



NEWSLETTER

APRIL
2011



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1 Accounting and Auditing

1. Expert Advisory Opinion

Revenue Recognition where sale value in foreign currency is covered by a forward contract

A. FACTS OF THE CASE

A listed manufacturing company with sales in the domestic as well as international markets has the following forex hedging strategy for currency risk:

1. The hedged exposure / forecasted cash flows are highly probable as they are based on the signed contracts, sales orders and purchase orders.
2. It maintains proper hedge documentation such as the forex policy, selection of hedge instruments, documents for each individual hedge undertaken etc.
3. There is always a one-to-one relation between the hedged exposure and the hedge instrument used by the company.
4. The relation of the hedged item vis-à-vis the hedge instrument is always effective and can be measured accordingly.

After entering into an export order, the company takes forward cover (for the same credit period as granted for sales) for the full amount of sales invoice which is receivable in the denominated foreign currency.

B. QUERY

1. Whether the exchange rate used to account the export sales should be:
 - a. The rate as on the date of the bill of lading, i.e. the date on which the property in the goods has passed on to the customer as per contract or
 - b. The rate as per the forward contract since finally the revenue will be realized from the customer at the forward rate as on the due date (assuming the payment is made as per the due date).
2. The exchange rate to be used to account the sales in case the customer fails to make the payment as on the due date as per the contract.

3. In case the company accounts for the export revenue based on the forward contract rate, will the company be complying the requirements as laid down in AS - 9, AS - 11, AS - 30, AS - 31 and AS - 32.

C. POINTS CONSIDERED BY THE COMMITTEE

1. The Committee noted that the query is related to the rate at which the export sales should be recognized and the treatment to be followed in case the customer fails to pay on the due date. The points such as accounting treatment of forward exchange contract taken to hedge the forex exposure, the treatment of changes in foreign exchange rates after initial recognition etc. have not been touched upon by the Committee.
2. As per paragraph 9 of Accounting Standard (AS) 11 : The Effects of Changes in Foreign Exchange Rates”

“A foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction.”

Hence, the Committee held that sales in the instant case should be recorded at the exchange rate as on the transaction date i.e. the date on which significant risks and rewards of ownership of goods are transferred to the buyer as referred to in paragraph 6.1 of Accounting Standard (AS) 9, ‘Revenue Recognition’.

3. The Committee further notes paragraphs 9.1 to 9.3 of AS 9, which provide for the basic parameters required for recognition of revenue such as measurability and certainty regarding collection towards such revenue.

Based on the aforesaid paragraphs, the Committee is of the view that revenue should not be recognized unless it is reasonably certain that the ultimate collection of the revenue will be made.

However, if uncertainty relating to collectability arises subsequent to revenue recognition, a separate provision for should be recognized based on Accounting Standard (AS) 4, ‘Contingencies and Events Occurring after the Balance Sheet Date’.

Thus in the case referred, at the balance sheet date, if it is probable that the receivables would not be recovered in future, a provision in that respect should be made as per the provisions of AS 4.

4. As regards the question raised by the querist relating to compliance with AS 9, AS 11, AS 30, AS 31 and AS 32, in case the company records revenue at the forward contract rate, the Committee clarifies that for accounting purposes:
 - a. The issue of recognition of revenue is independent of the accounting for foreign exchange transactions including hedging.
 - b. Accounting for foreign exchange transactions including hedging is governed by AS 11 and / or AS 30 depending upon the transaction. AS 31 is not relevant in the present case.
 - c. In case of highly probable forecast transactions where forward exchange contract is considered as cash flow hedge, the company should make disclosures as per the requirements of AS 32.

D. OPINION

1. The sales should be recognized at the rate on the date of the transaction, i.e., the date on which the significant risks and rewards of ownership of goods have been transferred to the buyer and not at the rate of forward exchange contract.
2. The revenue should not be recognized unless it is reasonably certain that the ultimate collection of the revenue will be made. However, if the uncertainty relating to collectability arises subsequent to recognition of revenue, a separate provision for the uncertainty should be recognized.
3. If the company accounts for revenue (sales) at forward contract rate, it will not be complying with the requirements of AS 9, AS 11, AS 30. AS 31 and AS -32 is not relevant in the present case.

2 Company Law

1. Dispatch of documents through electronic mode

The Ministry of Corporate Affairs (MCA) has notified that companies would be in compliance with Section 53 for dispatch of notice / other documents and Section 219(1) for dispatch of Annual Report, Balance Sheet etc in electronic form (e-mail) provided an advance opportunity is given to the member to register the e-mail address and changes therein from time to time with the company or with the concerned depository.

2. Limits raised for disclosures of employees salaries in Directors' Report

MCA has amended the Companies (Particulars of Employees) Rules, 1975 to disclose the details of employees drawing salaries not less than INR 60 lacs (INR 24 lacs earlier) per financial year / INR 5 lacs (INR 2 lacs earlier) per month in the Directors' Report approved by the Board of Directors on or after April 01, 2011.

3. Amendments to Director's Relatives (Office or Place of Profit) Rules, 2003

The following amendments vide Notification dated April 06, 2011 have been made:

- a. The monthly remuneration limits for appointment of relatives or partners of directors to an office or place of profit in companies [Section 314(1B) of the Companies Act] without the approval of the Central Government has been increased to INR 2.5 lacs (INR 0.5 lacs earlier).
- b. The appointment has to be approved by a selection committee which shall consist of independent directors and external expert in the respective field.. However for unlisted companies independent directors are not necessary but external experts in the respective field should be a part of the selection committee approving the selection of the relative to the office or place of profit in the company.

4. Certification of e-forms under the Companies Act by practicing professionals

For all electronic filing of documents under the Companies Act, practicing professionals registered as members of the professional bodies namely, ICAI, ICSI and ICWAI, are responsible of ensuring integrity of documents filed by them with MCA in electronic mode.

In addition to the penal actions against the companies and their officers in default for furnishing incorrect or false information in the documents as provided under the

Companies Act, 1956, action would also be initiated on receipt of any complaint, anonymous or otherwise, against such professionals also.

5. PAN Mandatory for Allotment of Director Identification Number (DIN)

In case of all Indian directors, Income Tax Permanent Account Number (PAN) will be a mandatory field while submitting the e-form DIN-4 through the MCA portal.

Further, in case of all existing DIN holders who have not furnished their PAN earlier at the time of obtaining DIN, have to furnish their PAN by filing DIN-4 eform by May 31, 2011.

6. Simplified procedure laid down for amalgamation of government companies

The MCA has simplified procedures that shall be adopted for the amalgamation of Government Companies under section 396 of the Companies Act, 1956.

7. General Cost Audit Orders issued for certain industries

The Cost Audit Branch of Ministry of Company Affairs has issued General Cost Audit Orders covering all Companies in the case of the under-mentioned Industries, meeting certain criteria of turnover / net worth/ borrowing / listing. Company covered under any of the above orders has to appoint a Cost Auditor within 90 days of commencement of the accounting year from which the above order becomes applicable to it.

Industries Covered	Net Worth Criteria	Turnover Criteria	Listing Criteria
<ul style="list-style-type: none">• Bulk Drugs• Formulations• Fertilizers• Sugar• Industrial Alcohol• Electricity• Petroleum• Telecommunications	Companies with net worth exceeding INR 5 crores are covered.	Companies with turnover (not of specific product) exceeding INR 20 crores are covered.	All companies, whether listed or to be listed, within or outside India are covered.
<ul style="list-style-type: none">• Cement• Tyres and Tubes• Steel Plant• Steel Tubes & Pipes	No net worth criterion required for coverage.	Companies with turnover (not of specific product)	All companies, whether listed or to be listed, within or

<ul style="list-style-type: none">• Paper• Insecticides		exceeding INR 100 crores are covered.	outside India are covered.
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8. Clarification for claiming exemption under section 212 of Companies Act

The MCA has clarified that, companies which desire to take benefit of the exemption (earlier notified vide Circular 02/2011) from publishing the financial statements of all the subsidiaries in its Annual Report, as mandated under section 212(8) of the Companies Act would have to fulfill all the conditions stipulated therein even if they are unlisted.

The clarification was issued in reply to representations from unlisted companies for removal of point (ii) mentioned in Circular 02/2011 which required all companies, willing to avail the exemption, to present in the annual report, the consolidated financial statements of the holding company and all subsidiaries duly audited by its statutory auditors.

9. Marking of companies having management dispute by ROC in MCA-21 system

The present electronic MCA-21 system provides the facility to the ROC to mark a company as “having management dispute” based on the complaints received by the ROC’s office. In case of such companies, the documents submitted remain unapproved till the ROC unmarks the same. As regards the marking system, the MCA has clarified that the marking will done only in cases where:

- a. The Court / CLB have directed to maintain the status quo with reference to any e-forms including the status of the directors in the said company
- b. The Court / CLB have granted injunction / stay in taking documents on record and the ROC is a party in such Court / CLB with directions being issued specifically to the ROC.
- c. In other cases, where the ROC is not a party and any such orders have been passed which have not been served to the ROC, the parties involved have to comply with such orders

10. Clarification on filing of e-form Form 32

The MCA has clarified that the ROC is not responsible for verifying the rightful claims / details of directors as submitted in e-form Form 32 in case of a dispute.

Further, the form 32 will be taken on records under the “Straight Through Process” (STP) mode i.e. the information given in the form will be taken on record by the ROC based on the statements of correctness given by the filing company and further verification of the said form by the practicing professional i.e. CA / CS, without any prejudice to the rights of the disputing parties to settle the dispute, if any, in any court of competent jurisdiction.

11. Appointment of agency for providing electronic platform for electronic voting

Section 192A of the Companies Act, 1956 read with the Companies (Passing of Resolution by Postal Ballot) Rules, 2001 recognizes voting by electronic mode by the postal ballot.

In order to have a secured electronic platform for capturing accurate electronic voting processes, the MCA has appointed National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited (CDSL) as agencies for providing and supervising the electronic platform used for electronic voting process by the companies subject to the condition that the above mentioned agencies obtain a certificate from Standardization Testing Quality Certification (STQC) Directorate, Department of Information Technology, Ministry of Communications and Information Technology.

12. Amendment in various forms

The MCA has revised the formats and included additional fields in e-forms viz, Form 2, Form 3, Form 18, Form 23C and Form 32 for online submission with effect from May 01, 2011.

Form 2: - Used for filing an application with Registrar of Companies (ROC) for return of allotment of shares.

Form 3: Used for filing an application with Registrar of Companies (ROC) for furnishing the details of contract relating to shares allotted for consideration other than cash.

Form 18: Used for filing an application with Registrar of Companies (ROC) for notifying the situation or change of situation of the company’s Registered Office.

Form 23C: Used for filing an application with Registrar of Companies (ROC) for applying to the Central Government for appointment of a cost auditor.

Form 32: Used for filing an application with Registrar of Companies (ROC) for intimating the ROC about details of appointment and changes therein of Managing Director, directors, manager, secretary etc.

3 Service Tax

1. Effective Date of applicability of service tax on new / amended services

Subsequent to Budget 2011, the Ministry of Finance vide its various notifications issued during April 2011 has made amendments/additions in respect of various services. Further it has notified May 01, 2011 as the effective date of applicability of service tax on such services covered by the above mentioned notifications.

2. Exemption provided to medical services

Full exemption with effect from May 01, 2011 has been provided to the services provided by any hospital, nursing home or multi-specialty clinic to any person for any health check-up or preventive care [covered under clause 105 (zzzz) of Section 65 of the Service Tax Act]. The tax on the said services was introduced with effect from July 2010.

3. Exemption withdrawn in respect of representation services provided

Existing exemption (under Notification No. 25/2006) for levy of service tax provided to services provided by a practicing chartered accountant / cost accountant / company secretary to clients, relating to representation before any statutory authority in the course of proceedings under any law, has been withdrawn with effect from 1st May 2011.

4. Exemption provided pursuant to enhanced coverage in Budget 2011

The Budget 2011 enhanced / modified the scope of “Commercial Training or Coaching Services” to cover all courses that are not recognized by law even if the “Commercial Training Centre (Institutes)” provides any other course recognized by any law in force. However, exemption is restricted to

- any preschool coaching and training
- any coaching or training leading to grant of a certificate or diploma or degree or any educational qualification which is recognized by any law

5. New services introduced in Budget 2011 notified

Service tax is applicable to following services with effect from May 01, 2011:

- a. Services provided by an air-conditioned restaurant and having license to serve alcoholic beverages, in relation to serving of food or beverage, including alcoholic beverages or both, in its premises [covered under clause 105 (zzzzv) of Section 65 of the Service Tax Act]. Further clarifications have been issued regarding whether service tax will be applicable in case of room service, service outside the restaurant (pool / open area) etc.
- b. Services provided by a hotel, inn, guest house, club or campsite in relation to providing of accommodation for a continuous period of less than 3 months [covered under clause 105 (zzzzw) of Section 65 of the Service Tax Act]. Subsequent clarifications have been issued relating to meaning of Tariff including in cases where there are differential tariff, seasonal tariff etc, taxability in case food is included in Tariff etc

6. Clarification - Services provided by visa facilitators chargeable to Service Tax

The Ministry of Finance has clarified that services provided in relation to assistance by a visa facilitator, for obtaining visa (such as procurement of visa, completion of immigration formalities etc) to a visa applicant or for foreign employer does not fall within the scope of “supply of manpower service”. Accordingly, the said services are not chargeable to Service Tax.

7. Clarification - Benefit of exemption not to be available to sub-contractors

The Ministry of Finance has clarified that, services provided by various Sub-Contractors such as Architect’s Service, Consulting Engineer’s Service, Construction of Complex Service, Design Services, Erection Commissioning or Installation Service, Management, Maintenance or Repair Service etc. in relation to Works Contract Service (WCS) in respect of construction of Dams, Tunnels, Road, Bridges etc are not exempt under Service Tax since they are specifically covered under various sub-clauses in (105) of section 65 of the Act. The WCS services rendered by the Main contractor to Owners will continue to be exempt.

In view of the above, above services cannot be covered under WCS and Service Tax will be chargeable / exempted as per provisions mentioned in the specific sub-clauses in (105) of section 65 of the Act, as applicable to such sub-contractors.

4 FEMA

1. Interest on Bank Deposits

The interest on deposits kept with Savings Bank Account, Non Resident (Ordinary) account and Non Resident (External) account have been raised by 0.50 percent. Accordingly, the interest rates earned in these accounts will be increased from 3.5 percent to 4 percent.

2. Liquidation of Post-Shipment Rupee Export Credit

Earlier, the Post-Shipment credit could be liquidated only by the proceeds of the export bills in respect of goods exported / services rendered. Further, subject to the mutual agreement between the bank and the exporter the Post-Shipment credit could also be liquidated / repaid out of balances in the Exchange Earners Foreign Currency (EEFC) Account or proceeds from any other unfinanced export bills.

However, from now the exporters with over due export bills can repay their overdue Post-Shipment Rupee Export Credit from their rupee resources.

3. Liberalization for imports

The limit for advance remittance for import of goods without standby Letter of Credit (LC) or bank guarantee has been raised from USD 100,000 to USD 200,000.

4. Reduction in terms of Trade Credit

Reserve Bank of India (RBI) has reduced the term of Suppliers' and Buyers' credit (trade credit) including the usance period of Letters of Credit opened for import of rough, cut and polished diamonds from upto 1 year to upto 90 days from the date of shipment.

5. Pledge of Shares for Business Purpose

Under the extant regulations, pledge of shares by Non Resident Investors in respect of FDI transactions required prior approval of RBI. RBI has now liberalized the regulations and delegated powers to Authorized Dealer Category I Banks (Banks) to allow pledge of shares of Indian company held by non resident investors in the following cases:

- a. Pledge in favour of an Indian bank to secure credit facilities for the resident investee company, subject to the following:

- i. In case the pledge is invoked, the transfer of shares should be in accordance with the FDI policy in vogue at the time of creation of pledge
 - ii. A declaration/ annual certificate from the statutory auditor of the investee company that the loan proceeds will be / have been utilized for the declared purpose should be submitted
 - iii. The Indian company has to follow the relevant SEBI disclosure norms
- b. Pledge of shares of an Indian company, held by non – resident investor, in favour of an overseas bank to secure credit facilities for the non resident investor/promoter of the Indian company or its overseas group company:
- i. Loan is availed only from an overseas bank
 - ii. Loan is utilized for genuine business purposes overseas and not for any investments either directly or indirectly in India
 - iii. Overseas investment should not result in any capital inflow into India
 - iv. In case the pledge is invoked, the transfer should be in accordance with the FDI policy in vogue at the time of creation of pledge
 - v. A declaration/ annual certificate from a Chartered Accountant/ Certified Public Accountant of the non-resident borrower that the loan proceeds will be / have been utilized for the declared purpose should be submitted.

6. Permission to open Escrow Accounts:

The erstwhile regulations permitted Banks to open Escrow accounts and special accounts on behalf of non – resident corporate entities only for the purpose of acquisition / transfer of shares / convertible debentures through open offers/ delisting/ exit offers, subject to compliance with the relevant SEBI regulations. In all other cases of opening/maintaining of Escrow accounts for FDI related transactions, the prior approval of RBI was required.

RBI has now permitted the Banks and SEBI authorized Depository Participants to open Escrow accounts in Indian Rupees on behalf of Residents / Non-Residents towards the payment of share purchase consideration and / or provide Escrow facilities for keeping securities to facilitate FDI transactions. These facilities will be applicable for both issue of fresh shares to the non- residents as well as transfer of shares from / to the non- residents.

Some of the conditions applicable to the Escrow account are given below:

- a. These accounts shall be non-interest bearing.
- b. No fund or non fund based facilities would be permitted against the balances in the escrow account.
- c. For the purposes of FDI reporting, the date of transfer of funds into the bank account of the issuer / transferor of shares shall be the relevant date of remittance.
- d. The Escrow account shall remain operational for a period of six months from the date of opening. The account shall be closed immediately after the completion of six months. Prior permission of RBI will be required in case the period of operation is to be extended beyond six months.
- e. The following are the permissible credits and debits into the Escrow Account.
 - i. **Permitted Credits into the Escrow account:**
 - Receipt of foreign remittance from non - resident for issue or transfer of shares
 - Receipt of rupee consideration by resident acquirer of shares from non – resident sellers.
 - ii. **Permitted debits from the Escrow account:**
 - Payment for issue / purchase of shares to resident seller / issuer or non – resident seller.
 - Remitting the balance funds to the investor or the entire funds in case the transaction does not materialize.

7. Payment guarantee on behalf of FIIs

Foreign Institutional investors (FIIs) are allowed to purchase shares or convertible debentures of an Indian company under the Portfolio Investment Scheme ('PIS'). However no fund or non – funds based activities are permitted to be undertaken by the FIIs.

Custodian banks are now allowed to issue Irrevocable Payment Commitments ('IPC') in favour of stock exchanges / clearing corporations of stock exchanges, on behalf of their FII clients. The issue of IPCs on behalf of the FIIs shall be in accordance with the RBI regulations on banks' exposure to capital markets.

8. Enhancement of limit for investment by FIIs in Corporate Bonds

The limit for investment in corporate bonds / non convertible debentures by FIIs has been increased as under:

No.	Corporate Bonds	Existing Limit	New Limit
1	Infrastructure Companies only, with a residual maturity of five years or more.	USD 5 billion	USD 25 billion
2	All Companies including Infrastructure companies	USD 15 billion	USD 15 billion

FIIs are also now permitted to invest in unlisted bonds of the infrastructure companies with a minimum lock in period of 3 years, however lock in would not be applicable for sale to other FIIs.

5 Income Tax – Case Laws

1. Large volume in shares not deciding factor to hold assessee trader

Ramesh Babu Rao vs. ACIT (ITAT Mumbai)

Facts: The assessee, a retired professor, offered gains from sale of shares as Short-term capital gains (STCG). In the return of income, the gain from sale made upto 30.09.2004 was offered as business income whereas the gain on sale made after 30.9.2004 was offered as capital gains. This was done since the Securities Transactions Tax (STT) was introduced w.e.f.1.10.2004 and making STCG which has suffered STT liable to tax at 10%.

The AO assessed the gains as business profits on the grounds that in the earlier years, the assessee had offered similar gains under “Income from business” and the volume of transactions was higher in the year under consideration. On appeal, the CIT (A) reversed the order of the AO relying on various decisions which held that the entries in the books of accounts should not be taken as a basis but the same is not to be ignored without a firm basis. He also held that the ratio of the turnover to the capital employed by the assessee was also not as huge as that of a regular trader.

Issue: Whether large volume of transactions in shares is a deciding factor to hold assessee as a trader?

Held: The H’ble ITAT confirming the decision of CIT(A) held that the assessee was an investor and the gains are assessable as capital gains due to the following reasons:

- a. Large volume cannot be a deciding factor to hold a person as a trader since the large turnover was because of bulk purchases and sales in a scrip. There were very few transactions of purchase and sale, as the assessee was purchasing in block of a particular share in large volume.
- b. The assessee was not a broker or sub-broker and did not do any speculative activity nor indulge in any sales without delivery. He did not have any office establishment. Further, the assessee was a good timer of purchase and sale of shares thereby substantially increasing his gains in the stock market
- c. The shares were shown as capital assets in the books of account;
- d. The assessee had not pledged any shares nor borrowed any funds.

2. Notional interest on interest-free security deposit is not includible in income from house property

Moni Kumar Subba vs. CIT (Delhi High Court – Full Bench)

Facts: The assessee had let out a house property for which she received a rent of Rs. 6.95 lakhs and an interest-free security deposit of Rs. 8.58 crores. The property was not subject to the Rent Control Act. The assessee considered Rs. 6.95 lakhs for determining the 'annual value' of the property. The AO determined the 'Annual Value' (ALV) u/s. 23(1)(a) by adding Rs. 30.41 lakhs of notional interest. The CIT (A) and Tribunal deleted the addition made by the AO and held that the notional interest could not be added either u/s. 23(1)(a) or u/s. 23(1)(b). On appeal by department, the matter was referred to the full bench.

Issue: Whether notional interest on interest-free security deposit is includible in income from house property?

Held: The H'ble High Court held that S. 23 (1)(a) requires determination of the "fair rent" being "the sum for which the property might reasonably be expected to let from year to year". The AO has to make an inquiry as to what would be the possible rent that the property might fetch. The AO may consider various factors while determining the fair rent though no particular test can be laid down and it would depend on facts of each case.

If he finds that the actual rent received is less than the "fair/market rent" because the assessee has received abnormally high interest free security deposit, he can undertake necessary exercise in that behalf. However, by no stretch of imagination, the notional interest on the interest free security deposit can be taken as determinative factor to arrive at the "fair rent".

The ALV fixed by the municipal authorities can be the basis of adopting the ALV for purposes of s. 23. However, the AO can ignore the municipal valuation for determining the ALV if he finds that the same is not based on relevant material for determining the "fair rent" in the market and there is sufficient material on record for taking a different valuation.

Note: In a recent decision by the H'ble Mumbai Tribunal in **Tivoli Investment and Trading Co v/s ACIT** it was held that if the AO finds that the actual rent received is less than the fair market rent because of the abnormally high interest-free security deposit, he can undertake necessary exercise in that behalf. However, the notional

interest on interest free security cannot be taken as determinative factor to arrive at fair rent.

3. Non residents are required to file the return of income in India even if the income is not chargeable to tax

VNU International B.V. [Authority for Advance Rulings (Income-tax)]

Facts:

- The applicant, VNU International B.V. (VNU), a Netherlands company is a 100% holding company of AC Nielsen ONG-MARG Pvt Ltd. (ACNOM), an Indian company.
- In 2003, under the Scheme of Arrangement, retail research business of ACNOM was demerged into ORG-IMS Research Pvt. Ltd. (ORG-IMS), an Indian company. Consequently, VNU received shares of ORG-IMS. VNU transferred shares of ORG-IMS to IMS-AG, a company incorporated in Switzerland. As per India-Netherlands Tax Treaty, gain arising, inter alia, on transfer of shares by tax resident of Netherlands is taxable only in Netherlands.

Issue: Whether the applicant is required to file a return of income under section 139 of the Act even when capital gain on sale of shares is not taxable in India?

Held: The H'ble AAR held that as per Article 13(5) of the India – Netherlands tax treaty the capital gains is taxable in the Netherlands and hence no liability arises on the Indian company to deduct tax u/s 195 of the Act.

Regarding filing of return of income, the authority ruled that the applicant is required to file the return of income as per the provisions of section 139 of the Act. The third proviso to section 139, while casting obligation to file return of income by a company, states that every company is required to file its return of income, **whether it has an income or a loss.**

In contrast, a person other than a company or a firm, is required to file return of income only if his/its total income “exceeded the maximum amount which is not chargeable to income-tax”. However, in case of company assessee, the legislature has omitted to include the expression “exceeded the maximum amount which is not chargeable to income-tax”. Where it is not necessary for a non- resident to furnish return under section 139(1) of the Act, the statute has specifically provided so e.g. under section 115AC(4) of the Act. Applicant is a foreign company under section 2(17) and therefore, for the above reasons, the Authority ruled that a non resident

company is required to file the return of income under section 139 of the Act even when its income by way of capital gain is not liable to tax in India.

4. Failure to apply s. 50C does not attract penalty u/s 271(1)(c)

Renu Hingorani vs. ACIT (ITAT Mumbai)

Facts: The assessee sold a flat for Rs. 63 lakhs and offered capital gains on the same, while stamp duty valuation was Rs. 72 lakhs. The AO added the difference of Rs. 9 lakhs to sale consideration and computed the capital gain accordingly. The same was accepted by the assessee. However, the AO levied penalty u/s 271(1)(c) which was confirmed by the CIT (A).

Issue: Whether failure to apply s.50C attracts penalty u/s 271(1)(c)?

Held: The H'ble ITAT held that the AO has not questioned the actual consideration received by the assessee and has made addition purely on the basis of application of provisions of s.50C. The assessee has not failed to furnish the relevant record as called by the AO and thus it does not amount to concealment of income or furnishing of inaccurate particulars of income. Merely because the assessee agreed for addition on the basis of stamp duty valuation, it would not be the conclusive proof that the sale consideration as per the agreement was incorrect & wrong. Accordingly, no penalty u/s 271(1)(c).

5. S. 14A disallowance of interest on borrowings on ground that assessee ought not to have used own funds for tax-free investments invalid

CIT vs. Gujarat Power Corporation (Gujarat High Court)

Facts: The assessee borrowed sum of Rs.3.83 crores on which it paid interest of Rs.17.31 lakhs. Further the assessee had also made investment of Rs.30.79 crores in shares, debentures and bonds and earned tax free income of Rs.5.68 crores. The AO disallowed the interest paid of Rs. 17.31 lakhs on the ground that if the assessee had not invested its own funds for earning tax-free income, it could have utilised the same for its business instead of borrowing interest bearing funds for its business and so there was a nexus between the borrowed funds and the tax free income. This was reversed by the CIT (A) and Tribunal on the basis that the assessee was justified in arranging its affairs so as to reduce the tax liability and that it was the right of the assessee to use its own funds in the manner in which it considers proper.

Issues: Whether disallowance of interest on borrowings u/s 14A can be made on ground that assessee ought not to have used own funds for tax-free investments?

Held: The Hon'ble High Court held that the assessee had made majority of the investments in tax free securities even before it obtained loan and only a small portion of investment was made subsequently. It was not disputed by the AO that borrowings have been used for the purpose of business. The assessee also had other sources of funds out of which the investments were made. While concurring with the views of the Tribunal, it was held that as borrowed funds were not used for earning tax-free income, no part of interest should be disallowed u/s. 14A.

6. CBDT Circular which specifies that for s. 40(b)(v), the partnership deed should specify the remuneration, is invalid

M/s Durga Dass Devki Nandan vs. ITO (HP High Court)

Facts: The assessee is a partnership firm and remuneration clause in its partnership deed states that its partners would be "working partners within the meaning of s. 40(b)" and "be paid a monthly salary as per the income-tax provisions". The AO relied on CBDT Circular No. 739 dated 25.3.1996 and held that since the deed did not specify the amount of remuneration payable to the partner or lay down the manner of quantifying such remuneration, the deduction was not admissible under the Act. This was reversed by the CIT (A). However, the Tribunal upheld the order of the AO on the ground that the agreement did not meet with the requirements of the circular and so deduction of salary paid to the partners was not admissible.

Issue: Whether partners' remuneration will be disallowed if the deed mentions that the remuneration shall be as per the provisions of the Act instead of specifying the amount of remuneration & method adopted for quantification as per the CBDT circular?

Held: The H'ble High court held that Section 40(b)(v) allows a deduction of payment of remuneration to working partners if it is authorized by the partnership deed and not in excess of the limits as prescribed therein. It does not lay-down any condition that the partnership deed should fix the remuneration or the method of quantifying remuneration. Accordingly, CBDT circular No. 739 dated 25.3.1996 which requires that either the amount of remuneration payable to each individual should be fixed in the agreement or it should lay down the manner of quantifying such remuneration goes beyond s. 40(b)(v).

The CBDT cannot issue a circular which goes against the provisions of the Act. It can only clarify issues but cannot insert terms and conditions which are not part of the main statute. A partnership deed which provides that the remuneration would be as per the provisions of the Act meaning thereby that the remuneration would not

exceed the maximum remuneration provided in the Act is valid and deduction is admissible and therefore, the assessee is entitled to the deduction.

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