by an additional Rs. 5,000 crores from Rs. 25,000 crores in interim budget.

- Rs 5000 crore for Warehouse Infrastructure Fund.
- Long term rural credit bank to provide support Rs 5000 crore to cooperative banks and RRBs, by NABARD.
- Rs 200 crore for proposed Producers' Organization Development Fund of NAABARD.
- Rs 100 crore for Kisan Television to provide real time information on various agriculture issues.
- Rs. 200 crore for Agriculture University in Andhra Pradesh and Rajasthan, and Horticulture University in Haryana, Telangana.
- Rs.1000 crore for proposed "Pradhan Mantri Krishi Sinchayee Yojna" for assured irrigation.
- Rs. 100 Crore for establishing two more institutions like Indian Agricultural Research Institute and Rs. 100 crores for setup of an "Agri-Tech Infrastructure Fund".
- Rs. 50,000 crore for Short Term Cooperative Rural Credit (STCRC) for credit flow to farmers and to avoid high cost market borrowings by NABARD.

INDIRECT TAX PROPOSALS

- Reduce excise duty from 10 percent to 6 percent on specified food processing and packaging machinery.

NANUBHAI DESAI & CO.
CHARTERED ACCOUNTANTS

Sir Vithaldas Chambers,
16, Mumbai Samachar Marg
Fort, Mumbai-400 001, INDIA.

Tel: +91 22 2204 2981, +91 22 2204 6359
Fax: +91 22 2288 0336
E-mail: admin@nanubhaidesai.com