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Contents

INCOME TAX

Domestic Taxation

Case law

1. Avaya Global Connect Ltd. Case (ITAT Mumbai)

Background & Facts

- 'The assessee, Avaya Global Connect Limited, formerly known as Tata Telecom Limited (TTL) is engaged in the business of providing voice communication solutions and manufacturing telephone instruments. The company had two divisions, namely Business Communications Divisions (BCD) which provides communication solutions and Tata Fone Division (TFD) which was involved in manufacture of EPABX systems and telephone instruments.
- The assessee transferred TFD to an Indian company, ITEL Industries Private Ltd. (ITEL) under a scheme of arrangement as approved by the Bombay High court, wherein all the assets and liabilities of TFD were to be transferred to ITEL. The amount of liabilities of TFD exceeded the amount of the assets, the excess amount of liabilities being credited to capital reserve account of TTL.
- Since the net worth was negative, ITEL was not under an obligation to pay any consideration for transfer, either to TTL or to its shareholders. Thus, the assessee, whilst filing the return of income, claimed that owing to the absence of consideration, no capital gain shall occur as it complied with all the conditions of 'demerger'.
- The Revenue, however, was of the view that the transfer of TFD to ITEL did not constitute a 'demerger' under section 2(19AA) of the Income-tax Act, 1961 (the Act) as the conditions of demerger were not satisfied & thus should be taxable. The Revenue also contended that the aforesaid transfer also falls within the definition of 'slump sale' under the Act and should be taxed accordingly.
- Following questions were posed to the Tribunal
    a. Whether the transfer of TFD division to ITEL can be termed as 'demerger'?
    b. If the transfer is not termed as 'demerger' than can it be termed as 'Slump sale'?
    c. Whether capital gains tax is leviable?

Decision & Conclusion

- Whether the transfer of TFD division to ITEL can be termed as demerger?

  - ✓ The Assessee contended that the company has satisfied all the vital conditions related to 'demerger'. The condition allied to the allotment of shares in ITEL shall be deemed to have been satisfied as the amount of the liabilities is more than the amount of the asset.
  - ✓ The Tribunal ruled that the transfer under consideration cannot be considered as a demerger, as all the conditions laid down in section 2(19AA) of the Income Tax Act are not satisfied. Furthermore, the Tribunal observed that ITEL did not issue shares to the shareholders of TTL in consideration for the transfer of TFD, as stipulated under section 2 (19AA).

- If the transfer is not termed as demerger than can it be termed as Slump sale?

  - ✓ The assessee contended that the transfer cannot be treated as 'Slump Sale' as it was pursuant to a court order. The assessee drew attention to the definition of 'slump sale'. The definition of slump sale is an exhaustive definition. It covers only transfer by way of sale and not any other mode of transfer like exchange, relinquishment, etc.. As per the facts of the case, TFD has been transferred in exchange of ITEL. Therefore, the assessee contended that the transfer does not amount to slump sale, as chargeable to tax under the provisions of section 50B of the Act.
  - ✓ The Tribunal seconded the contention of the assessee that the transfer is not under a 'slump sale'. As the transfer was done after obtaining approval of Bombay High Court, in terms of a scheme of arrangement amongst the share holders, such transfer cannot be termed as sale. The Tribunal therefore contended that transfer shall not attract the provisions of section 50B of the Act.

- Whether capital gains tax leviable or not?

  - ✓ The assessee asserted that TFD was a going concern and consequently it would not be possible to determine the cost of acquisition. Furthermore, there was no consideration paid or payable for the transfer, as the net worth was negative. Consequently, it will not fall within the ambit of the charging section, i.e., section 45 of the Act; dealing with the basis of charge of capital gains.
  - ✓ The Tribunal stated that computing capital gains for a going concern will be impossible as it will be difficult to arrive at the

cost of acquisition, cost of improvement, etc. So this transfer does not fall under capital gains tax.

- Conclusion

  - ✓ A scheme of arrangement resulting into transfer of an undertaking in the form of demerger shall provide desired capital gains tax exemption to the concerned company, even though does not meet with the conditions of demerger provided under the Act.
  - ✓ The tax consequences, however, for the recipient company as well as share holders in such case would require further & careful tax planning.

International Taxation

Case laws

1. Diamond Services International Pvt. Ltd. Case (Bombay High Court)

Background & Facts

- Gemological Institute of America (GIA) is the worlds largest & the most respected institute of gemological research & learning. GIA grades diamonds & issues a certificate stating the properties such as colour, crate, etc. of the diamonds.
- The assessee, Diamond Services International (P) Ltd. (DSI), is a company incorporated in Singapore and also a tax resident of Singapore. DIS acts as an interface between Indian customers, who wish to get the diamonds graded, and GIA.
- DSI collects diamonds & gems from Indian customers and sends the same to GIA for grading & certification. DSI would receive payments from the Indian customers for the same and remit it to GIA.
- The assessee applies to the Assessing Officer to secure certificate under section 197 of the Indian Income Tax Act, inter alia, entitling payment to be made without deduction of any amount of tax. However, the Revenue denied to issue such certificate on the ground that the grading of diamonds is a technical skill and it involves transfer of commercial knowledge and technical know how, payment for which shall be in the nature of royalty under Article 12 of DTAA with Singapore and Sec 9(1)(vi) of Indian Income Tax Act.
- The assessee, on the other hand, contended that the payments made by the Indian customers are for receiving the grading reports from GIA and that there is no technical knowledge, skill, etc. transferred by the assessee to the customers. Also, there is no transfer of any skill or knowledge of GIA to the customers in the issuance of grading reports.

Decision & Conclusion

- The Court referred to the submissions and arguments placed by the parties, viz. the assessee & the Revenue. The Court concurred to the contentions of the assessee, that the grading report was a statement of fact as to the characteristics of the diamond and did not amount to transfer of any technical skill or knowledge to the customers.
- The Court explained that in the subject under consideration there was no 'transfer of right to use', & thus the payment cannot be termed as "royalty" in Article 12 of the DTAA. If such person merely uses his

experience and technical know-how for a consideration without parting with that information, it cannot be considered as royalty.

- Accordingly the action of the Revenue in refusing to issue the certificate u/s 197 was without jurisdiction and the Court directed the Revenue to issue the certificate under section 197.

2. Chiron Behring GMBH & Co. Case (ITAT Mumbai Bench)

Background & Facts

- The assessee, Chiron Behring GMBH & Co. is a 'Limited Partnership' firm incorporated under the German laws. As per the taxation laws of Germany, the assessee was liable to trade tax in Germany.
- The assessee earned revenue in the nature of royalty and fees for technical services from an Indian company, assessed to tax under section 9(1) (vi) read with section 44D of the Income Tax Act (the Act) at the rate of 20 % (plus cess & surcharge).
- However, the assessee contended that they should be entitled to the beneficial rate of tax of 10% as per the DTAA between India & Germany (the Treaty), over the rate applicable as per the Act. The assessee averred that though partnership firm was a pass through entity as per German laws, the firm paid trade tax in Germany, which is in the nature of tax on profits of business of the firm.
- The Revenue, however, disagreed to the contentions of the assessee on the ground that assessee is not a tax resident of Germany, as per the Treaty. The Revenue relied on the OECD commentary which, mentions that the tax on limited partnerships was the liability of the partners and not that of the firm.
- The Revenue asserted that assessee is liable to pay trade tax in Germany which is considered as tax on turnover and cannot be treated as an equivalent to income tax & thus cannot enjoy the benefits of the treaty.
- The ITAT was thus confronted with the question, whether the assessee was a resident of Germany and consequently entitled to the benefit of the lower withholding rate under the India-Germany Treaty.

Decision & Conclusion

- The Tribunal held that for an assessee to be entitled to the benefits of the tax treaty, the assessee should be a person as defined in the tax treaty, be a resident of either India or Germany (in the present context) and should be liable to pay tax in its residence country by reason of domicile, residence, place of management, etc.

- The Tribunal thus held that Chiron is a tax resident of the Germany, as defined under Article 4 of the Treaty. Also Article 2 specifically mentions that the scope of the treaty extends to both income tax (Einkommensteuer) and trade tax (Gewerbesteuer) as may be levied under German laws. The assessee would therefore, qualify as a resident and is eligible for the lower withholding rate under the Treaty.
- Further the Tribunal opined that OECD commentaries may be referred only if the provisions of the Treaty are ambiguous or the language of the Treaty is unclear or admits any doubts in interpretation.

3. Anapharm Inc. – Advance Ruling

Background & Facts

- Anapharm Inc. is a Canadian company, providing clinical & bio-analytical services to various pharmaceutical companies. Product specific methods/ protocols are developed & used for evaluating the drugs. It entered into agreements with two Indian pharmaceutical companies, Sandoz Pvt. Ltd. & Ranbaxy Research Laboratories for rendering the above services in the development of new and/ generic drugs.
- Anapharm Inc filed an application with the AAR, to know whether the fee received by it from the Indian companies for undertaking clinical and bio-analytical studies would be taxed in India.
- According to the Revenue, the fees received by Anapharm from the Indian companies will be taxable in India as 'royalty' & 'fees for included services' under Article 12 of the India Canada DTAA (The Treaty). The Revenue asserted that the services provided by Anapharm are technical in nature & the test reports provided to the clients are actually a technical know how & experience of Anapharm.
- The applicant asserted that, the services rendered by them did not "make available" any technical know how or experience to the client for the fees received to be considered as 'fees for included services' under Article 12 of the Treaty. The applicant, in contrast, contended that the fees received should be taxable as business profits in India. But in absence of a permanent establishment in India, by virtue of Article 7 read with Article 5 of the treaty, the same will not be taxable in India.

Ruling by the AAR

- The AAR ruled that the fee paid by Sandoz Pvt. Ltd. & Ranbaxy Research Laboratories in respect of bioequivalence tests conducted by the applicant, is in the nature of business profits, as providing such services was the main activity, i.e. the business of Anapharm. Also under Article 7 of the

Treaty the same is not taxable in India as the applicant does not have a permanent establishment.

- The AAR referred to the protocol to Article 12 of the India – US DTAA, which is similar to the Article 12(4) of the Treaty. Accordingly, the technology will be considered as 'made available' if the recipient of service is enabled to apply the technology to independently perform the technical function on its own, without any assistance of the service provider.
- Moreover, the AAR asserted that the test reports are drug-specific hence the material furnished by Anapharm Inc will not in anyway help the client to facilitate further research and development of new drugs as contended by the revenue.

4. Small Business Corporation – Advance Ruling

Background & Facts

- Small Business Corporation ('SBC') is a non-profit Government controlled entity under the direct supervision of SMBA which is a Government department of the Republic of Korea. Government contribution toward SMBA serves as the source of operating and personnel expenses required during the execution of businesses by SBC.
- SBC has opened a liaison office in India, after obtaining permission from the RBI. The liaison office in India was established to promote Korean businesses in India and to act as an intermediate between the companies and government. As per the directives of RBI, all the expenses for the India office should be met exclusively out of funds received from the Korea office.
- Mr. Ji Hoon Lee was appointed as a General Manager at the India office. Remuneration is paid to Mr. Ji Hoon Lee out of Government funds received by SBC from the Republic of Korea. The applicant sought ruling for the taxability of remuneration paid to Mr. Ji Hoon Lee.
- The applicant contended that the remuneration received by Mr. Ji Hoon Lee, will be exempt from tax in India in terms of Article 20 of the DTAA between India and the Republic of Korea. The fundamental requirement of Article 20(1)(a) is that the remuneration should be paid by the Contracting State (Korea in our case). Even if it is paid out of funds allocated by the Government to the applicant specifically towards personnel expenses, the requirement of Article 20(1)(a) shall be satisfied. In an apparent bid to establish that the source of salary payment to Mr. Hoon Lee is the Government funds placed at the disposal of SBC, the applicant has filed an affidavit of the Administrator of SMBA.

Decision & Conclusion

- The AAR seconded to the contention of the applicant that payment through a fund of the government is as good as payment by the government itself. The expression “payment by a Contracting State” cannot be given a rigid or literal interpretation so as to cover the payments made directly by Government or a department of the Government. Even if the payment is made out of State’s funds set apart for that purpose, the requirement of Section 20(1) (a) will be satisfied.
- However, with the subject under consideration, it was difficult to substantiate whether the payment made to Mr. Ji Hoon Lee, was exclusively out of Government funds, as SBC is a corporate entity receiving funds from various sources. It would have been a different matter if the Government while sanctioning the contribution made specific allocation for the personnel expenses incurred by SBC.
- AAR demanded further evidence from the applicant, to substantiate that the personnel expenses are met out of the allocation made by the Government to the fund for this specific purpose. The applicant, however, failed to submit any further proofs.
- Thus, the AAR ruled the question raised by the applicant in negative & against the applicant.

REGULATIONS GOVERNING INVESTMENTS

Increase in External Commercial Borrowing limit

On 22nd September 2008, the government liberalized the norms for overseas borrowing by increasing the limit of borrowing from $100 millions to $500 million for infrastructure sector under Approval route. Borrowing above $100 million should have a minimum maturity period of 7 years. This route will be applicable with immediate effect.

In a view to expand the credit spread in the International financial markets, RBI further modified the all-in-cost ceilings in respect of ECBs with a minimum average maturity period of over 7 years. The revised all-in cost ceilings for ECBs shall be as follows.

Average Maturity Period	**All-in-Cost ceilings over 6 Months LIBOR**	
	Existing	**Revised**
Three years and up to five years	200 bps	200 bps
More than five years and up to seven years	350 bps	350 bps
More than seven years	350 bps	450 bps

The above amendments are only for the infrastructure sector. There is no amendment to the existing norms to the other sectors with regard to ECB norms. The borrowing limit for other sectors upto USD 50 million for Rupee Capital Expenditure under the approval route remains unaffected. All other aspects concerning ECB policy like eligible borrower, recognized lender, end-use of foreign currency expenditure for import of capital goods and overseas investments, average maturity period, prepayment, refinancing of existing ECBs and reporting arrangements shall continue to apply without any modification.

Amendments to the Listing of Equity Agreements

The Securities and Exchange board of India (SEBI) has made some amendments to the Equity listing agreement, to obtain greater lucidity and efficiency in the governance of listed companies. Amendments are made in clause 16, 19, 24 & 41, as explained below.

1. Rights Issue (Clause 16 and 19)

Particulars	Current Provision	Amendment
1. Advance Notice to the stock exchange for Book closure in case of right issue (Clause 16)	Listed company issuing Rights shares shall close its transfer books at least once a year and give a 21 days advance notice to the stock exchange.	SEBI has reduced the notice period to 7 days.
2. Prior intimation to the stock exchange regarding Board meeting where right issue would be considered (Clause 19**)**	The company has to inform to the Stock Exchange about the Board meeting that will be held for the proposal for Rights Issue with a prior notice of at least 7 days.	SEBI has reduced the notice period to 2 days.

2. Mergers (Clause 24)

Particulars	Current Provision	Amendment
Fairness Opinion of independent merchant banker	The company should disclose all the pre and post arrangements of capital structure as well as share holding pattern to the shareholders under section 393 of the Companies Act, through an explanatory statement.	Both the companies need to appoint two different merchant bankers for giving the fairness opinion to shareholders regarding the valuation of shares/assets done by the valuers. The fairness opinion of the merchant bankers shall be made available to the shareholders at the time of approving the resolution.

3. Amendments relating to submission and publication of Financial Statements (Clause 41)

Particulars	Current Provision	Amendment
Preparation and submission of financial	Incase a company submits un-audited	Un-audited financial results are required to be

results {Clause 41 (I) (d)}	financial results for the last quarter, audited financial results for the entire financial year are also required to be submitted, as soon as they are approved by the Board.	reviewed by the statutory auditors of the company (limited review) and copy of that report shall be provided to the Stock Exchange within 2 months from the end of the quarter.
Submission of financial results {Clause 41(I)(e)(i)}	In addition to furnishing of quarterly / year to date stand alone results to the stock exchange, a company may also submit consolidated results within 1 month from the end of the quarter.	Consolidated results may now be submitted within 2 months from the end of the quarter.
Manner of approval and authentication of financial results {Clause 41 (II)(d)}	The limited review report as specified in Clause 41(I)(c)(i) shall be placed before the Board of Directors or committee as mentioned in Clause 41(II)(b) before submitting the same at the Stock Exchange.	Such report will be placed before Board of Directors is required, only if there is a variation exceeding 10 %, between un-audited financials and audited financials amended pursuant to a limited review, mentioned in Clause 41(IV)(a).
Publication of financial results in newspapers { Clause 41(VI)(b)}	A company has an option to publish either standalone financials or consolidated financials in the newspaper, if it has submitted both, consolidated and standalone financial results, to SEBI.	It is now mandatory for a company to publish consolidated financial results, if it has submitted both, consolidated and standalone financial results, to SEBI.

The above amendments made to Clauses 16, 19, 24 and 41 of the equity listing agreement would be applicable with immediate effect. However, with regard to Clause 41, the provisions under sub-clause (VI) item (b) relating to submission and publication of the financial results shall be applicable from the second quarter for the current financial year.

Stamp Duty on P- Notes, Debentures slashed by the Government

The Government of India has trimmed down the stamp duty on debentures and promissory notes (P-Notes). The motive behind the lower stamp duty is to expand the bond market.

The new rate of stamp duty on the issuance of the debentures will be dependant upon the tenor of the debenture subject to 0.25% per year or Rs. 25 lakh which ever is lower.

The stamp duty on the P- Notes has been slashed by one-fifth. The new rates for P- Notes are as follows:-

Rates of Stamp Duty	**Amounts**
10 paise	Less than Rs. 250
15 paise	More than Rs. 250 but less than Rs. 1000
25 paise	More than Rs.1000

Hitherto, issue of debentures attracted stamp duty of an average 0.375 % of the value of issue & P- Notes attract stamp duty of 0.05 % on the value of issue. The introduction of e- payment system by several states shall make it easier & practical for administration of the revised rates.

ACCOUNTS & AUDIT

NEW FORMS UNDER COMPANIES ACT, 1956

New Forms for submission of desired documents/ information by the Companies with the Ministry of Company Affairs in electronic form have been recently notified. The new form shall be in force with effect from 28th September, 2008. The new forms prescribed by the Government vide the said notification are as under:-

1. Form No. 20B [Annual Return by a company having a share capital]
2. Form No. 21A [Annual Return by a company not having a share capital]
3. Form No. 23AC [for filing Balance Sheet and other documents]
4. Form No. 23ACA [for filing Profit and Loss Account and other documents]

THE COMPANIES BILL, 2008

The Union Cabinet recently approved the Companies Bill, 2008 for introduction of the same in the Parliament. With the passage of Bill in the Parliament and on its approval by both the Houses, the Bill shall replace the Companies Act, 1956 – the existing statute for regulation of companies in the country.

In view of the globally changing economic and commercial environment, the Union Cabinet has considered to have a comprehensive revision of the existing Companies Act, 1956.

The said new Companies Bill, 2008 will enable the corporates in India to operate in a best regulatory environment of international practices that fosters entrepreneurship, investments and growth.

Some silent features of the same are as under:

As per existing Companies Act, 1956	Proposed in the Companies Bill, 2008	Remarks
Minimum number of person required to incorporate a company is 2 in case of private company and 7 in case of public company.	Formation of One Person Company (OPC) to be allowed.	A single person will be able to set up a company.
Minimum paid up share	No criteria of minimum	It will be possible to

As per existing Companies Act, 1956	**Proposed in the Companies Bill, 2008**	**Remarks**
capital for forming - • Public Limited Company - Rs. 5 lacs • Private Limited Company - Rs. 1 lacs.	paid up share capital to start a company.	incorporate new company in future even without any paid up share capital.
Section 390 to 396 (Chapter V) deals with compromise, arrangements and reconstruction which include mergers and acquisitions which requires approval of High Court and other regulatory authorities like RBI, BIFR etc.	Single forum for approval of mergers and acquisitions, along with concept of deemed approval in certain situations.	Single forum may reduce the time period involve in mergers and acquisitions. However, with the constitution of Competition Commission of India (CCI) in due course, picture will change accordingly as CCI have its own approval route.
Present Act specifies minimum no of directors - in case of private Company – 2 - in case of public Company – 3 Listing agreement with the stock exchange requires appointment of independent directors on the board.	Independent directors shall constitute at least 33% of the total numbers of directors.	All companies are required to comply with the proposed amendment and have to appoint requisite independent directors on their board. Listed companies are additionally required to comply with listing agreement also.
Company limited by shares may issue shares with differential rights as to dividend, voting or otherwise subject to Section 86 read with Companies (Issue of Share capital with differential voting Rights) Rules, 2001 (“Rule”).	Shares with differential voting rights to be done away with.	Company will not be allowed to issue shares with differential voting rights.
Sec. 2(13) states that *“Director” includes any person occupying the*	Every company to have at least one director resident in India.	Company will not be allowed to appoint only foreign directors on its

As per existing Companies Act, 1956	Proposed in the Companies Bill, 2008	Remarks
position of director, by whatever name called. Thus, presently there is no provision regarding nationality of director.		board but have to appoint at least one director resident in India.
Sec. 79 allows companies to issue shares at discount.	Shares will not be allowed to issue at discount.	Company will not be allowed to issue shares at discount.
Present Act requires approval of the Central Government for the appointment of managing directors and whole time directors, if remuneration exceeds the ceiling prescribed in Schedule XIII.	Annulling the government's role in the appointment of managing directors and whole time directors, and in setting their remuneration. ***(Purpose*** *– Substitution of Government control by Shareholders' control).*	No Central Government approval will be required for the appointment of or setting/ revision of remuneration payable to managing directors and whole time directors.
Present Act requires approval of the Central Government for converting public limited company to private limited company	Transition of private limited company to public company and vice versa will not require Central Government's approval.	Company can covert its status (from public to private) without taking Government's approval. For conversion from private company to public limited company, only shareholders' approval is required.