NANUBHAI DESAI & CO.

June 2010 Part - II

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Contents

INCOME TAX

DOMESTIC TAXATION

GENERAL

Amendments to the TDS Rules

The Central Board of Direct Taxes (CBDT), vide issuance of a notification, has amended the rules relating to provisions dealing with date and mode of payment of Tax Deducted at Source (TDS), issuance of TDS certificate and filing of 'statement of TDS' (TDS return). Forms for TDS certificate have been revised to include the receipt number of the TDS return filed by the deductor. As per the notification, the Tax-deduction Account Number (TAN) of the deductor, Permanent Account Number (PAN) of the deductee, and receipt number of TDS return filed by the deductor will form the unique identification for allowing tax credit claimed by the taxpayer in his income-tax return.

Government Authorities (Pay and Accounts Officer or Treasury Officer or Cheque Drawing and Disbursing Officer) responsible for crediting tax deducted at source to the credit of the Central Government by book-entry are now required to electronically file a monthly statement in a new Form No. 24G containing details of credit of TDS to the agency authorised by the Director General of Income-tax (Systems).

Due date for furnishing TDS return for the last quarter of the financial year shall now be 15th May (from earlier 15th June). The revised due dates for furnishing TDS return are as under:

Date of ending of the quarter of the financial year	Due Date
30th June	15th July of the financial year
30th September	15th October of the financial year
31st December	15th January of the financial year
31st March	15th May of the financial year immediately following the financial year in which deduction is made

Due date for furnishing TDS certificate to the employee or deductee or payee is revised as under:

Category	Periodicity of furnishing TDS certificate	Due date
Salary (Form No.16)	Annual	By 31st day of May of the financial year immediately following the financial year in which the income was paid and tax deducted.
Non-Salary (Form No.16A)	Quarterly	Within fifteen days from the due date for furnishing the statement of tax deducted at source under rule 31A

Tax exemption for gratuity

The CBDT has notified that the maximum amount of gratuity entitled to exemption under sub-clause (iii) of clause (10) of section 10 of the Income Tax Act 1961, is Rs. 1,000,000. The notification will be applicable to employees who retire, or become incapacitated before retirement, or expire, or whose services are terminated, on or after the 24th May 2010.

CASE LAWS

Pirojsha Godrej Foundation vs. ADIT (ITAT Mumbai)

Returns processed under section 143(1) (a) cannot be reopened for reassessment under section 147 without justified "reasons to believe"

Pirojsha Godrej Foundation ("the assessee") was a charitable trust and was duly granted registration by the Commissioner of Income Tax, under section 12 A of the Income Tax Act and was also notified, for the relevant period, under section 10(23C) (iv) of the Act. The income tax return filed on 29th October, 2001, was processed under section 143(1) (a). However, on 26th May, 2004, the assessee was served a notice under section 148 and income of the assessee was proposed to be reassessed. The notice was issued on the ground that as the assessee had not invested the sum of Rs. 1.02 crores in investments specified under section 11(5), the said sum of Rs. 1.02 crores was chargeable to tax. Aggrieved by the Assessing Officer's ("AO's") proposal for re-opening of the assessment, assessee preferred an appeal before the CIT (A) but CIT (A) confirmed the action of the AO.

Aggrieved by the order of CIT (A), the assessee filed an appeal before the Tribunal.

Decision of the Tribunal

The Tribunal has allowed the appeal. The Tribunal held that:

- The reason that the violation of Section 11(5) read with section 13(1) (d) by the assessee led the amount of Rs. 1.02 crores to be included in the assessee's total income was contrary to the legal position. This did not result in the said amount being chargeable to tax in the hands of the assessee. The fact that the amount was not invested in the prescribed manner did not mean that it could be assessed as income.
- The reasons were required to be self explanatory and read as recorded by the assessing officer. No substitution, addition or deletion was permissible. No inference could be allowed to be drawn on the basis of reasons not recorded.
- The fact that only an intimation was passed under section 143(1) (a) was irrelevant because it was important to inquire whether the AO had proper "reasons to believe" that income had escaped assessment. In the absence of proper "reasons", the reopening was invalid.

Dr. Mansukh Kanjibhai Shah vs. ACIT (ITAT Ahmedabad)

Order under section 153A void if search warrant under section 132 was improper, assessee can retract admission of undisclosed income

Initially, survey action under section 133A of the Act was carried out at the premises of a trust in which Dr. Mansukh Kanjibhai Shah ("the assessee") was the Managing Trustee, which led to detection of unaccounted bank accounts. The assessee admitted unaccounted income of Rs. 1.93 crores. Search under section 132 was conducted on 29.10.2004 and cash of Rs. 1.93 crores was found and seized. The search warrant was in the names of "K. M. Shah Charitable Trust, Mansukhbhai K. Shah" (the trust and the assessee). The assessee retracted the admission on 24.12.2004. An assessment order under section 153A was passed in which the said sum was assessed in the hands of the assessee. The assessee challenged the validity of the proceedings under section 153A of the Act on the ground that the warrant was not in his name and there was no search under section 132. Hence, he could not be assessed under section153A. The CIT (A) held that the assessment under section 153A was valid on the finding that a search under section 132 had been conducted in the name of the assessee.

Decision of the Tribunal

Aggrieved by the order of CIT (A), the assessee preferred an appeal before the Tribunal. The Tribunal allowed the appeal and held that:

- The AO, to assume jurisdiction under section 153A, was required to fulfill following conditions:
  - The warrant of authorization should have been issued in the name of the assessee,
  - It should have been served on the assessee and,
  - A search had to be conducted on the assessee.
- The warrant of authorization issued under section 132 could not be regarded as issued in the name of the assessee in his individual capacity as the same was issued in the name of "K. M. Shah Charitable Trust, Mansukhbhai K. Shah". The assessee's name had appeared in the warrant and panchnama as the Managing Trustee of the Trust and not in his individual capacity. The search could not be regarded as conducted against the assessee in his individual capacity. When a warrant was issued in joint names, an assessment in individual capacity/status was invalid. Consequently, the section 153A proceedings were invalid.
- The assessee admitted on oath that the amount deposited in the accounts of the Trust was his unexplained personal money; however this was not conclusive as it had been retracted. An assessee was entitled to show that the admission was not correct or true. No independent or corroborative evidence was found to show that the money deposited in the bank account of the Trust belonged to the assessee in his individual capacity.

ACIT vs. GTL Ltd (ITAT Mumbai)

Retrospective amendment after passing order does not lead to "apparent mistake"

GTL Ltd. ("the assessee") had filed a return of income for the A.Y 1998-99 declaring the total income at Rs.11,62,10,850/- under section115JA of the Act. The AO had completed the assessment by passing an order which was subsequently rectified and modified on three other occasions. The AO after passing the rectification orders, had noticed that the provision of doubtful debts of Rs.18,99,254/- was not added back to the profit & loss account while computing deduction under section 115JA of the Act. The AO had subsequently passed an order under section 154 of the Act adding back the provision for doubtful debts under section 115JA of the Act. The assessee had challenged the order before CIT(A) who allowed the same relying upon the decision of the Bombay High Court in the case of CIT vs. Echjay Forgins (P) Ltd. [251 ITR 15]. The revenue had preferred an appeal against the order of CIT(A) before the Tribunal. The Tribunal confirmed the order of the CIT (A).

Thereafter, by the Finance Act, 2009 clause (g) had been inserted in Explanation to Section 115JA(2) of the Act w.r.e.f. A.Y. 1998-99 and subsequent years inter alia providing that provisions for doubtful debts and advances were disallowable while calculating profit under section 115JA of the Act. The amendment received the assent of the President on 19.8.2009, after the order of the Tribunal was passed.

The revenue had relied on the decision of the Karnataka High Court reported in 239 ITR 282 in support of its contention that an order which was not in accordance with the retrospective law could be rectified under section 154 of the Act. The Revenue preferred a miscellaneous application before the Tribunal contending that in view of the said retrospective amendment, there was a "mistake apparent from the record". While the assessee submitted that the revenue had not been able to point out the mistake apparent from record of the order on the date when it was passed.

Decision of the Tribunal

The Tribunal dismissed the Miscellaneous Application. The Tribunal agreed with the assessee that there was no mistake apparent from record in the order of the Tribunal. The Tribunal relied on the decision of Bombay High Court in Sudhir Mehta 265 ITR 548, where an order of the Tribunal was passed as per the prevailing law. The Bombay High Court in that case held that the proceedings got concluded before the Tribunal under the then existing law and, therefore, there was no mistake apparent from record in the order of the Tribunal.

INTERNATIONAL TAXATION

CASE LAWS

Hindalco Industries Limited vs. DCIT (ITAT Mumbai)

Despite TDS u/s 195, payer is liable as "agent" u/s 163. However, if payee is assessed, payer cannot be assessed as "representative assessee".

Facts of the case:

Alcam Aluminium Limited ("Alcan") was a company incorporated under the laws of Canada. After taking necessary approval from the Reserve Bank of India from time to time, Alcan had acquired 3,88,44,324 shares in Indian Aluminium Company Limited ("Indal") over a period of time. Alcan sold its entire holdings in Indal to Hindalco Industries Limited ("Hindalco"). It was prima facie evident that Alcan would be liable to pay tax in respect of gains made from sale of shares in Indal, since it would be governed by the provisions of section 45 read with section 48 of the Income Tax Act, 1961 ('the Act'). Under the provisions of section195 of the Act, any person responsible for paying to a non-resident any sum chargeable to tax under the Act, had an obligation to deduct income tax at the time of making payment at the rates in force. Under section 197(1) of the Act, the recipient of the payment could make an application to the AO for issue of a certificate regarding no deduction of tax or deduction of tax at a lower rate by the person making payment. Having regard to these provisions, Alcan filed an application under section 197(1) for issue of a TDS certificate on the basis that the capital gain was Rs. 317.71 crores and tax at the rate of 10% would be chargeable. The Assessing Officer ('AO') issued a certificate directing Hindalco to withhold Rs. 40 crores on a provisional basis subject to regular assessment. Hindalco complied with the same. During the pendency of the assessment proceedings against Hindalco, the AO issued an order under section 163 treating Hindalco as an agent of Alcan in respect of the capital gains. Thereafter, on 15.3.2004, the AO passed an order assessing the capital gains in the hands of Hindalco as an agent of Alcan in which, the rate of tax was taken at 20%. On 16.3.2004, an assessment order was passed in the case of Alcan itself, assessing the capital gains in its hands at the rate of 20%.

Against the order dated 20.2.2004, treating Hindalco as an agent of Alcan under section 163(1) of the Act, Hindalco filed an appeal before learned CIT(A), who, by order dated 21.2.2005, dismissed the said appeal. Against this order, Hindalco had filed appeal before the Tribunal. Against the order of the AO assessing capital gain in the hands of Hindalco as an agent of Alcan, Hindalco filed an appeal before learned CIT(A) who by order dated 31.3.2005 confirmed the assessment but deleted the levy of interest u/s. 234B of the Act. Against the said order of learned CIT (A), Hindalco and the revenue, both had filed appeal before the Tribunal.

Contentions of Hindalco Industries Limited:

The contentions were as follows:

- Hindalco stated that it could not be treated as an agent and representative assessee of Alcan under section 163 of the Act as the conditions contemplated under section 163 were not satisfied.

- It further stated that it had duly deducted tax at source as contemplated under section 195 of the Act and in such cases; it could not be again treated as an agent and representative assessee of Alcan.

- The order treating Hindalco as an agent of Alcan had been passed on 20.2.2004 i.e. after a period of two years and ten months from the end of the previous year in which Hindalco made payment to Alcan.

Contentions of the revenue:

The AO, by order dated 20.2.2004, treated Hindalco as an agent of Alcan for the following reasons:-

- Section 163(1) deals with 'Representative assessee-Special cases'. The relevant provisions of section 163(1) are given as under :-
  "For the purposes of this Act, 'agent' in relation to a nonresident includes any person in India-
  i) *Who is employed by or on behalf of the non-resident; or*
  ii) *Who has any business connection with the nonresident; or*
  iii) *From or through whom the non-resident is in receipt of any income, whether directly or indirectly; or*
  iv) *Who is the trustee of the non-resident; and includes also any other person who, whether a resident or nonresident, has acquired by means of a transfer, a capital asset in India………"*

- For the relevant A.Ys. i.e. 2001-02, the following facts were well established;

  – Hindalco had business connection with the non-resident i.e. Alcan
  – Alcan was in receipt of income directly from Hindalco, and

– Hindalco had acquired a capital asset in India by means of transfer from Alcan.

- Section 160(1)(i) clearly states that *'for the purpose of this Act, 'representative assessee' means :-*
  i) in respect of the income of a non-resident specified in sub-section(1) of section 9, the agent of the non-resident, including a person who is treated as an agent under section 163.

- Further, section 149(3), which prescribes the time limit for notice to be issued under section 148 for re-opening an assessment, stipulates the following :-
  "If the person on whom a notice under section 148 is to be served is a person treated as the agent of a non-resident under section 163 and the assessment, or re-computation to be made in pursuance of the notice is to be made on him as the agent of such non-resident, the notice shall not be issued after the expiry of a period of two years from the end of the relevant assessment year."

  In the present case, the relevant A.Y. was 2001-02, and thus notice under section 148 could be issued in the case of Hindalco for A.Y.2001-02 till 31.3.2004. This time limit had not expired.

On the basis of the above, Hindalco was held to be a representative assessee in relation to Alcan as it fulfilled the conditions laid down in section 163(1)(b) and section 163(1)(c) and further it had acquired from Alcan, a non-resident, capital asset in India by way of transfer of shares during A.Y. 2001-02.

Contentions of CIT (A):

- The CIT (A) stated that section 163 did not provide for a bar on taking action against a person where the conditions prescribed in the section were satisfied, merely for the reason that the non-resident had filed the return of income independently. The courts had held that there was no bar on the simultaneous assessment of the principal and agent.

- The CIT (A) further stated that Hindalco had obtained a certificate for deduction of tax at source under section 197, but that will not invalidate action taken by the AO under section 163. The proceedings under section 195 / 197 for deduction of tax at source and proceedings under section 163 were two separate proceedings. Thus the CIT (A) concluded that proceedings could be taken against the agent as representative assessee both for assessment as well as for recovery.

Analysis by the Tribunal:

The Tribunal dealt with the decision of the Kerala High Court decision in the case of Fertilizers & Chemicals (Travancore) Ltd., where the non-resident was having several representative assessees in respect of several heads of income and in this context, the High Court observed that there could be more than one assessment in respect of the income accrued or arisen to a non-resident provided, there were more than one representative assessees. The High Court meant that if some other income had been assessed in the case of the non-resident, the AO had jurisdiction to frame assessment on the agent of the non-resident in respect of some income that arose to the non-resident through the agent. This decision of the Kerala High Court was held not to be interpreted to mean that the same income could be assessed simultaneously in the hands of the non-resident and in the hands of the agent. The Tribunal held that such double taxation would go against the cardinal principles for levying tax on income. The Tribunal further held that when once assessment in the case of principal becomes final, the assessment of the same income in the hands of the agent could not be made.

Decision by the Tribunal:

- The Tribunal held that the income having been brought to a charge of tax in the hands of the principal could not be once again assessed in the case of a representative assessee. Therefore, the assessment of capital gains of Alcan in the hands of the Hindalco as agent of Alcan could not be sustained. The assessment order was, therefore, annulled.

- The Tribunal further stated that the only issue raised by the department pertained to deletion by the learned CIT (A) of the interest charged under section 234B. Since the relevant orders had already been quashed by the Tribunal while deciding the assessee's appeal, the departmental appeal was rendered infructuous and was liable to be dismissed on that ground.

- The appeal by Hindalco arising out of proceedings by the AO under section 250 of the Act, pursuant to the order of the CIT (A) dismissing appeal against order passed under section 147 read with section 163 of the Act, was dismissed. This was done on the basis that the assessment on Hindalco as agent of Alcan was held to be invalid and thus the appeal was rendered infructuous.

Airlines Rotables Limited vs. JDIT (ITAT Mumbai)

No PE under India-UK DTAA, if conditions for a PE to come into existence are not fulfilled.

Facts of the case:

Airlines Rotables Limited ("the assessee"), a UK company, entered into an agreement with Jet Airways Limited ("JAL") under which, it agreed to provide JAL with two segments of services, first, to carry out repairs and overhauling of aircraft components outside India and, second, to provide spares and components in the period the components were being repaired. To ensure that the spares and replacement components were readily available, the assessee maintained a stock of the components at the operating base of JAL in India. Though the stock was under the direct control of the assessee, it was in the possession of JAL as a bailee. The AO took the view that as the stock was kept in India with JAL, JAL constituted an "agent" and a "permanent establishment"(PE) in India under Article 5(4) (b) of the India-UK DTAA and that, 10% of the receipts was liable to tax in India. This was upheld by the CIT (A).

Contentions of the assessee:

The relevant material facts were explained by the assessee. It was contended that with a view to ensure adequate availability of necessary rotables, the assessee company maintained stock of replacement rotables at operational bases of JAL in India, as also at the assessee company's main depot in the UK. As regards the stock maintained at the UK, such stock was under direct control of the assessee company. However, since the assessee company did not have any storage or support facilities in India, the stock in India was in the possession of JAL itself as a bailee. The assessee handed over the consignment stock to JAL and it was kept in the warehouse located at the operating base. The stock remained property of the assessee company at all times and JAL was forbidden from loaning, pledging, selling, exchanging or encumbering any items from the stock – except as permitted under the agreement itself. Whenever need arose i.e. a component was sent for repairs or overhauling, JAL had a right to use replacement components from the said stock. Maintenance of this consignment stock in India was at the root of the dispute. However, the assessee contended that it did not have any PE in India and its business profits were not taxable in India. The assessee further contended that the AO should be directed to compute the total income of the assessee by applying the actual profit rates.

Contentions of the revenue:

- The AO relied upon Article 5(4) (b) of the DTAA which provided that *"A person acting in a Contracting State for or on behalf of an enterprise of the other Contracting State other than an agent of an independent status in whom paragraph (5) of this Article applies shall be deemed, to be a permanent establishment of that enterprise in the first-mentioned State if……he habitually maintains in the first-mentioned Contracting State a stock of goods of merchandise from which he regularly delivers goods or merchandise for or on behalf of the enterprise".*

- The AO also noted that it was not necessary that the person who managed and controlled the stock should be an employee of the foreign enterprise. In his view, the emphasis was on the fixed place of business, and given that the assessee's stocks were permanently kept at fixed places in India, with clear identification of each of stock item, the assessee had a fixed place of business in India.

- The AO, thus, concluded that the assessee had a PE in India under Article 5 of the India-UK DTAA, and that, accordingly, the receipts would be taxable in India as business receipts. The AO estimated 10% of gross receipts as the assessee's profits liable to be taxed in India.

CIT (A) held that:

- The assessee had a fixed place of business within meanings of Article 5 (1) and Article 5 (4) of the India-UK DTAA, since the assessee was having a fixed place of business in which goods were kept as stock for sale. The CIT (A) also observed that the issue of sale had to be understood in its widest meaning in relation to business transactions and added that the assessee company was engaged in the business of providing repairs to the faulty components of Boeing 737 of JAL.

- The CIT (A), further observed that:

  Faulty components were collected by the assessee company and after repairing they were sent to India. Stock of such goods and repaired parts / rotables was maintained in India from which delivery was to be made to JAL as and when needed. Thus, so far as the assessee was concerned, delivery of such repaired part amounted to sales, since income was arising out of such delivery of goods and the repaired part. Thus, benefit of clause (a) and clause (b) of Article 5 (3) was not available to the assessee.

- The CIT (A), thus, upheld the action of the AO in holding that the assessee had a PE in India. The CIT (A) also upheld taxability @ 10% of gross revenues earned from Indian operations by the assessee company. The assessee was aggrieved and was in further appeal before the Tribunal.

Observations by the Tribunal:

The Tribunal observed that:

- In order for a PE to come into existence under Article 5(1) ("the basic rule"), three criteria had to be satisfied viz:

  1) the physical criterion (existence of physical location)
  2) subjective criterion (right to use that place) and
  3) functional criterion (carrying on business through that place).

  It was only when the three conditions were satisfied that a PE came into existence. The onus was on the revenue to show that the assessee had a PE.

- Though the stock was stored at specific locations in India, such locations were not at the disposal of the assessee and the assessee could not carry out its business from that place. There was, consequently, no PE under Article 5(1). Even if there was a PE, the consideration relatable to the repairs done outside India was not taxable, as it was not "attributable" to the PE. The existence of a PE did not justify taxation of all profits, as the force of attraction principle could not be inferred in the given case. As regard to the consideration for the right to use the components, the business element thereof was over when the component was handed over to the airline. There was no "carrying on of business" from that location. Consequently, there was no PE under article 5(1);

- The argument of the revenue that there was a "Dependent Agent PE" under Article 5(4) (b) was also not correct. The rationale of a Dependent Agent PE was that the foreign enterprise carried on business through a dependent agent, who was integrated into the principal's business to a substantial extent. However, on facts, as JAL was neither the dependent agent of the assessee and nor was the assessee carrying on business through JAL, there was no PE under Article 5(4) (b);

- When a PE existed, even such a consideration, which may otherwise be taxable in the source country under Article 13, was taxable on net basis under Article 7. Therefore, merely because an amount was not taxable under Article 7 in the source country, it did not mean that the item would not be taxable under any other article in the source country concerned. As evident from a plain reading of the consideration clause in the agreement between the parties, consideration for use of replacement components was distinct and separate and the same could be segregated from the overall receipts. In this view of the matter, non taxability under Article 7 would still mean that application of Article 13 was to be considered and adjudicated upon.

Decision by the Tribunal:

The orders of the authorities on the issue of existence of the PE and for quantification of taxable income were dismissed. As the authorities had not examined whether the consideration for use of the replacement components was "for the use of industrial, commercial or scientific equipment" and taxable as "royalty" under Article 13(3) (b), the matter was remitted to the file of the CIT (A) for adjudication on the question of taxability.

Cartier Shipping Co. Ltd. vs. DDIT (ITAT Mumbai)

Despite cessation of PE, gains on transfer of PE asset are taxable under the Income Tax Act, 1961 and India-Mauritius DTAA.

Facts of the case:

Cartier Shipping Co. Ltd. ("the assessee") was a company registered under the laws of Cyprus which was later registered as a foreign company in Mauritius. Based on this registration in Mauritius, the assessee was issued a tax residency certificate by the Commissioner of Income Tax, Mauritius. On the strength of this certificate, the assessee claimed protection of India-Mauritius DTAA which was duly granted to him by the Assessing Officer ("AO").

The assessee owned a jack-up rig used for drilling of mineral oil. The rig was given on charter basis to Amer Ship Management Limited ("ASML"), an Indian company, which in turn leased it to Oil and Natural Gas Corporation ("ONGC"), for operations in Indian territorial waters. The chronology of events was as under:

– On 24.4.1997: the assessee entered into an agreement with Foramer SA, France, to sell the jack-up rig.
– On 15.9.1997: the surveyors boarded the rig and coordinated its move from Bombay High to the hand-over location outside India.

- On 19.9.1997: the assessee issued a bill of sale in favor of the purchaser.
- On 30.9.1997: the assessee obtained a port-clearance certificate and started moving the rig.
- On 3.10.1997: the charter agreement was terminated.
- On 6.10.1997: the rig was handed over outside India to the buyer .

The assessee informed the AO of the termination of the charter and that it had discontinued business operations in India and moved the rig outside territorial waters, though it did not mention the fact of sale of the rig. The AO re-opened the assessment under section 147 and took the view that as depreciation had been allowed on the rig, the difference between the sale consideration and WDV (Rs. 102 crores) was a short-term capital gain. This was confirmed by the CIT (A). In appeal to the Tribunal, the assessee argued that since sale of the rig had taken place on 6.10.1997 outside India, it had no tax implications in India and that the re-opening was invalid.

Two main issues that required adjudication were:

- Whether or not, the CIT (A) was justified in upholding validity of reassessment proceedings; and

- Whether or not, the CIT (A) was justified in upholding the addition of Rs. 111.16 crores on account of short term capital gain, on sale of rig.

Contentions of the assessee:

- The assessee contended that it had informed the tax authorities about the cessation of business in India with effect from 3rd October 1997, and since the assessee had wound up its business in India, it was of no concern to the tax authorities as to what did the assessee do with its assets. The assessee further contended that since it did not have any obligation to inform the Indian tax authorities about the disposal of its assets, this omission could not be construed as a lapse on the part of the assessee which was a sine qua non for initiating the reassessment proceedings after the end of four years from the end of the relevant assessment year. Thus, according to the assessee, there was no failure on its part, and as such the reassessment proceedings could not have been initiated in the present case. It was emphasized that the sale had taken place outside Indian territorial waters and it had no tax implications in India.

Contentions of the revenue:

- The revenue submitted that closure of business in India did not lead to an end of entire taxability of the assessee in India. The cessation of PE was relevant only for the purposes of taxability of business profits, and had no impact on the taxability of capital gains of alienation of the PE or its assets. It was assessee's statutory obligation to disclose the fact of sale of the oil rig under 'incomes claimed to be exempt from tax' in the income tax return in a transparent manner. The tax authorities were, thus, deprived of relevant information about sale of oil rig. It was contended that the gain on alienation of assets of the PE, or even PE itself, constituted capital gain chargeable to tax in India under the Income Tax Act, 1961, ("the Act") as also under the provisions of Article 13 of the India- Mauritius DTAA. The assessee was clearly at fault, was not operating in a fair and transparent manner, and had not discharged its obligations of giving full and complete disclosures in the income tax return. It was thus submitted that the case of the assessee was clearly covered by proviso to Section 147 which permitted re-opening of assessment even after the expiry of four years, from the end of the relevant assessment year, in a case in which the assessee failed to disclose fully and truly all material facts necessary for his assessment for that assessment year.

Observations of the Tribunal:

- The argument that the gains on transfer of PE/PE assets were taxable only if the PE existed was not acceptable because then the provision for taxability of gains on PE/ PE assets in the source country would be rendered redundant. The provisions could also then be avoided by simply deferring the transfer till the closure of the PE. This would lead to absurdity (Van Oord Dredging 105 ITD 97 referred to – PE's business profits can be taxed even if received after closure of the PE).

- The argument that the sale of the rig took place on 6.10.1997 outside India and after the termination of the charter was not correct, because the records pointed that the rig was first sold and as a consequence, the charter was terminated and the rig was moved to international waters for delivery to the buyer. It was not a case, where, the business came to an end and the rig was moved to international waters and then, by an unconnected event, the rig was sold.

Decision by the Tribunal

- It was, thus, clear that the movement of the rig to the international waters was clearly connected with and consequent to the sale of the rig, and necessary for fulfilling part of seller's obligations under the sale contract. The sale had taken place on 17.09.1997. The asset was a source of income in India for the assessee, and it had a business connection in India, which lead to taxability of income on sale "deemed to accrue or arise in India" under section 9(1). Moreover, the asset was also located in India at the material point of time. It was further stated that the date of delivery and the date of payment were relevant in as much as they completed the sale transaction but the date of sale was to be taken as the date on which sale invoice was "signed and delivered as a deed", as certified by London based Notary Public. The contention of the assessee that sale took place on 6th October 1997, i.e. after the PE came to an end, was, thus, rejected on merits. Thus, deferral of sale or receipt of sale consideration, on sale of PE or PE assets, did not influence the tax liability in connection with sale of PE or its assets.

- Thus, the assessee's challenge, either to reassessment proceedings or to the quantum additions confirmed by the CIT(A), could not be upheld. As far as quantification of addition was concerned, no grievances were raised before the Tribunal nor were any arguments addressed on that aspect of the matter. Thus the conclusions arrived at by the learned CIT(A) were approved by the Tribunal.

ACCOUNTS, AUDIT & INVESTMENT

ACCOUNTS AND AUDIT

Standard on Auditing (SA) 520 (Revised) "Analytical Procedures"

The Institute of Chartered Accountants of India (ICAI) has come out with a Standard on Auditing (SA) 520 "Analytical Procedures"

Scope of this SA

This Standard on Auditing (SA) deals with the auditor's use of analytical procedures as substantive procedures ("substantive analytical procedures"), and as procedures near the end of the audit that assist the auditor when forming an overall conclusion on the financial statements. The use of analytical procedures as risk assessment procedures is dealt with in SA 3152. SA 330 includes requirements and guidance regarding the nature, timing and extent of audit procedures in response to assessed risks; these audit procedures may include substantive analytical procedures

Objective

The objectives of the auditor are:

a) To obtain relevant and reliable audit evidence when using substantive analytical procedures; and

b) To design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor's understanding of the entity.

Effective Date

This SA is effective for audits of financial statements for periods beginning on or after April 1, 2010.

Standard on Auditing (SA) 700 (Revised) - "Forming an Opinion and Reporting on Financial Statements"

The Institute of Chartered Accountants of India (ICAI) has come out with a Standard on Auditing (SA) 700 (Revised) - "Forming an Opinion and Reporting on Financial Statements"

Scope of this SA

This Standard on Auditing (SA) deals with the auditor's responsibility to form an opinion on the financial statements. It also deals with the form and content of the auditor's report issued as a result of an audit of financial statements.

SA 7053 and SA 7064 deal with how the form and content of the auditor's report are affected when the auditor expresses a modified opinion or includes an Emphasis of Matter paragraph or an Other Matter paragraph in the auditor's report.

This SA is written in the context of a complete set of general purpose financial statements. SA 8005 deals with special considerations when financial statements are prepared in accordance with a special purpose framework. SA 8056 deals with special considerations relevant to an audit of a single financial statement or of a specific element, account or item of a financial statement.

This SA promotes consistency in the auditor's report. Consistency in the auditor's report, when the audit has been conducted in accordance with SAs, promotes credibility in the global marketplace by making more readily identifiable those audits that have been conducted in accordance with globally recognized standards. It also helps to promote the user's understanding and to identify unusual circumstances when they occur.

Objective

The objectives of the auditor are to:

c) Form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained; and
d) Express clearly that opinion through a written report that also describes the basis for the opinion.

Effective Date

This SA is effective for audits of financial statements for periods beginning on after April 1, 2011.

Errant auditors would need to pay investors

Audit firms may be asked to financially compensate investors for losses resulting from their lapses, with the Government planning to strengthen the mechanism for fixing responsibility for corporate frauds and protecting investors from their ill-effects. To make this feasible, an audit firm would be held accountable for its actions, regardless of whether the firm itself or its affiliate was the official auditor.

The Government is yet to work out the proportion of investors' losses the auditor will have to compensate. The options include capping the quantum of compensation and evolving a criterion for fixing amounts on a case-by-case basis.

The Government is keen on a legal framework so that victims of accounting malpractices could be duly compensated in the event of a scam. In order to achieve the same, the practice of certain audit firms setting up affiliates across the country needs to be fixed first. Currently, one audit firm in Hyderabad is not liable for anything that its Bangalore affiliate does. This needs to be changed.

The President of the Institute of Chartered Accountants of India (ICAI) observed that though the idea to have such a mechanism is good, there was a serious question mark over its feasibility. In case a big accounting scandal like Satyam breaks out, it would be literally impossible for the accounting firm to compensate. He suggested that either the Government cap a certain percentage of the money that the audit firm should pay or disqualify audit firms who have been involved in recurring defaults. He agreed that bringing all affiliates under one umbrella would create accountability.

Ministry of Corporate Affairs (MCA) shelves peer audit review plan

The Ministry of Corporate Affairs (MCA) has shelved its idea of auditing the books of listed companies by independent auditors. It was part of the joint plan of market regulator Securities and Exchange Board of India (SEBI) and the Ministry of Corporate Affairs (MCA) to conduct peer review of audits, which involves getting the audit reports of a company vetted by another auditor for a second opinion.

To start with, the proposal was intended to audit 30 companies on the Bombay Stock Exchange and 50 companies of the National Stock Exchange. It is now decided that the audit reports will be vetted by a panel of auditors appointed by the Financial Advisory Board of the Institute of Chartered Accountants of India

(ICAI), only for cases where any irregularities are found or regulatory or supervisory need requires a second opinion.

According to the earlier proposal, the audited balance sheets of all listed companies were proposed to be audited by independent auditors appointed by the Registrar of Companies in their respective regions. MCA had then decided to ask various other regulators to make the peer review of audit mandatory for companies regulated and supervised by them.

These included the Reserve Bank of India for banks, SEBI for listed companies and the Insurance Regulatory and Development Authority for insurance companies. The idea was to avoid accounting irregularities in at least those companies or financial entities where public funds are at stake.

However, sources at ICAI said the Government did not find enough trained auditors to check what another chartered accountant of 10-15 years of experience has done. Therefore, first such auditors have to be trained and then this review of audits should be made compulsory.

The peer review of audit was proposed in the aftermath of the Rs 7,000-crore accounting fraud by Satyam Computer Services, in which the founder of the IT firm confessed to manipulation of books.

SEBI had then recommended that all listed companies be audited by practicing chartered accountancy firms or individual auditors.

Ministry of Corporate Affairs (MCA) to ease paid-up capital norms for Companies

The Ministry of Corporate Affairs (MCA) has decided to relax the norms for companies to maintain minimum paid-up capital. According to the Companies Act 1956, the minimum paid-up capital for a private company is Rs 1 lakh and for a listed company Rs 5 lakh. A company can be set up with any amount, but within a time-frame of two years it should raise the capital to Rs 1 lakh and Rs 5 lakh for unlisted and listed companies, respectively. If a company fails to do so in accordance with the existing provisions of Section 560 of the Companies Act, the company will be deregistered and declared defunct.

Now it may be a good news for the companies that such entities may not be declared defunct immediately as is done now. Under a scheme prepared by the Ministry, such companies may opt for an option to exit business without attracting any penal provisions under the Companies Act. Alternatively, they may negotiate some more time with the regulator for raising the capital and continue with their business. In the process, earlier penal provisions may not apply.

The scheme could be a big relief to the both listed and unlisted companies. This is because once a company is declared defunct; the Registrar of Companies (RoC) can start criminal prosecution against the company. This relief may come as part of the comprehensive scheme being worked out by the Ministry to avoid criminal prosecution for delay in filing one's Balance-sheet with RoC.

At present, any company which has prepared a Balance-sheet for a given financial year is bound to file it with RoC by October of that financial year. Not doing so attracts criminal proceedings under Section 610 of the Companies Act 1956, plus a structure of penalties.

The proposed scheme is being termed 'Immunity from period of delay in filing returns and prosecution' and meant for all companies, public and private, listed or unlisted, and even subsidiaries or Indian arms of foreign companies operating in India. It is aimed at companies who are functional but have failed to comply with the requirement of mandatory filing of these returns with RoC. The idea is to do two things. First, make the present penalties more lenient. Second, remove the liability for criminal prosecution.

Another feature of the draft being discussed is that once a company opts for this scheme, the Ministry is to advise RoC to withdraw legal suits filed against the company for prosecution.

25% public exposure must for listed entities: Government

The Government recently made it mandatory for listed companies to raise public shareholding to 25%, with at least 5% dilution a year, a move that would attract more investors and check price share manipulation. According to the Finance Ministry's decision, all the listed entities will have to dilute at least 5% equity annually till they reach the threshold limit of 25%. In keeping with the budgetary promise, the Finance Ministry Mr. Pranab Mukherjee amended the relevant regulations to the effect that "the minimum threshold level of public holding will be 25% for all listed companies."

Accordingly, all listed entities will have to dilute at least 5% additional equity annually till they reach the threshold limit of 25%. Every listed company will have to fulfill this condition to remain listed on stock exchange.

For a company seeking listing, it would have to dilute 25% in one go in case the issue size is just up to Rs 4,000 crore. However, those already in the process of going public and have filed draft prospectus could disinvest stipulated 10% and later meet the condition.

At present, most companies dilute just 10% stake and the shares tend to trade at a premium. Giving the rationale for the decision, the Ministry said, "A disperse shareholding structure is essential for the sustenance of a continuous market for listed securities to provide liquidity to the investors and to discover fair prices." The decision would see large number of companies hitting the capital market within a year.

The move is in line with practices followed in developed economies globally. While the London Stock Exchange (LSE) requires 25% minimum public holding, the Singapore and Hong Kong Stock Exchanges also stipulate public share holding between 12% and 25%.

The requirement to offload equity by large number of listed companies may have implications for the disinvestment programme of the Government. The Government proposed to raise Rs 40,000 crore during the current fiscal by selling equity of state-owned companies.

So far, the Government had raised only Rs1,079 crore by selling its stake in the Satluj Jal Vidyut Nigam Limited (SJVNL). Several initial and follow-on public issues of PSUs like SAIL, Coal India, Power Grid, Engineers India Limited, MMTC and Hindustan Copper are in the pipeline.

Blue chip state-owned companies like Indian Oil Corporation (IOC) and mineral major NMDC will have to come out with fresh issues to meet the new norm.

Companies not complying with the minimum public holding norm of 25% will be delisted

Companies failing to comply with the minimum public holding norm of 25% could face delisting, suspension of trading or a fine of Rs 25 crore. The existing provisions that deal with listing norm violations will continue to be in effect. But these provisions will be more effective now with them getting incorporated in the Securities Contracts (Regulation) Rules.

The Government recently notified changes to the rules making it mandatory for listing companies to have 25% public shareholding. The move is in line with an announcement made by the Finance Minister Mr. Pranab Mukherjee in his 2009-10 budget speech. Market regulator SEBI may resort to provisions akin to those govern violation of the takeover code — a fine of Rs 25 crore — if stock exchanges seek invocation of such a provision. So far these norms were part of the listing agreement of stock exchanges. Typically, companies give an undertaking to stock exchanges that they will comply with the norms in six months, but do not adhere to it in some cases. As per the new norms, every listed company shall maintain public shareholding of at least 25%. If the public shareholding in a listed company falls below 25%, then the company is required to bring to the threshold within 12 months.

According to a report by securities research firm Edelweiss, 156 companies have promoter holdings of more than 75%. Dilution of promoters' stake in these companies will release shares worth around Rs 1,50,000 crore in the next five years. Eight state-run firms alone would see equity dilution to the tune of Rs 1,00,000 crore, the study shows.

Department of Industrial Policy and Promotion (DIPP) to define 'Group Company' soon

The Commerce and Industry ministry would come out with a definition of 'Group Company' soon, a clarification that would help global companies like to begin operations without violating norms.

Global retail players are seeking clarity on this issue to chalk out their India plans.

According to DIPP rules, wholesale trade of goods would be permitted among companies of the same group. But, such trade should not exceed 25 per cent of the total turnover of the wholesale venture and only for internal use.

DIPP would release the remaining five discussion papers on FDI policies by September 2010.

Highlights of the economic growth during 2009-10

- Indian economy (GDP) grew by 7.4% during 2009-10, higher than the estimated 7.2%.
- During 2008-09, the economy grew by 6.7%.
- Per capita income rose by 10.5% to Rs44,345 in 2009-10 against Rs40,141 during 2008-09.
- During the fourth quarter of 2009-10, the economy grew by 8.6%, against 5.8% in the year-ago period.
- Second quarter growth revised to 8.6% from 7.9%.
- Third quarter growth revised to 6.5% from 6%.

- Agriculture and allied sectors grew by 0.2% in 2009-10, against the estimated 0.2% contraction.
- Manufacturing sector expanded by 10.8% during 2009-10, against the estimated 8.9%.
- Electricity, gas and water supply growth was 6.5%, lower than the estimated 8.2%.

SEBI

SEBI allots corporate bond limits

India's market regulator Securities and Exchange Board of India (SEBI) recently said it has allocated investment limits in corporate bonds to Foreign Institutional Investors (FIIs).

SEBI said in a notification that unutilized investment limits for corporate bond investments were available for allocation to FIIs and the bidding took place on Bombay Stock Exchange's platform. These limits shall be utilized by the allocated entities within 45 days of the allocation.

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