September 2014

TAX UPDATES

(containing recent case laws, notifications, circulars)

Prepared in association with

KPMG cutting through complexity

BMR & Associates

Foreword

I am pleased to enclose the September, 2014 issue of FICCI's Tax Updates. This contains recent case laws, circulars and notifications pertaining to direct and indirect taxes.

Chairman, FICCI's Taxation Committee along with the FICCI Secretariat officials met Mr Shaktikanta Das, Secretary, Department of Revenue, on 12th August, 2014, to discuss certain urgent tax matters arising out of some circulars issued by the Central Board of Direct Taxes as also from the budget changes. The issues discussed *inter alia* included Circular No. 12/2014 dated July 18, 2014 regarding transfer or redeployment of technical manpower from an existing unit to a new SEZ unit, taxability of buybacks undertaken before the coming into force of Chapter XII-DA, taxation of indirect transfer of assets considered by the Shome Committee, pass through status for all Alternate Investment Funds (AIFs) etc.

FICCI had also organised an interactive session with the Hon'ble Finance Minister on 19th August, 2019. The FM shared his views on the economy, GST and other fiscal matters with the invited members.

On the taxation regime, the Delhi High Court, in the case of Siel Ltd., held that share sale transaction between joint venture (JV) partners resulting in loss is not a 'colourable device' as the said transaction had commercial or business reasons. The High Court observed that the Ministry of Industry had granted approval for purchase/sale of shares. Further, RBI had given no objection to the transaction permitting JV partners to acquire shares in the JV from the taxpayer. The reliance of the taxpayer on the valuation report was also accepted by the RBI when they granted express permission.

In a Service Tax matter, the Tribunal has decided that reinsurance service is an "Input Service" for insurance companies. The taxpayer who had availed reinsurance services from overseas companies was decreed to be eligible to avail CENVAT credit of service tax paid on the services received. The Tribunal observed that under section 101A of the Insurance Act, 1938, every insurer was obliged to insure with Indian Reinsurers, a prescribed percentage of sum assured on each policy. Since Reinsurance is a statutory obligation and co-terminus with the insurance policy, the Tribunal rejected the stand of the Revenue Authorities that reinsurance must have nexus with output service namely provision of insurance to customer

FICCI has invited suggestions and recommendations on tax matters from its constituents for inclusion in the FICCI's Pre-Budget Memorandum for the year 2015-16. All the members are requested to provide their feedback by 19th September, 2014.

A. Didar Singh

Recent Case laws

I. DIRECT TAX

High Court Decisions

Gains arising in the hands of Mauritian company from sale of equity shares and CCDs of an Indian company are not taxable as interest income in India

The taxpayer is a company incorporated in Mauritius and a tax resident of Mauritius. The taxpayer along with Vatika Limited (Vatika), an Indian company, invested in SH Techpark Developers Ltd (JV Company') to undertake development of a real estate project in India.

The taxpayer entered into a Securities Subscription Agreement (SSA) and a Shareholder's Agreement (SHA) with Vatika and the JV Company. The SHA recorded the terms of the relationship between the taxpayer, Vatika, and the JV Company, their inter se rights and obligations, including matters relating to transfer of equity shares and the management and operation of the JV Company.

As per the SSA, the taxpayer agreed to acquire 35 per cent ownership interest in the JV Company by making a total investment of INR1 billion in five tranches. The taxpayer agreed to subscribe to 46,307 equity shares having a par value of INR 10 each, and 882,585,590 zero per cent CCD having a par value of INR1 each, in a planned and phased manner. The SHA also provided for a call option given to Vatika by the taxpayer to acquire all the aforementioned securities during the call period and likewise, a put option was given by Vatika to the taxpayer to sell to Vatika all the aforementioned securities during the determined period.

Vatika partly exercised the call option and purchased 22,924 equity shares and 436,924,490 CCDs from the taxpayer for a total consideration of INR800 million. Subsequently, the taxpayer transferred further equity shares and CCDs to Vatika.

The taxpayer filed an application with the Authority for Advance Ruling (AAR), wherein the AAR concluded that the entire transaction which is embodied in the SSA, SHA, and other documents is a sham and the real transaction was only of the taxpayer granting a loan to Vatika. Based on Article 10 of the SHA, the AAR concluded that these agreements indicated that the taxpayer would receive a fixed rate of return. Accordingly, the AAR held that the entire gains on the sale of equity shares and CCDs held by the taxpayer re interest within the meaning of Section 2(28A) of the Act and Article 11 of the India-Mauritius tax treaty, and are taxable in India.

The taxpayer filed a Writ Petition before the Delhi High Court. The High Court observed that there was sufficient commercial reason for the taxpayer to have routed its investment from Mauritius into the real estate project in India through equity shares and CCDs. Thus, neither the legal nature of CCD's could be ignored nor the corporate veil between the Indian investee company and the Indian JV company be lifted.

Therefore, the High Court held that the gains from sale of equity shares and CCD's are not taxable as interest under the Act and the India-Mauritius tax treaty.

Zaheer Mauritius v DIT International Taxation II [WP (C) 1648/2013 &CM No 3105/2013] (Delhi)

Share sale transaction between JV partners resulting in loss is not a 'colourable device'

The taxpayer had entered into a JV agreement, followed by a first amendatory agreement with Plansee Tizit Aktiengesellschaft (Plansee), an Austrian company. The agreement was entered for setting up and forming the company Siel Tizit Ltd. for carrying on business of manufacture, sale, distribution, export, and other dealings in hard metals.

The two JV partners equally acquired the paid-up equity capital of 15 million equity shares of INR10 each. During the year under consideration, the JV declared rights issue of 6 million equity shares whereby, the taxpayer renounced its entitlement to subscribe 3 million equity shares of INR10 in the rights issue in favour of Plansee. Thereafter, Plansee's shareholding increased to 58.3 per cent, while the taxpayer's share holding decreased to 41.7 per cent.

Subsequently, the taxpayer and Plansee entered into an agreement, whereby Seil Tezit Ltd. proposed to offer 10 million fresh equity shares for cash at par on rights basis, but the taxpayer due to financial difficulties, was unable to subscribe the shares. Therefore, the taxpayer decided to renounce the rights in favour of Plansee.

Further, Plansee on request agreed to buy the taxpayer's 12.7 million shareholding for a consideration of USD 600,000, which on conversion, came to INR2.02 per share of face value of INR10 each. This resulted in book loss of INR101.2 million or indexed loss of INR136.2 million on capital account.

The AO did not accept the said capital loss challenging that the aforesaid transaction was a colourable device.

The Delhi High Court held that share sale transaction between JV partners resulting in loss is not a 'colourable device' as the said transaction had commercial or business reasons. The High Court observed that the Ministry of Industry had granted approval for purchase/sale of shares. Further, the RBI had given no objection to the transaction permitting JV partners to acquire shares in the JV from the taxpayer. The reliance of the taxpayer on the valuation report was also accepted by the RBI when they granted express permission.

CIT v. Siel Ltd (ITA No. 1616/2010 and ITA No. 1619/2010)

Commission paid to non-resident agent is not FTS

The taxpayer is a company engaged in manufacture and export of leather articles. For AY 2009-10, the taxpayer entered into an agency agreement with a non-resident agent to secure orders from various customers, retailers and traders, for export of leather shoes. As per the agreement the agent was eligible for a commission of 2.5 per cent on Free On Board (FOB) value which was claimed as allowable under Section 37 of the Act. The AO disallowed the taxpayers claim by invoking section 40(a)(i) and held that commission payment to the non-resident agent was in the nature of FTS and was taxable under Section 9(i)(vii).

The Madras High Court held that the commission paid to the agent was to secure orders for export of leather shoes and was therefore not in the nature of FTS. The non-resident agent did not provide any technical services to the taxpayer. The High Court relied on the Supreme Court ruling in the case of Toshuku Limited and GE India Technology.

The Commissioner of Income Tax v Faizan Shoes Pvt Limited (TCA 789 of 2013)

Depreciation not implicit under Rule 10; Actual allowance relevant for determining post amalgamation WDV

The taxpayer is an Indian Company and a subsidiary of U.K. Company, May and Baker Ltd. The U.K. Company was assessed to tax in India in respect of its profits in relation to its branch in India. The profits of the Indian Branch of the U.K. Company were determined as per the then existing Rule 33 of Income-tax Rules, 1962 (the Rules) and thereafter under Rule 10 of the Rules. The U.K. Company had an industrial undertaking in India which was hived off to taxpayer under a scheme of amalgamation (approved by Bombay High Court) in 1975. Accordingly, assets and liabilities of industrial undertaking were taken over by taxpayer under an amalgamation scheme. Schedule 'A' of the Scheme had set out value of fixed assets (at cost less depreciation) at INR 17.2 million and original cost of assets was INR25.4 million. For three AYs 1976-77, 1977-78 & 1978-79, taxpayer claimed that for granting depreciation, cost of assets should be taken at original cost, i.e., INR25.4 million or alternatively at INR17.2 million (cost less depreciation). Rejecting both these figures, AO granted depreciation on written down value (WDV) computed under Rule 10(ii) of the Rules. The AO arrived at the WDV of INR9.31 million after taking into account depreciation that would have been granted to the U.K. Company under the Act. Rule 10 stipulates as to how income accruing/arising to any non-resident person through or from any business connection / property in India should be computed when it cannot be definitely ascertained. In light of this Rule, profits and gains should be computed under the Act.

The Bombay High Court observed as per definition of 'actual cost' in Section 43(1) of the Act if no depreciation was actually allowed to the Amalgamating Company, then the original cost of the capital asset transferred pursuant to the amalgamation, would be taken into account for the purposes of allowing depreciation to the Amalgamated Company. The High Court thereafter examined whether any depreciation was actually allowed on fixed assets of Indian Branch of U.K. Company, when they were being assessed to tax in India. The High Court noted that, in extant case, U.K. Company was being assessed to income tax in India right from the AY 1960-61 in respect of profits of its branch in India which were calculated under Rule 33/ Rule 10 and there was nothing on record to show that while computing profits under the said rules, any depreciation was actually allowed to the U.K. Company. Setting aside the Tribunal's order the High Court held that there is no concept of depreciation being allowed on a notional basis or that the same can be granted implicitly. The High Court relied on the decision of Supreme Court in Madeva Upendra Sinai v. UOI [1975] 98 ITR 209 (SC). Accordingly, the High Court has taken WDV as per books of account at the time of transfer i.e. INR17.2 million (cost less depreciation) to grant the depreciation.

Rhone-Poulenc (India) Ltd. v. CIT [TS-504-HC-2014(BOM)]

Notice under 148 can be challenged by way of a writ petition

The taxpayer was engaged in the business of trading of shares. Noting that the taxpayer had offered short term capital gains taxable at concessional rate under Section 111A, notice for reopening under Section 148 of the Act was issued to the taxpayer in respect of AY 2007-08. The taxpayer filed its objection to said notice, which was rejected by tax officer. Aggrieved, the taxpayer filed a writ petition before the Bombay High Court against the initiation of reassessment proceedings.

The tax authorities inter-alia submitted that the Court should not exercise its jurisdiction under Article 226 of the Constitution of India in view of the Madras High Court ruling in case of Kalanithi Maran [TS-413-HC-2014(MAD)]. The Madras High Court had relying on the Supreme Court decision in the case of Chhabil Dass Agarwal [2014] 1 SCC 603 (SC) had held that a notice under Section 148 cannot be challenged under a writ petition. The tax authorities submitted that in view of the said ruling wherein Madras High Court did not exercise jurisdiction, the Bombay High Court should also do the same in taxpayer's case.

The Bombay High Court noted that Madras High Court proceeded on the basis that the dispute urged before it were with regard to adjudicatory facts and not with regard to jurisdictional facts as raised in taxpayer's case. The Madras High Court had also held that "when an assessment sought to be reopened by an Officer who is not competent to do so or where on the face of it would appear that the reopening is barred by limitation or lacks inherent jurisdiction, the court would certainly entertain a challenge to the reopening notice in its writ jurisdiction". The Bombay High Court noted that jurisdictional facts were those facts which give jurisdiction to enter upon enquiry, while adjudicatory facts come up for consideration after validly entering upon enquiry i.e. having jurisdiction. The Bombay High Court observed that in the taxpayer's case, the challenge was based on lack of jurisdiction in issuing the notice for reopening by tax officer on the ground that the precondition for issuing notice under Section 147 of the Act was not satisfied i.e. notice should not be on account of the change of opinion. Bombay High Court held that AO can acquire the authority to deal with the matter on adjudicatory facts only when the jurisdictional facts were satisfied. There could be occasions where jurisdictional facts could itself be a matter of factual enquiry i.e. leading of evidence and appreciation of facts. After discussing the facts of the case at hand the High Court came to a conclusion that there was no reason for the tax officer to have reasonable cause to believe that the income chargeable to tax had escaped assessment. Thus the Bombay High Court set aside the notice issued by tax officer for reopening under Section 148 of the Act and the writ petition was allowed.

Aroni Commercials Ltd v. ACIT & anrs. [TS-486-HC-2014(BOM)]

Absent new tangible material, reassessment exercise amounts to re-appreciation or review of facts provided with original return, hence not valid

The taxpayer had filed a return of income for AY 2006-07 and was scrutinized by the tax officer. The tax officer framed the assessment accepting explanations by the taxpayer. Later the tax officer issued a notice under Section 148 of the Act, dated 25 March 2013. The taxpayer in reply stated that he stays by his original returns and also requested reasons for reopening. The reasons for reopening stated that the taxpayer had failed to furnish details of amount added to his capital account during the AY under consideration and due to absence of information, the same needed to be brought to tax under Section 68 of the Act. Taxpayer objected to the reasons for reopening however the objections were rejected by the tax officer. Aggrieved, the taxpayer filed a writ petition against notice under Section 148 before the Delhi High Court.

The taxpayer contended that he could not be said to be faulted for the omission to discuss the materials on record. Also in absence of tangible material on record the tax officer had acted without any jurisdiction and was merely seeking to revisit the matter which in effect amounted to review or change of opinion.

The High Court noted the provisions of Section 147 of the Act and held that the tax officer is allowed to reopen the assessment and to issue notices if he had reasons to believe that any income chargeable to tax had escaped assessment for any Assessment Year. The High Court observed that in taxpayer's case no details as to what excited the tax officer's notice and attention was specifically mentioned. Also there was no mention of tangible material facts that lead to reasons to believe that income had escaped assessment. The entire exercise of reopening of assessment was not based on new tangible material on record and the same was re-appreciation or review of the facts that were provided along with the original return filed by the taxpayer. The concept of 'change of opinion' is an in-built test to check abuse of power by the tax officer. Hence, after 1st April, 1989, the tax officer has power to re-open, provided there is "tangible material" to come to the conclusion that there is escapement of income from assessment. Reasons must have a live link with the formation of the belief. Even in case of an assessment completed under Section 143 (1), the requirement of recording "reasons to believe" were mandatory as indicated by the text of Sec 147 of the Act. The High Court noted the division bench ruling in Orient Craft [2013] 354 ITR 536 (Delhi) wherein it was held that "Section 147 makes no distinction between an order passed under section 143(3) and the intimation issued under section 143(1). Therefore it is not permissible to adopt different standards while interpreting the words 'reason to believe' vis-à-vis Section 143(1) and Section 143(3) of the Act.

In light of discussion of above jurisprudence, the High Court concluded that the foundation of the tax officer's jurisdiction of a reassessment notice is the 'reasons to believe'. This should have a relation or a link with an objective fact, in the form of information or facts external to the materials on the record. Such external facts or material constitute the driver, or the key which enables the authority to legitimately re-open the completed assessment. In absence of this objective 'trigger', the AO does not possess jurisdiction to reopen the assessment. Thus, allowing taxpayer's writ petition the High Court quashed the reassessment notice.

Madhukar Khosla v. ACIT [TS-511-HC-2014(DEL)]

Formation of an Undertaking - Deduction under Section 80-IB

A proprietor was carrying on business of manufacturing of electronic goods from an undertaking in Jammu & Kashmir since 2002. The undertaking was entitled to deduction under Section 80-IB of the Act. On 1 April 2004, two partners were added and the business was carried on by the partnership (taxpayer). The AO held that the undertaking under proprietorship was converted into partnership and the partnership used the old machineries, which earlier were used by the proprietorship, and therefore was not entitled to deduction under Section 80-IB of the Act.

The Allahabad High Court held that the formation of the undertaking should not be confused with the ownership of the business. In the instant case, the undertaking was already in existence since 2002 and was not formed by splitting up or by reconstruction of the business. Consequently, the High Court held that the assessee is entitled to claim deduction under Section 80-IB of the Act.

CIT v. Prisma Electronics [Income Tax Appeal No.283 of 2010 – All HC]

If the undertaking satisfies all the specified conditions of Section 80-IB of the Act in the initial year, the undertaking is entitled to the benefit of 10 consecutive years

The taxpayer, a small scale Industrial company (SSI) was manufacturing CNC plates, was entitled to and was claiming deduction under Section 80-IB(3) of the Act for past 8 years. In the current year, in view of value of its plant & machinery exceeding INR10 million, the taxpayer lost its SSI status. Consequently, its claim under Section 80-IB(3) of the Act was denied.

The Karnataka High Court held that in the entire provision under Section 80-IB of the Act, there is no indication that these conditions had to be fulfilled by the taxpayer in all the 10 years. If the undertaking satisfies all the specified conditions in the initial year, the undertaking is entitled to the benefit of 10 consecutive years. Accordingly, the High court allowed taxpayer's claim under Section 80-IB(3) of the Act.

Ace Multiaxes systems Ltd. v. DCIT (I.T.A. NO. 477 OF 2013) (Kar)

Tribunal Decisions

Use of software and computer system to access portal for finding relevant information and matching their request amounts to Royalty

Reuters Transaction Services Limited (Reuters UK) is incorporated under the laws of UK and is a tax resident of UK. Reuters UK is engaged in the business of providing electronic deal matching systems enabling authorized dealers in foreign exchange such as bank, etc. to effect deals in spot foreign exchange with other foreign exchange dealers.

Reuters UK had entered into Dealing Services Marketing Agreement with Reuters India Private Limited (Reuters India) whereby Reuters India was to market the services of Reuters UK to the subscribers in India. The server of Reuters UK was located in Geneva. Reuters UK claimed that its revenue from the Indian subscribers are not liable to tax in India in terms of provisions of India-UK tax treaty as the same is not in the nature of Royalty or Fee for Technical Services (FTS).

The Assessing Officer (AO) concluded that the payments were in the nature of Royalty as well as FTS. Alternatively, the AO also contended that Reuters India would constitute a Permanent Establishment (PE) of Reuters UK in India.

Based on the facts of the case, the Mumbai Tribunal held as follows:

- By allowing use of software and computer system to access the portal of Reuters UK for finding relevant information and matching the requests of Indian clients/subscribers amounts to imparting of information concerning technical, industrial, commercial or scientific equipment. Effectively, the payments made by Indian clients/subscribers is towards use and right to use of equipment and information for processing their request of foreign exchange dealings and would constitute Royalty under Article 13 of the tax treaty.
- The Tribunal distinguished the ruling of the Delhi High Court in the case of Asia Satellite Telecommunication Company Limited [2011] 332 ITR 340 (Del) wherein the transponder capacity was used only for uplinking and downlinking of signals without any manipulations. However, in the current case, Reuters UK was providing media as well as necessary information and data equipment to the subscribers.
- With regard to the issue of PE under Article 5 of the tax treaty, the Tribunal observed that once the receipt has been characterised as Royalty then there is no requirement to go into the question of PE.

Reuters Transaction Services Limited v DDIT (ITA No 6947/Mum/2012)

Services which do not impart technical know-how or transfer any knowledge, experience, or skills, cannot be taxed as royalty

The taxpayer is a non–resident company incorporated in Thailand, engaged in the business of providing services to meet the needs of various GE Group companies. The taxpayer entered into a Master Service Agreement (MSA), 2005 with GE Countrywide Consumer Financial Services Ltd. (GEMFSL), in terms of which the taxpayer is required to provide accounting and finance support services, human resources services, legal and compliance services, risk management services, quality consultation and training, sales and marketing, information technology and system support, and strategic management assistance.

The taxpayer received payments from GEMFSL and proceeded to file a return of income disclosing 'Nil' income as the taxpayer did not have PE in India. However, the AO held that the amounts would fall under FTS as well as Royalty. The DRP held that such payments would fall within the scope of Royalty.

The Mumbai Tribunal relied on the Article 12 of the OECD commentary and explained the term 'industrial, commercial, or scientific' experience. The Tribunal held that the royalty payment received as consideration for information concerning industrial, commercial, scientific experience alludes to the concept of know-how. There is an element of imparting know-how to the other, so that the other person can use or has the right to use such know-how.

On this basis the Mumbai Tribunal held that where services do not impart technical know-how or transfer of any knowledge, experience, or skill, such services will not fall within the definition of ‘royalty’ under Article 12 of the India-Thailand tax treaty.

Since in the present case, lower authorities had not examined the nature of the service rendered by the taxpayer, the matter was remitted back to the AO to examine the nature of services and whether the same falls within the ambit of FTS.

GECF Asia Limited v. DIT (ITA no. 8922/Mum./2010)

Relief under Section 10A to be granted even though software development done partly outside STPI unit

The taxpayer claimed deduction under Section 10A of the Act for development and export of ‘computer software’. The taxpayer was the proprietor of EMac Technologies which was set up at Software Development Park, Dehradun, where it developed and exported PC Suit Software Chip used in Chinese mobile phones MT 6255. The taxpayer had initiated the development work on basic engine in Mumbai and transferred the same to Dehradun STPI. Thereafter, with the help of third party tools, known as Graphical User Interface (GUI), Skin Crafter and Digital Library, the taxpayer developed its final product, i.e. PC Suit Software, which was exported out of India. On this income, the taxpayer claimed deduction under Section 10A. Rejecting taxpayer’s claim for deduction, AO held that substantial development of software was carried out either outside STP premises and/or by using third party tools. The CIT(A) upheld the Order of AO. Aggrieved, by the same the taxpayer filed an appeal before Mumbai Tribunal.

The Mumbai Tribunal observed that the taxpayer developed basic engine facility at Mumbai. Further the same was developed into separate, superior software, a PC Suit Software called as MYSYNC, at STPI, Dehradun. The stage of development of PC suit software was possible only after basic engine was developed at Mumbai facility and PC suit software was distinct software which was further exported out of India.

The Tribunal noted that in co-ordinate bench ruling of Mumbai Tribunal in ISBC Consultancy Services Ltd [88 ITD 134] (Mum) the standard software was bought by the taxpayer from another company. Allowing Section 10A deduction, coordinate bench had held that the basic and standard software acted as a raw material for development of the software which was exported. In the instant case, the Tribunal noted that the taxpayer itself developed the basic engine and based on that created the end product, which was exportable software.

The Tribunal held that the basic engine and PC Engine Software are two entirely independent products. The Tribunal also considered a question that whether a unit at STPI loses its character of STPI unit, if some of the development work is done outside STPI and whether employment of third party tools be called as intervention, leading to denial of deduction. The Tribunal noted that as per the scheme of the STPI under the EXIM policy, undertaking in STPI was free to accept knowledge and/or the services or the product from any area including domestic Tariff area to manufacture or produce article or things and computer software.

This proved that even the Government recognizes the fact that not everything is done within ones' own premises to develop the software. In view of this, the Tribunal rejected revenue's objection with respect to third party tools and development outside STPI.

In view of above, the Tribunal concluded that development of PC suit software to be used as an interface with the personal computer was separate marketable product and hence eligible for deduction under Section 10A of the Act.

Ajay Agarwal (HUF) v. ITO [TS-474-ITAT-2014(Mum)]

Tax officer cannot mechanically apply Rule 8D for making a disallowance under Section14A

The taxpayer had filed his return of income for Assessment Year (AY) 2009-10. The tax officer noted that the taxpayer had earned exempt income, however audit report did not show disallowance of any expenses relating to exempt income. The tax officer held that part of expenses on account of salary, telephone and other administrative expenses must have been related to activities for earning exempt income. Accordingly, invoking Section 14A read with Rule 8D he made disallowance of Rs. 16.35 lakhs. In appeal before CIT(A) the taxpayer contended that he had taken certain portfolio management services (PMS) for which he made payments to various investment advisors. The taxpayer stated that those expenses as well as demat expenses and STT were debited to his capital account. He further submitted that expenses relating to salary, telephone and other administrative expenses were incurred by him for his professional income. Thus, he stated that disallowance made by AO was without any basis and without establishing any nexus. The CIT(A) agreed with the contentions of the taxpayer and deleted the disallowance. Aggrieved, the revenue preferred an appeal before the Tribunal.

The Tribunal noted that expenses in respect of exempt income were shown at nil in audit report and taxpayer had debited direct expenses on account of De-mat charges and STT in his capital account. It observed that "AO had presumed" that taxpayer must have incurred some expenditure under the heads salary, telephone and other administrative charges for earning exempt income. Further noting that the tax officer had made disallowance of INR1.6 million though total expenditure claimed by taxpayer was about Rs. 13 lakhs the Tribunal held the tax officer had merely adopted the formula of estimating expenditure on the basis of investments. But, the justification for calculating the disallowance was missing. The taxpayer had not claimed any expenditure in its P & L account, so, the onus was on the tax officer to prove that out of the expenditure incurred under various heads some were related to earning of exempt income. Also he had to give the basis of such calculation. In any manner disallowance of INR1.6 million as against the total expenditure of INR1.3 million claimed by the taxpayer in P & L account, is not justified. Provisions of Rule 8D cannot and should not be applied in a mechanical way. Facts of the case have to be analysed before invoking them. The Tribunal confirmed the CIT(A)'s order.

ACIT v. Iqbal M Chagala [TS-507-ITAT-2014(Mum)]

The Delhi Tribunal held that the view taken in the case of BMW India Pvt. Ltd. is in conformity with the special

bench ruling in the case of LG Electronics India Pvt. Ltd., and does not override the special bench

The taxpayer is the sole distributor of Bose products in India. The taxpayer characterised itself as a 'buy sell distributor' and selected Resale Price Method (RPM) to benchmark its international transactions. The advertising, marketing, and promotion (AMP) expenses were not benchmarked. The Transfer Pricing Officer (TPO) held that the taxpayer was a limited risk distributor and the AMP/sales of the company was much higher than that of companies selected as comparables. Based on the bright line test applying AMP/sales ratio, excessive AMP expenses were determined, and mark-up was applied to the same. The Dispute Resolution Panel (DRP) upheld the findings of the TPO. The taxpayer contended that since it is a distributor, it's case should be decided following the precedent laid down in BMW India Pvt. Ltd v. ACIT [2014] 146 ITD 165 (Del), as opposed to the decision of the special bench in LG Electronics India Pvt. Ltd. v. ACIT [2013] 140 ITD 41 (Del) which was principally deciding a case where the taxpayer was a licensed manufacturer.

The Tribunal held as follows:

The advancing of arguments that a distributor remuneration model is separate and distinct is accepted in L.G. Electronics, and is also brought out in parameter one of para 17.4 of L.G. Electronics' case. In the case of L.G. Electronics, the special bench had no occasion to analyse and consequently adjudicate on a distributor's case, and went on to candidly admit the fact that it is not possible to have a straight jacket formula for all eventualities. The view taken in BMW India Pvt. Ltd. was that a distributor remuneration model was distinct and peculiar. It is a well-accepted fact that the decisions in transfer pricing are fact specific. The Tribunal confirmed that the view taken in BMW India Pvt. Ltd. is in conformity of the special bench ruling and does not override the special bench. There is no conflict between the decisions in BMW India Pvt. Ltd. and L.G. Electronics.

In view of the ratio of the special bench order in L.G. Electronics, the Tribunal also held as follows:

- The transaction to be an international transaction and upheld the applicability of the bright line as a methodology for calculating AMP
- Directed the TPO to carry out a fresh search for selecting the comparables keeping the 14 parameters set out in para 17.4 of the order of the special bench in mind
- Directed the TPO to correctly calculate the AMP expenses by excluding the selling expenses
- TPO was to decide the application of mark-up by following the precedent laid down in L.G. Electronics.

Bose Corporation India Pvt. Ltd. [ITA No - 5178/Del/2011 & 263/Del/2013 (AYs-2007-08 & 2008-09)]

Chennai Tribunal deleted transfer pricing adjustment on transfer of shares without consideration, free of charge corporate guarantee, and trademark license fee.

The taxpayer is having a wholly owned subsidiary company in Dubai i.e. Redington Gulf FZE (RGF Gulf). The taxpayer first set-up a wholly owned subsidiary company in Mauritius in July, 2008 (RIML Mauritius). RIML

Mauritius, in turn, set-up its own wholly owned subsidiary in Cayman Islands (RIHL Cayman). Subsequently, on 13 November 2008, the taxpayer transferred its entire shareholding in RGF Gulf to RIHL Cayman without any consideration. Once this transfer of shareholding was made, RGF Gulf became a step down subsidiary of RIML Mauritius and the taxpayer. According to the taxpayer, the transaction was not an international transaction and provisions of Section 92 of the Act were not applicable.

The TPO held that transfer of shares made by the taxpayer is an international transaction falling within the TP regulations. Accordingly, the TPO determined the ALP of RGF Gulf. The taxpayer had outstanding corporate guarantee extended on behalf of its AEs for which no guarantee fee was charged. Adjustment was made by the TPO adopting a commission rate of 2 per cent on the outstanding corporate guarantee. The taxpayer paid trademark fee to its AE for use of the 'REDINGTON' trademark. TPO determined the ALP of the trademark fee at nil on the grounds that there was no rationale for such trademark fee payment.

The Chennai Tribunal held as follows:

Transfer pricing on gift transaction

- Section 92 of the Act provides that any income arising from an international transaction shall be computed having regard to the ALP. The computation of the ALP, therefore, is dependent on the income arising to the taxpayer from an international transaction.
- The AAR in various cases [Vanenburg Group B.V. [2007] 289 ITR 464 (AAR), Dana Corporation, Amiantit International Holding, Goodyear Tire and Rubber Co., Praxair Pacific Ltd. [2010] 326 ITR 276 (AAR), VNU International BV [2011] 334 ITR 56 (AAR)] had held that TP provisions would apply only to those international transactions, which are liable to income tax in India. However, in case of transfer of shares, TP provisions do not apply.
- In the present case, the shares were transferred by way of gift and no income arose in the hands of the taxpayer. Thus, ALP determination does not extend to this transaction and therefore, the gift of shares made by the taxpayer was not liable for TP provisions.

TP adjustment for corporate guarantee and trademark fees

- The Tribunal observed that the corporate and bank guarantees extended by the taxpayer were for the overall interests of its business. Relying on the decision in the case of Bharti Airtel Ltd v. ACIT [2014], the Tribunal upheld that the guarantee extended by the taxpayer is not an international transaction as the same does not have any bearing on profits, income, losses or assets of the taxpayer.
- The Tribunal observed there was nothing uncommon in the taxpayer making payment for the use of trademark. Such payment made is not unique to the taxpayer and it is for the taxpayer to decide the dynamics of its business. Tribunal upheld that any expenditure incurred by the taxpayer, if justified by commercial expediency, is an expenditure allowable for the purpose of taxation, and what is commercial expediency is something for the taxpayer to decide, and accordingly the TP adjustment was deleted.

Redington (India) Limited v. JCIT (ITA No.513/Mds/2014)

Chennai Tribunal rejects the TPO's approach of reducing cash discount, outward freight, and storage charges from selling price, with regard to computation of gross profit margin

Taxpayer purchased goods from its AE for re-sale in India and adopted RPM to determine the ALP of the goods purchased from the AE with Gross Profit Margin (GPM) as the Profit Level Indicator (PLI). Dispute was with regard to determination of selling price and the calculation of GPM of the taxpayer and the comparable companies. In relation to the same, the TPO/AO, made transfer pricing adjustments in relation to purchase cost from the AE and development and business promotion expenses. The TPO while calculating the GPM reduced the cash discount offered by the taxpayer for early realisation of outstanding dues on account of sales. The TPO also added the freight and storage charges by treating them as direct expenses incurred in relation to purchase of goods. Further, the TPO did not distinguish between brand promotion and marketing expense, and made an upward adjustment towards development and business promotion expenses.

The Tribunal held as follows:

- Tribunal stressed that cash discounts were offered by the taxpayer to its debtors for early realisation of payments, and were thus in the nature of financial charges. Further, cash discounts were in the nature of incentives for early payments for the sales made by the taxpayer. The Tribunal held that the TPO erred in equating cash discounts with trade discount and that the cash discounts in the present case were offered after the completion of sales, and hence are entirely different in nature from trade discounts, and therefore held that the contention of the TPO to reduce it from the selling price was mis-conceived.
- On the issue relating to reducing freight and storage expenses from selling price, Tribunal observed that these expenditures were towards cost of packing and transportation of goods from the warehouse of the taxpayer to the customers, and that the expenditure on outward freight is in the nature of selling and distribution expenses. The Tribunal held that by no stretch of imagination, can the freight and storage expenses be reduced from selling price to determine the cost of goods sold.
- With regard to marketing expenditure, the Tribunal followed the co-ordinate bench decision in the taxpayer's own case Panasonic Sales & Services (I) Company Limited v. ACIT (ITA No.1911/Mds/2011) for the AY.2007-08 wherein the Tribunal relied on the decision of the Special Bench in the case of LG Electronics India Pvt. Ltd. v. ACIT [2013] 140 ITD 41 (Del).

Panasonic Sales & Services (I) Company Limited v. ACIT (ITA No. 1957/Mds/2012)

Hyderabad Tribunal adjudicated on rejection of certain comparables from the standard ITES set selected by the TPO in three different rulings, consequentially dropping the average PLI as low as 10.78 per cent

The facts cover three Tribunal rulings pertaining to the AY 2009-2010 in the following companies (the taxpayers), all operating as captive service providers:

- Capital IQ

- Excellence Data
- Hyundai Motors

TPO rejected the documentation maintained by the taxpayers due to (i) Use of multiple year data (ii) Improper application of export filters (iii) Selection of functionally dissimilar companies. TPO undertook fresh search of comparables arriving at a set of 12 companies with an average PLI of 27.42 per cent before working capital adjustment. The TPO computed and allowed working capital adjustments in all the three cases. DRP confirmed the order of the TPO.

Tribunal's ruling

The taxpayers in their appeal to the Tribunal restricted their arguments to the comparables. Tribunal held:

- Infosys BPO Limited (Infosys) - to be rejected on the basis of functional dissimilarity on account of its brand value and huge asset base
- Genesys International Limited (Genesys) - to be rejected on functional dissimilarity
- Eclerx Services Limited (Eclerx) - to be rejected on functional dissimilarity
- Cosmic Global Limited (Cosmic) - to be rejected on turnover filter
- Acropetal Technologies Limited (Acropetal) - to be rejected on functional dissimilarity[1]
- Accentia Technologies Limited (Accentia) - to be rejected on account of extraordinary events during the year
- Crossdomain Solutions Private Limited (Crossdomain) - Due to variation between the information in the annual report and the figures adopted by the TPO, Crossdomain to be restored to the TPO/AO for fresh consideration on the PLI after considering the taxpayer's objections[2]

Further, the taxpayer in the case of Capital IQ, in addition to its contention on comparables selected by the TPO, also made its contentions on rejection of the two comparables selected by it, excluded by the TPO. Tribunal's findings on the same:

- Allsec Technologies Limited (Allsec) - to be included as comparable on the basis of the fact that Allsec is functionally comparable and cannot be rejected for a miniscule difference
- Cepha Imaging Private Limited (Cepha) - to be rejected on functional dissimilarity

On the taxpayer's[3] contention of risk adjustment of 1 per cent, the Tribunal asserted that the risk profile of each of the taxpayers differs, and therefore a standard deduction of 1 per cent cannot be adopted as a norm. The Tribunal directed the TPO/AO to examine the risk profile of the taxpayer and allow necessary deduction based on the facts of each case. The Tribunal also directed the TPO/AO to allow the working capital adjustment as already provided in the computation by the TPO.

[1] In the case of Hyundai Motors, since the taxpayer is also engaged in the provision of engineering design services, the Tribunal did not reject it on functional dissimilarity at segment level. However, due to lack of information on the segmental allocation of expenditure, Acropetal has been restored to the TPO/AO for fresh consideration on the PLI

[2] No objection has been raised to the Tribunal on selection of Crossdomain in the case of Capital IQ

[3] In the case of Capital IQ, the risk adjustment has not been discussed in the ruling

Capital IQ Information Systems (India) Private Limited v. ACIT (ITA No.170/Hyd/2014)

Excellence Data Research Private Limited v. ITO (ITA No.159/Hyd/2014)

Hyundai Motors India Engineering Private Limited v. DCIT (ITA No.255/Hyd/14)

Notification & Circulars

Tax treaty between India and Fiji notified

The Government of India has notified its tax treaty with the Government of Fiji on 12 August 2014. The tax treaty was signed on 30 January 2014 and would be effective from 1 April 2015.

The tax treaty expands the scope of a PE by including Insurance PE. The tax treaty taxes Royalty and FTS at 10 per cent, dividend at 5 per cent and interest at 10 per cent. The provisions of the tax treaty do not prevent the contracting States from application of the provisions of the domestic law and measures of tax avoidance or tax evasion by having clauses on limitation of benefit and exchange of information.

Notification No. 35/2014 dated 12 August 2014

CBDT clarifies on allowability of deduction under Section 10A/10AA on transfer of technical man power in the case of software industry

Section 10AA of the Act, interalia, provides for deduction in respect of the profits derived by a unit set up in Special Economic Zone (SEZ) from export of computer software or from providing any Information Technology Enabled Services (ITES). The said deduction is available if, inter alia, the new SEZ is not formed by split-up or reconstruction of an existing business or by transfer of used plant or machinery. However, the deduction is available if the earlier used plant and machinery will not exceed twenty per cent of total value of the plant or machinery used in new business. The tax department, in certain cases, has considered the transfer/redeployment of technical manpower from the existing units of a taxpayer engaged in computer software development to its new SEZ unit, as splitting up or reconstruction of the existing business and therefore, denied the deduction under Section 10AA of the Act.

In this regard, the software industry has represented before the Central Board of Direct Taxes (CBDT) that there is a limited pool available with a software developer of skilled, talented and experienced manpower with domain knowledge. Given the highly technical and competitive nature of software development, some technical persons having prior experience are required to manage the critical functions of software development in a new unit. Accordingly, the movement of technical manpower from an existing unit to a new SEZ unit should not be a constraint in availing deduction under Section 10AA of the Act. Attention was also drawn to the Instruction No.70, dated 9 November 2010 issued by the Ministry of Commerce which states that there is no bar on transfer of manpower to SEZ units. Also, there is a specific prohibition on transfer of plant or machinery from an existing unit to a new SEZ unit under Section 10AA, subject to a ceiling of 20 per cent but no such bar on transfer/redeployment of manpower has been explicitly laid down in the Section.

Recently, the CBDT has issued a Circular clarifying that mere transfer or re-deployment of existing technical manpower from an existing unit to a new SEZ unit in the first year of commencement of business will not be construed as splitting up or re-construction of an existing business, provided the number of technical manpower so transferred does not exceed 20 per cent of the total technical manpower actually engaged in developing software at any point of time in the given year in the new unit. Further the CBDT has clarified that the circular will be applicable only in the case of taxpayers engaged in the development of software or in providing IT Enabled Services in SEZ units eligible for deduction under Section 10A or 10AA of the Act.

Circular No. 12/2014, dated 18 July 2014

Employees' Provident Fund Organisation issues circular to its field officers to implement the proposed enhancement in statutory wage ceiling from INR6,500 to INR15,000

Under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (EPF Act) the statutory wage ceiling for enrolling employees, as well as for making contributions, is INR6,500 per month (except for some special classes of employees).

In the Union Budget 2014, this statutory wage ceiling is proposed to be revised to INR15,000 per month. In this context, the Employees' Provident Fund Organisation (EPFO) has issued a circular to its field officials for undertaking preparatory activities to implement these proposed changes.

The proposed enhancement of statutory wage ceiling is expected to have significant implications for the industry. All establishments covered under the EPF Act will need to revise their compliances. Employers will have to enroll new employees who become eligible because of this revision of statutory wage ceiling. Secondly, they will have to contribute mandatorily upto the monthly pay of INR15,000 (as defined under the EPF Act) for the eligible employees. This will result in increase in the cost of compliances under the EPF Act. For the employees, this may mean increased contributions under the EPF Act which may impact their net take home salary. The employees will also be eligible for corresponding higher benefits.

Source - www.epfindia.com

India's social security agreements with Finland and Sweden come into effect

India had signed Social Security Agreements (SSAs) with the Republic of Finland (Finland) and the Kingdom of Sweden (Sweden) on 12 June 2012 and 26 November 2012 respectively. The Indian Provident Fund authorities have now issued a circular notifying that these SSAs with Finland and Sweden will be effective from 1 August 2014.

The SSAs aim at achieving equality on the principle of reciprocity to benefit the employees and employers having cross-border operations by avoiding double payment of social security contributions.

The SSAs between India - Finland and India - Sweden envisage the following benefits:

- Exemption from social security contribution in the host country (Detachment)
    - The employees from one country deputed by their employers to the

other country on short-term assignments are exempted from social security contribution in that country. The period for detachment under the respective SSAs is as follows:

SSA	Period of detachment
India – Finland	Up to a period of 60 months
India – Sweden	Up to a period of 2 years

- Totalisation of contributory periods
- Export of benefits

The signing of the India – Finland and India - Sweden SSAs is a welcome step as it will help in cost savings and the social protection of international assignees in respect of deputation arrangement for employees, which in turn could lead to increase in economic activity between the countries.

Source - www.epfindia.com

II. SERVICE TAX

High Court Decisions

Allows refund to service recipient upon downward price revision, absent unjust enrichment

The taxpayer purchased natural gas through pipeline from Reliance Gas Transportation Infrastructure Limited ("RGTIL"). The transmission charges charged by RGTIL to the taxpayer were based on the tariff notified by the statutory authority. The initial tariff was reduced by the statutory authority resulting in excess transmission charges being collected by RGTIL from the taxpayer. RGTIL credited such excess amount collected to the taxpayers account by way of credit notes, however service tax liability was discharged by RGTIL on the initial tariff collected by it. Accordingly, the taxpayer filed an application for refund of proportionate service tax (remitted by RGTIL and borne by them) under section 11B of the the Central Excise Act, 1944 ("CEA"). On adjudication, the refund claim was allowed. However, the Revenue Authorities preferred an appeal before the Commissioner (Appeals) which was allowed on the ground that the refund claim should have been filed by the service provider and not the service recipient. Being aggrieved, the taxpayer preferred an appeal before the Customs, Excise and Service Tax Appellate Tribunal ("CESTAT") and it held that the refund claim can be filed by person who has borne the service tax burden. Since, in the instant case the burden of tax was borne by the taxpayer, the refund claim filed was maintainable and the order passed by the Commissioner (Appeals) was set aside. Accordingly, the Revenue Authorities filed the present appeal.

The matter came up for consideration before the Allahabad High Court ("HC"). As regards limitation, HC came to the conclusion that the claim was filed within the limitation period since the same was not challenged by Revenue Authorities. With regard to principle of unjust enrichment, HC observed that it was undisputed fact that the final product manufactured by taxpayer was an exempted product and hence, question of unjust enrichment does not arise as burden of duty has been borne by taxpayer. Thus, HC held that taxpayer was entitled to claim a refund of excess service tax paid consequent upon downward revision of transmission charged as taxpayer was the recipient of the taxable service and had borne the incidence of service tax. HC concluded that principle of unjust enrichment would not be applicable as taxpayer had not passed the burden of tax which has been amply established by adjudicating authority's order.

Commissioner of Customs, Central Excise & Service Tax vs Indian Farmers Fertilizers Cooperative Limited [TS 254 HC 2014 (ALL) ST]

Tribunal Decisions

Separate service contract for erection classifiable as Works Contract, composition benefit available

The taxpayer was involved in the business of manufacturing electricity transmission towers and parts and rendition of erection, installation and commissioning of such towers. The taxpayer during the material period was registered as a service provider under the taxable service category of works contract service, business auxiliary services, GTA services. The taxpayer used to enter into two separate contracts with its customers; one for supply of towers and other for erection and installation of such towers. For the contract for services of erection and installation of towers, taxpayer was availing the benefit of composition scheme for works contract services and was discharging service tax on the abated value of contract. The Revenue Authorities contended that contract for service is purely for provision of services and that there is no transfer of property involved in course rendering erection and installation services provided and also that the materials such as steel, cement, sand, metal, paint, etc are consumed while provision of services and thus services of taxpayer's services are not works contract services and thereby taxpayer is not eligible to avail benefit under the composition scheme. The Revenue Authorities contended that the nature of services provided by the taxpayer is actually classifiable under "Erection, Commissioning or Installation Service" and thus taxpayer is liable to discharge service tax at a higher rate. Accordingly, the taxpayer was adjudicated; differential service tax liability along with applicable interest and penalties were confirmed. Being aggrieved the taxpayer preferred the present appeal.

The matter came up for consideration before the Mumbai Bench of CESTAT which held it in favour of the taxpayer. The CESTAT observed that the contention of

Revenue Authorities that there is no transfer of property involved will not hold good because the materials such as steel, cement, sand, etc are embedded in the structure and are not consumed in the provision of services. Further, such fact was also illustrated by the taxpayer by way of photographs submitted of the installation site.

Separately, it was noted by the CESTAT that for a service to be classified under works contract service, there should be transfer of property and applicable tax on sales should be paid on transfer of goods. Accordingly, CESTAT noted that undoubtedly there was transfer of property in course of provision of services and also applicable sales tax was discharged by the taxpayer on transfer of goods. Further, the CESTAT also held that the Central Board of Excise and Customs ("CBEC") circular B1/16/2007 - TRU May 22, 2007 supports the case of the taxpayer to its services as works contract services. Accordingly, the CESTAT held that the instant contract for services involves both provision of services and transfer of goods and held the nature of services rendered under the service contract were works contract services

Gammon India Ltd vs Commissioner of Central Excise, Customs and Service tax, Nagpur [2014 TIOL 1344 CESTAT MUM]

Reinsurance service is an 'Input service' for insurance companies

The taxpayer was engaged and licensed to carry out life insurance business. The taxpayer has availed re-insurance services from overseas companies and had availed CENVAT credit of service tax paid on the services received. The credit was denied to the taxpayer solely on the ground that the services of re-insurance cannot be treated as input services, since such services are received after the insurance business takes place. Being aggrieved the taxpayer preferred the present appeal. The taxpayer submits that section 101A of the Insurance Act, 1938 ("IA") mandatorily requires every insurer dealing with insurance business to reinsure a specified percentage of sum assured with another insurance company. Further, the taxpayer also submits that according to the definition of Insurance service, the services of both insurance and re-insurance are liable to service tax. In addition to the above, the taxpayer also argued that Circular no 120(a)/2/2010- ST dated April 16, 2010, states that it is the reinsurer which provides insurance service to the insurance company. Thus, taxpayer argued that CENVAT credit had been rightfully availed by it.

The matter reached before Bangalore Bench of CESTAT for consideration. CESTAT observed that under section 101A of IA, every insurer was obliged to insure with Indian reinsurers, a prescribed percentage of sum assured on each policy. Since reinsurance is a statutory obligation and coterminous with the insurance policy, CESTAT rejected Revenue Authorities stand that reinsurance must have nexus with output service, viz. provision of insurance to customers. CESTAT noted that the percentage of insurance to be reinsured was linked directly to the premium collected from the insured persons. It was basically a transfer of portion of the risk, and thus, it can definitely be deduced that the reinsurer was indeed providing service to the insurance company, when it accepted to reinsure a portion of the insurance undertaken by the insurer. Therefore, CESTAT considered the impugned order to be unsustainable on merits and allowed the appeal with consequential relief to taxpayer.

PNB Metlife India Insurance Company Limited vs Commissioner of Central Excise, Service Tax and Customs, Bangalore [TS 259 Tribunal 2014 ST]

Revenue Authorities cannot demand higher tax for non-satisfaction with consideration

The taxpayer was engaged in providing services under the category of rail travel agent, rent-a-cab operator, air-travel agency, tour operator and banking and other financial services. The taxpayer was collecting uniform rate from its clients for the activity of sale and purchase of foreign exchange and discharged applicable service tax on such consideration. Revenue Authorities initiated proceedings against the taxpayer on the ground that it had not shown actual consideration received from its clients towards sale and purchase of foreign currency in the invoices. Accordingly, the Revenue Authorities demanded applicable service tax at 0.25 percent on the value since according to them, the taxpayer was charging a paltry exchange transaction fee to avoid payment of service tax under rule 6(7B) of The Service Tax Rules, 1994. Upon Adjudication the demand was confirmed on the taxpayer. The first appellate authority passed a stay order and directed the taxpayer to deposit 50 percent of service tax, which was complied with by the taxpayer. Subsequently, on merits, demand was confirmed against the taxpayer alleging that the taxpayer charged paltry exchange transaction fee as consideration towards its service, to avoid payment of service tax under rule 6(7B). Being aggrieved, the taxpayer preferred the present appeal.

The matter came up for consideration before the Bangalore Bench of CESTAT. CESTAT observed that in terms of the definition of Banking and Financial Services ("BoFS") read with the provisions of rule 6(7B), in case the consideration for sale / purchase of foreign exchange is shown separately in the invoice, service tax has to be paid on the consideration received and the option to pay service tax at 0.25 percent of gross amount of currency exchanged is not available. Further, CESTAT was of the view that rule 6(7B) was only an option available to a service provider and that the taxpayer cannot be forced to avail such option. CESTAT also observed that the Revenue Authorities, have mis-interpreted the clarification issued by CBEC vide letter F No 334/1/2008. Further, the CESTAT also clarified that, it was nowhere specified in the Statute that service tax could be demanded by the Revenue Authorities, where consideration charged by the taxpayer was not as per their expectations. CESTAT held that the Commissioner (Appeals) order was totally contrary to the provisions of law, equity and justice since without any evidence, it proceeded to question the appropriateness of the quantum of consideration charged by the taxpayer to its customers. Furthermore, it was also held that the whole proceedings had arisen because of lack of understanding of the legal provisions by the lower authorities, thus penalty imposed under section 78 was not justifiable. CESTAT set aside impugned order demanding service tax at 0.25 percent of gross amount of foreign currency exchanged and also directed the Revenue Authorities to refund 50 percent of service tax which was deposited by the taxpayer, without further litigation.

FCM Travel Solutions (India) Pvt Ltd Vs Commissioner of Central Excise, Customs and Service Tax Hyderabad-II [TS 262 Tribunal 2014 ST]

Credit of service tax paid can be availed on basis of challan even after detection by Revenue Authorities

The taxpayer was engaged in the business of manufacture of sugar, molasses, etc. The taxpayer received various services from Foreign Service providers classifiable under taxable service category of Merchant Banking Services, but did not pay service tax on such services under reverse charge mechanism. Upon detection by the Revenue Authorities, the taxpayer discharged applicable service tax liability by making payment by way of TR-6 challan and availed credit of such tax paid. The Revenue Authorities disallowed such credit alleging that it is availed based on ineligible document as per rule 9(1)(b) of CENVAT Credit Rules, 2004 ("CCR"). The Commissioner (Appeals) held the matter in favour of the taxpayer. However, the Revenue Authorities preferred an appeal interalia contending that rule 9(1)(b) of CCR provides restriction on availing CENVAT credit on supplementary invoices / challans not issued in the normal course of business. Conversely, the taxpayer argued that challan was a specified document under CCR and vide Notification No 13/2011-CE(NT) dated March 31, 2011, clause (bb) was inserted to restrict availment of credit based on challan on account of fraud, collusion etc. In the present case, the period in dispute was prior to introduction of such notification.

The matter came up for consideration before the Chennai Bench of CESTAT, where the CESTAT inter alia observed that there is no dispute as to credit of service tax paid can be availed on basis of challan. It was further observed that credit against a challan could be denied only for the period post insertion of clause (bb) in rule 9(1); credit availed on account of fraud, collusion etc. CESTAT placed reliance on the decision in case of 'Metafab', wherein it was held that amendment to rule 57E of erstwhile Central Excise Rules, 1944 vide Notification No. 6/97-CE was not applicable to period prior to amendment. CESTAT in the present case held that similarly, denial of credit on the basis of challan for the reason of fraud, collusion, suppression of facts etc, would not be applicable for period covered prior to Notification No 13/2011-CE(NT). Thus, rejecting Revenue Authorities contention, CESTAT held that credit availed on the basis of challan as specified under rule 9(1)(e) could not be denied. Accordingly, CESTAT upheld the order of Commissioner (Appeals) and dismissed the appeal by the Revenue Authorities.

Commissioner of Central Excise, Salem Vs M/s Sakthi Sugars Limited [TS 281 Tribunal 2014 ST]

III. VAT/ CST/ENTRY TAX

High Court Decision

Provision of documents relied upon by the Revenue Authorities to the taxpayer in the interests of natural justice

The taxpayer was a private limited company registered under the Companies Act, 1956. The Revenue Authorities conducted a survey at the warehouse of the taxpayer. Following the survey, several records, documents, books etc were seized from the premises of the taxpayer. Relying upon the seized documents, the Revenue Authorities issued show cause notices to the taxpayer.

The taxpayer contended that despite several requests, the copies of the seized documents were not made available to it for the purpose of drafting responses to the show cause notices. On the other hand, the Revenue Authorities were of the opinion that if the original copies of the seized books were made available to the taxpayer, there was a reasonable risk that the taxpayer would meddle with the documents.

After having failed at obtaining copies of the seized documents, the taxpayer preferred a writ petition before the Allahabad HC which allowed the writ. The HC reasoned that the taxpayer had the right to have the material which the Revenue Authorities have relied upon to arrive at a prima facie opinion that the proceedings against the taxpayer should further proceed. Further, the HC also held that the test of reasonableness and the principles of natural justice also require that if the taxpayer is put to notice, he must know the material that is being relied upon by the Revenue Authorities in order to give an effective reply. Accordingly, the writ petition of the taxpayer was allowed

Sony India Private Limited vs State of Uttar Pradesh [2014 TIOL 1265 All HC]

Sale not taxable in India merely because the sales of goods occurred after and not before the goods were cleared for export

The taxpayer was a company registered under the local and Central Sales Tax Act, 1956 ("CST"). It exported and sold certain goods to a buyer in Nepal. The taxpayer claimed such sales as exempt from sales tax under section 5(1) of the CST; however the Revenue Authorities rejected the claim of the taxpayer on the ground that the taxpayer had failed to establish that the transfer of property in goods to the buyer was preceded by and not followed by the clearance of the goods in question for export out of India. It was established on record that the title in the goods was transferred to the buyer after the goods had crossed the customs frontiers of India.

The matter ultimately came up for consideration before the Delhi HC which held in favour of the taxpayer. The HC explained the true and correct scope of section 5(1) of the CST. It held that the said section covered two types of sales. The first type of sale is one where the sale or purchase occasions such sale (also called as an export sale) and the second is one where the transfer of documents to title of the goods is after the goods have crossed the customs frontiers of India. The HC held that the lower authorities only considered the first type of sale while deciding the eligibility of exemption for the taxpayer. Further, it was also held that the case of the taxpayer was squarely covered by the second limb of section 5(1) of CST and the failure on part of the taxpayer to establish that the transfer of title in goods occurred prior to the export of goods, was immaterial

Remari India Private Limited vs Commissioner of Sales Tax, Delhi [2014 VIL 200 Del HC]

'Same Goods Theory' no longer applicable, exemption allowed if the local sale / purchase inextricably linked to the export of goods

The taxpayer sold toughened glass to Titan Energy Systems Limited, with the use of which, the latter exported solar module, accessories and CIGS module. The taxpayer claimed exemption from the payment of sales tax under section 5(3) of the CST. On the other hand, the Revenue Authorities contended that the same was not eligible for exemption because the same goods were not exported. Hence, the sale in question was liable to be taxed as an interstate sale.

The matter came up for consideration before the Allahabad HC which held in favour of the taxpayer. The HC reasoned that the test to determine the eligibility of exemption under section 5(3) of the CST is whether there is an in-severable link between the local sale or purchase and export. The HC held that it was clear that the local sale and the export was inextricably linked and therefore, a claim under section 5(3) of the CST was justified. Accordingly, in terms of the decision of the Supreme Court in State of Karnataka vs Azad Coach Builders Private Limited [2010 TIOL 70 SC], wherein it was also held that the 'same goods theory' was no longer applicable; the claim of the taxpayer was allowed

Allied Glasses Private Limited vs Commissioner of Commercial Taxes [2014 TIOL 1261 All HC]

If discounts not reflected in tax invoice, deduction not permissible

The taxpayer was a company engaged in the sale and marketing of electronic goods and IT products. For the relevant period, the Revenue Authorities disallowed the deductions claimed by the taxpayers as trade discounts effected by issuing credit notes. The Revenue Authorities contended that the said discounts were not mentioned at the time of issue of tax invoices and the credit notes were issued at the end of the month, hence they were not eligible for deductions.

The matter came up for consideration before the Karnataka HC which held against the taxpayer. The HC explained that once the sale invoice is issued and the sale price is collected with tax, the aggregate of such tax is called the total turnover. Further, to arrive at the taxable turnover, certain deductions are allowed under the Karnataka Value Added Tax Act, 2003 ("KVAT"). One such permissible deduction is that the amount paid by way of discount which is reflected in the sale invoice. Given that in the instant case, the discounts were allowed by issuing a credit note and after the completion of the sale, the same could not be allowed as trade discounts.

State of Karnataka vs Samsung India Electronics Limited [STRP 19 / 2012 and STRP 383- 388 / 2012 HC Kar]

Writ petition cannot be filed against the reassessment proceedings without filing objections with the Revenue Authorities

The taxpayer was a manufacturer of cement and registered under the Tamil Nadu Value Added Tax Act, 2006 ("TNVAT"). For the period under consideration, the Revenue Authorities issued notices to the taxpayer for reassessment of its tax liability on the basis of the inspection report of the Enforcement Officer. The Enforcement Officer called upon the taxpayer to file its objections within a period of 15 days and also afforded the taxpayer a hearing.

The taxpayer preferred a writ petition before the Madras HC on the ground that Enforcement Officer could not act as the AO and framed the revision of assessment. Further, the report of the Enforcement Officer cannot be simply adopted by the AO without the application of mind and as a quasi- judicial authority, it is incumbent upon the AO to make assessment with a fresh mind without the influence of the inspection report.

The matter came up for consideration before the Madras HC which held against the taxpayer. The HC held that before taking recourse to file a writ petition, the taxpayer is obliged to avail the opportunity to afforded to it in response to the objections of the Enforcement Officer. Further, writ jurisdiction can be exercised by the HC only in limited cases where the notice is defective on account of violation of fundamental rights, principles of natural justice, ultra vires the relevant law, miscarriage of justice etc. The HC further held that the question of waiver of alternate remedy will arise only if the abovementioned cases arise. Given that there was ample opportunity given to the taxpayer to present its case before the Enforcement Officer, the writ petition was held to be not maintainable

Ultra Tiles Private Limited vs Assistant Commissioner [2014 (46) GST 262 Mad HC]

IV. CUSTOMS
Tribunal Decisions

Special Additional Duty ("SAD") refund under notification no 102/2007-Cus available only in case the imported goods are resold without changing the form in which they were imported

The taxpayer was engaged in the business of laying proflex roofs for its clients. The taxpayer imported raw materials in process of laying roof and paid SAD under section 3(5) of Customs Tariff Act, 1975. In the final invoice raised by the taxpayer, the value of the imported material was not specifically shown. Further, taxpayer also raised invoice for its works contract services rendered on a per square meter basis. Accordingly, the taxpayer made an application for claiming refund under notification number 102/2007 - Cus dated September 14, 2007 of the SAD paid. Adjudicating authority rejected refund claim on the grounds that the taxpayer has not sold imported goods on "as such" basis. The first appellate authority upheld the order of the adjudicating authority. Consequently, the taxpayer preferred the present appeal inter-alia arguing that it has paid applicable VAT / CST on sale of goods in course of works contract services and to support its arguments, it relied on Posco India Delhi Steel Processing Ltd Vs CC Kandla 2012-TIOL-1769-CESTAT-AHM and CC Kandla Vs Posco India Delhi Steel Processing Centre Ltd [2012] (299) ELT 263 (Guj). On the other hand, the Revenue Authorities argued that no sales tax is paid at the time of clearance of goods and sales tax is paid only on deemed sales' component in the works contract and thus, the taxpayer is not eligible to obtain SAD refund.

The matter came up for consideration before the Ahmedabad Bench of CESTAT. CESTAT observed that the facts of the taxpayer's case of CC Vs Posco India Delhi Steel Processing Centre Private Ltd (supra) were different from the present case. The CESTAT noted that in the present case, the imported raw materials lost their original identity in course of provision of works contract services. Further, the CESTAT also observed that quantity of raw material used in the final product was not identifiable, as the part of the unused materials remained property of the taxpayer. Further, CESTAT also observed that it was not made clear whether VAT / CST paid on the final invoices was only in respect of imported goods or also on other materials / consumables used in course of provision of works contract services. Thus, the appeal filed by the taxpayer was rejected

M/s Proflex Systems Vs Commissioner of Customs, Ahmedabad [2014 TIOL 1315 CESTAT AHM]

V. CENTRAL EXCISE

High Court

Pre- deposit / stay / other interlocutory orders appealable before HC

The issue for consideration before the Andhra Pradesh HC was whether a writ against an order for pre-deposit was maintainable in view of the alternate remedy of appeal before the HC. The contention of the taxpayer was that section 35G of the CEA contemplates only the final order of the CESTAT as an appealable order, therefore, there was no alternate remedy available to the taxpayer except invoking the writ jurisdiction.

The HC decided the matter against the taxpayer and held that interlocutory orders passed by the CESTAT are also appealable within the scope of section 35G of CEA. The HC held that the words used in the CEA are 'every order passed in appeal'. The words 'every order passed in appeal' contemplate a number of orders, not one or singular and such orders can be passed on several issues and problems in connection with the appeal. Further, the words used are 'in appeal' and not 'on appeal'. Had the words used been 'on appeal', it would mean that the section only contemplates the inclusion of the final order of the CESTAT. However, that is not the intention of the legislature because unless there is an appeal, there cannot be any application for waiver of pre-deposit. Accordingly, in terms of the judgment of the Madras HC in Metal Weld Electrodes vs Elian Industries [2014 (299) ELT 3 (Mad)], the writ of the taxpayer was held to be not maintainable

Patel Engineering Limited vs Commissioner of Central Excise [2014 (305) ELT 234 AP HC]

Refund of CENVAT Credit cannot be denied on the ground that there was no physical export

The taxpayer, holding a valid excise registration, submitted refund claims in respect of CENVAT Credit on inputs used in manufacture of its product as per rule 5 of the CCR. The Revenue Authorities were of the opinion that the taxpayer had not physically exported the goods, but merely supplied it to a 100 percent Export Oriented Unit ("EOU"), therefore the refund claim was liable to be rejected.

The matter came up for consideration before the Gujarat HC which held in favour of the taxpayer. The HC held that the Revenue Authorities seriously erred in holding that refund claims were liable to be rejected given that there were no physical exports but only deemed exports. The HC also pointed out the fault of the Revenue Authorities in not considering the ruling of the SC in the case of Commissioner of Central Excise vs NBM Industries [2012 (276) ELT 9 (Guj)] wherein it was held that refund claims could not be rejected on the ground that there were no physical exports but only deemed exports; which squarely covered the case of the taxpayer. Accordingly, the claim of the taxpayer was allowed

E I Dupont India Private Limited vs Union of India [2014 (305) ELT 282 Guj HC]

Filing of ARE - I mandatory for claiming rebate under CCR

The taxpayer was a merchant exporter of medicines. He sought rebate under rule 18 of the CCR which was rejected on the ground that the taxpayer had not complied with the procedure described in notification no 19 / 2004 - Central Excise. The taxpayer admitted non - compliance with the procedure laid down in the notification, but contended that the lapse was on account of ignorance on his part and since the goods were actually exported, non - compliance of procedure could be overlooked and condoned.

The matter came up for consideration before the Allahabad HC which held against the taxpayer. The HC held that it could not be doubted that the provision of rebate was formulated for the benefit of the taxpayers, but it was equally true that the Government of India has to lay down a procedure to discourage scrupulous and mischievous behaviour. Additionally, the HC also held that ignorance of law is no excuse, therefore the taxpayer's plea of ignorance could not be granted. Further, the HC held that the said notification clearly said that rebate can be claimed in the manner laid down in the procedure. The procedure is the foundation in respect of verification of commodity sought to be exported and such a requirement cannot be merely directory, but has to be read as mandatory. Accordingly, the claim of the taxpayer was rejected.

Vee Excel Drugs and Pharmaceuticals Private Limited vs Union of India [2014 (46) GST 246 HC All

Tribunal Decisions

Credit not to be denied based on shortage of input in internal stock report of the taxpayer

The taxpayer was engaged in the manufacture of polyester film. The taxpayer conducted a survey of inventory and realized that there was shortage of inputs in its factory on which they had taken credit. The Revenue Authorities initiated proceedings against the taxpayer and confirmed duty demand. The taxpayer argued that there was no actual shortage of the inputs and produced reconciliation statement of the entire figures. On the other hand, the Revenue Authorities argued that shortage was evident from the management's own stock taking of the inventory.

The matter came up for consideration before the Delhi Bench of CESTAT which held in favour of the taxpayer. The CESTAT found that the entire case of the Revenue Authorities was based on the inventory made by the taxpayer himself during the course of internal stock taking. Additionally there was no allegation or evidence that indicated that the taxpayer cleared the inputs without payment of duty. Accordingly, the CESTAT held that there was no justification to confirm the excise duty demand

Ester Industries Limited vs Commissioner of Central Excise [2014 (46) GST 400 CESTAT Del]

Input Service Distributor is only a facility; does not deal with recovery

The taxpayer took credit on the strength of invoices issued by its head office which was the input service distributor ("ISD"). The Revenue Authorities denied the credit so availed on the ground that the input services were attributable to trading activities. The taxpayer contended that the ISD was responsible for wrong distribution of the credit and therefore the taxpayer could not be held liable.

The taxpayer urged that w.e.f. April 1, 2011 'trading' has been deemed to be an 'exempted service' by introducing an explanation to rule 2(e) of CCR. Further, the explanation states that the same has been introduced for the removal of doubts. Therefore, the taxpayer contended that such explanation is merely clarificatory in nature and demands retrospective application. Accordingly, in terms of circular no 943 / 4 / 2011 – Central Excise, credit of common inputs and input services subject to restriction of utilization of credit upto 20 percent of the total duty liability, could be availed for input services used in trading prior to April 1, 2008.

The matter came up for consideration before the Mumbai Bench of CESTAT which held against the taxpayer. The CESTAT held that ISD is only a facility provided under the CCR and does not deal with recovery. Therefore, since the taxpayer availed wrongful credit, proceedings had to be initiated against him only. Relying upon the decision of the Mumbai Bench of CESTAT in the case of Mercedes Benz India Private Limited vs Commissioner of Central Excise, Pune [2014 TIOL 476 Mum CESTAT], the CESTAT held that 'trading' cannot be considered as an exempted service prior to April 1, 2011. Further, it was also held that the apportionment of common input services used in trading and manufacturing activities could be done on the basis of the turnover. Accordingly, the CESTAT held that the taxpayer was liable to reverse proportionate credit pertaining to trading

Clariant Chemicals India Limited vs Commissioner of Central Excise, Raigad [2014 VIL 140 Mum CESTAT]

Construction industry qualifies as 'institutional consumer' for the purposes of legal metrology

The taxpayer was a manufacturer of cement. Under the Legal Metrology Act, 2009 ("LMA") there is a statutory requirement to affix Maximum Retail Price ("MRP") on packages sold to dealers for further sale to consumers in retail. The taxpayer had complied with the regulations under the Legal Metrology (Packaged Commodities) Rules, 2011 ("PC Rules"). Apart from the retail sale packages, the taxpayer also cleared cement in 50 kilo packs to various bulk consumers like builders, developers, industrial users who used the cement for construction purposes as raw material. As per rule 3(ii) of the PC Rules, the manufacturer is not obligated to declare the MRP on cement packages weighing more than 50 kilos. Accordingly, the taxpayer did not declare the MRP on the packages and marked the packages with specific declaration 'Not for Retail Sale - meant for industrial consumer / institutional consumer / RMC consumption'. Since the taxpayer cleared these packages to the class of consumers mentioned above, it availed concessional rate of duty in terms of notification no 4 / 2006- Central Excise.

Conversely, the Revenue Authorities were of the view that the taxpayers were not eligible for the concessional rate of duty because buyers such as builders, developers cannot be considered to be industrial / institutional consumers. Therefore, the taxpayer was required to discharge excise duty at tariff rate.

The matter came up for consideration before the Mumbai Bench of CESTAT which held in favour of the taxpayer. The CESTAT reasoned that builders / developers engage in construction activity and the same is considered to be a 'service'. This is also evidenced by the fact that there is a service tax levy on such activity. The contention of the Revenue Authorities that the sale is not to consumers like transportation, airways, railways, hotels etc and developers / builders are not specifically included in rule 3(ii) of the PC Rules, therefore builders / developers do not qualify as institutional / industrial consumers is erroneous. Further, airways, railways, hotels etc do not form any class therefore, the principle of ejusdem generis cannot be applied to interpret 'any other service institution'. For the purpose of this specific rule, any service institution would qualify as institutional consumer. Accordingly, the appeal of the taxpayer was allowed.

Heildelberg Cement India Limited and Ultratech Cement Limited vs Commissioner *of Central Excise [Appeal no E / 88158 & 89194 / 13 & E / 86253 / 14 Mum CESTAT]*

Notification & Circulars

Maharashtra VAT Authorities reduce late fees to encourage non-filers to file VAT returns for the period upto February 2014

Maharashtra VAT authorities have allowed defaulting dealers to file returns for any of the periods upto February 2014 before September 30, 2014 by paying Rs 1000 as late fee for each return, instead of Rs 5000. However, such partial exemption benefit is available on the condition that such dealers must discharge the tax along with applicable interest and also file the returns before September 30, 2014

Trade Circular 13T of 2014 dated August 2, 2014

Customs Exchange rates notified effective from August 8, 2014

CBEC notifies exchange rates effective August 8, 2014 in supersession of Notification No 53/2014-Cus (NT)

Notification No 57/2014-Cus (NT) dated August 7, 2014

Maharashtra VAT issues a circular clarifying the impact of various amendments introduced in Budget 2014-15

Maharashtra VAT Authorities list out amendments to Maharashtra Value Added Tax Act, 2002 ("MVAT") and other State governed Acts pursuant to Budget 2014-15

Trade Circular 15T of 2014 dated August 6, 2014

Delhi Value Added Tax (Second Amendment) Rules, 2014 notified

Import tariff value of Gold has been increased and notified to be 428 / 10 grams and Import tariff value of Silver has been amended and notified to be USD 688 / kilogram. New tariff values for 10 other import items also notified.

Circular No 6 of 2014-15 dated August 4, 2014