

# NEWSLETTER

December 2015

## MVDCO ADVISORY SERVICES



CONTENTS	
Income Tax	2
FEMA	5
Audit	7
VAT	10
Mutual Fund	12



# INCOME TAX

## Income Tax case laws

### Suvaprasanna Bhattachary – Kolkatta Tribnal

**Re: Penalty proceedings under section 271(1)(c) rws 274 for concealment of income or furnishing of inaccurate particulars of income.**

#### The Kolkatta High Court made following observations:

- The order of assessment nowhere spells out or indicates that the AO was of the view that the assessee was guilty of either concealing particulars of income or furnishing inaccurate particulars of income.
- The AO will have to arrive at a prima facie satisfaction during the course of proceedings. With regard to the assessee having concealed particulars of income or furnished inaccurate particulars, before he initiates penalty proceedings. There must be 'prima facie' satisfaction of the AO that the case may deserve the imposition of penalty and this should be visible from the order passed during the course of the proceedings.
- Supreme Court's decision suggests that the satisfaction need not be recorded in a particular manner but from a reading of the assessment order as a whole such satisfaction should be clearly visible.

- The next argument that the show cause notice u/s.274 of the Act which is in a printed form does not strike out as to whether the penalty is sought to be levied on the for “furnishing inaccurate particulars of income” OR “concealing particulars of such income”. On this aspect the court observed that in the show cause notice u/s.274 of the Act the AO has not struck out the irrelevant part. It is therefore not spelt out as to whether the penalty proceedings are sought to be levied for “furnishing inaccurate particulars of income” or “concealing particulars of such income”.

The Court therefore held that the orders imposing penalty in all the assessment years have to be held as invalid and consequently penalty imposed is cancelled.

## **DCM Ltd – Delhi Tribunal**

**Re: Section 14A read with Rule 8D**

The Delhi Tribunal made following observations:

- As envisaged under Section 14A(2), the AO has neither recorded his satisfaction on the calculation of disallowance made by the Assessee nor given reasons as to how the claim of expenditure in relation to tax free income has been incorrectly made by the assessee. The AO has mechanically invoked Rule 8D.
- The AO has not established any nexus between the investments made and the expenditure incurred under the head interest expenditure and administrative expenses, before disregarding the disallowance suo moto made by the assessee u/s 14A of the Act.
- Further, as held by Delhi High Court, disallowance u/s.14A cannot exceed the amount of exempt income.

## **AMCO Power Systems – Karnataka High Court**

**Re: Section 79 – Eligibility of Carry forward and set-off of Loss**

51% shares of the assessee Company was held by holding Company. In the relevant year, the holding Company transferred 45% of its shares to another 100% subsidiary Company. The AO disallowed assessee's claim for set off of brought forward loss relying on Section 79 since the voting power of the holding Company was reduced from 51% to just 6%.

# INCOME TAX *(cont.)*

The Karnataka High Court held that

The expression “not less than 51% of voting power ....” Used in Section 79 indicated that **only voting power is relevant and not shareholding pattern**, Despite the transfer of shares, the holding Company still commands effective control over the assessee Company. The objective of Section 79 is to prevent misuse of losses carry forward by new owner. Therefore allowing the claim of the assessee, the high court held that the losses could be carried forward and set-off even if there is change in shareholding since effective control over the assessee Company is unchanged.

---

## Import of Goods into India – Evidence of Import

An importer is required to submit as evidence of import, (a) the exchange control copy of the Bill of Entry for home consumption; (b) the exchange control copy of the Bill of Entry for warehousing, in the case of 100% Export Oriented Units (EOUs); or (c) Customs Assessment Certificate or Postal Appraisal Form as declared by the importer to the Customs Authorities.

With the establishment of Free Trade Warehousing Zones / SEZ Unit warehouses, imported goods can be stored therein, for re-export / re-selling purposes for which Customs Authorities issue **Ex-Bond Bill of Entry**. All the banks are advised to consider the Bill of Entry issued by Customs Authorities named as Ex-Bond Bill of Entry or by any other similar nomenclature, as evidence for physical import of goods.

Further, in cases where goods have been **imported through couriers**, the **Courier Bill of Entry**, as declared by the courier companies to the Customs Authorities, may also be considered as evidence of import of goods.

## Review of FDI Policy

Department of Industrial Policy & Promotion (DIPP) has reviewed Foreign Direct Investment (FDI) Policy on various sectors and issued Press Note 12 making sweeping amendments. A few of them are:

- Subject to the provisions of FDI Policy, foreign investment in '**manufacturing sector**' is under automatic route. A manufacturer is permitted to sell its products manufactured in India through wholesale and/or retail, including through e-commerce without Government approval.
- FDI is permitted under automatic route in **LLPs** operating in sectors/activities where 100% FDI is allowed under automatic route and there are no FDI-linked performance conditions.
- **Investment by NRIs** under Schedule 4 of FEMA (Transfer of Issue of Securities by Persons Resident outside India) Regulations ie. Under non repatriable basis, will be deemed to be domestic investment at par with the investment made by Indian residents.
- A Company, trust and partnership firm incorporated outside India and **owned and controlled by non-resident Indians** will also be eligible for investments under Schedule 4 of FEMA Regulations and such investment will also be deemed domestic investment at par with the investment made by Indian residents.
- Limit of foreign investment cap for **Credit Information Companies** have been increased from 74% to 100% under automatic route.

- Foreign investment in **Construction development projects** have gone under major liberalisation. They are:
    - Each phase of the construction development project will be considered as a separate project for the purposes of FDI Policy.
    - Conditions on minimum area of development have been totally done away with.
    - Conditions on minimum requirements of funds have been totally done away with.
    - A foreign investor will be permitted to exit and repatriate foreign investment before the completion of project under automatic route, provided lock-in period of 3 years has been completed.
    - Transfer of stake from one non-resident to another non-resident, without repatriation of investment will neither be subject to any lock-in period nor Government approval.
    - Earning of rent/income on lease of the property, not amounting to transfer, will not amount to Real Estate business and therefore will not be construed as prohibitory activity.
  - Subject to all the conditions mentioned for FDI in Single Brand Product Retail Trading, a Single Brand Product Retail trading entity operating through brick and mortar stores, is permitted to undertake **retail trading through e-commerce**.
  - Foreign investment up to 100% under automatic route is permitted to set up **Duty Free Shops** ie. Shops set up in custom bonded area at International Airports, International Seaports and Land Custom stations where there is transit of international passengers.
-

## Consolidated Financial Statements – Companies Act 2013

### **Back Ground:**

Erstwhile only clause 32 of the listing agreement mandated listed companies to publish Consolidated Financial Statements with the principles as referred in AS 21, 23 and AS27. Neither the Companies Act, 1956 nor applicable Accounting Standards requires other companies (un-listed public and private) to prepare Consolidated Financial Statements. However such unlisted companies were allowed to prepare consolidated financial statement voluntarily following the principles as referred in AS 21, 23 and AS27.

### **Position under Companies Act, 2013 (Applicable for fy 2014-15)**

With insertion of Section 129(3) in the Companies Act 2013 ("Act"), all companies including unlisted and private companies with one or more subsidiaries will in addition to separate financial statements now have to prepare Consolidated Financial Statements ("CFS"):

*As per an explanation to section 129(3) of the 2013 Act, the word "**subsidiary**" shall **include associate company and joint venture**.*

### **The Act also provides that;**

- Such CFS shall be prepared in the same form and manner as that of the parent company.
- Such CFS shall be laid before the annual general meeting of the Company along with the laying of its financial statement.
- Company should also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries in **Form AOC-1**.
- The requirements of the Act relating to the preparation, adoption and audit of the financial statements of a parent company will, mutatis mutandis apply to CFS.

### **Principles & Manner of preparing CFS:**

Rule 6 of Companies (Accounts) Rule, 2014 ("Accounts Rule") deals with the manner of consolidation and provides that the CFS of the company shall be made in accordance with the provisions of **Schedule III of the Act and the applicable accounting standards**.

## **Exemption in preparation of CFS (Proviso to Rule 6):**

- A company which is not required to prepare consolidated financial statements under the Accounting Standards, it shall be sufficient if the company complies with provisions on consolidated financial statements provided in Schedule III of the Act.
- An intermediate wholly owned subsidiary company whose immediate parent is an Indian company is not required to prepare consolidated financial statement.
- Subject to any other law or regulation, a company which does not have a subsidiary or subsidiaries but has one or more associate companies or joint ventures or both as the case may be is not required to prepare CFS for the financial year 2014-15. (CFS is applicable from FY 2015-16 onwards).
- A company having only foreign subsidiary/ies need not prepare CFS for the financial year 2014-15.(CFS is applicable from FY 2015-16 onwards).

## **Schedule III requirements:**

Schedule III of the Act, which lays down the format for preparation of financial statements, contains the following general instructions for preparation of CFS:

- ✓ Where a company is required to prepare CFS, it shall mutatis mutandis follow the requirements of this Schedule as applicable to a company in the preparation of balance sheet and statement of profit and loss.
- ✓ In addition, the CFS shall disclose the following as additional information.
- ✦ In respect of each subsidiary, associate or joint venture,
  - % of net assets as % of consolidated net assets
  - % share in profit & loss as % of consolidated profit or loss.

The above disclosure shall be given separately for Indian and Foreign subsidiary, associates and joint venture.

- For minority interest in all subsidiaries, % of net assets and % share in profit or loss as % consolidated net assets and consolidated profit or loss
- ✓ All subsidiaries, associates and joint ventures (whether Indian or foreign) will be covered under CFS provisions.
- ✓ Company shall disclose the list of subsidiaries or associates or joint ventures which have not been consolidated in the CFS along with the reasons of not consolidating.



## **Relevant Accounting Standards dealing with CFS:**

The relevant Accounting Standard that deals with the guidance on preparation of CFS is Accounting Standard (AS) 21, 'Consolidated Financial Statements'. In addition, AS 23, 'Accounting for Investments in Associates in Consolidated Financial Statements' and AS 27, 'Financial Reporting of Interests in Joint Ventures' deal with accounting for investments in associates and joint ventures, respectively, in the CFS.

## **Previous Year Figures:**

Schedule III of the Act, which lays down the format for preparation of financial statements, contains the following general instructions for preparation of CFS:

- ✓ Where a company is required to prepare CFS, it shall mutatis mutandis follow the requirements of this Schedule as applicable to a company in the preparation of balance sheet and statement of profit and loss on standalone basis.

Para 5 of schedule III states that except in case of first financial statements after incorporation, the comparatives for the immediately preceding FY for all items of financial statements including notes shall be given

There is no specific exemption is given to the Companies who are preparing CFS for the first time for the disclosure in respect of corresponding previous year figures. However there is transitional provision in AS 21 which states that on the first occasion that CFS are presented, comparative figures of the previous period need not be presented.

Referring to the above stated provisions, it seems that, the Act and related rules is not clear on this respect. As per our opinion, Company shall disclose the previous year figures and hence preparation of CFS of the corresponding previous year is must.

Please note that some of the companies have referred to transitional provisions as referred in AS 21 in notes to CFS and accordingly opted for not to disclose previous year figures being first time preparation of CFS.

## Sale in the course of Import –

### S.5(2) of the Central Salestax Act, 1956 ( C.S.T. Act, 1956)

Transactions of sale in the course of import are exempt from levy of salestax u/s. 5(2) of the C.S.T. Act, 1956.

S.5(2) reads as under:

*“S.5 When is a sale or purchase of goods said to take place in the course of import or export-*

(1) ----

(2) *A sale or purchase of goods shall be deemed to take place in the course of the import of the goods into the territory of India only if the sale or purchase either occasions such import or is effected by a transfer of documents of title to the goods before the goods have crossed the customs frontiers of India.....”*

As seen for above, there are two limbs of sale which can be covered by section 5(2).

First limb covers such sale which occasions movement of goods from foreign country to India.

This can be said to be direct import purchase by buyer and export sale by foreign party. This transaction is exempt u/s. 5(2) of the C.S.T. Act, 1956.

The second limb covers sale which is effected by transfer of documents of title to goods before the goods crosses the Customs Frontiers of India.

In this discussion we are concerned with first limb and hence discussion herein is restricted to that extent only and the second limb is not discussed here.

### Example:

A in India requires certain specific precise materials from a foreign country and accordingly places an order with B giving such precise specification. B in turn places an order with C (foreign supplier) giving same precise specification and imports they said material with knowledge that it will be imported & delivered to A.

Accordingly B imports from C and delivers & sells to A.

**So since there is inextricable link between local sale by B to A and import by B from C, said transaction is exempt from tax u/s. 5(2) of the C.S.T. Act, 1956:**

- (1) Such sale or purchase in India must itself occasion such import, and not vice versa, i.e., import should not occasion such sale.
- (2) The import of the concerned goods must be effected as a direct result of the concerned sale or purchase transaction.

- (3) A sale or purchase can be treated to be in the course of import if there is a direct privity of contract between the Indian importer and the foreign exporter and the intermediary through which such import is effected merely acts as an agent or a contractor for and on behalf of Indian importer.
- (4) An obligation to import must arise from contract between importer & local customer.

**To establish such inextricable link, it is suggested that in purchase order by local customer, there should be terms and conditions inter alia as under:**

- a) You shall source/procure the above goods only from your overseas principal i.e. M/s\_\_\_\_\_. The goods must be manufactured / assembled as per configuration specified by us.
- b) It is specifically agreed that the ordered goods to be imported by you from the overseas supplier into India, are only and specifically for the performance of this contract.
- c) The goods which will be imported by you for performance of this contract shall be delivered to us only and shall not, in any case, be diverted to anyone else.
- d) Any cancellation of the PO implies that the consignment is to be returned to the overseas supplier and any charges that are to be incurred for retuning the shipment will be borne by us.
- e) Breach of any of the above mentioned conditions shall be breach of this contract.

In short, utmost case should be taken in structuring the transaction so as to be eligible for tax exemption.

# Mutual Fund

## Mutual Fund:

**Mutual funds** represent another way to invest in stocks, **bond**, or cash alternatives. You can think of a **mutual fund** like a basket of stocks or **bonds**. Basically, your money is pooled, along with the money of other investors, into a **fund**, which then invests in certain securities according to a stated investment strategy. The fund is managed by a fund manager who reports to a board of directors. By investing in the fund, you own a piece of the pie (total portfolio), which could include anywhere from a few dozen to hundreds of securities. This provides you with both a convenient way to obtain professional money management and instant diversification that would be more difficult and expensive to achieve on your own. Every mutual fund publishes a prospectus. Before investing in a mutual fund, get a copy and carefully review the information it contains, such as the fund's investment objective, risks, fees, and expenses. Carefully consider those factors as well as others before investing.

## Stock:

A stock is ownership in a company. When you buy a stock, you buy a piece of the company. So if the company does well, you do well. Congruently, if the company tanks, your stock tanks. Just like bonds, there are many types of stocks because there are many different types of companies out there. Large company stocks (large cap), mid cap stock, small cap stock, international stock, emerging stock, tech stock, etc. Historically, stocks have an annual average return of 10.8% which hold for one year and more is exempt from tax, Stock carry inflation and income both in long run if invested wisely through mutual fund or registered Portfolio Management Scheme (PMS) run by big fund house. However, remember that with more return comes more risk. So when investing in stocks, keep in mind that you have to be able to handle the extra risk or volatility to reap the potential reward in the long run.

## Bonds:

The best way to describe a bond is to think of it like a loan. You loan your money to the government or a company, and in return they pay you interest for the term of that loan. Typically bonds are considered conservative types of investments because you can choose the length and term of the bond and know exactly how much money you will get back at the end of the term or "maturity." There are many types of bonds; government bonds, corporate bonds, short-term bonds, long-term bonds, municipal and inflation protected bonds, etc. Generally bonds are less risky than stocks and the main way you lose money on a bond is if the company or government issuing the bond defaults on their obligations. Historically, bonds have an annual average total return of 6.3%. The Income tax is payable on Income from Bond both in terms of Capital Gain and interest income. It is better than cash but still not that great.

*Bonds are subject to market risk and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price.*

## Mutual Fund

### Advantages

#### **Advanced Portfolio Management:**

You pay a management fee as part of your expense ratio, which is used to hire a professional portfolio manager who buys and sells stocks, bonds, etc. This is a relatively small price to pay for help in the management of an investment portfolio.

#### 1. **Dividend Reinvestment:**

As dividends and other interest income is declared for the fund, it can be used to purchase additional shares in the mutual fund, thus helping your investment grow.

#### 2. **Risk Reduction (Safety):**

A reduced portfolio risk is achieved through the use of diversification, as most mutual funds will invest in anywhere from 50 to 200 different securities - depending on their focus. Several index stock mutual funds own 1,000 or more individual stock positions.

#### 3. **Convenience and Fair Pricing:**

Mutual funds are common and easy to buy. They typically have low minimum investments some around Rs.500/- and they are traded only once per day at the closing net asset value (NAV). This eliminates price fluctuation throughout the day and various arbitrage opportunities that day traders practice. The most popular investment in Mutual Fund is SIP (Systematic Investment Plan) which you can invest on daily or monthly basis over the period of time and take advantage of timing of market in long run for better returns.

### Disadvantages

#### 1. **High Expense Ratios and Sales Charges:**

If you're not paying attention to mutual fund expense ratios and sales charges, they can get out of hand. Be very cautious when investing in funds with expense ratios higher than 1.20%. While direct investment in stock will cost you only 0.1% on purchase and sell which is very less if you invest and monitor your stock carefully.

#### 2. **Management Abuses:**

Churning, turnover and window dressing may happen if your manager is abusing his or her authority. This includes unnecessary trading, excessive replacement and selling the losers prior to quarter-end to fix the books.

# Mutual Fund *(cont.)*

### 3. Tax Inefficiency:

Like it or not, investors do not have a choice when it comes to capital gain payouts in mutual funds. Due to the turnover, redemptions, gains and losses in security holdings throughout the year, investors typically receive distributions from the fund that are an uncontrollable tax event.

### 4. Poor Trade Execution:

If you place your mutual fund trade anytime before the cut-off time for same-day NAV, you'll receive the same closing price NAV for your buy or sell on the mutual fund. For investors looking for faster execution times, maybe because of short investment horizons, day trading, or timing the market, mutual funds provide a weak execution strategy.

Stocks and bonds both have their advantages and disadvantages depending on what you are looking for. For example, risk-averse investors looking for safety of capital and who prefer a known periodic payment structure (i.e. coupon payments) for a limited time frame would be better off investing in bonds. On the other hand, investors who are willing to take on greater risks than bondholders and who would prefer the benefit of having partial ownership in a company and the unlimited potential of a rising stock price would be better off investing in stocks.

However, the disadvantage of stocks versus bonds is that stocks are not guaranteed to return anything to the investor while the coupon payments and principal of bonds are. Thus, the possibility for high returns is greater with stocks but so is the possibility of losing money.

For most investors, a combination of stocks and bonds is the best situation. By diversifying your investments and putting some money into both stocks and bonds you ensure some safety while leaving some opportunity for above-average returns in your stock investments.

## Stocks

### Advantages

- Stocks typically have potential for higher returns compared with other types of investments over the long term.
- Some stocks pay dividends, which can cushion a drop in share price, provide extra income or be used to buy more shares.
- Bonus and Split of shares gives extra liquidity for the stock and will give better returns over the period.

# Mutual Fund *(cont.)*

## Disadvantages

- Stock prices can rise and fall dramatically.
- There is no guaranteed return.

## Bonds

### Advantages

- Bonds tend to rise and fall less dramatically than stocks, which means their prices may fluctuate less.
- Certain bonds can provide a level of income stability.
- Some bonds, such as U.S. Treasuries, can provide both stability and liquidity.

### Disadvantages

- Historically, bonds have provided lower long-term returns than stocks.
- Bond prices fall when interest rates go up. Long-term bonds, especially, suffer from price fluctuations as interest rates rise and fall.

As you can see, each type of investment has its own potential rewards and risks. Mutual Fund investment are subject to market risk and depends on fund managers and expense ratio Stocks offer an opportunity for higher long-term returns compared with bonds and mutual fund but come with greater risk. Bonds are generally more stable than stocks but have provided lower long-term returns.

By owning a mix of different investments, you're diversifying your portfolio. Doing so can curb the risks you'd assume by putting all of your money in a single type of investment.

We strongly recommend investment in Mutual Fund by choosing various schemes according to each one risk appetite and it carries advantages and disadvantages of Stock and Bonds. If at all if one have to invest directly in stock can invest through registered Portfolio Management Scheme.

**Disclaimer:** This is only writer's view about the Investment objective, There may be different views and perception of other people, which we respect and honour.