September 2016

TAX UPDATES

(containing recent case laws, notifications, circulars)

Prepared in association with

KPMG
cutting through complexity

Foreword

I am pleased to enclose the September issue of FICCI's Tax Updates. This contains recent case laws, circulars and notifications pertaining to direct and indirect taxes.

An interaction on the draft Model GST law was held by the FICCI's Task Force on GST with Mr Ram Tirath, Member-GST and other officials of the Central Board of Excise and Customs on 10th August, 2016. The concerns on the various provisions of the Model GST Law were placed before the Central Government officials.

FICCI's comments on the draft Model GST law have been submitted to the Central Government on August 18, 2016 and to the Empowered Committee of State Finance Ministers on August 20, 2016. A FICCI delegation led by Mr. Y. K. Modi, Past President, FICCI, met the Revenue Secretary and other senior officers in a meeting convened by the Ministry of Finance on August 19, 2016 and represented the concerns and suggestions on the Model GST Law. A delegation led by Mr. Harsh Mariwala, Chairman FICCI's Task Force on GST, participated in the deliberations with the Empowered Committee of State Finance Ministers held on August 30, 2016 to discuss various matters related to GST. A Press Release containing the points raised by the FICCI delegation was also issued. The aforesaid documents can be accessed on the FICCI website.

On the direct tax front, the Delhi High Court in the case of Steria (India) Ltd. held that payment for managerial services cannot be taxed as Fees for Technical Services (FTS) in view of the Most Favoured Nation (MFN) clause under the India-France tax treaty. Accordingly, the said payments are not subject to withholding of tax under Section 195 of the Income-tax Act, 1961. The High Court observed that the MFN clause given in the protocol to the tax treaty cannot be interpreted restrictively. The definition of FTS provided in Article 13(4) of India-U.K. tax treaty excludes managerial services. Therefore, applying the MFN clause under the tax treaty read with the definition of FTS under the India-U.K. tax treaty, 'managerial services' will be outside the ambit of FTS.

We do hope that this newsletter keeps you updated on the latest tax developments.

We would welcome any suggestions to improve the content and the presentation of this publication.

A. Didar Singh

Recent Case laws

I. DIRECT TAXES

High Court Decision

Payment for managerial services cannot be taxed as FTS on application of MFN clause under the India-France tax treaty

The taxpayer is a public limited company registered in India providing IT driven services for its clients' core businesses. The taxpayer is assessed to tax as a resident in India. Steria France is a non-resident company incorporated in France as a limited liability partnership. Steria France centralises technical skills for carrying on management functions such as legal finance, human resources, communication risk control, information systems, controlling and consolidation, delivery and industrialisation, technology and management information services. Steria France does not have any office presence or personnel in India and a Permanent Establishment (PE) in India.

The taxpayer entered into a management service agreement with Steria France. Under the said agreement, Steria France was to provide various management services to the taxpayer with a view to rationalise and standardise the business conducted by the taxpayer in India. These services are provided by Steria France through telephone, fax, e-mail, etc. and no personnel of Steria France visited India for providing such services.

The taxpayer filed an application before the AAR seeking a ruling on whether the payment made for the management services provided by Steria France is taxable in India in the hands of Steria France under the tax treaty. Further, if the payment is not subject to tax in the hands of Steria France in India, whether Steria India will be liable to withhold tax under Section 195 of the Act. The AAR ruled that the protocol could not be treated as a part of the tax treaty itself. The restrictions imposed by the protocol to the India-France tax treaty using MFN clause were only to limit the taxation at source for the specific items mentioned therein. The restriction was only on the rates. Further, the 'make available' clause provided in the India-UK tax treaty could not be read into the expression FTS occurring in the tax treaty unless there was a notification under Section 90 of the Act issued by the Central Government to incorporate the less restrictive provisions of the India-UK tax treaty into the India-France tax treaty.

The High Court held that on perusal of the MFN clause under the protocol of the tax treaty, the High Court finds no warrant for the restrictive interpretation of the protocol. The words 'a rate lower or a scope more restricted' occurring in the protocol envisages that there could be a benefit on either score i.e. a lower rate or more restricted scope. One does not exclude the other. The benefit of protocol could accrue in terms of lower rate or a more restrictive scope under more than one tax treaty which may be signed after 1 September 1989 between India and a third state which is an OECD member.

The purpose of the protocol is to afford a party to the tax treaty the most beneficial provisions that may be available in another tax treaty between India and another OECD country. The AAR has failed to notice the wording of the protocol which makes it self-operational. Once the tax treaty has itself been notified, and contains the protocol, there was no need for the protocol itself to be separately notified or for the beneficial provisions in some other tax treaty between India and another OECD country to be separately notified to form part of the tax treaty.

The definition of FTS occurring in Article 13(4) of the India-U.K. tax treaty excludes managerial services. By virtue of MFN clause the same benefit is available under India-France tax treaty. In the present case, Steria France has provided managerial services to the taxpayer in terms of the management services agreement. Once the expression 'managerial services' is outside the ambit of FTS, then the question of withholding of tax on payment for the managerial services, would not arise. Therefore, it was not necessary for the Court to further examine the second part[1] of the definition. The Tribunal in the case of DCIT vs ITC Ltd. [2002] 82 ITD 239 (Kol) had held that the benefit of the lower rate or restricted scope of FTS under the India-France tax treaty was not dependent on any further action by the respective governments. It was held that the more restricted scope of FTS as provided for in a tax treaty entered into by India with another OECD member country shall also apply under the India-France tax treaty with effect from the date on which the India-France tax treaty or such other tax treaty enters into force. The payment made by the taxpayer for the managerial services provided by Steria France cannot be taxed as FTS under the tax treaty. Accordingly, the said payments are not subject to withholding of tax under Section 195 of the Act.

Steria (India) Ltd vs. CIT (W.P. (C) 4793/2014 & CM Appeal 9551/2014) (Delhi High Court) – Taxsutra.com

Since the situs of the IPR was not in India, income accruing from the transfer of its right title and interest is not taxable in India. The situs of the intangible asset is attached to its owner

The taxpayer, an Australian Company, is in the business of brewing beer, also owned various trademarks and Intellectual Property Rights (IPRs) in relation to its business. By entering into Brand License Agreements (BLA), certain trademarks and IPRs were licensed to its subsidiaries in various jurisdictions (including its step-down subsidiary in India (I Co). Such trademarks and IPRs were also registered in India. The BLA provided I Co, an exclusive right to use the four registered trademarks and IPRs in the Indian territory for a royalty fee which was subject to withholding taxes in India.

In 2006, the taxpayer entered into a composite sale-purchase agreement (ISPA) with X Ltd for transfer of shares of one of its down-stream subsidiary along with the trademarks and IPRs (including the ones licensed to I Co.) and grant of perpetual license in relation to its brewing IP confined to India. Pursuant to the terms of the ISPA, the BLA between I Co. and the taxpayer was terminated in respect of the four trademarks and IPRs licensed to it. Also, as per the ISPA, the trademarks and IPRs were assigned to the nominee of X Ltd (Y Ltd).

[1] Whether any of the services envisaged under Article 13(4) of the India-UK tax treaty are 'made available' to the taxpayer by the tax treaty with France

The taxpayer approached the AAR seeking a ruling on whether the receipts on the transfer of rights, titles and interest in trademark and grant of an exclusive perpetual license to Y Ltd is taxable in India. The AAR held that income attributable to the grant of perpetual license was not taxable in India. However, held that income from transfer of rights, title and interest in trademarks and IPRs accrued in India.

The High Court held that the termination of the BLA was a precondition to the ISPA and descended with the ruling of the AAR. The situs of the IPRs was a tricky issue, unlike the tangible assets which had a physical presence in India. The Act does not currently provide for any deeming fiction to determine the situs of the intangible asset, unlike the case where Explanation 5 to Section 9(1)(i) of the Act provided for situs in respect of shares or interest in a company incorporated/registered outside India. In the absence of specific provisions governing the same, internationally accepted principles may be adopted to determine the situs of the intangible asset. The situs of the IPRs may thus be determined using the principle of 'mobilia sequuntur personam' whereby a fiction is created to effect that the situs of the owner of the intangible asset would be the closest approximation of the situs of the intangible asset. As the situs of the IPR is not in India, the income received from the transfer of right, title or interest in the IPRs is not taxable in India.

CUB Pty Limited vs UOI & Ors [2016] 71 taxmann.com 315 (Del)

Both employer's and employees' provident fund contribution is covered by the amendment of Section 43B of the Act and hence the taxpayer is entitled to deduction of provident fund contribution

The taxpayer, a Public Sector Undertaking (PSU) of the Government of Bihar is engaged in the business of warehousing. During the Assessment Year (AY) 2003-04, the AO observed that the contribution made by taxpayer was after the due date statutorily prescribed and thus disallowed payments of employer's contribution to Employee Provident Fund (EPF) under Section 43B of the Act. The AO also disallowed employees contribution to PF treating the same as income from other sources under Section 2(24)(x) read with Section 36(1)(va) of the Act. The CIT(A) deleted the addition made by the AO in respect of the delayed payment towards employer's EPF contribution. However, addition for delayed payment towards employees' contribution to EPF was retained. The same was confirmed by the Patna Tribunal on further appeal. Aggrieved with the Tribunal's ruling, the taxpayer filed an appeal before Patna High Court.

High Court's ruling

On perusal of the decision of the Supreme Court in the case of CIT vs Alom Extrusions [2009] 319 ITR 306 (SC), it indicates that it does not specifically refer to the employees' contribution or employer's contribution and both have been treated on the same footing. So far as difficulties in complying with the due date under the EPF Act vis-à-vis the previous year of the income-tax are concerned, there can be no distinction between the payment of employees or employer's contribution and the same difficulties would be faced for both.
While examining the issue as to whether there can be any distinction between employer/employees contribution with respect to Section 43B applicability, the

High Court in the present case relied on the Bombay High Court ruling in the case of CIT vs Ghatge Patil Transports [2014] 368 ITR 749 (Bom) and Punjab and Haryana High Court ruling in the case of CIT vs Hemla Embroidery Mills [2014] 366 ITR 167 (P&H) wherein the High Courts have held that both the employees' and employer's contributions are covered by the amendment of Section 43B of the Act after considering Alom Extrusions' case. The High Court further clarified that although technical reading of Section 43B and the provisions of sub-section (2) of Section 24(x) read with Section 36(1)(va) of the Act creates the impression that the employees' contribution would continue to be treated differently under a different head of deduction, as the head of deduction is separate under Section 43B and Section 36 of the Act but on a broader reading of the amendments made to Section 43B and as per the intention of Parliament, there appears to be sufficient justification for taking the view that the employees' and the employer's contribution ought to be treated in the same manner. Accordingly, following the Bombay and Punjab and Haryana ruling, the High Court in the present case has held that the amendment to Section 43B proviso is applicable to employees' PF contribution also. Accordingly, addition for delayed payment towards employees' contribution to EPF was deleted.

Bihar State Warehousing Corporation Ltd vs CIT (Miscellaneous Appeal No.302 of 2008) – Taxsutra.com

Reference made by the AO to the Transfer Pricing Officer set aside, as no opportunity of being heard allowed by the AO

The taxpayer imported raw material from Indorama Petrochem Limited (IPL). During the assessment proceedings, the AO required the taxpayer to explain why TP provisions should not be made applicable in respect of the said transaction. The taxpayer submitted that IPL was not an AE of the taxpayer as defined in Section 92A of the Income Tax Act, 1961 (the Act) and both the companies are independent in terms of management and Board of Directors. The AO, without giving any further opportunities to the taxpayer, referred the case to the TPO for ALP determination. Similar references were made by the AO for Assessment Years (AYs) 2011-12 and 2012-13. The taxpayer filed three writ petitions (AYs 2010-11, 2011-12 and 2012-13) involving a common question of law regarding the procedure adopted by the AO while making a reference to the TPO under Section 92CA of the Act.

High Court ruling

- The main issue is whether it was incumbent on the AO to have given the taxpayer an opportunity of being heard before making a reference to the TPO under Section 92CA(1) of the Act.
- Section 92CA contains certain jurisdictional prerequisites for making a reference by the AO to the TPO. Where the taxpayer raises a threshold objection that it has not entered into any international transaction within the meaning of Section 92B of the Act, it is imperative for the AO to deal with such an objection on merits before making a reference to the TPO. Where the AO decides to make a reference, he/she has to record the reasons as to why he/she considers it necessary and expedient to make such a reference to the TPO.
- CBDT's Instruction No. 3 of 2003 categorically states that in order to

make a reference to the TPO, the AO has to satisfy himself/herself that the taxpayer has entered into an international transaction with its AE.

- Opportunity of being heard to the taxpayer is essential where an objection is raised on the jurisdiction of the AO to make a reference to the TPO. It appears to be implicit in the very nature of the procedure that is expected to be followed by the AO even though Section 92CA(1) does not state a hearing to be given to the taxpayer.
- The High Court relied upon the decision of the Bombay High Court in the case of Vodafone India Services (P) Limited vs Union of India [2014] 361 ITR 531 (Bom) wherein it was observed that where the objection is raised on the applicability of Chapter X of the Act, it becomes necessary for the AO to consider the objection at the very threshold i.e. before determination of ALP.
- The CBDT has specifically accepted the legal position as explained by the Bombay High Court in the aforesaid decision which is reflected in the Instruction No. 3 of 2016 dated 10 March 2016, which clarifies the correct legal position and is to be applied even in the present case where a reference was made by the AO to the TPO before the date of the said Instruction.
- The High Court set aside references made by the AO to the TPO for all the three relevant AYs since the taxpayer was not afforded an opportunity of being heard as required by law.

Indorama Synthetics (India) Ltd. vs ACIT - Delhi High Court - W.P.(C) 6422/2013 & CM No.14002/2013 (Stay), W.P.(C) 4558/2014, W.P.(C) 12072/2015

Berry ratio can only be applied in limited circumstances where value of the goods are not directly linked to the quantum of profits and the profits are mainly dependent on expenses incurred

- The taxpayer, subsidiary of Sumitomo Corporation Japan (SCJ), entered into transactions of (a) purchase and sale of goods (trading transactions) where purchase and sale are back to back transactions and title to goods is acquired only briefly (i.e. flash title) and (b) provision of support services (indenting transactions), where goods are supplied directly by the supplier to the purchaser. In the TP report, the taxpayer applied TNMM as MAM using Berry ratio, i.e. Gross Profit (GP) to operating costs, as the PLI. For computing GP on trading transactions, the taxpayer reduced cost of sales from aggregate value of sales made to AEs and non-AEs. This GP was then added to commission earned from indenting transactions to compute the total GP which was then divided by operating expenses to compute the Berry ratio. The Berry ratio was computed at 1.79 per cent while weighted average PLI of comparables was 1.18 per cent and the transactions were at arm's length.
- TPO rejected the use of Berry ratio for following reasons - (a) since denominator excluded the cost of goods, the PLI worked out for TNMM was not in accordance with Rule 10B(1)(e) of the Income tax Rules (the Rules) as the TNMM could be applied only in determining net profit to the costs incurred, sales affected or assets employed; (b) Berry ratio cannot be used in case where intangibles are used and in the given case, the taxpayer had developed a supply chain and human assets intangibles which resulted in

commercial and strategic advantage of the taxpayer resulting in enhanced profit potential of the AE; (c) Berry ratio was sensitive to the cost base and it was difficult to accurately compute cost base of comparable companies as costs are accounted by companies differently.

- TPO held that functions performed and risks undertaken in trading and indenting transactions were similar and compared AE transactions in indenting segment with non-AE transactions in the trading segment. Thus, the TPO made adjustment in indenting segment, considering gross margin earned in trading segment with non-AEs as the commission rate on the Free on Board (FOB) price of the goods sourced through the taxpayer in respect of indenting transactions with the AEs. The DRP upheld the TPO's order.

High Court's ruling

- Before making an ALP adjustment, MAM must be identified for ALP computation. The TPO rejected Berry ratio and discarded TNMM but did not select MAM for ALP computation and imputed the character of trading transactions to the indenting transactions which was rightly rejected by the Tribunal as it was not permissible for TPO to recharacterise the transaction. Tribunal's finding that indenting transactions of the taxpayer were in the nature of facilitating trade is correct.
- Tribunal erred in proceeding to determine the ALP on the basis of commission rate for indenting transactions with non-AEs, without further examination as to the similarity between the two transactions. Tribunal effectively used CUP method for imputing the ALP of indenting transaction with AEs but since CUP requires high degree of similarity between controlled and uncontrolled transactions, it was necessary for the Tribunal to conduct a further in-depth inquiry as to the relevant uncontrolled transactions.
- The High Court held the TPO's decision of rejecting use of Berry ratio as unsustainable, citing the following reasons:
- Rule 10B(1)(e)(i) mandates that the net profit margin realised could be computed having regard to 'any other relevant base'. Berry ratio is a ratio of operating profits to operating expenses. In cases where operating expenses is considered as a relevant base, there would be no difficulty in using Berry ratio as the PLI in terms of Rule 10B(1)(e)(i) of the Rules. The High Court cited the use of Berry ratio by Internal Revenue Service in the U.S. in the case of E.I. Du Pont DE Nemours & Co. vs United States: 608 F.2d 445 (1979) and further mentioned that Berry ratio is held to be appropriate by OECD Guidelines and Treasury Regulations of the U.S. in certain circumstances. Japan has also accepted use of Berry ratio in certain circumstances.
- There is no cogent material to hold that the taxpayer had developed supply chain and human resources intangibles.
- Berry ratio has limited applicability and can be used effectively only in cases where the value of goods have no role to play in the profits earned by a taxpayer and the profits earned are directly linked with the operating expenditure incurred by the taxpayer. Fundamentally, operating expenses adequately represent all functions performed and risks undertaken. For this reason Berry ratio is effectively applied only in case of stripped down

distributors, i.e. distributors with no financial exposure and risk in respect of the goods distributed by them.

- Berry ratio would not be an appropriate PLI in cases of taxpayers having substantial fixed assets or using intangibles as a part of its business.
- The use of Berry ratio would give unreliable results if the product mix of the comparables is different from the product mix of the taxpayer. Accordingly, the High Court remanded the matter back to the Tribunal for a fresh examination of the issues.

Sumitomo Corporation India Pvt. Ltd. vs CIT - Delhi High Court - ITA 381/2013, ITA 738/2015, ITA 382/2013, ITA 702/2014 - AYs 2007-08, 2008-09, 2009-10 and 2010-11

Tribunal Decisions

Marketing services for expansion of business overseas are not in the nature of FTS

The taxpayer is a stock broker company in India and carries on the business of brokerage on behalf of its institutional clients. During the year under consideration, the taxpayer company made payments to its subsidiaries in the U.K. and Singapore for providing marketing support services and towards the expansion of its business in the U.K. and Singapore along with the European region and the South East Asian countries respectively.

As consideration for their services, the taxpayer company remunerated the subsidiaries by reimbursing their costs along with a service fee of 29 per cent on the costs. No tax was deducted at source on such reimbursement of costs made to the subsidiaries. The Assessing Officer (AO) considered that the taxpayer company was bound to deduct tax at source on the entire remittance (including reimbursement) since the entire payment made to the non-resident subsidiaries constituted FTS and were taxable in their hands. Pursuantly, the AO disallowed the payment made as reimbursement to the subsidiary for non-deduction of tax at source. The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the disallowance by observing that tax was required to be deducted on gross payments by the taxpayer.

The Kolkata Tribunal held that the services provided by the subsidiaries were in the nature of marketing services of introducing foreign institutional investors to invest in the capital markets in India. Article 12(4) of the India-Singapore tax treaty and Article 13(4) of the India-U.K. tax treaty is the same as Article 12(4)(b) of the India-U.S. tax treaty and thus the Memorandum of Understanding to the India-U.S. treaty could be used as aid to understand if services constituted as FTS. Given the language used in the tax treaties, unless services also make available technical knowledge, skill, experiences, etc. to the recipient of the services, the same do not qualify as FTS under the tax treaties. Since no technical service was being made available to the taxpayer by its subsidiaries, payments did not fall within the definition of FTS as per the provisions of the tax treaties.

As the subsidiaries had no PE in India, the said payments could not be taxed in India even as business profits. The provisions of the tax treaties being more beneficial to the taxpayer, the Tribunal did not analyse the taxability in terms of the Act by considering it as academic in nature. In considering the retrospective amendment in Explanation 2 to Section 195(1) of the Act with effect from 1962, the Tribunal held that it is not possible to fasten a liability to deduct tax at source basis a retrospective amendment. Reliance for the same was placed on the decision in the case of DCIT vs Subhotosh Majumder (2016) 65 taxmann.com 42 (Kol). As no income was chargeable to tax in India, relying on the Supreme Court's decision in case of GE India Technology Centre P Ltd vs CIT [327 ITR 456 (SC)], the Tribunal directed the AO to delete the disallowance.

Batlivala & Karani Securities (India) (P.) Ltd [2016] 71 taxmann.com 142 (Kol)

Principles have been laid down for computing interest under Section 234B on re-assessment or recomputation under Section 153A of the Income-tax Act

The taxpayer was assessed as a firm in respect of AYs 2005-06, 2008-09 and 2009-10. It was then converted in to a company in August 2012. The taxpayer's returns were accepted under Section 143(1) originally and there was no assessment under Section 143(3) of the Act. Consequently, pursuant to search and seizure operations, a notice was issued under Section 153A of the Act. During its pendency, the taxpayer filed an application under Section 245D to the Settlement Commission. As per the Settlement Commission's order, proceedings were finalised by order under Section 143(3) read with Section 153A and 245D(4) of the Act. The AO levied interest under Section 234B of the Act considering the order passed by Settlement Commission invoking provisions of Section 234B(3) of the Act. There were no appeals against the order of the Settlement Commission, however, appeals were preferred against rectification orders passed under Section 154 of the Act. On appeal, the CIT(A) dismissed the appeal of the taxpayer upholding the AO's orders.

The Tribunal observed that the interest liability under Section 234B(1) is attracted if there is any shortfall of any advance tax from the first day of the assessment year till the completion of/processing of return for the first time. In case of reassessment and redetermination of income either under Section 147 or under Section 153A, the statute provides for further levy of interest on the higher amount of tax determined in the reassessment proceedings. The period of levy is from the date of first order either under Section 143(1) or 143(3) or 147 or 153A as the case may be to the date of revised order. Where intimation under Section 143(1) of the Act was issued levying interest under Section 234B(1) of the Act, the subsequent proceedings will attract only Section 234B(3) on the enhanced income/tax whereas interest levied originally under Section 234B(1) will stand as such. Thus, there is levy of interest from the first day of the assessment year till the completion of assessment/processing for the first time on the returned income/assessed income under Section 234B(1) of the Act and a further enhancement of interest under Section 234B(3) on the additional tax determined in the reassessment proceedings for the later period. There are two separate calculations of interest under Section 234B(1) and 234B(3) of the Act. Since interest was already demanded in earlier proceedings only fresh demand has to be raised under Section 234B(3) of the Act.

The amendment brought out by the Finance Act, 2015 modifies the then existing provisions which are applicable for the impugned assessment years. In fact under the new Section 234B(3) of the Act, it was provided that interest will be calculated on the enhanced amount from the period commencing on 1 April next following the relevant financial year for which advance tax was payable and ending on that date of the reassessment or recomputation under Section 147/153A of the Act.

MBG Commodities (P) Ltd. vs DCIT (1321/Hyd/2015) – Taxsutra.com

CUP method accepted for purchase of heavy earthmoving machinery and change of method by the taxpayer during TP assessment proceedings upheld

The taxpayer operates as a sole distributor of heavy earth moving machines and spare parts manufactured by its Associated Enterprise (AE) for sale to independent customers in India and South Asia. It is also engaged in the business of manufacturing of machinery and provides warranty and after sale services to its customers.

The international transactions included purchase of machinery, heavy earthmoving machines, machines [Completely Knocked Down (CKD) and Semi Knocked Down (SKD)], spare parts, plant and machinery and receipt of commission income from its AE. The taxpayer had selected Transactional Net Margin Method (TNMM) as the Most Appropriate Method (MAM) with Net Profit on Sales (NPM) as the Profit Level Indicator (PLI) in the Transfer Pricing (TP) Report. The taxpayer's NPM fell within 5 per cent variation range of average NPM of two comparables.

The Transfer Pricing Officer (TPO), during the assessment proceedings, computed average NCP (as against NPM used by the taxpayer) of 13 comparable companies and proposed an adjustment in respect of international transaction relating to purchase of machinery, CKD/SKD and spare parts. The TPO also proposed an adjustment on account of selling and distribution expenses by using bright-line test. The TPO further added 15 per cent of markup on the bright-line, and made an adjustment towards the creation of marketing intangibles for the AE.

Before the Dispute Resolution Panel (DRP), the taxpayer requested for adopting Comparable Uncontrolled Price (CUP) method as MAM for the international transaction of purchase of machinery. The comparable price data of the products sold by the AE to the independent distributors in different geographical locations and to the taxpayer was submitted. The DRP rejected the taxpayer's plea for change of MAM and it also rejected all other pleas of the taxpayer and prima facie upheld the approaches adopted by the TPO.

Tribunal ruling

- Where the comparables are available, CUP is undisputedly, the best method for computing the Arm's Length Price (ALP). Accordingly, in the instant case, CUP method is the MAM. One of the essential pre-requisite is to undertake reasonably accurate adjustment to eliminate material factors affecting price, cost or the profit arising from such transaction. Adequate weightage is also required to be given to the market condition of different geographical locations.
- Merely for the reason that in its TP study report, the taxpayer had adopted TNMM as the MAM, cannot prevent the taxpayer to apply CUP method if there is reasonable data available for comparability analysis.
- In relation to reliability of the data, it would always be the onus of the taxpayer to show the basis of

comparability analysis and veracity of the data used for comparability.

- Taxpayer to furnish its revised TP study report on the basis of CUP method. It shall be the duty of the taxpayer to provide the sale data of the AE in terms of sale price of the taxpayer in India as well as other geographical locations, which are claimed to be comparable price.
- The TPO/AO shall compute the ALP using this data applying CUP method. In case the data is found to be not adequate and no adjustment can be made to eliminate material differences, the TPO/AO shall proceed to determine ALP in accordance with other methods upon granting adequate opportunity of hearing to the taxpayer.
- As the Tribunal allowed CUP as the MAM for the transaction of purchase of machinery, it remitted the grounds in relation to adjustment on account of transactions of purchase of finished goods, CKD/SKD and spare parts back to the TPO for fresh comparability analysis.

Liugong India Private Limited vs ACIT (ITA No. 1482/Del./2015)

Taxpayer is qualified to be a resident of India based on the tie-breaker provisions of India-Sri Lanka tax treaty

Where a person qualifies as a resident of more than one country, the tax treaties provide the manner in which such person's residency could be determined in favour of one of the countries. Recently, the Mumbai Tribunal in the case of Shalini Seekond held that the taxpayer is qualified as a resident of India based on the tie-breaker provisions of India-Sri Lanka tax treaty.

Shalini Seekond v. ITO (ITA No. 3877/Mum/2012) – Taxsutra.com

Notifications/Circulars/ Press Releases

CBDT issues a press release on paperless PAN and TAN application process

Central Board of Direct Taxes (CBDT) issued a press release introducing the DSC based application procedure on the portals of Permanent Account Number (PAN) service providers for fast tracking allotment of PAN and Tax Deduction and Account Number (TAN) to company applicants. As per the new process PAN and TAN will be allotted within one day after completion of valid online application.

Similarly, a new Aadhaar e-Signature based application process for Individual PAN applicants has been made available on the portals of PAN service providers.
CBDT press release, dated 22 July 2016

CBDT press release, dated 22 July 2016

India's Social Security Agreement with Japan will come into effect from 1 October 2016

The Social Security Agreement between India and Japan was signed on 16 November 2012. The Ministry of External Affairs has issued a press release notifying that the Social Security Agreement (SSA) between India and Japan will come into effect from 1 October 2016.

This SSA aims at achieving equality on the principle of reciprocity to benefit employees who are posted in another country, by their employers. The India-Japan SSA is the seventeenth SSA to come into effect.

The countries with which India has effective SSAs are Belgium, Germany, Switzerland, Denmark, Luxembourg, France, Republic of Korea, Netherlands, Hungary, Finland, Sweden, Czech Republic, Norway, Austria, Canada and Australia.

Key potential benefits under the India-Japan SSA

- Exemption from social security contribution in the host country
- Totalisation of contributory periods
- Lump-sum refunds
- Export of benefits

The notification of entry into force of the SSA between India and Japan is a welcome step as it can help save costs in international assignments between the two nations as well as take into account the social protection of international assignees. This could lead to increased economic activity between the two countries.

http://mea.gov.in/press-releases.htm?dtl/27088/IndiaJapan_Social_Security_Agreement, accessed on 10 August 2016

II. SERVICE TAX

Decisions

Levy of service tax on restaurant services upheld and levy of service tax on hotel accommodation struck down

The issue in the instant case was whether service tax was applicable on composite contracts of provision of food in an air-conditioned restaurant and provision of short-term accommodation in a hotel.

The Delhi High Court upheld the levy of service tax on the service portion of composite contracts for supply of food and drinks on the basis that even if some part of the composite transaction involves rendition of service, the Union Government is empowered to tax (i.e. levy service tax) such portion and there is no overlapping between levy of Value Added Tax/Central Sales Tax by the state government.

On the other hand, the High Court has struck down the levy of service tax on short-term hotel accommodation on the ground that levy of luxury tax by the state government entirely covers the subject matter of taxation and the Union Government lacks legislative competence to levy service tax on the same.

Federation of Hotels and Restaurants Association of India and Ors. vs Union of India and Ors. [2016-VIL-452-DEL-ST]

Levy of service tax on contract manufacturing of alcohol upheld

The issue in the instant case was whether service tax was applicable on the activity of contract manufacturing of alcoholic liquor for human consumption by one entity for another.

The Delhi High Court upheld the levy of service tax on contract manufacturing of alcoholic liquor for human consumption on the basis of the following:

- The taxable event for levy of state excise duty is the manufacture by oneself and not manufacture by one party for another and therefore, the activity in essence and substance is a service performed by one for another.
- In case of manufacture by one party for another, the transaction partakes the character of rendition of service which is the aspect sought to be taxed by the Union Government for which it is competent to legislate.

Carlsberg India Pvt. Ltd. and Ors. vs Union of India and Ors. [2016-TIOL-1646-HC-DEL-ST]

Circulars/Notifications/ Press Releases

Clarification on service tax on hiring of goods without the transfer of the right to use goods

On the issue of applicability of service tax on hiring of goods without transfer of the right to use goods, the Central Board of Excise and Customs (CBEC) has clarified that the terms of the contract have to be examined carefully against the backdrop of the criteria laid down by the Supreme Court in BSNL vs Union of India [2006(2) STR 161 SC] such as goods must be available for delivery, consensus ad idem as to identity goods, vesting of legal right to use the goods in transferee, etc.

Circular No. 198/08/2016 - ST dated 17 August 2016

Clarification on service tax on freight forwarders on transportation of goods

On the issue of applicability of service tax on services of freight forwarders on transportation of goods from India, the CBEC has *inter alia* clarified that where the freight forwarder is merely an agent who charges the rate prescribed by the airline/carrier/ ocean liner (located outside India), the services would qualify as 'intermediary' services and be liable to service tax. On the other hand, where the freight forwarder undertakes the responsibility for actual transportation with discretion to negotiate rates, the services would qualify as 'transportation of goods by air/sea' and would not be liable to service tax.

Circular No. 197/7/2016 – ST dated 12 August 2016

Compliance with guidelines on provisional attachment of property

In the backdrop of non-compliance with legal provisions and administrative instructions regarding provisional attachment of property without giving an opportunity of being heard by service tax officers, the CBEC has directed the Chief Commissioners to issue standing orders to provide proper opportunity to the taxpayer before attachment of property considering the observations made by the Allahabad High Court in a recent judgment.

Circular No. 196/06/2016 – ST dated 27 July 2016

Permission to pay service tax through non-electronic modes

The CBEC has directed the jurisdictional Deputy/Assistant Commissioner to exercise the discretion of allowing payment through non-electronic means judiciously and rationally so that there are no unwarranted refusals.

Instruction No. F. No. 137/08/2013 – ST dated 22 July 2016

III. CENTRAL EXCISE

Decisions

Moulds produced, if consumed within the factory premises will

enjoy exemption under Notification No. 67/95-CE

The taxpayer, a manufacturer of photocopier parts, television parts, telephony apparatus also, manufactures moulds, which are used within the factory for the manufacture of parts. During the EA Audit, Central Excise officers observed that the taxpayer has issued invoices for moulds, but have failed to pay excise duty claiming the benefit under Notification No. 67/95-CE.

The Department alleged that duty on such moulds is payable as the moulds were transferred to the taxpayer's other unit situated at Noida for the reason that the benefit of Notification No. 67/95-CE will not be available to the taxpayer in as much as the moulds have been cleared from the factory. The duty demand was confirmed by the original authority and the appellate authority and consequently appeal has been preferred before the Tribunal.

The taxpayer before the CESTAT submitted that the transfer is as a part of closing down of the factory and shifting the entire factory to Noida. Further, the conditions specified in the notification is not violated in as much as the factory itself has moved to Noida and since the moulds in question continues to be used within the factory, it cannot be said that the moulds have been cleared out of the factory. The fact also remains that in case duty is paid on the moulds on its transfer to Noida, such duty will be available as CENVAT credit.

Considering the above, the CESTAT allowed the appeal.

Hartech Plastic Pvt Ltd vs CCE [2016-TIOL-2030-CESTAT-DEL]

Circulars/Notifications/Press Releases

'First Sale Value' for articles of jewellery or parts of articles of jewellery

Notification has been issued for fixation of the 'Tariff Value' in respect of the excisable goods classified under HS Code 7113 i.e. 'Articles of jewellery or parts of articles of jewellery or both' of the First Schedule to the Central Excise Tariff Act, 1985.

Notification No. 33/2016 CE (N.T) dated 26 July 2016

IV. CUSTOMS

Circulars/Notifications/Press Releases

Removal of mandatory warehousing requirements for EOUs, STPIs, EHTPs (Units)

Notification 52/2003-Cus exempts specified goods when imported for use in the units, from payment of custom duty, subject to various conditions. The notification also, provided for 'warehousing of imported goods'. The units, therefore, had to obtain a license as a 'warehouse' under Section 58 of the Customs Act, 1962 (the Customs Act) and permission under Section 65 of the Customs Act, as a manufacture-in-bond facility.

In line with the government's objective of 'Ease of Doing Business', it has been decided to do away with the need to comply with warehousing provisions. As a consequence, these units shall stand de-licensed as warehouses under the Customs Act.

In view of the above, the warehousing bond register shall not be required to be maintained effective 13 August 2016. Further, the system of sending re-warehousing certificates to the customs station of import shall also stand dispensed effective 13 August 2016.

Circular No. 35/2016 - Cus dated 29 July 2016

Foreign Trade Circulars/Notifications/Press Releases

Deduction of state/central taxes collected from the customers while calculating foreign earnings for SFIS/SEIS Schemes

The FTP specifies that 'service providers shall be entitled to duty credit equivalent of the foreign exchange earned by them'.

The state/central taxes payable by the customer to governments are collected from the customer by the service provider on behalf of the concerned government. Hence, such taxes are not earnings of the service provider, as per the above provisions.

In light of the above, attention of all RAs, is drawn towards the above provisions for strict compliance and calculation of the entitlement only on the basis of receipt of foreign exchange earned by exporters, which do not include the taxes collected.

Trade Notice No.11/2015-20, dated 21 July 2016

Closure of EPCG authorisations in case of supplies to SEZ units, which have been made prior to 1 April 2015 and where exports proceeds have not been realised through Foreign Currency Account (FCA) of the SEZ unit

As per Foreign Trade Policy provisions, it is not mandatory that DTA units supplying goods under EPCG scheme to SEZ units had to realise payment from Foreign Currency Account (FCA) of SEZ unit, to discharge Export Obligation (EO). Moreover, Rule 30(8) of SEZ Rules, 2006 does not stipulate that it is mandatory for SEZ units to make payment to EPCG authorisation holders from FCA of the unit.

In consultation with SEZ Division of Department of Commerce, that closure/redemption/EODC may be allowed in cases where EPCG authorisation holder has made supplies to SEZ units and has not realised the proceeds from the Foreign Currency Account (FCA), in case of supplies which have been made prior to 1 April 2015.

However, it is further clarified that exports to SEZ units which have been made prior to 1 April 2015 and where export proceeds have not been realised through Foreign Currency Account (FCA) shall be taken in to account for discharge of EO.

Trade Notice No. 10/2016, dated 20 July 2016

Refund of CENVAT credit cannot be denied on the ground that it is filed for a year and not on a quarterly basis

The issue is whether the taxpayer is eligible for the refund of CENVAT credit that remained unutilised due to clearances under international competitive bidding. Further, adjudicating authority had rejected the said refund claim on the ground that the taxpayer has filed a single claim for the period January 2014 to December 2014, while Notification No 27/2012 stipulates for filing of quarterly refund claims. The authorities also rejected the refund claim on the ground that shipping bill, which is a document indicated as per a rule for evidencing export, duly certified was also not produced.

Aggrieved by such an order, the taxpayer filed an appeal before the first appellate authority. The first appellate authority allowed the appeal in favour of the taxpayer. Revenue being aggrieved by the order, filed an appeal.

The Mumbai Tribunal held that:

- The show cause notice did not require the respondent taxpayer to show cause for rejection of the claim on the ground that clearances made to international competitive bidding cannot be considered as exports. In the absence of such allegation, revenue cannot take this as a ground for setting aside the impugned order.

- Notification No- 27/2012 contemplates for filing of refund claims of unutilised CENVAT credit quarterly, but it does not bar the taxpayer from filing refund claim for the entire period, which may be more than a quarter. In the absence of any explicit bar, refund claims, if otherwise eligible, cannot be rejected on the ground that they are not filed quarterly.

Hence, the appeal was rejected and a refund allowed to the taxpayer.

CCE. vs Fabrimax Engineering Pvt Ltd [2016-TIOL-1926-CESTAT-MUM]

V. VAT

Notifications/Circulars/ Press Release

Rajasthan

Unified common refund application in Form No. 20 for e-refund has been made available by the Rajasthan Government on the departmental web portal for all the dealers registered under Rajasthan Value Added Tax, 2003, The Central Sales Tax, 1956, Rajasthan Tax on Entry of Goods into Local Areas Act, 1999 and Rajasthan Tax on Luxuries (in Hotels and Lodging Houses) Act, 1990.

Circular No. 07/2016-17 F.16 (95)/Tax/CCT/14-15/1169 dated 8 August 2016

Bihar

In respect of any consignment of goods above INR10,000 being imported into Bihar from any place outside the state of Bihar by an e-commerce company registered in the Patliputra circle, Patna on behalf of a person other than a registered dealer, then, generation of electronic transaction identification number shall be based on information uploaded in Form D- IXA.

Notification No. Bikri Kar/Vividh-43/2011-3055 dated 10 August 2016

Jharkhand

With effect from 22 July 2016, equipments purchased or to be purchased for installation of solar plants has been granted exemption from VAT. However, the said exemption is subject to transition in the GST regime in the future.

Notification No. S.O-81 dated 22 July 2016

Decisions

Licensing of technology through donor seeds for production of BT cotton hybrid seeds is deemed sale subject to VAT

In the present case, Mahyco Monsanto Biotech (India) Private Limited (MMB or the petitioner) has filed a writ petition with the Bombay High Court (HC) on the issue of levy of VAT on a transaction of transfer of 'BG technology' which kills specific insects effecting cotton crop.

The petitioner submitted that the transaction of granting the technology falls within the ambit of grant of permissive use rather than a transfer of a right to use. It is, therefore, a service and not a deemed sale within the meaning of Article 366(29A) (d) of the Constitution of India. The essence of a 'transfer', is the acquisition of a right by the transferee, and the corresponding loss of it by the transferor. A transfer of the right to use goods depends on who has effective control over the goods. The transaction is squarely covered by BSNL judgment. The 'twin test' specified in this judicial pronouncement i.e. a) transferee has legal right on such goods and to the specific exclusion of transferor; b) transferor again cannot transfer same right to any other person is not fulfilled because MMB can transfer the technology to more than one transferee at the same time. MMB also submitted that this judgment applies to tangible as well as intangible goods. Thus, the transaction is in the nature of grant of permissive use liable to service tax. MMB exercises sufficient control over the technology by means of providing NOC, testing the seeds of sub-licensee and providing approvals which are essential for commercialisation of seed by sub licensee.

Further, as held by the Supreme Court in various cases, a transaction can be subject to either service tax or a VAT and not both. Thus, the present transaction is liable only to service tax and not VAT. In the petition it was also, prayed that in the event the court held that the transaction is liable to VAT, then the High Court should pass an order directing Union of India to transfer the funds collected in the form of service tax to the VAT department directly and not to demand the same from MMB.

The state on the other hand, argued that the effective control is transferred to a sub-licensee to the extent of 50 donor seeds through which the technology is transferred and it is the sub-licensee who has the right to use those 50 donor seeds and additional donor seeds produced by the sub-licensee as they desire. Further, as per the sub-licensing agreement, the sub-licensee is not bound to return to Monsanto any portion of the initial 50 seeds and nor any additional donor seeds produced by him. The control and ownership of the same continues to be with the sub-licensee and no permission/approval is required from Monsanto for sale of these seeds to cotton farmers.

The HC further stated that the BSNL test argued by the taxpayer does not have global or universal applicability and it depends on a case to case basis. In the present case, the ratio of BSNL judgement is not applicable. Further, the most fundamental aspect of permissive use of goods is that at the end of the period for which the use is granted, the goods must be returned to the transferor. In the present case, the sub-licensee is not bound to return to MMB any portion of the initial 50 seeds given under the agreement nor any additional donor seed that the sub-licensee has produced.

Given the above, the HC has held that the transaction is in the nature of transfer of right to use goods and the same is subject to VAT. Further, with regard to the prayer of transfer of funds from Union to State government, HC declined to enter into such debate and left it to MMB to adopt suitable proceedings in this matter.

Mahyco Monsanto Biotech (India) Pvt Ltd vs the Union of India and others [TS-316-HC-2016(BOM)-VAT]