NEWSLETTER

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M. V. DAMANIA & Co.

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INTERNATIONAL TAX

ACIT v. Dufon Laboratories (Mumbai ITAT) on Transfer Pricing

ACIT v. Dufon Laboratories (Mumbai ITAT) on Transfer Pricing

Facts: The Indian Company (ICO) was engaged in the business of processing and export of chemicals. ICO sold majority of its products to its Associated Enterprise in USA (AE). ICO also had sales comprising of about 2.5 % of its sales to other independent smaller enterprises of Asian countries. These independent enterprises purchased in smaller quantities and sold to small time buyers in Asian countries. The AE bought in larger quantities and eventually sold to big Corporates in USA and Europe.

The average price charged by ICO to these smaller independent entities were Rs. 617/- per kg. Whereas the average price charged to the AE was Rs. 440/- per kg.

The Assessee Company contended that there are significant differences in quantity sold, geographical and customer profiles. The price charged to the independent entities is not the right basis for the price to be charged to the AE for the purpose of arriving the arms f length price. The Assessing Officer rejected the claim of the Assessee Company and made adjustment by adopting the transfer price based on average realisation from independent entities.

Incidentally, the profit margin of the Assessee Company was 49% even without considering the adjustments, where as the AE had incurred losses.

Issue:
Whether the Assessing Officer was justified in making the transfer price adjustment.

The Mumbai Tribunal held that:

- The turnover quantity to AE was more than 50 times that of the non-AEs. Such difference in magnitude would have significant impact on prices.
- In Ranbaxy Laboratories Ltd, the Tribunal held that a particular entity in a particular country should be compared with a similar entity in the same country as geographical locations would, in several ways, influence transfer pricing.
- The AE dealt with high profile Corporates in competitive markets of USA and Europe compared to the sales to non-AEs that was very small in quantity who were small players in South East Asian countries.
- The adjustment made by the Assessing Officer would result in transfer pricing being higher to the price recovered by the AEs from their customers.

Accordingly the Tribunal, accepting the contention of the Assessee Company held that no adjustment was necessary and the transactions with AEs were on Arms f Length Price.

ADIT v. Bureau Veritas, France (Mumbai Tribunal) on FTS, and
Goldcrest Exports v. ITO (Mumbai Tribunal) on next page..

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ADIT v. Bureau Veritas, France (Mumbai Tribunal) on FTS:

Facts: The Assessee was French Company. It has a PE in India. The PE broadly has two kinds of activities ? Marine services and Certification services. The marine services included inspection, testing and survey of ships. The certification services included ISO certification and occupational, health and safety certification.

The PE had made provision for technical fees payable to the Head Office. The Assessee contended that the amount provided was towards allocation for reimbursement of actual expenses incurred by the Head Officer.

The Assessing Officer contended that the payment made by the PE to the head office represented payment towards FTS and since tax was not deducted at source, the same was disallowed under section 40(1)(ia) of The Act and added back to the income of the PE.

The ITAT held that:

Article 13 of The India-France Treaty restricts the scope of the FTS to payments which **gmade available h** the technical knowledge, experience etc. As the payment represented the allocation of technical and administrative expenses, it was not for any specific technical services that made available the technical knowledge or experience. Therefore such payment was not covered under Article 13 of the India-France treaty and hence not taxable.

Goldcrest Exports v. ITO (Mumbai Tribunal)

Facts: The Assessee Company (GCE) was engaged in the business of export and import of various commodities. Through an independent broker, it entered into a contract for export of certain commodities to a UK Company. Later on it cancelled the contract on the ground that the contract was entered into by the broker not them. UK Company claimed compensation for non-compliance with the contract and resorted to arbitration. The arbitration award was passed against the GCE. The compensation was based on the difference between market price of the agreed commodities and the contract price. GCE was also asked to pay interest from the date of the arbitration award till the date of actual payment.

GCE made provision in the books of accounts for the compensation and interest payable thereon and claimed the same as business expenditure.

The Assessing Officer disallowed the claim the Company on the ground that tax was not deducted at source in respect of the provision.

The Mumbai Tribunal held that:

The compensation was paid in compliance of the trading contract of GCE with the UK Company. Therefore the compensation was in the nature of gBusiness Income h and covered by Article 7 of the Treaty between India and UK.

The contract was entered into by an agent, who was not a dependent agent on the UK Company and therefore there did not exist a PE in India. In absence of PE of UK Company in India, there was no tax liability. Consequently there was no requirement of withholding tax on such payment.

The interest awarded in an arbitration award looses its original character and partakes the character of judgment debt. Therefore interest partakes the character of compensation and consequently there is no obligation to withhold tax on interest as well.

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INCOME TAX

Document Identification Number

Income Tax department introduces Document Identification Number - DIN for tax filing & correspondence:

AMENDMENT AS PER FINANCE ACT 2010

- Under provisions of newly inserted Section 282B, income-tax authority is required to allot computer generated Document Identification Number before issue of every notice, order, letter or any correspondence to any other income-tax authority or to assessee or any other person and such number shall be quoted thereon.
- It also provides that every document, letter, correspondence received by income-tax authority or on behalf of such authority, shall be accepted only after allotting and quoting of a computer generated Document Identification Number.
- In order to cover entire gamut of services mentioned in section 282B on pan-India basis, it would be essential to have requisite infrastructure and facilities in place.
- It is proposed to amend provisions of section 282B so as to provide that Document Identification Number will be required to be issued on or after 1st July, 2011.

ANALYSIS OF SAID AMENDMENT:

- Taxpayers will now have to procure 'new number' for filing returns and making any communication with Income Tax department
- Unique Document identification number (DIN) will be quoted on "every" income tax-related communication, including returns to be filed next year for financial year 2010-11 similarly in lines with PAN and TAN.
- According to new guidelines brought out by Central Board of Direct Taxes, DIN will be mandatory "in respect of every notice, order, letter or any correspondence" with department by taxpayers.
- DIN will be generated by the I-T department and is claimed to be useful for assesses in:
  - Error-free filing of tax returns,
  - Claiming refunds and
  - Other communication with department

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- Numbers will be generated and allotted by 'Aykar Sampark Kendras'.
- I-T officials will also be allotted numbers in order to streamline process and number has to be produced thereon for every activity with department
- According to section 282B of Income Tax Act dealing with DIN if document sent to tax authority does not bear this unique computer-generated number then "such document, letter or any correspondence shall be treated as invalid and shall be deemed never to have been filed"
- DIN is claimed to have been aimed at bringing more transparency in tax administration.

Compiled by : Yogendra Jain

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Accounting Policies, Changes in Accounting Estimate and Errors Major items of GAAP differences (IFRSs vis a vis Indian GAAP):

S.No	Particulars	As per IFRSs	As per Indian GAAP
	Relevant Text	**IAS 8** **Accounting Policies, Changes in Accounting Estimate and Errors**	**AS 5** **Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies**
1.	Change in Accounting Policy	Requires Retrospective application of changes in accounting policy by adjusting opening balances of equity statement of the earliest period presented and other Comparative figure presented accordingly.	Retrospective effect is given in current year income statement with appropriate disclosures.
2.	Change in Accounting Estimate	Prospective effect, by reporting in income statement of current year and future, if applicable	Similar to IFRS
3.	Correction of Errors	Comparatives figures are restated and, if the error occurred before the earliest prior period presented, the opening balances of assets, liabilities and equity will be restated.	Restatement is not required. The effect of correction is included in current year income statement with separate disclosure as Prior Period items.
4.	New Accounting Pronouncement	New accounting pronouncement that have been issued but are not yet effective at the end of the reporting period needs to be disclosed. Possible impact of said new pronouncement if reasonably estimated needs to be disclosed.	Not Required.

Provisions, Contingent Liabilities and Contingent Assets Major items of GAAP differences (IFRSs vis a vis Indian GAAP).. cont.

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Provisions, Contingent Liabilities and Contingent Assets Major items of GAAP differences (IFRSs vis a vis Indian GAAP):

S.No	Particulars	As per IFRSs	As per Indian GAAP
	Relevant Text	**IAS37** **Provisions, Contingent Liabilities and Contingent Assets**	**AS29** **Provisions, Contingent Liabilities and Contingent Assets**
1.	Recognition of provisions	Based on legal and constructive obligation both.	Primarily based on legal obligation
2.	Discounting of Provision	Where the effect of the time value of money is material, the amount of a provision should be the present value of the expenditures expected (Discounted Value) to be required to settle the obligation.	The amount of a provision should not be discounted to its present value.
3.	Contingent Assets	Requires certain disclosures in respect of contingent assets in the financial statements where an inflow of economic benefits is probable.	In contrast to this, as a measure of prudence, the Accounting Standard does not even require contingent assets to be disclosed in the financial statements. However contingent assets are mentioned in Directors Report.
4.	Constructive obligation	The effect of recognizing provision on the basis of constructive obligation is that, in some cases, provision will be required to be recognized at an early stage.	There is no binding on creating provision for constructive obligation.
5.	Restructurings cost	Constructive obligation needs to be considered at the time of provisioning of restructuring cost. Constructive obligation includes formal announcement of restructuring scheme/ its major features even though actual implementation of the same is not yet started.	A provision for restructuring costs is recognized only when the recognition criteria for provisions are complied with and corresponding liability is reliably estimated.
6.	Changes in existing decommissioning , restoration and similar liabilities.	Provisions needs to be adjusted for changes in amount/ timing of future cost / discounting factors	No specific guidance

Compiled by Bharat Jain

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