October 2016

TAX UPDATES

(containing recent case laws, notifications, circulars)

Prepared in association with

Foreword

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

A brief update of the representations made by FICCI in the last few weeks is as below:-

- A FICCI delegation led by Mr. Harsh Mariwala met the State Finance Ministers of Maharashtra, Kerala and Haryana to discuss issues related to Goods and Services Tax.
- FICCI participated in the meeting of the Seventh Standing Committee on TDS convened by the Government on September 20, 2016.
- A FICCI delegation led by Mr. J.K. Batra also attended the meeting convened by Department of Industrial Policy and Promotion in relation to the Budget. FICCI made representation on tax issues which need to be examined by the Government and requested DIPP to send the same to the Ministry of Finance for appropriate action.
- A FICCI delegation led by Mr. Hariharan, Partner, Dhruva Advisors, met the members of the Income Tax Simplification Committee on October 19, 2016. The Committee is headed by Justice Easwar and was set up by the Finance Minister last year for suggesting measures to simplify the direct tax laws. The second report of the Committee is due for submission to the Government on November 15, 2016.

The Taxation Division of FICCI is in the process of finalizing FICCI's Pre Budget Memorandum 2017-2018 for submission to the Government. A meeting of the Taxation Committee was held on October 14, 2016 to discuss the points for inclusion in FICCI's Pre Budget Memorandum 2017-2018.

In the direct tax regime, the Authority for Advance Ruling (AAR) in the case of Mahindra-BT Investment Company (Mauritius) Limited held that the capital gains arising from the transfer of shares are not taxable in India in view of Article 13(4) of the India-Mauritius tax treaty. The AAR while agreeing with the commercial rationale of the holding structure held that there is nothing wrong in the applicant holding the shares of an Indian company and eventually transferring the same to another company which fulfills conditions stipulated in the option agreement. The AAR examined the minutes of the board meetings held in Mauritius where key financial decisions were taken and held that the control and management of the applicant was not wholly in India as contemplated in erstwhile section 6(3) of the Income-tax Act, 1961.

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 TAX

High Court Decisions

Issuance of scrutiny notice under Section 143(2) of the Act cannot be a ground to reject AAR application since it does not address any specific question

The taxpayer filed its income-tax return for Assessment Year (AY) 2012-13. The tax department issued a notice under Section 143(2) of the Act. The notice is in general terms and all the questions are covered under the said notice under Section 143(2) of the Act. The taxpayer acknowledged the receipt of the notice. Subsequently, the taxpayer applied for an advance ruling under Section 245R of the Act. However, the AAR rejected the application invoking proviso to Article 245R(2) of the Act citing the reason that the issue was pending before income-tax authority.

The High Court held that the terms of notice issued by the AO under Section 143(2) of the Act indicates that it does not address any specific question. It does not even disclose application of mind to the returns save and except the fact that they conform to the instructions which compelled the AO to issue a scrutiny notice on account of the international transaction reported by the taxpayer. The Delhi High Court in the case of Hyosung Corporation vs AAR [2016] 382 ITR 371 (Del) and L.S. Cable & System Limited vs CIT (W.P. (C) 8799/2015, dated 13 May 2016) (Delhi High Court) had dealt with the identical notices and held that such notices ipso facto would be insufficient to attract the automatic rejection route under proviso to Section 245R(2) of the Act. Consequently, the AAR ruling rejecting the application is untenable.

Sage Publications Ltd U.K. vs DCIT (W.P. (C) 5870/2016) – Taxsutra.com

Deduction under Section 80HHC is denied due to non-filing of audit report

The taxpayer conducts an exports business in the name and style of Lotus International. The taxpayer derived income from the share of profit from firm and export business. For AY 1995-96, the taxpayer filed return of income and claimed deduction under Section 80HHC of the Act. The AO denied the claim of deduction holding that the mandatory certificate from a chartered accountant for claiming deduction under Section 80HHC of the Act was not enclosed with the return of income. The CIT(A) upheld the order of the AO. The Tribunal allowed the taxpayer's appeal and held that it was eligible for Section 80HHC deduction.

The High Court on perusal of Section 80HHC of the Act, observed that twin conditions necessary for claiming the deduction are i.e. i) the taxpayer should be an exporter and convertible foreign exchange is required to be received in the given time in India; ii) report from a chartered accountant is mandatory. The High Court disapproved the manner in which the claim has been allowed by the Tribunal on the basis of computation of total income alone and not even uttering a word about the audit report to claim deduction. There is no reason to allow the claim when sub-clause (4) of Section 80HHC mandates filing of an audit report in support for claiming deduction. The High Court rejected the taxpayer's reliance on Kerala High Court ruling in the case of Seeyan Plywoods vs ITO & Another [1999] 238 ITR 295 (Ker) and Bombay High Court rulings in Khatau Junkar Ltd. & Another vs K.S. Pathania & Another and JCT Ltd. & Another v. Hari Kishan & Another [1992] 196 ITR 55 (Bom).

CIT vs Kamaljeet Singh Aluwalia (Income Tax Appeal No. 62/2000, dated 8 September 2016)

Amendment made for issuing demand notices under Section 200A of the Act, levying fee for delay in filing a TDS statement is to be prospective in nature

During the year under consideration the tax deductible at source was deducted by the taxpayer and it was also deposited. However, there was a delay in filing the Tax Deducted at Source (TDS) statements. The tax department issued demand notices under Section 200A of the Act calling upon the taxpayer to pay a late filing fee under Section 234E of the Act. Subsequently, the taxpayer approached the High Court by challenging constitutional validity of Section 234E of the Act.

High Court ruling

Section 200A was inserted with effect from 1 April 2010, it provides that TDS statement should be processed and intimation should be issued to the deductor. However, there was no reference for fee payable under Section 234E of the Act. Section 234E providing levy of fees for default in filing TDS statement was inserted with effect from 1 July 2012. Similarly, imposition of penalty under Section 271H for default in furnishing of incorrect information in such statement was inserted with effect from 1 July 2012. Subsequently, with effect from 1 June 2016, Section 200A has been amended to provide that fee under Section 234E can be computed at the time of processing of the return and intimation could be issued specifying the sum payable by the deductor as fee under Section 234E of the Act.

Section 234E has come into force on 1 July 2012. One may say that since Section 234E is charging section for fee, the liability was generated or had accrued, if there was failure to deliver or cause to be delivered the TDS statement within the prescribed time. However, Section 234E of the Act cannot be read in isolation and is required to be read with the mechanism and the mode provided for its enforcement. When Section 234E was inserted in the Act simultaneously, Section 271H was also inserted. However, exception provided under Section 271H provides that no penalty shall be levied if the person proves that after paying tax with the fee and interest the amount is credited and he has delivered statement within one year from the time prescribed for submission of statement.

Prior to Section 271H of the Act, the enforceability of requirement to file return under Section 200(3) and Section 206C(3) was by virtue of Section 272A(2)(k) which provide penalty for default in furnishing TDS/TCS statement. However, when Section 234E was inserted with effect from 1 July 2012 simultaneously, a second proviso was added under Section 272A(2) with effect from 1 July 2012 providing that no penalty shall be levied where failure relates to TDS/TCS statement referred to in Section 200(3) or Section 206C which is delivered or cause to be delivered for TDS or TCS, as the case may be, on or after 1 July 2012.

On reference to Section 272A(2)(k) it indicates that where failure relates to TDS/TCS statement referred to in Section 200(3) or Section 206C, no penalty shall be imposed for TDS after 1 July 2012. Hence, the mechanism provided for enforceability of Section 200(3) or 206C(3) for filing TDS/TCS statement under Section 272A(2)(k) is done away in view of insertion of Section 271H providing for penal provision for such failure to submit return. When Parliament has simultaneously brought about Section 234E, Section 271H and the aforesaid proviso to Section 272A(2), it can be said that, the fee provided under Section 234E is contemplated to give a privilege to the defaulter to come out with rigor of penalty under Section 271H(1)(a), if he/she pays the fee within one year and complies with the requirement of Section 271H(3).

When a privilege is given to a particular purpose, it cannot be said that it is a levy of fee since it creates a counter benefit or reciprocal benefit in favour of the defaulter in the rigors of the penal provision. The provisions of Section 234E would meet with the test of quid pro qua. It was observed that when any provision is inserted for liability to pay tax or the fee by way of compensatory in nature and the manner of its enforceability is also required to be considered and examined. However, if the mode and the manner are not expressly prescribed, the provisions may also be vulnerable.

Unless it is expressly provided or impliedly demonstrated, any provision of statute is to be read as having prospective effect and not retrospective effect. Therefore, amendment made in Section 200A can be read as having prospective effect and not having retrospective effect. Accordingly, the demand under Section 200A for computation and intimation for the payment of fee under Section 234E could not be made in purported exercise of power under Section 200A for the period of respective AY prior to 1 June 2015.

When the intimation of the demand notices under Section 200A is held to be without authority of law so far as it relates to computation and demand of fee under Section 234E, it has been observed that the question of further scrutiny for testing the constitutional validity of Section 234E would be rendered as an academic exercise because there would not be any cause on the part of the petitioner to continue to maintain the challenge to constitutional validity under Section 234E of the Act. Accordingly, notices issued under Section 200A of the Act for computation and intimation for payment of fee under Section 234E as they relate to for the period of tax deducted prior to 1 June 2015 are set aside.

Sri. Fatheraj Singhvi and others vs UOI and others (Writ Appeal Nos. 2663-2674/2015, date 26 August 2016)

Reference by the AO to the Transfer Pricing Officer is valid if the AO is satisfied that it is necessary and expedient to refer the case and such opinion of the AO is approved by the Commissioner

The AO referred the case of the taxpayer to the TPO for computation of ALP of specified domestic transactions under Section 92CA(1) of the Act. The taxpayer raised objections against the reference to the TPO and the subsequent notice issued by the TPO. The AO prepared a detailed report and submitted the same to the Principal Commissioner. In his report the AO stated his/her reasons, why the taxpayer's objections were not valid. The Principal Commissioner of Income-tax (PCIT) rejected the taxpayer's objections.

High Court's ruling

- The High Court referred to the observations in the case of Veer Gems1, wherein the High Court had examined the TP provisions with emphasis on the reference by the AO and it was held that:

    - The TPO would not be competent to decide the issue of correctness of the reference made by the AO. His duty would be to determine the ALP in accordance with Section 92C of the Act.

    - Chapter X does not contain any provision requiring the AO to hear the taxpayer and consider the objections before making a reference to the TPO, however, has certain safeguards wherein the reference has to be made with the prior approval of the Commissioner.

    - While framing the assessment in terms of the TPO report under Section 92CA(3) of the Act, there is nothing to prevent the AO from considering the objections of the taxpayer, that there was no international transaction.

    - DRP would also have the power to nullify the variations arising out of the TPO's order if it is found that there had, in fact, been no international transaction and that therefore, the reference itself was invalid

    - It is not necessary for the High Court to judge whether there was any international transaction between the petitioner and the AE and such issue must be left to be judged while framing final assessment.

- The High Court noted that, in the present case, there is prima facie material suggesting that the directors of the taxpayer, in aggregate, held more than 20 per cent of the shares in voting power in Writers & Publishers Pvt. Ltd. (WPPL) and Bhaskar Infrastructure Limited (BIL) and the aggregate expenditure incurred by the taxpayer towards WPPL and BIL exceeded INR5 crore. Thus, the High Court dismissed the taxpayer's petition and allowed a TP procedure to be carried on further without interjecting at the intermediary stage of reference to the TPO.

- However, the question whether Clause (vi) of Section 40A(2)(b) of the Act would cover only the individual holding of the director and the relatives of the director of the taxpayer or the aggregate of the holdings was not concluded.

[1] Veer Gems vs ACIT (2013) 351 ITR 35 (Guj High Court)

D. B. Corp Limited vs DCIT (Special Civil Application No. 5035 of 2016)

Methods prescribed under the law need to be applied for ALP determination for intra-group services and Order of Customs department for imports can be considered for determination of ALP

Payment of technical fees

The taxpayer entered into an agreement with its AE to avail technical services in twelve fields and the AE was obliged to provide technical assistance in any of the twelve areas listed in the agreement as and when requested by the taxpayer. The taxpayer was able to provide a benefit test only in respect of three services out of the total twelve services listed in the agreement. Accordingly, the TPO made an adjustment on a pro-rata basis i.e. three by twelve services. The CIT(A) upheld the adjustment while the Tribunal deleted it.

High Court's ruling

The High Court upheld the Tribunal's order and observed as under:

- the agreement of the taxpayer is similar to a 'retainer agreement', i.e. it is upon the taxpayer to decide whether it requires all the services or not.

- the tax department did not apply any of the prescribed methods specified under Section 92C of the Act to determine ALP for availing services.

- the finding of the AO attributing nil value to nine of the services listed in the agreement, which were not availed of by the taxpayer was not justified.

Import of pigments

The taxpayer imported pigments from its AEs for trading and was also engaged in trading of non-pigments purchased both from AEs and non-AEs. The TPO adopted Transactional Net Margin Method (TNMM) but rejected the external comparables selected by the taxpayer and resorted to internal TNMM by comparing the margin earned by the taxpayer in case of pigments which were purchased from the AE with non-pigments purchased from third parties and made an adjustment. The CIT(A) upheld the adjustment while the Tribunal deleted the same and by relying on Rule 10B(2)(a), held that while the product characteristic is very important in case of Comparable Uncontrolled Price Method, the same cannot be ignored in case of TNMM.

High Court's ruling

Application of customs order - The High Court dismissed the appeal and observed that the data used in the anti-dumping order relates to the year under consideration. The levy of anti-dumping duty by the government on the products imported in India whether by way of predatory pricing policy or otherwise is a clear indication of the fact that the said product is being exported to the country by foreign parties at a very low price and hence, it shall be considered to be at ALP.

CIT vs Merck Ltd (ITA No. 272 of 2014)

Tribunal Decisions

On furnishing PAN by the recipient transporter contractor, immunity

from deducting tax at source is available to all payers irrespective of whether it was under a contract or a sub-contract

The taxpayer is an individual engaged in export of chemical, surgical and clinical goods. The taxpayer needs to incur transport charges in relation to purchases i.e. carriage inward and in relation to exports to Bangladesh i.e. carriage outward. The AO observed that the taxpayer was required to deduct tax at source on the transport charges under the Section 194C of the Act. The AO held that since the taxpayer has failed to deduct tax, the payment will be disallowed under Section 40(a)(ia) of the Act. The CIT(A) upheld the order of the AO. Before the Tribunal, the taxpayer contended that by virtue of Section 194C(6)2 of the Act since Permanent Account Number (PAN) of transporters were furnished, there was no need to deduct tax at the time of making payment to the contractor undertaking carriage of goods.

A plain reading of Section 194C(6) of the Act makes it clear that on the contractor undertaking transport of goods in the course of his/her transport business, furnishing PAN to the person making such payment/credit, the payee shall not be required to deduct tax from such payment to the transporter. On furnishing the PAN from the recipient transporter-contractor, the immunity from deducting tax under Section 194C(1) shall be available to all payers by virtue of 194C(6), in relation to all goods transport charges irrespective of the fact, whether it was under a contract or a sub-contract. The Tribunal held that if the taxpayer complies with the provisions of Section 194C(6) of the Act, disallowance under Section 40(a)(ia) does not arise just because there is violation of provisions of Section 194C(7) of the Act. Accordingly, the Tribunal deleted the disallowance made under Section 40(a)(ia) of the Act.

The Tribunal relied on Mumbai Tribunal ruling in the case of HCC-L&T Purulia Joint Venture (ITA Nos. 1644, 3041/MUM/2010) and CBDT Circular No. 05/2010 wherein it was clarified that PAN based immunity and exemption from deducting tax at source to transporters was extended in all transport contracts.

Soma Rani Ghosh vs DCIT (I.T.A. No. 1420 /KOL/ 2015) – Taxsutra.com

SEZ unit is eligible to claim deduction under Section 10AA of the Act notwithstanding the fact that the overseas customer is only the source of income available to the taxpayer

The taxpayer is engaged in the business of software development and providing information technology enabled services namely data processing and it exports this from the Noida SEZ unit. During the year under consideration, the taxpayer claimed deduction under Section 10AA of the Act. The AO denied the claim holding that majority of invoices were addressed to the taxpayer with the other SEZ's address and very few were bearing the Noida SEZ address. The AO by making several other observations came to the conclusion that the taxpayer is not doing any data

[2] Section 194C(6) - No deduction shall be made from any sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor during the course of plying, hiring and leasing goods carriages, where such contractor owns ten or less goods carriage at any time during the previous year and furnishes a declaration to that effect along with his PAN, to the person paying or crediting such sum.

processing work from its Noida SEZ units and the only source of income available to the taxpayer is from its overseas customer namely Galileo in the shape of commission on bookings done by the travel agents on Galileo's GDS. Accordingly, the AO denied the claim of deduction under Section 10AA of the Act. However, the CIT(A) allowed the claim of the taxpayer.

The Tribunal relied on the decision of ACIT vs Amadeus India Pvt. Ltd. [2001] 79 ITD 407 (Del) wherein similar functions and similar types of certificates have been issued to the taxpayer about the transmission of software. Further, the export value declared by the exporter has been found to be in order and accepted by the authorised officer. The Tribunal in that case allowed the claim of deduction. It was held that the CIT(A) was justified in equating the facts of the present case with that of Amadeus India. The profit and loss account show data processing software export, software development services income. Further, the auditor's report has certified that the taxpayer has been engaged in the development of computer software and information technology enabled product and services. The Tribunal did not find infirmity in the CIT(A) order in coming to the conclusion that the taxpayer is eligible to claim deduction under Section 10AA of the Act in view of the decision in the case of Amadeus India. Accordingly, it has been held that the taxpayer is eligible for the claim of deduction under Section 10AA of the Act.

DCIT vs Inter Globe Technology Quoteint Pvt. Ltd. (ITA No. 419/Del/2011) – Taxsutra.com

Arm's length principle cannot be invoked where replacement of self-declared prices of international transactions by ALP results in lowering of the taxpayer's income chargeable to tax

- The taxpayer followed a Transfer Pricing (TP) policy of marking-up its operating expenses by a margin of 20 per cent for purposes of invoicing its overseas Associated Enterprises (AEs). During the course of assessment proceedings, the taxpayer broadly faced two challenges.
  - An arm's length cost plus margin of 29.53 per cent was determined by the Transfer Pricing Officer (TPO) as against the margin of the taxpayer of 20 per cent.
  - The cost of Intra-Group Services (IGS) (say 10) received by the taxpayer from its AEs was held to be 'nil' (taxable income = 29.53 + disallowance on account of IGS 10 = 39.53).
- Before the Dispute Resolution Panel (DRP), the first adjustment was deleted and mark-up rate of 20 per cent was restored since it was found to be at Arm's Length Price (ALP). However, DRP declined to reverse the second adjustment on account of IGS (taxable income = 20 + Disallowance on account of IGS, 10 = 30).

Tribunal's ruling

- The Tribunal addressed the limited issue of whether the approach adopted by Revenue was sustainable in the eyes of law in view of embargo placed by Section 92(3) of the Income

Tax Act, 1961 (the Act). The Tribunal expressed the view that since the mark-up rate of 20 per cent was held to be at arm's length, disallowance of costs on account of IGS (i.e. 10) would result in diminution of operating expenses by the same amount, which would trigger a correlative downward adjustment in gross revenues by a factor greater than such disallowance by 20 per cent (viz. 10 + 20 per cent of 10 = 12). Effectively, in the Tribunal's view, for each unit of disallowance in costs, the gross revenue of the taxpayer would need to be correspondingly adjusted downwards by an amount of 1.20, thereby resulting in pro-rata net reduction in taxable income of the taxpayer in comparison to what had been reported in its income tax return.

- Section 92(3) of the Act provides that computation(s) with reference to arm's length principle cannot be carried out in a manner which is derogatory to entries recorded by the taxpayer in its books of account whereby it results in reduction of self-declared income chargeable to tax. Accordingly, the adjustment on account of IGS was deleted and the taxpayer's returned position was restored.

Mercer Consulting India Pvt Ltd vs DCIT (I.T.A. No. 1085/Del/2016)

AAR Decisions

Programme-fees received by non-profit US University are not taxable in India

The applicant had entered into an agreement with Northwest Universal Education Private Ltd. (Northwest/an Indian company). The applicant is a non-profit public benefit corporation formed for the purposes of providing education. Further the school of management (UCLA Anderson School of Management) is college affiliated and running under the umbrella of the applicant and that college provides executive education programmes. Vide agreement, applicant agreed to launch a management programme for the duration of 60 days for training senior executives of the companies/corporations having a minimum working experience of eight years. The applicant agreed to send its professors for training the senior executives working in India on management techniques. There are various modules to be undertaken under the agreement which are of the duration of four days, five days, 10 days, 12 days, etc. The Indian counterpart (Northwest) was to arrange the place for conducting these short duration programmes in India. The agreement also clarified that relationship between the applicant and Northwest would not be in the nature of - independent contractor/joint venture/employment agency/partnership. The applicant has filed an application with the AAR on the taxability of consideration it earns from Northwest for holding these educational programmes.

The AAR observed that the applicant's activity is an educational activity and was directly covered under Article 12(5)(c) of India-USA tax treaty. *The* AAR relied on another AAR ruling in the case of UC Berkeley Center for Executive Education, USA wherein it was held that since the nature of the activity by the applicant was educational in nature, it could not amount to fees for included services or at any rate royalty particularly because of the provision of Article 12(5)(c) of the treaty.

The AAR had further held that the applicant could not be said to have a Permanent Establishment (PE) in view of AAR ruling in Eruditus Educational Private Limited. Every time the programme is undertaken in India, it was Northwest that had arranged for the place for conducting the programmes. AAR further noted that Northwest was not bound to arrange for the same place and it may arrange different locations for conducting the programme. AAR thus held that there cannot be any fixed place of business on the part of the applicant. The AAR thus rejected the tax department's contention that applicant formed a PE in India and held that from any angle there cannot be a PE as defined in Article 5 of the tax treaty.

It was also held that the programme fee received by the applicant was not taxable as royalty.

The Regents of the University of California [AAR No. 1656 of 2014] – Taxsutra.com

Capital gain arising on transfer of shares of an Indian company is not taxable under the India-Mauritius tax treaty, control and management is held outside India

The applicant's shares are held by Mahindra Overseas Investment Co. (Mauritius) Limited, a company incorporated in Mauritius and BT Holding Limited, a company incorporated in the United Kingdom in the ratio of 57:43. The applicant's board of directors comprises of three directors resident in Mauritius, one director resident in the United Kingdom and one director resident in India. The control and management of affairs of the applicant is exercised by the board of directors whose meetings were conducted in and chaired in Mauritius.

Mahindra & Mahindra Ltd. (M&M), a company incorporated in India and British Telecommunication PLC (BT), a company incorporated in England entered into a joint venture agreement to form Mahindra British Telecom Ltd. (now known as Tech Mahindra Limited (TML) on 19 August 1986. The shares of TML were held by M&M and BT in the proportion of 57:43.

TML and SBC services (now known as AT&T) entered into a commercial agreement on 28 December 2004.

The applicant was incorporated in Mauritius on 9 May 2005. The applicant had acquired 8 per cent holding in TML which is listed on Bombay Stock Exchange and National Stock Exchange in India. The shares were acquired in two tranches in financial years 2005-06 and 2006-07. An agreement was entered into between TML and the applicant on 23 June 2005 wherein the applicant agreed to subscribe and invest in TML on a partly paid basis. The applicant agreed to subscribe 99,31,638 equity shares at a price of INR67 per share.

A multiparty agreement named as 'Option Agreement' was executed between AT&T, M&M, BT, TML and the applicant on 10 May 2005. As per the Option Agreement, AT&T will be granted options over the shares representing 8 per cent of the enlarged fully diluted shares of TML upon achieving certain specified milestones. AT&T achieved the milestones and decided to exercise the option. The applicant consequently transferred 98,70,912 shares of TML to AT&T at USD3.5022 per share and realised long-term capital gain of INR900 million (approximately).

In the instant case, earlier the AAR had held3 that it is not bound to give a ruling on the said transactions intended to circumvent SEBI guidelines issued in public interest. The matter was taken to the Bombay High Court by the applicant. The High Court noted that the agreement entered into in 2004 between TML and AT&T was not acted upon due to commercial reasons and that the draft prospectus filed with the Securities Exchange Board of India (SEBI) in 2006 had disclosed the agreement entered into by the applicant with AT&T. The High Court restored the questions to the AAR for a ruling holding that there had been no breach of SEBI guidelines and SEBI had not issued any show cause notice or adjudication order for contravention of its guidelines.

The AAR held that the tax department's emphasis on the fact that the applicant was not set up for a commercial purpose and was holding shares only for ultimately transferring the same to AT&T is misplaced. With an objective to motivate AT&T to give business to TML, it was agreed commercially between the applicant, TML and AT&T that AT&T would be offered an opportunity to become a shareholder of TML only when it had given a certain level of business to TML for which certain milestones were set. It was only after such milestones were achieved that the option was exercised. There is nothing unusual or abnormal about such conditions in an Option Agreement.

[3] Mahindra-BT Investment Company (Mauritius) Ltd. [2012] 24 taxmann.com 296 (AAR)

On perusal of minutes of the board meetings held in Mauritius relating to buy-back of shares, final closing for sale of shares held in TML, appointment of tax advisor, approval of financial statements, dividend declaration and distribution, etc. indicate that the control and management of the affairs of the company particularly all financial affairs were situated only in Mauritius.

The Supreme Court in the case of V.VR.N.M. Subbayya Chettiar vs CIT [1951] 19 ITR 168 (SC) held that the term affairs must mean affairs which are relevant for the purpose of the Act and which have some relation to income. There is no substantial evidence to show that any important affairs of the applicant relevant for the purpose of the Act were being controlled from India.

AAR placed reliance on the decision of CIT vs Nandlal Gandalal [1960] 40 ITR 1 (SC) wherein the Supreme Court held that the expression 'control and management' means de facto control and management and not merely the right or power to control and manage. There is no force in the argument that since the real transaction was between TML and AT&T, the control and management of the applicant should be treated as in India.

Mahindra-BT Investment Company (Mauritius) Limited [A.A.R. No 991 of 2010] – Taxsutra.com

Contract for the glazing and cladding was a composite contract and thus the entire amount received by the foreign company was taxable in India

The applicant, a company registered under the laws of Singapore, is engaged in the business of executing contracts in relation to structural glazing and wall cladding works. The applicant set up project offices in India for the purpose of executing the contract works awarded to the company. Delhi International Airport Private Limited (DIAPL) floated a global tender for various works in connection with the development of T3 terminal at Delhi Airport.

Larsen & Toubro (L&T) won the contract. Thus the main contract was awarded by DIAPL to L&T and L&T in turn awarded the contract (for entire external and internal façade for the glazing and cladding systems for Piers, fixed link bridges and nodes) to the applicant (sub-contractor). The currency of the contract was in Indian Rupees and place of payment was in Delhi, however pursuant to an option given the payment was also made in Singapore Dollars in Singapore.

The applicant filed an application before the AAR, submitting that the scope of its work could be broadly divided into a) Offshore supply to goods b) Installation and other works to be executed at the airport. The contract was an offshore supply contract with respect of supply of goods, the title was passed to L&T Offshore and also the payment was received in Singapore and therefore no income accrued/arose or deemed to accrue or arise in India to make it taxable in India. With regard to the offshore supply of goods, it negotiated and concluded the supply of goods and materials from various third party suppliers/manufacturers outside India and, therefore, all the activities in connection with the offshore supply were carried outside India.

The applicant also submitted that no income could be attributable to the PE of the applicant i.e. Project office in India since the profits earned by way of off-shore supplies to L&T were not directly or indirectly attributable to that PE. The PE (Project Office) in India oversees the installation of structural glazing works and wall cladding works for DIAPL and it had no connection (directly or indirectly) in the offshore supplies and the off-shore supplies executed by it; it was an independent scope of work.

The AAR held that there was only one contract agreement to be executed by the applicant for the entire internal and external façade and rejected applicant’s artificially bifurcating contract into supplies affected and services rendered. It has rejected the applicant’s submission that the profits could not be attributable to the PE in India. The PE in India had come into existence long before the design of materials and equipments for offshore supply started. The contract document shows that it was being manned by personnel deployed for design of goods and materials to be selected and procured. The goods have been cleared from customs in India by the project office and customs duty has also been paid by the project office. In these circumstances, to say that PE had no role in respect of supply of goods and materials is incorrect.

Even though the sale was concluded outside India the applicant was responsible for installation work in India at its own expenses which was concluded through the project office (i.e. PE) in India. The applicant bore the risk and insurance with respect to the plants and materials until completion and insurance covers entire replacement cost including the removal of debris and making good of affected works.

Applying the intention principle under the Sales of Goods Act, it was concluded that in the present case the intention of the applicant would pass only when the installation and erection of entire works will be completed. DIAPL and L&T never intended to buy materials on standalone basis. The undertaking of all these responsibilities, even after making a sale to L&T outside India, shows the intention. Buying of insurance in the name of the applicant instead of L&T till it reaches the site in India is a clear proof that risk does not pass to L&T/DIAL till the goods are not used for the works as per the contract.

The AAR held that the contract was a composite contract and thus the entire amount received by the applicant from L&T was taxable in India.

MERO Asia Pacific Pte Ltd (AAR No. 981 of 2010) – Taxsutra.com

II. SERVICE TAX

Service Tax - Decisions

Construction services provided to Housing Board is exempted from Service tax

The issue involved in the instant case was whether Service tax would be applicable on construction services provided to Haryana Housing Board.

The High Court held that Haryana Housing Board qualifies as 'Governmental authority' since it is set up under a State legislation and wholly controlled by the State Government and accordingly, construction services provided to the Haryana Housing Board would be exempted from Service tax.

M/s Bharat Bhushan Gupta & Company vs. State of Haryana and others [2016-VIL-459-P&H-ST]

Power of arrest cannot be used by bypassing procedure laid down in the Service tax laws

The issue in the instant case is whether the revenue authorities could bypass the adjudication procedure and proceed with arrest and detention merely on the ground of suspicion of evasion of Service tax.

The Delhi High Court held that without any determination of the amount of Service tax arrears, resort to the extreme measure of arrest and detention was impermissible in law on account of the following reasons:

- In order to be satisfied that a person has committed an offence, an enquiry has to be conducted by giving an opportunity to the person sought to be arrested; and

- The only possible exception could be in case of a habitual evader of Service tax where such person does not file Service tax returns, commits repeated defaults, etc.

Makemytrip India Pvt. Ltd. vs. Union of India & Ors. with Ibibo Group Pvt. Ltd. Union of India & Ors. [2016-TIOL-1957-HC-DEL-ST]

Clinical pharmacology and clinical research services provided in respect of goods made available by foreign customer is liable to Service tax

The issue involved in the instant case was whether the activity of clinical pharmacology and clinical research in respect of goods made available by service recipient would be liable to Service tax.

The Authority for Advance Rulings (AAR) held that place of provision of the said activities is in India and such services would be liable to Service tax on the basis of the following rationale –

- The Applicant provided such services on the basis of formulations made physically available by the service recipient; and

- In case of services provided in relation to goods made physically available by service recipient, the Service tax law does not provide that the services should be provided qua the specific goods.

M/s Steps Therapeutics Ltd. v. Commissioner of Customs, Central Excise & Service tax, Hyderabad [Ruling No. AAR/44/ST-1/27/2016]

Contribution received by members of a club for establishing a club is liable to Service tax

The issue involved in the instant case was whether money contributions received from prospective members of a club for establishing a club is liable to Service tax.

The AAR held that such contributions are received for providing various facilities in the club and therefore such contributions are liable to Service tax since a club and its members are deemed to be separate persons and an activity carried out by a club for its members would be construed as a 'service'.

M/s Avadh Infratech Ltd., Gujarat v. Commissioner of Central Excise, Surat [Ruling No. AAR/44/ST-I/29/2016]

Services of outbound and inbound shipment do not qualify as 'intermediary services'

The issue involved applicability of service tax on freight margin recovered from customers towards outbound and inbound shipment of goods is liable to Service tax as intermediary services.

The AAR held that in case of outbound shipment, since destination of goods is outside India, hence, service tax will be exempt in terms of Place of Provision of Services Rules 2012. However, prior to 1 June 2016, services of inbound shipment being covered under the Negative list of services is exempted from Service tax. With effect from 1 June 2016, service tax shall apply on transportation of goods by vessel from a place outside India.

With respect to differential freight margin retained by the applicant, the AAR held that the said services would not qualify as 'intermediary' services since the arrangement between the applicant and airlines/ shipping lines is separate and distinct from the relationship with its customer and on principal to principal basis and the applicant does not contract with the airlines/ shipping lines on behalf of its customer.

M/s Global Transportation Services Pvt. Ltd. v. Commissioner of Service tax, Mumbai [Ruling No. AAR/ST-1/23/2016]

Notification/Circulars/ Press Releases

Exemption to renting of precincts of religious places amended

The exemption provided to renting of precincts of religious places has been amended to include a condition that such religious places should be owned or managed by an entity registered as a charitable or religious trust or institution under the Income tax laws. Further, it has been clarified that the term 'religious precincts' should be widely interpreted to include all immovable property within the outer boundary walls in which the religious place is located.

Notification No. 40/2016 – ST dated 6 September2016 and Circular No. 200/10/2016 – ST dated 6 September 2016

Exemption on license fee or spectrum user charges paid to Government amended

The Service tax exemption on services by way of granting telecommunication license and right to use radio frequency spectrum by the Government during the financial year 2015-16 has been amended to extend the scope of such exemption to services provided for the period prior to 1 April 2016.

Notification No. 39/2016 – ST dated 2 September2016

Abatement on services of transport of passenger through Regional Connectivity Scheme airports

Abatement of 90 percent for services of transportation of passengers embarking from or terminating in a Regional Connectivity Scheme (RCS) airports for a period of one year (from the date of commencement of operations of such RCS airports), has been granted subject to condition of non-availment of CENVAT credit.

Notification No. 38/2016 – ST dated 30 August 2016

Clarification in relation to water supply services provided to Government

In relation to Service tax exemption on services in relation to water supply provided to Government, a local authority or a governmental authority, it has been clarified that the exemption cover a wide range of activities and it includes the activity of construction of tube wells.

Circular No. 199/09/2016 – ST dated 22 August 2016

III. CENTRAL EXCISE

Decisions

Once the activity is considered amounting to manufacture and duty is duly discharged CENVAT credit on same cannot be denied

The taxpayer is manufacturer of high carbon ferro chrome (HCFC), classifiable under HS Code 7202.00. They are availing CENVAT credit on inputs & capital goods. The taxpayer purchased low grade HCFC on payment of duty, processed the same and resultant High Grade Carbon HCFC was cleared on payment of applicable Excise duty treating the process as manufacture activity. The department was of the view that no manufacture was involved as the input consumed (low grade HCFC) and final product (high grade HCFC) both fell in the same HS Code 7202. A show cause notice was issued raising the above allegations and proposing demand/recovery of CENVAT credit along with interest, besides proposal for imposing penalty.

Before the CESTAT, the counsel for the taxpayer submitted that the clearance were made on payment of Excise duty. The credit availed on inputs is sought to be denied on the sole premises that the activity does not amount to manufacture.

The taxpayer submitted that it is settled law that once duty on the final products has been accepted then the benefit of CENVAT credit cannot be denied on the ground that the activity does not amount to manufacture. Considering the contentions made by the taxpayer and relying on the Mumbai Tribunal judgment in the case of *Uttam Galva Steels Ltd vs CCE.* the appeal was allowed.

Andhra Ferro Alloys Ltd vs Commissioner of Central excise and Commissioner of Customs, Visakhapatnam-I **[2016-TIOL-2296-CESTAT-HYD]**

Notification/Circulars/ Press Releases

Supply of goods manufactured by EOU's without payment of Central Excise duty against Advance License /Authorization

Representations have been received regarding the applicability of Notification 22/2003 – CE, when goods manufactured by EOU's are supplied to Advance License / Authorization holder. The said notification seeks to deny the exemption from Excise Duty on inputs in case where goods cleared in DTA are non-excisable or Nil rated Custom duty. In this regard, it has been clarified that Notification 23/2003 – CE has been issued in respect of goods manufactured by EOU's and cleared in DTA, specifically exempts Central Excise Duty, when the goods are supplied to Advance License / Authorization holder. In fact, clearance from EOU or DTA unit to Advance License / Authorization holder has been allowed without payment of duty, as both the cases are of 'Import Substitution'. In case of supply of goods to Advance License / Authorization holder, the export obligation is cast upon person holding Advance License / Authorization and in case of default in the export obligation, recovery procedures is provided in law.

It was further clarified that if EOU's are made to pay back the amount availed as exemption on the inputs used in the supplies made to Advance License / Authorization holder, then EOU's would be placed in disadvantageous position when compared to DTA unit, which supply manufactured goods to Advance License / Authorization holder without payment of duty and without reversal of CENVAT credit.

Circular No 1046/34/2016 – CX dated 16 September 2016

IV. CUSTOMS DUTY

Notifications/Circulars Press Release

Admissibility of un-utilized CENVAT credit of DTA unit converted into EOU

The Circular No. 77/99 - Cus dated 18 November 1999 was provided for lapse of unutilized balance of Modvat credit on conversion of DTA unit into EOU. Circular 77/99-Cus was issued in view of the erstwhile Rule 100 H of Central Excise Rules, which specifically prohibited EOU's from availing Modvat Credit of Inputs / Capital Goods under Rule 57A and 57Q. But consequent to supersession of Central Excise Rules 1944 by Central Excise Rules, 2002, there is no provision similar to Rule 100 H of CER, 1944 which prohibits the EOU from availing Cenvat Credit of Inputs/ Capital Goods.

Moreover, Rule 17 of Central Excise Rules 2002, which deals with the removal of goods by an EOU, was amended with effect from 6 September 2004 to allow use of Cenvat credit for payment of duty by an EOU. Rule 10 of CENVAT Credit Rules, 2004 provides in unambiguous terms that if manufacturer transfers his factory on account of change in ownership or lease, then the manufacturer shall be allowed to transfer the CENVAT credit lying unutilized in his accounts to transferred entity. EOU is also a manufacturer, and hence this rule apply to them. Accordingly, the Circular No. 77/99 – Cus dated 18.11.99 has been withdrawn and on conversion from a DTA unit to EOU, the transfer of unutilized CENVAT credit lying in the books of DTA unit on the date of conversion into EOU unit is admissible.

Circular No 41/2016-Customs, dated 30 August 2016

V. VAT

Decisions

Payments made to a sub-contractor for works contract, shall not form part of 'total turnover' for purpose of computation of turnover tax

The taxpayer, in the present case, is in the business of engineering and is registered under the Karnataka Sales Tax Act, 1957 (Sales Tax Act). The contracts which are secured by the taxpayer are the works contracts and a part thereof, is generally assigned to sub-contractors. Such sub-contractors are also registered under the Sales Tax Act and had submitted returns and paid taxes for the execution of works contract. The taxpayer contended that since the sub-contractors were the parties who executed works contract and the transfer of property in goods involved in execution of works contract had already been taxed in the hands of sub-contractor, the payment made to sub-contractors could not be taken into account while computing total turnover of the taxpayer i.e. main contractor.

The contention of the taxpayer was not accepted by the Assessing Officer as well as the Karnataka Appellate Tribunal. In the revision petition filed before the Karnataka High Court against the decision of Appellate Tribunal to include the part of works contract executed by the sub-contractors in the total turnover of the taxpayer, the High Court decided against the taxpayer affirming the view taken by the Appellate Tribunal. The taxpayer challenged High Court judgment before the Supreme Court.

The taxpayer specified that sales tax is payable on the transfer of property in goods involved in execution of works contract. Further, the definition of turnover includes the aggregate amount for which goods are bought or sold. Thus, the transfer of property in goods is essential criteria to constitute a sale and also for the calculation of turnover / total turnover. In works contract, the property in goods involved in execution of works contract passes as movable but on the theory of accretion. Further, property is transferred only once by accretion which is taxed as a sale. The taxable person is the sub-contractor executing the works contract and the main contractor who assigns the work to sub-contractor to execute the work, cannot be a transferor, nor any property in goods vest in the main contractor, when the contract is executed by a sub-contractor. Hence, in the present case, there is no sale of goods involved in execution of works contract from sub-contractor to taxpayer. It was also contended that since sub-contractors have executed the works contract and have also paid taxes on such transfer of property in goods involved in execution of works contract, the inclusion of such value in the total turnover of taxpayer would amount to double taxation. In this regard, the taxpayer relied upon the pronouncement of Andhra High Court in its own case wherein it was held that no tax shall be payable on payments made to sub-contractor.

Revenue, on the other hand contended that there is a distinction between ‘taxable turnover’ and ‘total turnover’. As the issue involved herein is related to the turnover tax for which the total turnover becomes relevant i.e. aggregate amount for which goods are bought or sold, without considering any deductions from the turnover on account of payments made to sub-contractor. Accordingly, the payments made to the sub-contractors is also includible in the hands of the taxpayer. Further, the Revenue also contended that the HC was correct in holding that sales tax is leviable at a single point whereas turnover tax is leviable at a multi-point (both at the hands of the main contractor and sub-contractor) and accordingly, the question of double taxation does not arise.

The Supreme Court held that the total amount paid or payable to the dealer as a consideration for 'transfer of property in goods' which is involved in execution of the works contract, is to be treated as 'total turnover'. Sales tax law specifically restricts the total turnover in respect of those goods only where the property has been transferred and hence, the transfer of property in goods becomes necessary event. Accordingly, unless there is a transfer of property, the amount paid cannot be included in the ‘total turnover’. Further, once the work is assigned by the main contractor to a sub-contractors, the main contractor ceases to execute the works contract as property passes by accretion and there is no property in goods with the contractor which is capable of a retransfer, whether as goods or in some other form. Hence, the amount paid to the sub-contractor is not for transfer of property in goods from sub-contractor to the main contractor i.e. taxpayer.

In view of the above, the Supreme Court held that payments made to the sub-contractors shall not be taken into consideration while computing 'total turnover'.

Additional Deputy Commissioner of Commercial Taxes vs. Larsen and Toubro Limited - [TS-354-SC-2016

Notifications/Circulars/ Press Release

Chhattisgarh

With effect from 22 August 2016, the rate of tax on Mobile phones has been increased from 5 percent to 14.5 percent.

Notification No. F-10-34 /2016/CT/V (68) dated 22 August 2016

Maharashtra

With effect from 17 September 2016, VAT rate for goods falling under Schedule C has been increased from 5.5 percent to 6 percent and that for goods falling under Schedule E from 12.5 percent to 13.5 percent.

Further, in relation to any other kind of motor spirit mentioned in Schedule D, the VAT rate has been changed from '26 per cent + Four rupees fifty paise per litre' and '25 per cent + Four rupees fifty paise per litre' to '26% + Six rupees per litre' and '25% + Six rupees per litre' respectively.

Notification No. VAT. 1516/CR-123/Taxation-1- dated 16 September 2016

The facility to upload the MVAT and CST Return in the new automation process has been started from 29 August 2016. Further, the department has also provided the detailed procedure and the revised due dates for uploading the return in the new system.

Trade circular no. 22T of 2016 dated 26 August 2016

Gujarat

In order to promote ease of doing business in the state of Gujarat and to ensure reduction in the cost of compliance for tax payers, the Government of Gujarat has decided to facilitate the tax payers to provide single common user ID to log into the portals associated with the provision of e-services for the purpose of the Gujarat Value Added Tax Act, 2003, the Central Sales Tax Act, 1969, the Tax on Entry of Specified Goods into Local Area Act, 2001, Profession Tax Act, 1976, Entertainment Tax Act, 1977 and the Luxury Tax Act, 1977 with effect from 1 September 2016.

Resolution No. G. R. No. GST-1016-1068-GST Cell dated 1 September 2016

Kerala

The procedures for check post has been streamlined for the clearance of goods into/out of the state of Kerala by issuing the guidelines for not imposing security deposit for the cases involving technical reasons, to avoid the delay in clearance of goods.

Circular No. 15/ 2016 No.C1-1880/2016/CT dated 27 August 2016

Andhra Pradesh

The formats for VAT waybill, CST waybill and Advance CST waybill have been modified to incorporate all the relevant options to ensure declaration of all required details by the dealers at the time of transportation of goods.

CCT's Ref No. AI (1)/18/2016 dated 9 September 2016