NEWSLETTER

JULY 2011

M. V. DAMANIA & Co.

INTERNATIONAL TAX

Verizon Data Services India Pvt. Ltd. vs. CIT

Facts: The applicant is an Indian Company – a wholly owned subsidiary of American Company. It was engaged in the business of providing services relating to development and maintenance of telecom software solutions and certain information technology related services on a captive basis to its Verizon US parent Company.

In order to build in efficiency built into the system and improve the productivity, the parent Company seconded certain employees of its affiliated Company in USA (USCO) engaged in the similar business of activity to the Indian Company.

The highlight of the secondment agreement was:

▪ The USCO deputed three persons to India.
▪ Each of these persons was to function directly under the direction, control and supervision of the INDCO.
▪ The USCO was neither responsible nor liable for performance of the deputed persons.
▪ The deputed persons would continue to be on the payroll of USCO.
▪ The USCO would pay the salary of the seconded employees and the INDCO would reimburse the salary so paid by the USCO, net of taxes.

Issue: Whether the reimbursement of salary paid to the USCO taxable as income accruing to the USCO? Whether any tax is required to be withheld on such payment?

The Tribunal held:

▪ It was mentioned in the agreement that while the seconded employees are providing services to the INDCO, they continue to remain the employees of the USCO. Their employment can only be terminated by the USCO. This means that the managerial services that they perform were performed on behalf of the USCO and not as employees of INDCO.

▪ The capacity in which the person receives amount determines its taxability. The USCO receives amount from INDCO for deputing persons in India for providing managerial services. The application of income by the USCO while making payment of salaries to its employees has nothing to do with its accrual. The amount paid to the employees is by virtue of their employment with the USCO.

▪ The nature of both the receipts viz. one in the hands of USCO

cont.

for rendering managerial services and two in the hands of employees by way of salaries springs from two different sources and are of different character. By correlating the two neither the nature nor the substance of the transaction would change to give it the character of reimbursement.

▪ Therefore the amounts paid by the INDCO represent income accruing to the USCO.

▪ From the MOU to the DTAA, it was clear that the "make available" clause does not apply to non-technical services. Since the services rendered will come within the purview of Managerial services, the payments were Fees for Included services under Article 12(4) of the DTAA as well as Fees for technical services under section 9(1)(vii) of the Act and tax will have to be deducted at source under section 195 of the Act.

cont.

INTERNATIONAL TAX *(cont.)*

ITO vs. Mahavirchand Mehta – Mumbai Tribunal

Facts: The taxpayer is a resident of UAE. During the year under consideration, he earned short term capital gain on sale of shares in India.

The tax payer contended that since he was resident of UAE, in terms of Article 13 of the DTAA, it is only UAE who has right to tax the capital gain.

The Assessing Officer rejected the claim of the assessee on the ground that he has actually not paid any tax in the UAE. He further observed that to claim the benefit of Article 13, it is not sufficient for the tax payer to be just "Resident of the other contracting State" but he also has to prove that he has actually paid tax on the income in respect of which the benefit is claimed.

Issue: Whether the expression "liable to tax" used in Article 4(1) of the DTAA implies that the person should actually be liable to pay tax in that contracting State?

The Mumbai Tribunal held:

The Tribunal held that the term "liable to tax" does not mean that the person should be actually liable to tax in that contracting state. It is enough if the other contracting State has a right to tax that person, whether or not such right is exercised.

Relying on the decision of Green Emirates Shipping & Travel, the tribunal observed that the avoidance of double tax is not dependent on tax being actually paid in one of the contracting States. The proposition that double tax avoidance is not permissible unless the tax is actually paid is contrary to the intent of Section 90 of The Income Tax Act.

To avail the benefit of the DTAA, all that is necessary is that the person should be liable to tax by reason of domicile, residence, place of management, incorporation etc.

Thus the tax payer will be able to avail the benefit of the DTAA between India and UAE.

Compiled by: Mr. Malay Damania

IFRS

INTRODUCTION TO IFRS 13: "FAIR VALUE MEASUREMENT"

A. Introduction:

IFRS 13 Fair Value Measurement that was issued on 12 May 2011 defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. Prior to the introduction of IFRS 13 there was no single source of guidance on fair value measurement and inconsistencies in guidance added to the complexity of financial reporting.

IFRS 13 establishes a single framework for all fair value measurements when fair value is required or permitted by IFRS. IFRS 13 does not change when an entity is required to use fair value, but rather, describes how to measure fair value under IFRS when it is required or permitted by IFRS.

B. Reason for issuing IFRS 13:

To reduce complexity and improve consistency in application when measuring fair value. Many IFRS require or permit entities to measure or disclose the fair value of assets, liabilities, or equity instruments. But prior to the issuance of IFRS 13, the guidance on how to measure fair value was limited and, in some cases, the guidance was conflicting. IFRS 13 consolidates and clarifies the guidance on how to measure fair value.

To enhance disclosures for fair value. New disclosures will help users to better assess the valuation techniques and inputs used to measure fair value.

To increase convergence with US GAAP, which has also been amended by the FASB.

C. Scope and objective

IFRS 13 applies to assets, liabilities and an entity's own equity instruments that, under other IFRSs, are required or permitted to be measured at fair value or when disclosure of fair values is provided. It does not apply to share-based payment transactions within the scope of IFRS 2 Share-based Payment and leasing transactions within the scope of IAS 17 Leases. These standards still refer to their measurement requirements as fair value. However,

cont.

both standards have been amended to clarify that for items within their scope, the term 'fair value' is applied based on guidance in the respective standard rather than based on the guidance in IFRS 13. IFRS 13 also does not apply to measurements that are similar to but not fair value, e.g. net realisable value or value in use.

D. Key Terminology:

Fair value	The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.
Active market	A market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.
Exit price	The price that would be received to sell an asset or paid to transfer a liability.
Highest and best use	The use of a non-financial asset by market participants that would maximise the value of the asset or the group of assets and liabilities (e.g. a business) within which the asset would be used.
Most advantageous market	The market that maximises the amount that would be received to sell the asset or minimises the amount that would be paid to transfer the liability, after taking into account transaction costs and transport costs.
Principal market	The market with the greatest volume and level of activity for the asset or liability.

E. Key principles and requirements

The following table provides an overview of the key principles and requirements of IFRS 13:

Area	Key principles and requirements
General principles	• Fair value is an exit price • Measurement considers characteristics of the asset or liability and not entity-specific characteristics • Measurement assumes a transaction in the entity's principal (or most advantageous) market between market participants • Price is not adjusted for transaction costs • Measurement maximises the use of relevant observable inputs and minimises the use of unobservable inputs • Three-level fair value hierarchy is extended to all fair value measurements
Specific application principles	• Non-financial assets – measurement is based on highest and best use • Financial assets and liabilities with offsetting risks – allows measurement of net exposures in limited circumstances • Liabilities and an entity's own equity instruments – quoted prices are used if available; if not, then quoted prices for an identical item held as an asset are used before resorting to other valuation techniques
Disclosures	• Fair value hierarchy disclosures are extended to non-financial assets and liabilities measured at fair value • Information about non-recurring fair value measurements introduced

cont.

Introduction to IFRS 13: "Fair value measurement" (cont.)

	• Effect on profit or loss for recurring fair value measurements categorised within Level 3 • Information about fair value disclosed for items not measured at fair value but for which fair value is disclosed • More detail in interim financial statements for fair value of financial instruments
Other	• Leases and share-based payments are out of the scope of IFRS 13, as is the determination of value in use for impairment testing and net realisable value for inventories • The standard is applied prospectively from 1 January 2013 • Early application is permitted

F. Fair value hierarchy

When measuring fair value, an entity is required to maximise the use of relevant observable inputs and minimise the use of unobservable inputs. IFRS 13 includes a fair value hierarchy (described in the table below) which prioritises the inputs in a fair value measurement.

Fair value hierarchy:.

	Level 1	Level 2	Level 3
Definition	Quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date	Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly	Unobservable inputs for the asset or liability
Example	Quoted prices for an equity security that trades on the London Stock Exchange	Interest rates and yield curves observable at commonly quoted intervals, implied volatilities and credit spreads	Projected cash flows used to value a business or non-controlling interest in an entity that is not publicly listed

G. Valuation techniques and inputs:

IFRS 13 describes three different valuation techniques that may be used to measure fair value (which would be classified within the hierarchy above based on the inputs used in the valuation technique):

▪ Market approach: uses prices and other relevant information from market transactions involving identical or similar assets or liabilities

▪ Income approach: converts future amounts (e.g., cash flows or income and expenses) to a single current (discounted) amount

▪ Cost approach: reflects the amount required currently to replace the service capacity of an asset (frequently referred to as current replacement cost, which differs from the cost incurred)

Management must use valuation techniques that are appropriate in the data is available. In some cases, this will result in more than one technique being used (for example, using both an income and a market approach to value a business or cash-generating unit). Regardless of the technique(s) used, entities are required to maximise the use

Introduction to IFRS 13: "Fair value measurement" (cont.)

of observable inputs and minimise the use of unobservable inputs. When multiple valuation techniques are appropriate, management evaluates the results and selects the point within any indicated range that is most representative of fair value in the circumstances.

H. Effective date of transition:

IFRS 13 is applicable prospectively for annual period beginning on or after 1st January 2010. Early application is permitted. The new disclosures are only required for period beginning after IFRS 13 is adopted ie comparative disclosures for prior period are not required.


Compiled by: Mr. Bharat Jain

INFORMATION TECHNOLOGY

IT Problems with Solutions

If your PC is taking ages to boot up and is very slow while running programs, it might be due to a number of factors.

Problem 1 : You keep getting a "your system is running low on virtual memory" message

Perhaps you're more than familiar with this scenario: You're working on your PC and notice performance getting gradually slower and slower. Programs become harder to open and close. You wait forever for Web pages to be displayed. And then, you get some serious-sounding "virtual memory is too low" message, like the one in the following graphic.

Don't worry: This message isn't as scary as it sounds.
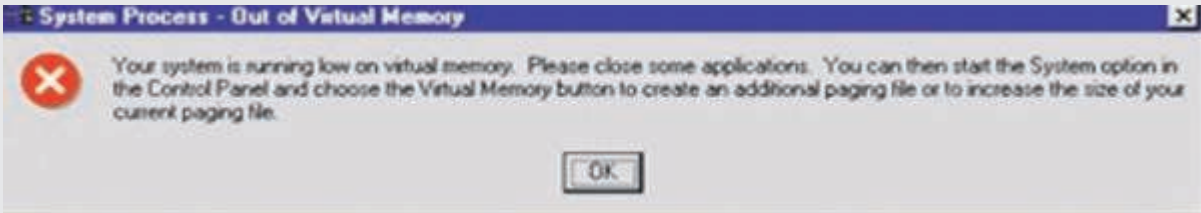
Virtual memory is the space your computer uses when it's short of RAM (Random Access Memory), which is the memory used when running programs like Microsoft Office Word or Microsoft Office PowerPoint.

So what can you do to correct this problem and prevent this message from coming up in the future? The following solution is suggested to keep your computer from displaying the "virtual memory minimum is too low" message.

The first solution is to increase your computer's virtual memory settings. To do so, you first need to determine how much RAM you currently have.

cont.

Problem 2: Not enough RAM

RAM stands for Random Access Memory and is used as a temporary storage memory by your computer. This memory is in use when tasks are being executed by different programs. Hence, you should have enough RAM memory to process all the tasks at hand; if you don't have enough RAM then this might cause the major slow down of your computer while it is booting up or processing tasks.

How to know if your computer has enough RAM

The programs that are installed on your computer usually ask for the RAM required to be present in Computer. If your computer has been running at a normal speed before the installation of such programs and has crucially slowed down with time, you might need to add more RAM on your computer system.

Also, if your computer is slowing down every time you are processing large files, or it freezes while executing several programs at once, these might be some common signs that you need to add extra RAM.

Add more RAM to your computer *(For Windows 7, Windows Vista, Windows XP)*

If you keep getting that dreaded "Your system is running low on virtual memory" message—even after you increase your computer's virtual memory—then you may need to buy more memory for your computer. To really work well:
- Windows 7 needs at least 1 GB of RAM to run.
- Windows Vista needs at least 512 MB of RAM to run, but for some applications (like Tally,) 1 GB or more of RAM is recommended.
- Windows XP needs a minimum of 256 MB of RAM, but for some applications (like Tally,) 1 GB or more of RAM is recommended.

Note: The more RAM you have, the better performance of Pc's.

Problem 3: Temporary files have built up on your hard disk

Some tasks might require you to leave the system files working for several days which will create temporary files in your hard disk. This is another reason because of which your computer is slowing down and is taking time to boot up as these type of files tend to be memory consuming. Cleansing your temporary files including your Internet history including cookies gives you a larger amount of hard disk space to work with.

How to delete Temporary Files

- To delete all temporary files you need to run CCleaner twice in a week for best results.
- When you finish removing the temporary files, reboot your computer.

IT Problems with Solutions (cont.)

Problem 4: Your computer has been infected

If your computer has been infected by a virus, a malware, a worm or a Trojan, it might have cause the slow down of your computer system and even freeze several tasks at hand. Hence, you should run a virus scan and remove all the infected files found on your system.

How to delete Trojans & Virus from your system

■ To delete all Trojans or Virus you have to update & run antivirus programme daily
■ To secure PC"S from Trojans or Virus at every time scan USB & Pen Drive Connections

Problem 5: Not enough space on the hard disk

Adding very bulky programs will automatically slow down your computer system. Hence, I will suggest users with a hard disk capacity of 1GB to leave at least 250MB free and those who have a higher hard disk storage capacity to leave at least 20% of the total capacity free. This will hence allow your computer to have enough space for both for temporary files and file swapping.

Defragmenting your hard disk - run Defraggler twice in a week for best results.

You can select Defragment utility for your hard disk to gather some dispersed spaces that can be used by the computer again.

Disk fragmentation slows the overall performance of your system. When files are fragmented, the computer must search the hard disk when the file is opened to piece it back together. The response time can be significantly longer.

Disk Defragmenter is a Windows utility that consolidates fragmented files and folders on your computer's hard disk so that each occupies a single space on the disk. With your files stored neatly end-to-end, without fragmentation, reading and writing to the disk speeds up.

When to run Disk Defragmenter

In addition to running Disk Defragmenter at regular intervals—monthly is optimal—there are other times you should run it too, such as when:
■ You add a large number of files.
■ Your free disk space totals 15 percent or less.
■ You install new programs or a new version of Windows

Compiled by: Miss. Sampada Patil