

## India

# Corporate Update – November, 2007\*

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## India

### LEGAL

#### Bonus Act

#### Amendment to The Payment of Bonus Act:

Presently the Payment of Bonus Act covers those employees who are drawing salary or wage not exceeding Rs.3500/-p.m. In respect of such employees, the Bonus as is payable under the Act, shall be calculated on a salary not exceeding Rs.2500/- p.m.

The Government has issued an ordinance on 27th October, 2007 to amend the Payment of Bonus Act, make changes in the eligibility of employees to bonus based on salary drawn under the Act.

In terms of this ordinance, employees drawing salary or wages not exceeding Rs.10,000/- p.m will now be entitled to bonus under the Act. The ordinance also lays down that the computation of bonus will now be made on a salary or wage not exceeding Rs.3500/- instead of Rs.2500/- earlier.

The above ordinance is deemed to have come into force on the first day of April, 2006 and hence will be applicable for the F.Y. 2006-2007, onwards

The above may be noted for information, guidance and necessary compliance.

## India

### LEGAL

#### Company Law

##### Extension of Time for filing Charge Documents:

Companies are now permitted to file registration/ modification/ satisfaction of charge in Form 8, 13 and 17 upto a period of 300 days from the date of the event without approaching Company Law Board (CLB) for condonation of delay. Additional fees as prescribed in terms of Section 611 (2) of the Companies Act, 1956 shall, however, be levied for the delay beyond 30 days.

However, the present system of filing application for condonation of delay before CLB in terms of Section 141 will continue in respect of:

- a. where the delay is beyond 300 days from the date of event;
- b. rectification of register of charges,
- c. when documents are sought to be filed by the lenders.

The abovesaid provisions have come into effect from 27th Oct., 2007 vide CLB's order dated 27th Sep., 2007. Prior to this, any delay beyond 60 days in case of creation/modification of charge and 30 days for satisfaction of charge required CLB's approval.

## India

### TAX

#### Income-Tax

#### Rule 3 of Income Tax: Rules Dealing with valuation of perquisites notified on 7th November, 2007

**Major changes brought about by amendment to Rule 3 of the Income Tax Rules, 1962 (Vide notification number 217/2007 dated 07/11/2007 are in brief given below :-**

1. Perquisite value, for accommodation (except in hotel) provided by the employer, has been reduced with retrospective effect from financial year 2005-06 and is to be computed as per following table:-

Applicable in	Perquisite Value for Accommodation
Cities having population exceeding 25 lakhs	15% instead of 20% of salary
Cities having population between 10 lakhs and 25 lakhs	10% instead of 20% of salary
In other Cities	7.5% instead of 15% of salary

2. Perquisite value shall be determined and taxed in the hands of the employee on which FBT is not payable for use of motor car, traveling, touring, accommodation and any other expenses paid, free food and non-alcoholic beverages, any gift or redeemable vouchers/ token, expenses including membership fees and annual fees, club expenditure or any other conveyance or amenity, service, right or privileges provided by such employer.

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### TAX

#### **Supreme Court Ruling on (AS 22)**

The Hon'ble Supreme Court has held that the Accounting Standard 22 (AS 22) on "accounting for taxes on income" in so far as it relates to deferred taxation is neither ultra vires nor inconsistent with the provisions of the Companies Act. (J.K. Industries Ltd.: Case)

#### **Important Case:**

#### **CIT vs Vinay Cement Ltd ( Supreme Court)**

Contribution made towards provident fund etc; after the close of the accounting period but before the due date for filing of the return of income are allowable as a deduction u/s 43B(b) of the Act even for assessment years prior to the deletion of the second proviso by the Finance Act 2003 wef 1.4.2004.

#### **Press Report:**

#### **I-T Department urges SC to revisit BPO tax ruling in the case of Morgan Stanley**

As per the press reports, income tax department has filed a review petition in the Supreme Court, for reviewing its decision in the case of Morgan Stanley, recently given. (Source: The Economic Times)

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### TAX

#### Fringe Benefit Tax

##### **Rule for Determination of Fair Market Value of Employees Stock Option Plan (ESOP) for Levy of FBT notified:**

The Finance Act, 2007 amended the provisions of the Income-tax Act to provide that employers will be liable to pay fringe benefit tax on the value of ESOPs granted to employees as and when the ESOPs are allotted or transferred to the employees. The value of ESOPs for the purposes of levy of FBT shall be the fair market value of the ESOPs on the date of vesting of the options as reduced by the amount actually paid, or recovered from, the employee.

Explanation (i) to clause (ba) of sub-section (1) of section 115WC of the Income-tax Act defines “fair market value” to mean the value determined in accordance with the method as may be prescribed by the Board. Accordingly, a new Rule 40C has been notified by the Board.

The new Rule 40C will take effect from the 1 st April, 2008 and will, accordingly, apply in relation to the assessment year 2008-2009 and subsequent years.

The Rule as notified provides for valuation of shares allotted under ESOP by companies whether listed or not, on stock exchange.

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### TAX

#### Transfer Pricing

##### Important Decision on Transfer Pricing:

An important decision on Transfer Pricing has been rendered by ITAT Delhi Bench 'H' in the case of Mentor Graphics (Noida) Pvt. Ltd. [ITA NO. 1969/D/2006] in respect of A.Y. 2002-03. This is a case where a foreign company outsourced software development to a captive subsidiary in India.

The ITAT decided the case on facts, in favour of the tax payer and laid down important principles as must be taken into account by the Transfer Pricing Officer (TPO).

The following principles were laid down:

1. Transfer Pricing is not an exact science. Determination of arms length price is an art where mathematical certainty is not possible and some approximation cannot be ruled out.
2. Analysis must be carried out in a judicial manner and after taking into account all the relevant facts and circumstances of the case.
3. Minimum requirement is to show that controlled international transaction was properly examined and ALP fixed objectively, honestly and in a bona fide manner as required by the statutory regulations. The requirement of the statutory regulation was thoroughly discussed by the ITAT in Aztech Software & Technology Services Limited (107 ITD 141) (Bangalore Bench).

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4. In making searches for potential comparable companies, not only turnover and operating profit but functions performed and risk profile are also to be considered.
5. Even when Transactional Net Margin Method (TNM method) is applied, functional profile, assets employed, risk assumed of controlled and uncontrolled transactions are to be seen while screening comparable companies.

In the determination of the ALP, the tribunal held that the first step is to analyse the specific characteristic of the controlled transactions which are likely to affect its open market value. On selection of the comparables and the appropriate method of determining the ALP, a functional analysis is to be carried out to identify functions, risk and assets (FAR) of uncontrolled transactions and comparison should be carried out with characteristics of the controlled transaction. It was emphasized that if there are material and significant differences in the risk involved then comparables identified are not correct.

The Tribunal also held that as per the Indian regulations if there are differences which can be adjusted then adjustments are required to be made. "If the difference between companies are so material that adjustment is not possible, then comparables are required to be rejected".

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As per facts of the case the assessee was developing specific software for its parent company. The software developed was used by the parent for integrating the same with other software components developed by itself. The whole software supported by the hardware manufactured by the parent is sold as a package in the open market. The assessee was therefore a contract software development support service provider. Most of the business risks such as contract risk, market risk, credit risk, warranty risk, price risk etc. were borne by parent company. The IPR in the intangibles that were provided to the assessee for carrying out development services were owned by the parent company.

The above characteristics of the controlled transaction were not kept in mind by the TPO to find comparables and therefore the ITAT held that the order of the TPO making the adjustment was not sustainable. The ITAT also came to the conclusion that the TPO committed several minor and major errors while determining the ALP. The errors noted by the ITAT are as under:

1. The TPO took into account companies which were dealing with their related companies either as subsidiaries or as parent companies. The controlled transactions were taken into account as comparables which the ITAT held to be against the very basics of the transfer pricing guidelines.
2. The contradiction in the approach of TPO was noticed when he insisted that only data for the financial year was relevant but for his own use, he had taken into account data for financial year 2003-04 i.e. data relating to two years later.

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3. The TPO did not take into account specific characteristics of the controlled transaction while searching for comparables and failed to apply the FAR test to controlled or potentially comparable uncontrolled companies/transactions.
4. TPO refused to consider specific characteristics of transaction, functions performed and assets employed as has been done in this case. The provisions of Rule 10B have been ignored. The wide difference in the ratio of operating margins between 3.16 per cent to 37.89 per cent in final selection of comparables by the TPO was considered to be a pointer to the fact that the selection made was faulty.

For the aforesaid reason, the ALP determined by TPO was not considered to be sustainable.

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### TAX

#### Cenvat

#### **Notification No. 39/2007-Central Excise (N.T.), dated 14-11-2007**

In exercise of the powers conferred by section 37 of the Central Excise Act, 1944 (1 of 1944) and section 94 of the Finance Act, 1994 (32 of 1994), the Central Government hereby makes the following rules further to amend the CENVAT Credit Rules, 2004, namely:-

1. (1) These rules may be called the CENVAT Credit (Tenth Amendment) Rules, 2007.

(2) They shall come into force on the date of their publication in the Official Gazette.

2. In the CENVAT Credit Rules, 2004, in rule 3, in sub-rule (5), after the second proviso, the following proviso shall be inserted, namely:-

“Provided also that if the capital goods, on which CENVAT Credit has been taken, are removed after being used, the manufacturer or provider of output service shall pay an amount equal to the CENVAT Credit taken on the said capital goods reduced by 2.5 percent for each quarter of a year or part thereof from the date of taking the Cenvat Credit;”.

[F.NO. 267/01/2004-CX.8]

## India

### TAX

#### Service-Tax

##### **Date of Payment of Service Tax Amended:**

Vide Notification No.39/2007, the date of payment of service tax to the Central Government has been extended to 6th day of the month immediately following the calendar month in which the payments are received, if the duty is deposited electronically through internet banking.

In any other case, there is no change in date of payment of duty.

Where the assessee is an individual or proprietary firm or partnership firm, the service tax shall be paid to the credit of the Central Government by the 6th day of the month if the duty is deposited electronically through internet banking, or, in any other case, the 5th day of the month, as the case may be, immediately following the quarter in which the payments are received, towards the value of taxable services:

However, the service tax on the value of taxable services received during the month of March, or the quarter ending in March, as the case may be, shall be paid to the credit of the Central Government by the 31st day of March of the calendar year.

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### Important Dates to remember For the month of December, 2007

Due Date	Obligation	Challan/ Forms
15th Dec	Advance FBT for quarter ending December, 2007.	283
15th Dec	Advance Income Tax for Companies (Quarter III).	280
15th Dec	Advance Income Tax for Non Corporate Assessees.	280

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