

# NEWSLETTER

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# DIRECT TAX

## Kamal Wahal – Delhi High Court

*Section 54F – Sale of house property by husband – New house property purchased in the name of wife.*

### Facts:

The assessee had inherited his 50% share in a house property. He sold this property which was long term capital gain for him. He then

purchased a new house property in the name of his wife and claim exemption under section 54F. The exemption was disallowed by the AO stating that the new property was not in the name of the assessee

### The Delhi High Court held that:

The assessee had purchased the

new property in the name of his wife and not some stranger. There was no dispute that the source of investment in new house property was the sale proceeds of the inherited house. Therefore the assessee was eligible for exemption under section 54F even if the new property was purchased in the name of his wife.

## Tarsen Kumar – P & H High Court

*Revised Return – Intimation under section 143(1)(a) does not constitute assessment.*

### Facts:

With respect to AY 2005-06 the assessee had filed his Return of Income on 26.07.2005. The Return was processed and intimation u/s. 143(1)(a) was issued on 08.12.2005

along with refund of Rs. 240/-. The assessee subsequently realized that he had not claimed credit of Rs. 360,000/-. He therefore filed a revised return on 26.09.2006.

The AO held that the return was invalid as the same was filed after the issuance of intimation u/s. 143(1)(a).

### On filing of writ petition, the P & H High Court held that:

The intimation u/s. 143(1)(a) does not constitute assessment so as to disentitle the assessee to file the revised return. It was held that the return was valid and the assessee was entitled to refund as claimed in the revised return.

cont.





# INTERNATIONAL TAX

## Bosch Ltd - Bangalore Tribunal

*Whether payment made to German Company towards rendering of a) Repairs services and b) Preventive maintenance services constitute Fees for Technical Services?*

### Facts:

The assessee was a manufacturing Company in India with both imported and local plant and machinery. Annual Maintenance contracts were entrusted to foreign suppliers. Likewise repairs contracts were also entrusted to foreign suppliers who were residents of Germany.

The assessee made payments towards repairs services and maintenance services to German Companies. In view of the assessee these payments were business profits for the German Companies and in absence of any PE not chargeable to tax in India.

The AO and CIT(A) concluded that both the payments were in the nature of Fees for Technical Services and were liable for withholding tax of 20%.

### **The Bangalore Tribunal held considering following two nature of transaction:**

1. Whether payment for rendering repairs services amounted to FTS?

The documents suggest that the machinery has to be repaired and not to be modified or improved. Every repair need technical skill or expertise but can any activity that involves skill or expertise be called technical service? Repair means 'to put something damaged, broken or not working correctly back into condition or make it work again'.

This definition presupposes

existence of machinery which is damaged and which has to be brought back to its original working condition. This cannot be done without knowledge about the machinery and the skill to bring it back to its original working condition.

The definition of the word 'service' denotes an activity to help achieve something or result in something useful or purposeful.

Explanation 2 to Section 9(1)(vii) not only contains positive constituents of services being managerial, technical or consultancy services but also enumerates which are not included in technical services.

In case of Lufthansa Cargo Ltd – Delhi High Court had held that the payments made by the Company to the non-resident

*cont.*

workshops outside India do not constitute payment of fees for managerial, technical or consultancy services as defined in Explanation 2 to Section 9(1)(vii).

Referring the same case the Tribunal held the payment to the German Companies do not come within the purview of FTS and hence not chargeable to tax in India

2. Whether payment towards 'Preventive maintenance services' amounted to FTS?

The nature of services rendered by German Companies included assistance in analyzing and solving technical problems and dysfunctions by locating and mending the cause of dysfunction by providing telephonic advice, analysis and assistance to the machine operator and for preventive measures.

Such kinds of services rendered by German Companies were not that of mere repair services but towards technical assistance and preventive maintenance. This clearly falls within the purview of definition of FTS.

The assessee was therefore liable to withhold tax from the payment made towards preventive maintenance which amounted to FTS.

*Secondment Agreement – Foreign parent Company seconded employees to Indian Company – Reimbursement of actual expenses incurred – Is it income for foreign Company or is it FTS or is it not taxable?*

### **Facts:**

The assessee Company (“Abbey India”) is an Indian subsidiary of group Company of Abbey UK. Abbey UK had outsourced certain services to another Indian Company – Msource – to provide certain financial and insurance services to customers of Abbey UK. Abbey UK also entered into a consultancy agreement with Abbey India to supervise and oversee functions of Msource in India.

For the same purpose, agreement for secondment of staff was made between Abbey UK and Abbey India. Abbey UK seconded its trained staff to Abbey India. As per the terms of this agreement, secondees were under direct management, supervision and control of Abbey India. Abbey UK was not responsible for any loss or damage caused by the works of secondees. The secondees would perform the tasks at such place as instructed by the assessee Company.

Abbey UK, however, remained the employer of the secondees. Abbey UK was responsible to pay remuneration and other social benefits and statutory payments as an employer. Abbey India was to reimburse all the expenses incurred by Abbey UK in respect of the seconded employees. Abbey UK deducted tax u/s. 192 in respect of Salary paid to these secondees. Entire cost of Salary of these secondees as incurred by Abbey UK along with the administration cost incurred on them was reimbursed by Abbey India. No tax was deducted on this reimbursement amount which was claimed as expense by the assessee Company.

The AO disallowed the entire amount of reimbursement stating that Abbey UK provided managerial services to the assessee, which constituted “fees for technical services” u/s. 9(1)(vii).

### **The Bangalore Tribunal held as follows:**

#### **Who is the ‘real and economic employer’ of the secondees under the agreement?**

If the secondees had to be on the pay roll of Abbey India, they had to sever their employment with Abbey UK thereby losing all the benefits like pension contribution, social security, insurance contribution under the UK law. Therefore the employment status with Abbey UK was kept intact. The real test of employer-employee relationship is right to hire or accept secondment, right to control and supervise, right to instruct, right to terminate services etc. All these rights were with the Indian Company by virtue of the secondment agreement. The OECD model convention also holds the view that in case of secondment arrangement, the person under whose control and supervision they are employed should be considered as real and economic employer. The mere fact that they are on the pay roll of Abbey UK does not lead to conclusion that Abbey UK is actual employer.

It was therefore held that Abbey India was the real and economic employer of the secondment employees.

#### **Whether reimbursement of expenses to Abbey UK constituted any income in the hands of Abbey UK?**

The secondment agreement stated that in consideration for secondment of staff by Abbey UK, the assessee shall make payment equivalent to the remuneration, pension contribution, statutory payments and any other sum incurred by Abbey UK applicable to each employee during their secondment period.

## *Abbey Business Services - Bangalore Tribunal*

The Tribunal relied on the decision of Supreme Court in case of TISCO and Tribunal decision in case of IDS Software and held that such reimbursement of salary and other related cost under secondment agreement cannot be regarded as income chargeable in the hands of Abbey UK.

### **Whether payment made by assessee to Abbey UK constituted FTS u/s. 9(1)(vii)?**

The agreement was only for secondment of staff and not to provide any service. Mere secondment of staff does not tantamount to provision of any service. No services were provided by Abbey UK to the assessee. It only deputed secondees to the assessee. The reimbursement of salary and related cost did not contain any mark up and therefore there was no element of profit or income to it.

It was therefore held that reimbursement of salary and other administration cost cannot be categorized as Fees for Technical Services u/s. 9(1)(vii).

### **Whether payment made by assessee to Abbey UK constituted FTS under Article 13 of the DTAA between India and UK?**

The requirement of 'make available' concept needs to be satisfied for the payment to fall under the definition of FTS under this treaty. It is quite evident that there is no make available of technology, Process, skills or expertise by Abbey UK to the assessee. Therefore reimbursement of salary and the related cost cannot be regarded as FTS under the treaty.





# TRANSFER PRICING

## Capgemini India Pvt. Ltd. - Mumbai Tribunal

### **Fact:**

The assessee Company Capgemini India is a subsidiary of US based Capgemini group (parent Company) providing software development services to its parent Company.

In its Transfer Pricing Study, it benchmarked its international transactions by applying Transactin Net Margin Method (TNMM) as the most appropriate method and arrived at arms f length margin of 13.70% over cost.

The Transfer Pricing Officer (TPO) rejected the claim of the assessee in respect of working capital adjustment, extra ordinary expenses on ESOP, adoption of multiple year data, usage of Consolidated Financial Statement and introduction of additional comparables with high related party transactions and recomputed the margin at 27.82%

over cost.

### **The Mumbai Tribunal dealt with each of the key issues as follows:**

#### **Whether ESOP cost, being extra ordinary in nature be excluded while computing margin of the tax payer?**

Extra ordinary costs need to be excluded while computing the margin between the tested party and the comparable Companies in identical situation. ESOP being extra ordinary in nature must be therefore excluded.

#### **Whether Consolidated Financial Statements of comparable Companies be considered for computing arms' length margin?**

Consolidated Financial Statements should not be considered as they include results of different overseas jurisdiction

having different market and geographical conditions which cannot be comparable with the tax payer. Thus stand alone financials and not consolidated need to be considered.

#### **Whether high loss making Companies have to be considered, when high profit making Companies are considered as comparable?**

Comparable Companies cannot be rejected on the basis of high profit or loss. A comparable can only be ignored when abnormal business conditions exist.

#### **Whether Companies with disproportionately high turnover have to be excluded considering that they have higher margins as compared to the Companies with low turnover?**

*cont.*

# TRANSFER PRICING

*Capgemini India Pvt. Ltd. - Mumbai Tribunal*

The concept of economies of scale is relevant only in case of manufacturing Companies which have high fixed cost where rise in turnover leads to reduction in per unit cost thereby increasing profit margins. The main asset in service industry is manpower which has direct correlation with turnover. Therefore high turnover cannot be the basis of rejection in software development sector. However minimum turnover criteria can be applied in order to select functionally comparable Companies.

**Whether working capital adjustment is allowed to account for the difference in working capital requirement of the tested party with the comparable companies?**

Working capital adjustment enhances the comparability of the tax payer with the comparable Companies. Such adjustment should not be denied merely on the ground that the same has not been made by the tax payer in the TP study report.



*Compiled by: Malay Damania*



# NON CTS CHEQUE BOOKS

*You can still use your Non-CTS-2010 cheque books till July 31, 2013*

The Reserve Bank of India once again announced (dated March 18, 2013) that it has extended the deadline for banks to ensure withdrawal on Non Cheque Truncation System (CTS)cheque till July 31, 2013. Now you as a bank account holder can continue to use your old format cheques for another four months up to July 31, 2013. This is the second time RBI extended this deadline, earlier 2012, the apex bank had asked all banks to withdraw the non CTS cheques, and accept only those cheques which conform to new standards from January 1, 2013, but in December 2012, the RBI had extended the deadline to convert to the new standard CTS-2010 by three months to March 31, 2013.

FYI, the CTS-2010 eliminates the current practice of physically presenting a cheque to the payee bank, thereby substantially reducing the time for cheque clearance.

In this announcement RBI also directed all banks not to ask for EMI (Equated monthly Installments) PDC's (Post Dated Cheques) from the customers either CTS cheques or Non CTS cheques, where ECS (Electronic Clearing System)/RCES (debit) facility is available. Further banks has been directed to take a mandate from the customer (borrower) to direct debit his account for equal monthly installments.

So, if you are taking loans from the Bank then no need to issue post dated cheques to bank, if ECS/RCES(debit) facility is available in your Bank/Branch/Station. This direction will reduce number of cheques transaction is Banks.

The circular also indicates "all cheques issued by banks (including DDs/POs) with effect from the date of this circular shall necessarily conform to CTS-2010 standard."



*Compiled by: Brajeswar Pandey*