M V DAMANIA & CO.
CHARTERED ACCOUNTANTS

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E-Trade Mauritius Ltd. (AAR)

Facts and Background of the case:

The Applicant Company was incorporated in Mauritius and had a Tax Residency Certificate issued by Mauritius Government. It is a subsidiary of a USA based Company. It received capital contribution and Loans from the US Company which was utilised to purchase shares of ILFS Ltd. in India. The Foreign Investment Promotion Board (FIPB) approved such purchase of shares. Accordingly the shares were purchased and duly registered with the Company. It even received the dividends that were declared during the period it owned the shares.

Subsequently in the year 2007, it sold the shares of ILFS Ltd. To HSBC Violet Investment (Mauritius) – a Company incorporated in Mauritius and thereby earned Capital Gain that is chargeable to tax in India. According to the Article 13(4) of the India - Maritius Tax Treaty, such Capital gains is not chargeable to tax in India The Applicant Company therefore seek AAR Ruling to determine whether in view of Article 13(4) of the Treaty, such Capital Gain on sale of shares will be taxable.

Contention of the Revenue:

The Department contended that although the legal ownership of the Company visibly vests with the applicant Company, the real and beneficial owner of the Capital Gains was the Parent Company in USA which controlled the Applicant Company. The Applicant Company was only used as a conduit to take benefit of the exemption available in the Indo-Mauritius Treaty thereby to avoid Capital Gain Tax. On receipt of the sale consideration, the Applicant Company declared dividend and diminish the capital to allow the funds to flow to the parent Company.

It further argued that even after the Supreme Court decision in the Azadi Bachao Andolan case, the question of colorable devise is still open for examination and it is up to the Revenue to examine the real nature of transaction.

Contention of the Applicant:

The Applicant contended that they havea valid Residency Certificate issued by Mauritius Authorities. The concept of beneficiary Ownership is irrelevant in the context of Article 13 of The Treaty as the same applies only to Article 10 and 11 of The Treaty on Dividend and Interest. The applicant further states that in view of Circular No. 682 and 789 and also Supreme Court decision in the case of Azadi Bachao Andolan, the inquiry proposed to be made by The Revenue is a futile exercise.

AAR Ruling:

It was held by the Advance ruling authority that if a Resident of a third country, in order to take advantage of a tax treaty sets up a conduit entity, legal transactions entered into by that conduit entity cannot be declared invalid. The colorable devise adopted through dishonest methods can be looked into to judge the legal validity of transaction from tax angle. However, any tax avoidance is not objectionable if it is within the framework of law and is not prohibited by law.

The AAR held that on facts of the case the subsidiary is a separate legal entity and has its own corporate structure. Merely because the USA parent Company had provided funds to the Applicant Company and played a role in negotiating the sale transaction does not lead to any conclusion that the shares were in reality owned by the parent Company.

The AAR held that the ground realities of mutual business and economic relationships between a Holding and a Subsidiary Company must be respected. It is unrealistic to expect that subsidiary Company should run its business independent of any control and assistance from Holding Company.

All the legal formalities for purchase of the shares and their subsequent transfers had been complied with and the consideration had been received by the Applicant, it is difficult to assume that the Capital Gain had not arisen to the Applicant Company.

Consequently the Capital Gain will not be chargeable to tax in India.

Our Comments:

It is yet another attempt by the Revenue to deny the Treaty benefit of the exemption available on the Capital Gains to an entity set up in Mauritius. However this will put at rest the doubts in the foreign investors as regards the availability of Capital Gains exemption for entity set up in Mauritius.

Although the AAR Rulings are applicable only to that particular transaction, it has a lot of persuasive value.

Van Oord ACZ India vs. CIT (Delhi High Court)

Facts and Background of the case:

Karnataka High court in the case of Samsung Electronics had held that the person making payment to the non-resident is required to withhold tax under section 195 for every payment that they make to the non-resident. Such person cannot step into the shoes of the Assessing Officer to examine whether such payment constitutes taxable income in the hands of non-resident recipient or not. In case such person is of the opinion that such payment is not income for the non-resident, he must approach the Assessing Officer and obtain a certificate under section 195(2) or 197 for lower or no deduction of tax from the payment.

Delhi High Court disagreeing with the above decision of the Karnataka High Court ruled that the tax is required to be withheld from the payment to the non-resident only in case where such receipt in the hands of non-resident constitutes taxable income in India. The Delhi High court referred to the Supreme Court decision in the case of Transmission Corporation of India where it was observed by the apex court that the obligation to deduct tax at source would be attracted only when the sum was chargeable to tax in the hands of the non-resident recipient.

The court agreed with the observation of the special bench of the Tribunal in the case of Mahindra and Mahindra v. DCIT wherein it was held that when the amount to be remitted to non-resident is not chargeable to tax in India in view of the domestic law or the Treaty between the countries, the person responsible for making such payment is not required to withheld tax from such payment. He cannot be considered as the *"assessee in default"* if the payment so made is not taxable in India.

Thus the High Court held that since the reimbursement of expenses made to the Foreign Company is not taxable in India, Van Oord ACZ India was not required to deduct tax at source from the payments made to its parent Company and thus no disallowance can be made under section 40(a)(ia) for non-deduction of tax.

This decision is a great relief for the Companies making remittances abroad which are not taxable under the Act or Treaty, who were under great dilemma pursuant to Samsung Electronics decision by the Karnataka High Court.

Compiled by : Malay Damania

Fair vale concept in International Financial Reporting Standards

SR No.	IFRSs	Initial Recognition	Subsequent Measurement
1	IFRS 1 -First Time Adoption of IFRSs	x (deemed cost)	As per respective IFRSs
2	IFRS 2 -Share- based Payment	x	x
3	IFRS 3 -Business Combinations	x	As per respective IFRSs
4	IFRS 5 -Non- current Assets Held for sale and Discontinued Operations	x	x
5	IAS 16 -Property, Plant, and Equipment	(cost)	x
6	IAS 17 -Leases	x	Not Applicable
7	IAS 19- Employee Benefits (for plan assets)	x	x
8	IAS 20 -Governments Grants	x	x
9	IAS 26 -Accounting and Reporting by Retirement Benefit Plans	x	x
10	IAS 28 -Investments in Associates	x	x
11	IAS 36 -Impairment of Assets	Not Applicable	x (recoverable amount)
12	IAS 38 -Intangible Assets	(cost)	x
13	IAS 39 -Financial Instruments: Recognition and Measurement	x	x (for some)
14	IAS 40 -Investment Property	(cost)	x
15	IAS 41 -Biological Assets	x	x

Note:
x- Denotes fair value concept may be used

Compiled by : Bharat Jain

SEBI Update- Retail Investor

Application Supported by Blocked Amount (ASBA)

With the Stock markets stabilizing after global recessionary scenario, public interest in IPO's and FPO's has been on a high. With SEBI making the ASBA route open for application in public issues, industries as well as investors are expected to reap maximum benefit of the same.

In its continuous Endeavour to combat investor grievances and making the public issue facility more efficient, SEBI vide its circular dated 30th December, 2009 has clarified about the introduction of ASBA as a supplementary route for investors to apply in public issues.

Now, what exactly is ASBA.

ASBA stands for Application Supported by Blocked Amount.

ASBA means an application for subscribing to an issue containing an authorisation to block the application money in a bank account.

Currently, when an investor applies to a public issue through non-ASBA route, his application money is withdrawn from his Bank Account and gets deposited in the Escrow account of the issuer company. Until the allotment process is completed, which takes around 15-20 days, (max 22 days which has been recently reduced to 12 days) the issuer company earned interest on that amount, and if the issue is heavily oversubscribed the interest amount can even cover up the share issue expenses. The unalloted amount is refunded thereafter. So the amount is out of reach for the investor for at least 20-25days.

With introduction of ASBA, the amount remains blocked in the account of the investor and the amount is withdrawn only to the extent of allotted shares. The investor gains here completely as there is no loss of interest for him and as soon as he knows that the amount has been unblocked due to non-allotment he can utilize the same for applying in another public issue.

ASBA Process :

An ASBA investor, i.e retail individual investor or QIB's (w.e.f 1.5.2010 vide circular dated 6th April,2010) shall submit an ASBA form physically or electronically through the internet banking facility, to the SCSB(Self Certified Syndicate Bank) with whom, the bank account to be blocked, is maintained. The SCSB shall then block the application money in the bank account specified in the ASBA, on the basis of an authorisation to this effect given by the account holder in the ASBA. The application money shall remain blocked in the bank account till finalisation of the basis of allotment of the issue or till withdrawal/ failure of the issue or till withdrawal/ rejection of the application, as the case may be. The application data shall thereafter be uploaded by the SCSB in the electronic bidding system through a web enabled interface provided by the Stock Exchanges.

Once the basis of allotment is finalized, the Registrar to the Issue shall send an appropriate request to the Custodian Banker of SCSB for unblocking the relevant bank accounts and for transferring the requisite amount to the issuer's account designated for this purpose. In case of withdrawal/ failure of the issue, the amount shall be unblocked by the SCSB on receipt of information from the pre-issue merchant bankers through the concerned Registrar to the Issue. The Lead Merchant Banker shall ensure that adequate arrangements shall be made to collect all ASBA applications and to consider them similar to non-ASBA applications while finalizing the basis of allotment.

ASBA facility is available for public issues as well as right issues. ASBA investors also have the right to revise their bids as non-ASBA investors.

Conclusion:-

As far as investor is concerned, the ASBA route has no drawbacks for him to accept it as an option provided the bank where he holds the bank account provides the ASBA facility. The list of banks providing this facility is available on the SEBI website.

However, the stock brokers are expected to loose a huge amount of business in terms of the commission they received for accepting applications.

Also the issuer company will not be able to earn interest in Escrow Account to cover up for their share issue expenses as the amounts will be received only on allotment, however they can gain in terms of chances of the issue getting fully subscribed will increase.

As far as SEBI is concerned, it is always in a Win-Win situation as always.

Compiled by : Nimish Ashar (Pune)