October 2013

TAX UPDATES

(containing recent case laws, notifications, circulars)

Prepared in association with

Foreword

I am pleased to enclose the October 2013 issue of FICCI's Tax Updates. This contains recent case laws, circulars and notifications pertaining to direct and indirect taxes.

The Shome Forum has concluded the first set of meetings for exchange of views between the trade & industry representatives and the Government on tax related issues. Last meeting of the Forum was held on September 26, 2013, wherein, FICCI and CII jointly represented the taxation issues of the 'Financial Services Sector'. Ministry of Finance has issued some notifications/Circulars on matters relating to indirect taxes following the discussions in the Forum. We expect some more clarifications/amendments from the Ministry soon.

On the taxation regime, the Central Board of Direct Taxes notified the final Safe Harbour Rules after public consultations. These rules shall be applicable for a period of five years as against two years provided in the draft rules. The threshold of Rs. 100 crores for IT, ITES and KPO sector as proposed by the draft rules has been done away with. The final rules also provide for a time bound procedure for determination of the eligibility of the taxpayer and of the international transactions for safe harbor. It is hoped that the safe harbor rules will bring the much needed certainty and clarity in the transfer pricing regime of the sectors covered by the rules.

Further, the Government has also notified the much-awaited General Anti Avoidance Rules (GAAR) that will come into effect from 1 April 2015. Keeping in line with measures for building investors confidence, the GAAR Rules have provided for monetary threshold, non-applicability of the GAAR to the FIIs which do not take the treaty benefit and grandfathering of investments made before August 30, 2010. The Rules will help allaying the investors' fear about the uncertainty with regard to the implementation of the GAAR provisions.

The Empowered Committee of State Finance Ministers (EC) met in New Delhi on 19th September, 2013 to review the progress of the work done by the three Committees set up earlier this year to examine various aspects of GST such as exemptions, thresholds, interstate supplies, GST network, dual administrative control etc. The Empowered Committee will be meeting again after a month to review the reports of these committees. The EC has also set up another committee to examine the report of the Parliamentary Standing Committee on the Constitution Amendment Bill relating to GST which has been presented in Lok Sabha on 7th August, 2013. Any tangible movement on GST is expected in EC's next meeting.

We are in the process of compilation of FICCI's Pre Budget memorandum for 2014-15. We look forward to your valuable suggestions for inclusion in the Memorandum.

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

Import contract without 'license' illegal; expense on transfer of contractual obligation is to be disallowed under explanation to Section 37

The taxpayer was engaged in trading of various goods, in local as well as international markets. During AY 2004-05, the taxpayer had entered into transactions with Swiss Singapore Overseas Enterprises Pvt. Ltd., UAE (SSOE), for import of furnace oil of a specified quantity. The taxpayer did not hold requisite license issued by the concerned authority, and so the oil was not imported legally. Accordingly, in order to avoid criminal / penal proceedings, the taxpayer approached its sister concern BGM Exim Ltd, which had license, to import the products. The taxpayer purchased furnace oil from its sister concern and paid 'commission' of Rs. 28 lakhs, for transfer of contractual liability for importing furnace oil from SSOE. Unable to elicit a satisfactory explanation for the expense from the taxpayer, the AO disallowed the expense. The AO's order was then reversed by the CIT(A). However, the Tribunal confirmed the AO's original order, disallowing the expense.

The Gujarat High Court, upholding the Tribunal Order, held that the payment was not allowable under Explanation to Section 37(1) of the Act. The High Court in coming to this conclusion observed that the amount of commission was essentially paid for the transfer of a contractual obligation. However, as per the prevalent law, a license was necessary for importing furnace oil, which was not available with the taxpayer. The High Court further held that even by ignoring the term "commission" and simply considering the character of the payment 'in substance', it cannot be justified that there was any valid claim for allowing payment as a consideration for transfer of a contractual obligation. The High Court noted the principles laid down by the Supreme Court in the case of Prakash Cotton Mills v. CIT [1993] 201 ITR 684 (SC), wherein it was held that when the payment for imports are composite in nature, (i.e. partly compensatory and partly penal), the authority had to bifurcate the two components and give a deduction of that component which was compensatory in nature and refuse deduction of that component which was penal in nature. As the taxpayer failed to show the compensatory nature of the commission, the claim was disallowed.

Overseas Trading and Shipping Co. Pvt. Ltd. v. ACIT [TS- 453-HC-2013 (Guj HC)]

No withholding of tax is required on payment of service tax levied on fees for technical/professional services

The taxpayer was a project of the Government of Rajasthan for the infrastructure development and civic amenities in certain areas and cities in the State of Rajasthan. In relation to this project, the taxpayer appointed the technical and project consultants along with limited companies and corporate consulting firms. The taxpayer deducted income-tax at source from the payments it made and deposited the same as per the relevant provisions of the Act and the return for the same was filed in due time. The taxpayer's main consultants were charging service tax at the prevailing rates on the fees was paid as per the agreement by the taxpayer. The tax was deducted on fees and other payments of expenses as part of the contract. However, no tax was deducted on service tax in view of the terms of contract. The AO raised a demand along with interest thereon on account of a default in complying with withholding tax provisions on the amount paid as service tax. The CIT(A) dismissed the AO's order. The Tribunal dismissed the tax department's subsequent appeal against the CIT(A) order.

The High Court observed that, as the Tribunal had considered the agreement and recorded a finding that as per the terms of contract, amount of service tax was to be paid separately, therefore, the amount was not subject to withholding tax provisions. Further referring to the provisions of Section 194J of the Act, and Circular no. 4/2008 and No.275/73/2007-IT(B) dated 28 April 2008 and 30 June 2008 respectively, the Court stated the words "any sum paid", used in Section 194J of the Act, related to fees for professional services/technical services. As per the terms of agreement, the amount of service tax was to be paid separately and was not included in the fees for professional services/technical services. The High Court thus concurred with the order of the lower authority, which was in accordance with the provision of Section 194J of the Act.

CIT (TDS) v. Rajasthan Urban Infrastructure Development Project (DB ITA No. 235/2011, DB ITA No. 222/2011, DB ITA No. 239/2011)

Tribunal Decisions

Payment for supply of standard software is in the nature of 'Royalty'

The taxpayer, an Indian company, engaged in the telecommunication business made payments to various non-resident companies towards the purchase of standard software required for its telecommunication network. In response to an application under section 195(2) of the Act, the Assessing Officer (AO) held that the payments for purchase of software were in the nature of a 'royalty' and accordingly tax was required to be deducted from these payments.

The issue for consideration before the Mumbai Tribunal was whether the payments made by the taxpayer towards purchase of standard software were in the nature of 'royalty' under the provisions of the Act and under the respective tax treaties.

Based on the facts of the case, the Tribunal, inter-alia, observed and held as follows:

- In the instant case, as the payment was for supply of software only, and not for embedded software (wherein software is supplied as part of the equipment), the decision of the Karnataka High Court in the case of CIT v. Synopsys International Old

Limited [2012] 28 taxmann.com 162 (Kar HC) and CIT v. Samsung Electronics Co. Ltd. and others [2012] 345 ITR 494 (HC Kar), wherein the payments for supply of software were held to be in the nature of royalty, would be applicable. The decisions of the Delhi Special Bench and the Delhi High Court in the case of Motorola Inc v. DCIT [2005] 95 ITD 269 (Del), DIT v. Ericsson A.B [2012] 343 ITR 470 (Del HC) and DIT v. Nokia Networks OY [2012] 25 taxmann.com 225 (Del HC), wherein it was held that the payments for embedded software were not in the nature of royalty, were not applicable to the instant case.

- Purchase of 'off-the-shelf' or 'shrink wrapped' software amounted to transfer of part of the copyright and transfer of the right to use the copyright for internal business as per the terms and conditions of the agreement.
- Accordingly, the payments made by the taxpayer towards purchase of standard software were in the nature of 'royalty' and tax was required to be deducted from these payments.

DDIT v. Reliance Infocom Ltd [2013][TS- 433-ITAT][MUM]

Service tax collected by non-resident shipping company, forms part of presumptive income taxable under Section 44B(2) of the Act; Theory of 'element of profit' not applicable under Section 44B

The taxpayer was a company incorporated in Hong Kong and was engaged in the business of operations of ships in international waters. The taxpayer computed total income at the rate of 7.5 percent of total collection as per the provisions of Section 44B read with Section 172 of the Act. The taxpayer, while filing return of income, excluded the component of service tax while computing presumptive income at the rate of 7.5 percent under Section 44B of the Act. The AO ordered that service tax to be included in the computation of presumptive income under Section 44B of the Act. The Dispute Resolution Panel (DRP) confirmed the order of AO.

The Mumbai Tribunal held that the 'theory of element of profit' would not apply to the aggregate amount as specified in sub-section (2) of Section 44B. The Tribunal held that the levy of tax on sale of goods or services was reflected in bills, and the amount received on account of service tax was a part of the price of carriage/shipped service and hence would be in the nature of a trading receipt. Thus service tax would form part of turnover for computing presumptive profit under Section 44B of the Act. The Tribunal also held that if the element of profit was the only criteria for inclusion or exclusion of any amount, the demurrage charges or handling charges should not have been included in the aggregate amount for the purpose of determining the presumptive income, because they did not represent an element of profit; it was not the legislature's intention to exclude items without a profit element. Further the Tribunal also relied on the decision of Supreme Court in the case of Chowringhee Sales Bureau (P) Ltd. vs. CIT [1973] 87 ITR 542. The Tribunal also distinguished ruling of Bombay High Court in the case of CIT v. Sudarshan Chemicals Industries Ltd. [2000] 245 ITR 769 (Bom) [relied upon in Islamic Republic of Iran Shipping Lines v. DCIT [2011] 11 taxmann.com 349 (Mum), stating that it was related to provisions of Section 80HHC, which itself provided for a definition of turnover. The Tribunal also noted that there are various decisions of Mumbai and Delhi Tribunal that have taken divergent views.

China Shipping Container Lines (Hong Kong) Co. Ltd. v. ACIT [TS-428-ITAT-2013(Mum)]

Disallowance under Section 14A is also applicable to shares held as stock-in-trade

The taxpayer was a dealer and trader in shares and securities and was also engaged in the business of Futures & Options (F&O) in shares and securities. During the year under consideration the taxpayer had an earned dividend on shares which was then claimed as exempt under the Act. The taxpayer made disallowance of INR 1 million under Section 14A of the Act while computing taxable business income. The AO held that since Rule 8D of the Rules was applicable and mandatory during the year under consideration, the expenditure incurred by the taxpayer in relation to the shares held as stock-in-trade would be disallowed under Section 14A(1) read with Rule 8D of the Rules.

In appeal, the Mumbai Tribunal held that:

- The purpose for which the shares were purchased and held would not impact the applicability of Section 14A. Section 14A came into play irrespective of the head of income (on account of it arising qua a trading asset) under which the income was assessable. Accordingly, Section 14A also applies to shares held as stock-in-trade;
- Though the expenditure was incurred for the purpose of the business of share trading, the said business yielded taxable and non-taxable income. It was the integral activity of the purchasing and holding of shares which generated two separate streams of income. Accordingly, some of the expenditure had to be attributed to the dividend income;
- The argument that investment in shares yielding tax-free dividend income had been made out of the taxpayer's own funds and so no interest expenditure had been incurred in relation to the dividend income, was not acceptable. No presumption of investment of own funds, on ground of its sufficiency can be drawn, on the basis of Reliance Utilities and Power Ltd [2011] 313 ITR 340 (Bom). In arriving at the disallowance under Rule 8D, the amount as per Rule 8D(2)(ii) qua shares held as stock-in-trade would be restricted to 20 percent thereof;
- Rule 8D(2)(iii) which prescribes the ratio of indirect expenditure required to support an investment did not need to be modified, because although the expenditure prescribed for disallowance was based only on one variable (the average value of investments), the prescribed allocation ratio of 0.5

percent of the investment value qua indirect expenditure was nominal and not unduly harsh;

- Depreciation, an economic and accounting concept which was statutorily recognized and provided was only a charge on capital account, i.e., a capital expenditure. It had to be excluded in computing the Section 14A disallowance.

The Tribunal chose to follow Special Bench decision in the case of ITO vs. Daga Capital Management (P) Ltd. [2009] 117 ITD 169 (Mum)(SB) over Karnataka High Court decision in the case of CCI Ltd v. JCIT [2012] 71 DTR 141 (Kar) and held that disallowance under Section 14A applied irrespective of the fact that the shares in question were held as stock in trade or investment.

DCIT v. Damani Estates & Finance Pvt. Ltd. (ITA No.3029/Mum/2012 dated 17 July 2013)

Higher rate of depreciation allowed on windmills to bank in the capacity of lessor

The taxpayer was a company engaged in business of banking. It had purchased windmills for a total price of INR 275.4 million that were put to use on 19 March 2004; depreciation was claimed on them at 80 percent, amounting to INR 110.1 million. The AO in its assessment order stated that the taxpayer, being a Banking organization, could not engage in any other business, such as generation of electricity, under the Banking Regulation Act. Further, depreciation at the higher rate was available only to those engaged in generation and distribution of electricity, which the taxpayer was not. The AO accordingly held that the transaction was a financing arrangement and hence disallowed the depreciation claim. The CIT(A) upheld this order.

The Ahmadabad Tribunal allowed the appeal, relying on the Supreme Court ruling in ICDS Ltd. v. CIT [TS-8-SC-2013] and Mumbai Tribunal ruling in Development Credit Bank Ltd v. DCIT [ITA No. 300/Ahd/2001 and 4892/Ahd/2003]. The Tribunal also relied on the ruling of the Coordinate Bench n the taxpayer’s earlier case for AY 2002-03 [ITA no. 2572/Ahd/2006] where it was held that it was not mandatory for the taxpayer to use the asset itself and that depreciation would be allowed as long as the asset was used for business purposes by the taxpayer. Further, as the leasing income from same assets was treated as business income, the requirement of Section 32 that the asset had to be used for the purposes of the business was held to be fulfilled. Accordingly, it was held that the taxpayer was eligible for the depreciation on its windmills.

ACIT v. UTI Bank Ltd. [TS-468-ITAT-2013(Ahd)]

Benevolent proviso to Section 201(1) inserted with effect from 1 July 2012 restricting a defaulting TDS deductor’s liability only to interest, applicable retrospectively. Payment of Waterfront Royalty to Gujarat Maritime Board to be subject to withholding tax under section 194J or 194I of the Act

The taxpayer was developing, constructing, operating and maintaining a port on a Build, Own, Operate, Transfer (BOOT) basis. The taxpayer had been granted the right to use a water-front in pursuance of a Concession Agreement entered with the Gujarat Maritime Board (GMB) against payment of charges to be computed on the basis of actual throughputs achieved in the month. In the books of account the taxpayer had entered the impugned payment as 'wharfage charges' for AY 2006-07 and 2007-08. During the assessment proceedings, the AO noticed that the taxpayer had been deducting tax on waterfront royalty paid to GMB under Section 194J and not Section 194I. The AO therefore treated the taxpayer in default under Section 201(1) and also levied interest under Section 201(1A).

On the issue of characterisation of payment, the Tribunal held that the payment shown by the taxpayer in its books of account as wharfage was, in substance, nothing but payment made for using the land together with a structure on the margin or shore of navigable waters alongside which vessels were brought to be conveniently loaded or unloaded. Waterfronts are part of land and therefore any payment in lieu of its use would squarely fall under the definition of rent as given in section 194I of the Act. In no case one could justify deduction of tax at source under Section 194J on the impugned payment. However, the Tribunal observed that Proviso to Section 201(1), inserted with effect from 1 July 2012, restricted the deductor's liability to interest, when the deductee had offered income subject to TDS in his return of income and paid taxes thereon. The said proviso not only sought to rationalize the provisions relating to deduction of tax at source but was also beneficial in nature in that it sought to provide relief to the deductors of tax at source from the consequences flowing from non/short deduction of tax at source. As per the new proviso, on furnishing of a certificate by the Chartered Accountant, subject to certain conditions levied, the payer would not be held as an taxpayer in default under Section 201(1) and the payer would have to pay only the interest, if any, till the date of return of income filed by payee. Relying on CIT v. Chandulal Venichand & Ors [1994] 209 ITR 7 (Guj) and Allied Motors (P.) Ltd. v. CIT [1997] 224 ITR 677 (SC), the Tribunal held that the above proviso would apply retrospectively to the case of taxpayer and set aside the matter to the file of the AO with a direction that the interest should be levied only till the date of return of income filed by deductee after due verification.

Gujarat Pipavav Port Limited vs. ADIT [TS-408-ITAT-2013(Rjt)]

AO bound to follow DRP directions

In instant case, the DRP vide its directions under Section 144C(5) directed the AO to tax the amount received by the taxpayer for services rendered under its International Transfer Agreement and Consultancy Services Agreement as 'Fees for Technical Services', holding that the taxpayer had made available technology to the Indian entity. However, the AO while passing the final assessment order continued to assess the above receipts as business income, ignoring the directions of the DRP. The taxpayer also filed rectification application before the AO, which was not disposed of, even though 3 years had lapsed from the date of the application.

On appeal to the Tribunal, the Tribunal observed that the DRP had issued directions specifically mentioning that the amount received by the taxpayer had to be taxed as a Fee for Technical Services. The directions of the DRP were binding on the AO. Section 144C(13) uses the word 'shall' with regard to instructions to be followed by the AO. From the plain reading of the provisions of the section it was clear that AO had no choice but to pass an order as per the DRP's directions. A panel consisting of three Senior Commissioners of the Income-tax Department, had been given powers to decide issues raised in the draft orders submitted by AOs. AOs, being lower in rank than the Commissioners in the departmental hierarchy, were supposed to follow the orders of the collegiums of the Commissioners. Secondly, the Panel had the benefit of the submissions of the taxpayers before it decides the issues. The application under Section 154 of the Act for rectification of the mistake was also filed by the taxpayer with the AO, vide a letter dated 23 November 2010 wherein the taxpayer brought to the notice of the AO its 'inadvertent non-compliance' with the DRP's instructions. The taxpayer contended that the AO's open defiance of the directions of the DRP, its non-disposal of the taxpayer's application filed under Section 154 of the Act and the taxpayer's request to direct the AO to follow the orders of the DRP, compelled the taxpayer to approach the Tribunal. Helplessness of the taxpayer is evident from the fact that it is ready not to press other grounds of appeal, if the AO is directed to act as per law. If even for its rightful claim an taxpayer has to approach a judicial forum, then it has to be held that AO had miserably failed in performing his duties. As a representative of the State, he is duty bound to collect only 'due' taxes and not only taxes. On two counts, behavior of the AO can be held to be perverse-first he did not obey the instructions of the panel, and second, he did not take any action with regard to the rectification application filed by the taxpayer. Accordingly, the Tribunal directed the AO to pass fresh assessment order as per the directions of the DRP within 30 days of receipt of the order.

Diamond Management & Technology Consultants Ltd. v. ADIT [ITA No. 8978/Mum/2010 and ITA No. 9049/Mum/2010]

Section 50B of the Act dealing with slump sale not applicable to transfer of undertaking for non-monetory consideration

The taxpayer transferred its manufacturing division to Novapan Industries Limited under the scheme of amalgamation. In consideration of the transfer, Novapan Industries issued shares of INR 62.8 million and transferred investments valued at INR 252.4 million to the taxpayer. The net worth of the taxpayer as on the effective date was INR 68.1 million. The taxpayer had filed a NIL return which was accepted by the AO. Under a reassessment proceeding, the AO treated the transfer as slump sale and applying Section 50B computed taxable gain to be INR 247.1 million. The CIT(A) deleted the addition.

On departments appeal the Tribunal held that as there is no monetary consideration for transfer of the manufacturing division, the transfer cannot be considered to be a slump sale within the meaning of Section 2(42C) and consequently Section 50B is not applicable.

Zinger Investment Private Limited v. ITO [ITA.No.275/ Hyd/2013]

Amount received on account of delay in open offer process is capital gain, not interest income

The taxpayer is a company incorporated in Mauritius holding shares in Castrol India Ltd. Castrol UK announced open offer for acquisition of 20 percent issued capital of Castrol India Ltd in March 2000. The open offer process was delayed on account of various regulatory issues. As a result, the taxpayer could offer its holding only in October 2001 which was accepted in November 2001 and purchase price along with interest from March 2000 to November, 2001 was received by the taxpayer. The taxpayer considered the interest payment as part of the sales consideration and claimed the resulting gain to be exempt under Article 13(4) of the India-Mauritius Treaty. The AO taxed the interest received as interest income. The CIT(A) upheld the contention of the AO.

The receipt in the instant case is not an income arising from debt claim and there is no debtor-creditor relationship as per Article 11 of the treaty. The taxpayer further contended that additional consideration was received in respect of the period prior to the tender of the shares. Therefore there was no debt created in favor of the taxpayer.

The Tribunal held that the interest was received due to delay in the process of open offer after its announcement and not due to delay in payment of consideration after acquiring the shares. Accordingly the additional amount received by the taxpayer was held to be part of consideration for computation of capital gain and not as interest income.

Genesis Indian Investment Co. Ltd. v. CIT [I.T.A. No. 2878/Mum/2006]

Pune Tribunal held that capacity under-utilisation adjustment could be claimed on the profit margin of the tested party so as to facilitate comparison with comparable uncontrolled entities

The taxpayer was engaged in the manufacture of water heaters and sold them and spare parts for them for its associated enterprise (AE). In the first year of operations, the taxpayer was able to utilise only 21 percent of its installed capacity. The taxpayer determined the arm's length price (ALP) of its international transactions using Transactional Net Margin Method (TNMM) and compared its profit margin (after excluding fixed costs related to its start up phase and un-utilised capacity) with unrelated comparables. The Transfer Pricing Officer (TPO) and the DRP denied the economic adjustments on the grounds that as per Rule 10B(1)(e)(iii) of the Rules, adjustments are permissible only on the margins of the comparables.

Tribunal held that as per Rule 10B(1)(e)(i) of the Rules, for determination of the ALP using TNMM, the net profit margin of the enterprise realised from the international transaction was to be determined. This net profit margin was to be compared to the net profit margin of the taxpayer from uncontrolled transactions or to the net profit margins of comparable uncontrolled enterprises. Hence, the net profit margin of the tested party might be adjusted to facilitate its comparison to comparable uncontrolled entities or transactions as per

Rule 10B(1)(e)(i) of the Rules itself. The Tribunal clarified that the lack of a specific provision to compute adjustments in the profit level indicator of the tested party in Rule 10B(1)(e)(iii) of the Rules did not bar a taxpayer from computing such an adjustment. The Tribunal upheld the capacity under-utilisation adjustment claimed by the taxpayer and restored the matter to the AO to verify the material submitted on the capacity utilisation of the comparables.

Ariston Thermo India Ltd. v. DCIT (2013) [TS-221-ITAT-2013(PUN)-TP]

Premium profits earned by a distributor were adequate compensation for excessive advertising, marketing and promotion

BMW India Pvt. Ltd. was engaged in the import of completely built units of BMW's motor vehicles, related spare parts and accessories from its AEs and in assembling of completely knocked down kits of certain products imported from its AEs, for further resale in the Indian market. Taxpayer characterised itself as a distributor, also performing low-value added assembly functions and selected the Resale Price Method (RPM) as the primary method and TNMM as the secondary method to establish the arm's length nature of its international transactions. TPO held that by incurring the advertising, marketing and promotion (AMP) expenditure over and above the bright line, the taxpayer provided brand promotion services to its AE and that it should have been compensated with the excessive AMP cost so incurred along with a mark-up of 15 percent. DRP upheld the same but directed exclusion of amounts pertaining to after-sales support costs and salesman bonus from the AMP calculation.

Tribunal held that since the taxpayer was not an intervener in the proceedings before the Special Bench in the case of LG Electronics India Pvt. Ltd1, it was not precluded from advancing arguments on facts and law which were either not addressed before the Special Bench or considered consequently by the Special Bench. However, the Tribunal clarified that the Special Bench ruling would apply to the taxpayer wherever facts and laws so demand. The Tribunal held that the taxpayer in this case had performed more services than a normal distributor would and that the AMP activities performed by the taxpayer had contributed to the brand building for its AE. The Tribunal, in view of the Special Bench ruling, also held that brand building for the AE was an international transaction and that bright line was an accepted method for calculating non-routine AMP expenditure. It was also held that no further compensation was required to be made by the AE as the same has been received by way of the premium profits earned by the taxpayer and facts demonstrated that the compensation for higher marketing services was embedded in the pricing arrangement for import of goods. The Tribunal took a view that in absence of any provision under the Act, the revenue could not insist for direct compensation of the excessive AMP expenditure. The taxpayer is free to adjust and apply any method which it finds most suitable to manage its affairs.

BMW India Pvt. Ltd. v. ACIT (ITA No. 5354/Del/2012)

Notifications/Circulars/ Press releases

India signs tax treaty with Latvia

The GOI signed an agreement with the Government of Latvia on 18 September 2013 for avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income (tax treaty). The tax treaty is expected to provide tax stability to residents of India and Latvia, facilitate mutual economic cooperation and stimulate the flow of investment, technology and services between India and Latvia.

Key highlights of the tax treaty are as follows:

- Business profits will be taxable in the source state if the activities of an enterprise constitute a Permanent Establishment (PE) in the source state;
- Dividends, interest, royalties and fees for technical services will be taxed both in the country of residence and in the country of source;
- Provisions for effective exchange of information including exchange of banking information between the tax authorities of India and Latvia have been incorporated; and
- Anti-abuse provisions have been incorporated to ensure that the benefits of the tax treaty are availed of by genuine residents of the two countries.

Press release dated 18 September 2013 – www.pib.nic

With assent from the President of India on 29 August 2013, the Companies Bill 2012 has become the Companies Act, 2013. The Ministry of Corporate Affairs (MCA) further notified 98 sections of the Companies Act 2013 which has become effective from 12 September 2013. The draft rules under the Companies Act 2013 have also been released in two sets on 9 September 2013 and September 20, 2013. Public comments on the same have been invited within a period of one month for its respective release date. In all, rules relating to 22 chapters have already been released for public comments.

Social Security Agreement between India and Republic of Hungary comes into effect

India signed a Social Security Agreement (SSA) with the Republic of Hungary on 02 February 2010. The Indian authorities have now issued a circular notifying that the SSA with Republic of Hungary will be effective from 01 April 2013.

The SSA between India and Republic of Hungary envisages the following benefits:

- Exemption from Social Security Contribution in the host country (Detachment);
- Totalization of contributory periods;
- Export of Benefits.

The circular also clarifies that an employee may apply for the COC through his employer in the prescribed format and submit it to the jurisdictional Regional Provident Fund commissioner (RPFC). After verification of details, the COC will issued by the RPFC.

The signing of the India-Republic of Hungary SSA is a welcome step: it will result in cost savings and social protection of international assignees in respect of deputation arrangement for employees, which in turn will lead to an increase in economic activity between the two countries.

Employees' Provident Fund Organisation directs its field offices to expedite exemption applications of private PF Trusts

The Indian Government has permitted employers to establish and manage their own private PF Trusts, subject to conditions prescribed under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (EPF Act).

Private PF trusts became attractive because they promised faster settlements of employee claims as well as greater transparency regarding PF accumulations. However, it was important that such private PF Trusts were recognized under the Act for employees to get tax benefits.

As approvals are required under both the Act and the EPF Act to run a recognized provident fund trust, companies that do not have approvals under the EPF Act are required by the Finance Act, 2013 to obtain the approval by 31 March 2014. This timeline has been extended several times in the past.

In the above context, Employees' Provident Fund Organisation (EPFO) has now directed its officers to expedite the disposal of pending applications asking them to send the pending application to the Head Office (New Delhi) by 15 November, 2013 after ensuring that the application is proper.

With the deadline of 31 March 2014 close, those companies who fail to obtain exemption under the EPF Act may lose their recognition under the Income Tax Act. This could have an adverse tax impact for their employees.
Since the PF office is providing an impetus to the approval process for private PF trusts, companies running such trusts may utilize this opportunity to get timely approval for their PF trusts.

II. SERVICE TAX

Tribunal Decisions

Collection of toll by a concessionaire who has constructed the road on a 'Build-Operate-Transfer' basis does not give rise to a service tax liability on the concessionaire under 'business auxiliary services'

The taxpayer Ideal Road Builders Pvt Ltd Mumbai, were engaged in the business of construction of highway by virtue of a contract awarded by the Public Works Department of the Government of Maharashtra. They were authorized to collect tolls from the users of the road as a compensatory measure for the work undertaken. The Revenue Authorities contended that the taxpayer was required to discharge service tax liability on the aforesaid activity under the category of "Business Auxiliary Service". The matter reached before the CESTAT.

CESTAT held that since the taxpayer carried out the entire activity on a Build-Operate-Transfer' basis, the collection of toll was not being done on behalf of the Government of Maharashtra and no services were being rendered by the taxpayer in this regard. The taxpayer was authorized to collect the toll charges from the users of the roads on the basis of the concession agreement between the Public Works Department of the Government of Maharashtra and the taxpayer for construction of roads. In this regard, reliance was placed upon Circular No 152/3/2012 ST, dated February 22, 2012.

Ideal Road Builders Pvt Ltd v Commissioner of Service Tax, Mumbai [2013 (31) STR 350 (CESTAT-Mumbai)]

Online learning/e-learning or CD ROMs containing live virtual class does not fall under Commercial Training or Coaching Services ("CTCS"), hence not leviable to service tax

The taxpayer was selling CD-ROMs containing "live virtual classes" on certain subjects to various purchasers. The Revenue Authorities demanded service tax under the category CTCS on the value of such CD ROMs since the same were provided to enhance the skill or impart knowledge of the purchasers.

CESTAT held that unlike in a regular coaching, in this case no agreement or institute existed and nor was there any contact whatsoever between the students and the teacher. The activities could not be leviable to service tax under the said category.

Sun Microsystems India Pvt Ltd v Commissioner (LTU), Bangalore [2013 (31) STR 505 (CESTAT-Bang)]

Permanent transfer of intellectual property right does not amount to rendering of service and hence not liable to service tax

Taxpayer entered into an out of court settlement with Purolite International Ltd USA ("Purolite") to settle all disputes except certain pending litigations. As per the agreement, Purolite agreed to irrevocably transfer to taxpayer all claims, rights and interests necessary to use Purolite's technology and information in perpetuity without any geographical or customer restrictions. Consequently, the taxpayer became co -owner in the Purolite technology and entitled to assign, sell, license, transfer or convey interests for a specified consideration. This transfer was sought be levied with service tax by the Revenue Authorities. The matter reached before the CESTAT.

CESTAT held the above transfer not to be a taxable service under "intellectual property rights service" as defined in the Finance Act, 1994 ("Finance Act"). In order to constitute intellectual property under section 65 of the Finance Act, it should either be a trade mark, design, patent or any other similar intangible property under any law in force in India. As per the decision of the US District Court of Pennslyvania, the aforesaid information obtained in contravention of the US law related to trade secrets / confidential information. There being no law in India in relation to the same, the confidential information received by taxpayer was not intellectual property.

Also as per the settlement agreement, the taxpayer became a co-owner of the intellectual property. It was not a temporary transfer or a permission to use or enjoy the intellectual property right. A permanent transfer of intellectual property right does not amount to rendering of service.

Thermax Ltd v CCE, Pune-I [2013-TIOL-1092-CESTAT-MUM]

Exclusion in respect of railways from the purview of "commercial or industrial construction service" would cover construction of Metro Stations

The taxpayer undertook civil construction of viaduct and stations of Delhi Metro Railway Project for Delhi Metro Corporation ("DMRC") under turn-key contracts. No service tax liability was discharged on the same. This was disputed by the Revenue Authorities and the matter reached before the CESTAT.

CESTAT held that the definition of "commercial and industrial construction service" as provided in section 65(25b) excludes activities relating to railways. There being no statutory distinction envisaged between a mono rail or metro rail or any other kind of rail, the term railways had to be given the widest possible meaning to include all types of railway lines. Taxpayer was hence not liable to pay service tax under the category "commercial or industrial construction service" on its activities.

Afcons Infrastructure Ltd V CCE Mumbai-II [2013-TIOL-1125-CESTAT-MUM]

III. VAT/ CST/Other State Level Taxes

High Court Decisions

Purchase of materials for expansion of business did not constitute an

activity in the course of business, hence not liable to entry tax

The taxpayer filed a writ petition challenging the liability towards entry tax. They purchased plant and machinery for the purpose of expansion of their unit, without paying the entry tax under the Madhya Pradesh Entry Tax Act, 1976 on the ground that entry tax liability was triggered only upon entry of goods in the course of business.

The HC held that the taxpayer was not liable to entry tax because purchase of materials for expansion of business could not be said to be an activity 'in the course of business'.

Surya Roshni Ltd v State of MP [2013] 60 VST 250 (MP)

Processing of fresh milk into Pasteurized milk being a manufacturing process, polythene films used in packing are taxable at a concessional rate of tax under the Tamil Nadu General Sales Tax Act, 1959 ("TNGST")

The taxpayer, a co-operative milk producers' federation, purchased polythene films for use in packing milk and milk products. Concession was claimed on tax rate under section 3(3) of the TNGST on the purchases on the ground that they were packing materials being used vis-à-vis manufacture. This was opposed by the sales Revenue Authorities and the matter reached before the HC.

The HC held that when fresh milk, is converted to recombined or pasteurized milk, there is 'manufacture' and the taxpayer was entitled to the benefit for purchase of polythene sheets to be used as packing material for the sale of pasteurized milk

Tamil Nadu Co-Operative Milk Producers' Federation Ltd v State of Tamil Nadu [(2013) 62 VST (190) (Mad)]

Civil work for building including sanitary and electrical fittings was a composite and indivisible contract even if two different agreements signed, consequently value of both to be included for the purpose of composite scheme

The taxpayer signed two contracts for civil work and sanitary and electricity work for the Lucknow Development Authority ("LDA"). The taxpayer tried to avail the composition scheme for sales tax purposes but only vis a vis one contract which was opposed by the sales Revenue Authorities. The matter reached before the HC.

The HC held that the taxpayer had taken the contracts for the civil work as well as electricity and sanitary, wherein a separate amount was fixed by the LDA. A building contract could also be an indivisible contract. The two contracts taken together was a composite and indivisible one, the intention between the parties being not to supply the materials in the course of the contract, but as and when such material was embedded in the contractual work involved, it became the property of the customer. There being absence of sale or transfer of property as movable property, the taxpayer constructed the entire works according to the specification contained in the agreement and therein received payment. Thus, both the contracts need to be factored for the purposes of availing composition scheme under UP Trade Tax Act, 1948.

Shakun Udyog v Commissioner, Trade Tax, Lucknow [(2013) 062 VST (0269)]

Tribunal Decisions

Hearing aid enhances the quality of hearing of a person suffering from auditory handicap, hence to be treated as an aid/implement used by handicapped persons making it an exempted item under West Bengal VAT Act, 2003 ("WBVAT Act")

The taxpayer was engaged in reselling various items like electrical goods, sports and medical goods, household utilities, hearing aids, furniture etc and claimed VAT exemption for hearing aids on the ground that they are aids for handicapped persons. The Revenue Authorities held that "hearing aid" did not merit this exemption from payment of tax. The matter reached before the West Bengal Taxation Tribunal ("WBTT").

The WBTT relying on Wildex India Pvt Ltd v STO, Central Section, Kolkatta-15 wherein a similar matter came up for consideration, held that the words "handicapped persons" as appearing in the entry at Serial No 2 of the Schedule A to the WBVAT Act should not be confined only to physically disabled persons. The word handicap means hindrance in common parlance and has a very wide connotation, encompassing all types of impairments and disabilities which generally puts an individual to a disadvantage in fulfillment of a role that is normal for that individual. Since hearing aid enhances the quality of hearing of a person suffering from auditory handicap, it should be treated as an aid/implement used by handicapped persons and hence is an exempted item.

C C Saha Ltd and another v Sales Tax Officer, New Market Charge and Others [(2013) 63 VST (99) (WBTT)]

IV. CUSTOMS

High Court Decisions

Refund and interest on belated refund can be availed even in the absence of specific provision in the Customs Act, 1962("Customs Act")

The taxpayer filed refund application under section 27 of the Customs Act in terms of Notification No 102/2007-Cus dated September 14, 2007 which resulted in a delayed payment of the refund amount and a consequent claim of interest. The claim of interest on delayed refund was opposed by the Revenue Authorities on the basis of Circular No 6/2008-Cus dated April 28, 2008 ("Circular"). The taxpayer approached the Madras HC vide a writ petition in this regard.

The HC held that the Circular was inconsistent with the provisions of the Customs Act, and the Customs Tariff Act, 1975 ("Customs Tariff Act"). Section 3(5) of the Customs Tariff Act provides for levy of additional duty to counterbalance sales tax, value added tax, local taxes or any other charges. The taxpayer had satisfied the terms and conditions on which exemption from payment of additional duty was granted. Hence provisions of the Customs Act relating to refund became applicable, including refund of additional duty.

The HC further held that the grant of exemption under section 25(1) of the Customs Act was an independent exercise; however, the conditions to be fulfilled for refund and the procedure for the same is found in section 27 of the Customs Act as made applicable under section 3(8) of the Customs Act. A combined reading of these provisions clearly shows that refund application should be filed and entertained only under section 27 of the Customs Act. The HC concluded that the Circular cannot override the provisions of section 27 and 27A nor can deny the taxpayer the right granted by the provisions of the Customs Act and Customs Tariff Act. Accordingly, interest was granted.

KSJ Metal Impex Pvt Ltd v Under Secretary (Cus), MF (DR) [2013 (294) ELT 211 (Mad)]

Tribunal Decisions

Taxpayer qualifies as an 'importer' even if agreements for high sea sale were entered and benefit under Notification No1/2011, Cus, dated January 6, 2011 cannot be denied on account of high sea sale

Taxpayer availed benefit under Notification No 1/2011-Cus, dated January 6, 2011. The Revenue Authorities disputed the eligibility inter alia on the ground that taxpayer would not qualify as the 'importer' for the purposes of this notification.

The matter reached before CESTAT and it was held that the taxpayer would clearly qualify as importer under section 2(26) of the Customs Act inter alia by relying upon the fact that the taxpayer was filing the bills of entry and issuing the relevant purchase orders. The CESTAT also noted that the taxpayer's application for essentiality certificate (necessary for the benefit of the notification) was entertained by the Ministry of New and Renewable Energy and appropriate certificate was issued to the taxpayer.

APCA Power Pvt Ltd v CC, Kandla [2013 (293) ELT 402 (CESTAT-Ahmd)]

Compliance to condition of declaration on invoices is mandatory for claiming refund of additional customs duty ("SAD") under Notification No 102/2007-Cus and taxpayer is not immune from such requirement. In the absence of the declaration, refund not available

The taxpayer sought to avail the benefit of refund of SAD vide Notification No 102/2007-Cus, dated September 14, 2007. This was objected to by the Revenue Authorities on the ground of non-compliance with the requirement of declaration in the invoices under para 2(b) of the Notification.

The matter reached before the CESTAT, which held against the taxpayer. The CESTAT noted that there existed nothing in the notification to discriminate between a manufacturer and a trader and an importer of goods claiming refund has to mandatorily insert the relevant declaration on the invoice. The CESTAT concluded that benefit under a notification cannot be said to be directory (as opposed to mandatory), if the benefit is granted subject to conditions, stipulations and limitations to safeguard interest of public revenue. Failure to make such a declaration cannot be said to be a technical lapse when non-compliance with such declaration disentitles the benefit. When the law is clear that invoices issued should carry the declaration as a mandatory condition, there is no discretion permitted by law

Astra Zeneca Pharma India Ltd v CC, New Delhi [2013 (294) ELT 574 (CESTAT-Del)]

V. CENTRAL EXCISE

High Court Decisions

Taxpayer entitled to claim Cenvat credit attributable to inputs contained in taxable waste/ byproducts during manufacture of exempted goods

The taxpayer was manufacturer of intravenous fluids wherein plastic scrap was generated as waste. Exemption was availed on clearance of waste and scrap under Notification No 89/95-CE dated May 18, 1995. The availment of this exemption was opposed by the Revenue Authorities, as having been wrongly availed on the ground that waste was not final product and that it was not applicable to units where excisable goods other than the exempted goods were additionally manufactured. The matter finally reached before the HC.

The HC held that the waste and scrap was final product and an excisable item. The plastic scrap generated in the manufacturing process has been treated as final product on which Excise Duty had been paid under the Central Excise Tariff Heading 39.15. Also in view of clarificatory circular issued by the Central Board of Excise and Customs ("CBEC") dated August 29, 2000, waste and scrap fall under definition of final products under Rule 57AA(C) and was thus entitled to credit

Albert David Ltd v CCE [2013 TIOL-621- HC-ALL-CX (Allahabad HC)]

Tribunal Decisions

Addition of electrolytes and charging batteries of two wheelers before delivery to customers does not amount to manufacture of two wheelers

The taxpayers were dealers in motorcycles and scooters receiving duty paid two wheelers from the manufacturers and selling the same in the market. These two wheelers had dry batteries and the taxpayer being dealers, add electrolytes and charge the same. The Revenue Authorities alleged that the taxpayer's addition of electrolyte etc amounts to 'manufacture' and would be liable to excise duty. The matter reached before CESTAT.

CESTAT held that the taxpayers were receiving duty paid two wheelers in complete and finished condition from the manufacturers. The addition of electrolytes in the dry batteries was not incidental to the completion of the two wheelers and did not amount to manufacture as per the provisions of section 2 (f) of the Central Excise Act, 1944. The manufacturers paid duty on complete two wheelers that contained a battery. The taxpayers were only adding the electrolyte, which is nothing but a liquid which contains ions and can be decomposed by electrolysis. The batteries are then charged before delivery to the customer. This process undertaken could not be said to be conversion of incomplete or unfinished article i.e. two wheelers into complete or finished two wheelers

Sudarshan Motors V CCE, Nagpur [2013-TIOL-1193-CESTAT-MUM]

Benefit cannot be denied merely because the formal application for availing benefit under Notification No 50/2003-CE was filed subsequent to clearance of goods

The taxpayer set up a new unit for manufacture of hair oil, shampoo and face cream in Haridwar. They sought registration under Rule 9 of the Central Excise Rules, 2002 ("Central Excise Rules") before the Deputy Commissioner of Central Excise. The registration was granted on submission of the requisite documents. Additionally, the taxpayer obtained a drug license and commenced commercial production. Meanwhile, the taxpayer started clearance of their final product by claiming benefit of Notification No 50/2003-CE. The Revenue Authorities disputed the exemption on the ground that the formal letter notifying that the taxpayer would be availing this benefit was filed later. The matter reached before the CESTAT.

CESTAT, relying on certain judicial precedents like Bombay Processors v CCE, Mumbai [2005 (184) ELT 371 (Tri-Mumbai)], held that the taxpayer was required to apply for the availment of the notification giving details. These had already been furnished by them in their first letter. Subsequently they filed a formal application to avail benefit along with requisite documents. Merely because the formal letter was filed subsequently, the same cannot be ground for denial of the benefit prior to the date. Also while issuing invoices they were claiming the benefit of the aforesaid notification, there was enough intimation to the Revenue Authorities about availment of the said benefit.

Herbal Concepts Healthcare Pvt Ltd v CCE, Meerut-I [2013 (294) ELT 570 (CESTAT-Del)]

Certificates, recommendations and acceptance by the local authorities are sufficient evidence of substantial expansion to avail benefit of exemption under Notification No 50/2003-CE dated June 10, 2003

The taxpayer, manufacturers of canned software, was also engaged in the service of digitization of maps. The main equipment required for these activities was computers and its peripherals. They claimed the area based exemption under Notification No 50/2003-CE dated June 10, 2003, the exemption available only if the manufacturers set up a new unit or undertook substantial expansion by increasing installed capacity existing prior to exemption claim by more than 25 percent.

The Revenue Authorities were of the opinion that the taxpayer had not invested in the requisite 4 CD writers required for the expansion. The taxpayer submitted details of investments and relied on the certificates issued by the District Industries Centre of the State Government ("DICSG") stating that they had undertaken substantial expansion of their capacity for manufacture of canned software.

CESTAT held that the certificates issued by the DICSG and the recommendation given by the Range Superintendent, accepted by the Revenue Authorities at the relevant time had to be given more weightage than statements recorded by an investigation agency four-five years later from a few employees. Having accepted the claim at the relevant time, raising an objection over a minuscule investment after five years was unjustified

NIIT GIS Ltd v CCE, Chandigarh [2013 (294) ELT 447 (CESTAT-Del)]

Blending of duty paid unleaded motor spirit and High Speed Diesel ("HSD") with multifunctional additive will not amount to manufacture as there is no change in characteristics use of the resultant product

The dispute in question was whether conversion of motor spirit into motor spirit power and of HSD into HSD turbojet by mixing small quantities of multifunctional additives would amount to manufacture.

CESTAT, relying on one of its earlier decisions, held that blending of duty paid unleaded motor spirit and HSD with multifunctional additive did not amount to manufacture as there was no change in the characteristics / use of the resultant product

Piyush Awasthi v CCE, Delhi-I [2013 (294) ELT 249 (CESTAT-Del)]

Notification & Circulars

New circular clarifying several ambiguities in VCES scheme

This detailed new circular clarifies several ambiguous aspects about availing the service tax amnesty scheme under VCES

Circular No 170/5 /2013 - ST dated August 8, 2013

Clarificatory circular on customs duty exemption for import of ash handling systems, water treatment plant and coal transportation facilities etc required for Ultra-

Mega/Mega Power Projects under Heading 9801 (Project Imports)

It has been clarified that the customs duty exemptions available to the core power plant assets for specified power projects would also be available for import of the aforementioned ancillary assets to such power projects. The issue was clear in the corresponding excise exemption notification

Circular No 33/2013-Cus dated August 23, 2013