July 2015

TAX UPDATES

(containing recent case laws, notifications, circulars)

Prepared in association with

KPMG

cutting through complexity

Foreword

I am pleased to enclose the July 2015 issue of FICCI's Tax Updates. This contains recent case laws, circulars and notifications pertaining to direct and indirect taxes.

A delegation led by Mr. Dinesh Kanabar, Chairman of FICCI's Taxation Committee appeared before the Committee chaired by Justice A. P. Shah constituted by the Government to examine the matter of levy of Minimum Alternate Tax ('MAT') on Foreign Institutional Investors (FIIs) for the period prior to April 1, 2015. It was represented before the Committee that the levy of MAT was never intended for FIIs since the time the concept of MAT has been introduced. Therefore, the question of levy of MAT does not arise.

Mr. Harshvardhan Neotia, Senior Vice President, FICCI, along with Chairs of the Taxation Committee had a meeting with Mr Jayant Sinha, Hon'ble Minister of State for Finance, on 10th June, 2015 to discuss certain tax related issues. Apart from measures to improve the tax environment in general, there was considerable discussion on measures to improve the mechanism for dispute resolution in tax matters. The Hon'ble Minister requested for proposals which could expedite the dispute resolution process. He assured that these would be included in the draft of the GST Bill. Subsequently, these could be considered for adoption in the Direct Taxes laws also.

In another important meeting, a delegation led by Mr. Harsh Mariwala, Chairman, FICCI's Task Force on GST, appeared before the Select Committee of Rajya Sabha on GST on 25th June, 2015 in Mumbai and placed before it FICCI's concerns arising from the Constitution (122nd Amendment) Bill, 2014 relating to GST.

On the taxation regime, the Delhi Tribunal in the case of Aspect Software Inc. held that the receipts from supply of 'contact solutions' comprising sale of hardware and license of embedded software is not royalty under Article 12 of the India USA treaty. The Tribunal noted that the payment was for a copyrighted article and represents the purchase price of an article and therefore, such payment is not in the nature of royalty. Further, the 'implementation service' is inextricably and essentially linked to the supply of software and does not make available any technical knowledge, experience, etc. and therefore, these services are not taxable as 'fees for included services' under the tax treaty. It was further held that the taxpayer does not carry on business in India through a building site or construction and consequently, there is no 'installation permanent establishment' of the taxpayer in India.

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 Decision

Income earned from investment made in shares through a Portfolio Management Scheme is capital gains and not business income

The taxpayer is engaged in the business of finance and films. During the assessment years 2006-07 and 2008-09, the taxpayer had invested money in shares through the Portfolio Management Scheme (PMS) of Kotak Securities Limited. Since there were regular transactions of sale and purchase of shares, the AO held the same to be 'business income'. However, the taxpayer claimed that income from sale of shares has to be treated as capital gains, instead of business income.

The Karnataka High Court relied on the decision of Delhi High Court in the case of Radials International v. ACIT [2014] 367 ITR 1 (Del) where it has been held that employment of PMS for investment in shares could not be treated as business income. The Karnataka High Court held that investment through PMS, which may deal with the shares of the taxpayer so as to derive maximum profits, cannot be termed as business of the taxpayer. It would only be a case of a more careful and prudent mode of investment, which has been undertaken by the taxpayer. Funds which lie with the taxpayer can always be invested (for earning higher returns) in the shares either directly or through a professionally managed PMS and by doing so, it would not mean that the taxpayer is carrying on the business of investment in shares.

The High Court observed that profits from such investment, either directly or through a professionally managed firm, would still remain as profits to be taxed as capital gains as the same will not change the nature of investment, which is in shares, and the law permits it to be taxed as capital gains and not as business income. The Act does not prohibit the taxpayer from making investments in capital assets after using borrowed funds. The Tribunal has also considered this aspect of the matter and decided in favour of the taxpayer. Relying on the CBDT Circular No.4 dated 15 June 2007, the High Court held that the findings of the Tribunal are in conformity with the guidelines issued by the said Circular.

CIT v. Kapur Investments (P) Ltd. (ITA No. 158/2014, ITA NO.159/2014) - Taxsutra.com

Tribunal Decision

Disallowance under Section 40(a)(i) of the Act is not applicable on purchases made by non-resident Associated Enterprises as per the non-discrimination clause under the India-Japan tax treaty

The taxpayer, an Indian company, is a wholly owned subsidiary of Mitsubishi Corporation, Japan which a general is trading company headquartered in Tokyo. During the Assessment Year (AY) 2010-11, the taxpayer made a payment for purchase of goods from its Associated Enterprises (AEs). The Assessing Officer (AO) held that the taxpayer was required to deduct tax at source on the payment made to the AEs under the provisions of Section 195 of the Income-tax Act, 1961 (the Act). Having not deducted tax, the AO made a disallowance under Section 40(a) (i) of the Act.

The Delhi Tribunal held that in order to invoke the provisions of Section 40(a)(i) of the Act, it is essential that the amount payable by the taxpayer to a foreign company should be chargeable to tax in the hands of such foreign company. Following the earlier decision of the Tribunal, the Delhi Tribunal in the present case held that AEs did not have any Permanent Establishment (PE) in India. Therefore, the offshore sales made by them to the taxpayer in India would not generate any income chargeable under the Act.

The Tribunal observed that the non-resident is entitled to the benefit of Article 24(3) of the India-Japan tax treaty since there is no provision under Chapter XVII-B of the Act which stipulates deduction of tax at source from payment for the purchases made from an Indian resident. On comparison of an Indian enterprise purchasing goods from an Indian party vis-à-vis from a Japanese party, there is discrimination in terms of disallowance of purchase consideration under Section 40(a)(i) in so far as the purchases from a Japanese enterprise are concerned.

The Tribunal observed that the provisions of Article 24(3) shall be restricted to the extent of applicability of Article 9 of the tax treaty. Whatever has been provided in Article 91 of the tax treaty shall remain intact and will have a superseding effect over the mandate of Article 24(3) of the tax treaty. It does not render Article 24(3) redundant in totality. A conjoint reading of these two Articles brings out that if there is some discrimination in computing the taxable income in regards to the substance of Article 9, then such discrimination will continue as such. But, in so far as rest of the discriminations covered under Article 24(3), those will be removed to the extent as provided.

Disallowance under Section 40(a)(i) is an independent component of the computation of total income which is distinct from any transfer pricing adjustment. Article 24 read with Article 9 prohibits the deletion of enhancement of income due to execution of transactions at Arm's Length Price (ALP), but permits the deletion of enhancement of income due to the disallowance under Section 40(a)(i) of the Act. The Transfer Pricing Officer (TPO) has not proposed any transfer pricing adjustment in respect of the 'trading segment' of the taxpayer under which the purchases in question were made.

Accordingly, it has been held that the taxpayer is entitled to the benefit of Article 24 of the tax treaty and disallowance cannot be made under Section 40(a)(i) of the Act.

Mitsubishi Corporation India Private Limited v. DCIT (ITA No.945/Del/2915)

Receipts from supply of 'contact solutions' comprising sale of hardware and license of embedded software is not royalty under Article 12 of the India-USA tax treaty

The taxpayer is a corporation incorporated in USA and is engaged in the business of provision of hardware, software and rendering of support services that enable call centre companies to better manage customer interactions via voice, email, web and fax. The taxpayer derives its revenue primarily from supply of 'contact solutions', software license and provision of services including, installation, maintenance and professional services. The taxpayer has two subsidiaries in India, one of them being Aspect Contact Center Software India Private Limited (Aspect India) which is involved in the business of installation of equipment and providing marketing support to the taxpayer. For the year under appeal, the taxpayer earned revenues from Indian customers on account of licensing of software i.e. 'contact solution', sale of hardware, implementation services, maintenance services and professional services.

Supply of software

The Delhi Tribunal observed that all the 'contact solutions' are manufactured in the USA and the supplies are made from outside India to various customers on ex-work/Free on Board basis. Perusal of the agreements of the taxpayer with the end user and also with the channel partner indicates that a product comprising of both hardware and software is sold to the end customer. Further, the taxpayer retains all the intellectual property rights in reference to software and the end user is merely provided with limited right to use the licensed product solely for internal use. The issue is covered in the favour of the taxpayer by the decision of the Delhi High Court in the case of DIT v. Ericsson A.B. [2012] 343 ITR 470 (Del) and DIT v. Nokia Networks OY [2012] 253 CTR 417 (Del). Even where the software is separately licensed without supply of hardware to the end users, the terms of the license agreement are similar to the facts of DIT v. Infrasoft Ltd. [2013] 39 taxmann.com 88 (Del). Accordingly, there was no transfer of any right in respect of copyright by the taxpayer and it was a case of mere transfer of a copyrighted article. Therefore, it is not in the nature of royalty under Article 12 of the India-USA tax treaty. However, the receipts would constitute as business receipts in the hands of the taxpayer and is to be assessed as business income subject to the taxpayer having business connection/PE in India.

Implementation services and maintenance services

In the present case, the implementation service is inextricably and essentially linked to the supply of software. In view of the above decision that the supply of software is not taxable as 'royalty' under the tax treaty, Article 12(4)(a) would not apply to both implementation and maintenance services. Further, the services provided by the taxpayer does not make available to the end user/channel partners any technical knowledge, experience, skill, know-how or processes so as to enable them to apply the said technology. Accordingly, it was held that 'implementation services' do not qualify as fees for included services under the tax treaty.

Attribution of profit

In the case of Convergys Customer Management Group Inc. v. ADIT [2013] 34 taxmann.com 24 (Del), it was held that an overall attribution of profits to the PE is a transfer pricing issue and no further profits can be attributed to a PE once an ALP has been determined for the Indian associate enterprise, which subsumes the functions, assets and risk (FAR) profile of the PE. The above view was expressed by the Delhi Tribunal considering the Central Board of Direct Taxes (CBDT) circular No. 5 of 2004, dated 28 September 2004, various decisions and the OECD guidelines. Accordingly, where an associated enterprise (which also constitutes a PE) is remunerated on arm's length basis taking into account all the risk taking functions of the multinational enterprise, nothing further would be left to attribute to a PE.

Aspect Software Inc. v. ADIT (ITA Nos. 1124 & 1125/Del/2014 – AY 2004-05 and 2010-11)

Fees paid to an overseas loan-arranger is neither interest nor fees for technical services and therefore, withholding of tax is not applicable

The taxpayer had entered into a 'Term Loan Facility Agreement' with Finnish Export Credit Ltd., who is the lender. HSBC, Hong Kong, had arranged for the loan as an 'arranger' and the U.K. based company, HSBC Bank, PLC acted as a facility agent. Pursuant to the said agreement, the taxpayer was liable to pay arranger's fee to HSBC, Hong Kong. The taxpayer considered the amount as 'interest' and deducted the tax under Section 195 of the Act, while remitting the said amount and deposited the same in the treasury of Government of India. Thereafter, the taxpayer filed an appeal before the Commissioner of Income-tax (Appeals) [CIT(A)] under Section 248 of the Act, contending that the arranger's fee did not fall within the definition of interest under Section 2(28A) of the Act and therefore, such a remittance does not require Tax Deduction at Source (TDS). The CIT(A) held that the payment of arranger fee is not only in the nature of interest but also it is in the nature of fees for technical services under Section 9(1)(vii) of the Act.

The Tribunal observed that perusal of the definition of interest under Section 2(28A) of the Act indicates that the term 'interest' covers firstly, the interest payable in any manner in respect of any money borrowed or debt incurred and, secondly, such interest payable includes any service fee or other charge in respect of the money borrowed or debt incurred or in respect of any credit facility which has not been utilised. However, in the present case the arranger is not the lender and any fee paid to him is not in respect of the borrowing, because no debt has been incurred by the taxpayer in favour of the arranger vis-a-vis the money borrowed. The arranger is merely a facilitator who brings a lender and a borrower together for facilitating the loan/credit facility.

The Tribunal observed that the service fee or other charge does not bring within its ambit any third party or intermediary who has not given any money. The fundamental proposition permeating between various kinds of payments which have been termed as 'interest' in Section 2(28A) of the Act is that, these payments are paid/payable to the lender either for giving loan or for giving the credit facility. Nowhere the definition suggests that payment of interest includes some kind of fee paid to a third party who has not given any loan or any credit facility. The arranger fee paid is not a part of debt or loan payable to the lender but it has been paid for facilitating the loan for the borrower from the lender. The relationship between the borrower and lender is a key factor to bring the payment within the ambit of definition of interest under Section 2(28A) of the Act. The arranger fee may be inextricably linked with the loan or utilisation of loan facility but it is not a part of interest payable in respect of money borrowed or debt incurred, because the relationship of a borrower or a lender is missing.

Though, the fees of an arranger may depend upon the quantum of loan or loan facility arranged but to be included within the meaning of the term ‘interest’, it has to be directly in respect of money borrowed. It is a kind of compensation paid by the borrower to the lender. Thus, an arranger is only an intermediary/third party and accordingly, any fee paid as arranger fee cannot be termed as ‘interest’ under both the limbs of the definition provided under Section 2(28A) of the Act. Therefore, the taxpayer was not liable to deduct tax for such payment, as it does not fall within the ambit of interest.

The Tribunal observed that the term ‘managerial’ essentially implies control, administration and guidance for business and day to day functioning. It includes the act of managing by direction, regulation or superintendence. In the present case, arranging of a loan cannot be equated with lending of managerial services at all. It is also not in the nature of ‘consultancy services’ because the arranger did not provide any advisory or counseling services. The arranger was neither involved in providing control, guidance or administration of the credit facility nor was it involved in day-to-day functioning of the taxpayer in overseeing the utilisation or administration of the credit facility. It was not in charge of the entire or part of the transaction of arranging services, hence, it cannot be termed as managerial or consultancy services within the meaning of Section 9(1)(vii) of the Act. Accordingly, the arranger fee cannot be taxed under Section 9(1)(vii) of the Act and therefore, no tax was deductible at source on such payment.

Idea Cellular Limited v. ADIT (ITA No. 1619/Mum/2011, Assessment Year 2010-11)

Long-term capital loss on sale of shares/units liable to securities transaction tax is allowed to be set-off against long-term capital gain on sale of land

The taxpayer is a pharmaceutical company engaged in manufacturing and sale of pharmaceuticals. For the FY 2006-07, the taxpayer had set-off long-term capital loss on sale of shares and on sale of mutual fund units against the long-term capital gains arising from sale of land. The AO held that the losses claimed cannot be allowed since the income from long-term capital gain on sale of shares and mutual funds are exempt under Section 10(38) of the Act.

The Mumbai Tribunal held that nowhere has any exception been made with regard to long-term capital gain arising on sale of equity shares. The whole genre of income under the head capital gain on transfer of shares is a source, which is taxable under the Act. If the entire source is exempt or is considered as not to be included while computing the total income, then in such a case the profit or loss resulting from such a source does not enter into the computation at all. However, if a part of the source is exempt by virtue of a particular provision of the Act for providing benefit to the taxpayer, then it cannot be held that the entire source will not enter into computation of total income.

Section 10(38) of the Act provides exemption of income only from transfer of long-term equity shares and equity oriented funds and also states certain conditions for exempting such income i.e. payment of securities transaction tax and whether the transaction on sale of such equity share or unit is entered into on or after the date on which chapter VII of Finance (No.2) Act, 2004 comes into force. If such conditions are not fulfilled then exemption is not given. Thus, the income contemplated in Section 10(38) of the Act is only a part of the source of capital gain on shares and only a limited portion of source is treated as exempt and not the entire capital gain (on sale of shares).

The concept of income includes loss which will apply only when the entire source is exempt or is not liable to tax and not in the case where only one of the incomes falling within such source is treated as exempt. Accordingly, the long-term capital loss on sale of shares would be allowed to be set-off against the long-term capital gain on sale of land in accordance with Section 70(3) of the Act.

Raptakos Brett & Co. Ltd. v. DCIT (ITA Nos.3317/Mum/2009 & 1692/Mum/2010; AY: 2007-08)

Transferred manpower from existing units to new special economic zone units does not exceed 50 per cent of total manpower in a new unit and therefore, Section 10A deduction is available to the taxpayer's new units

The taxpayer is engaged in the business of software development both on-site and off-shore. The first unit i.e. BPO undertaking at Noida was found to be eligible for the claim of deduction under Section 10A of the Act, as in the past. The taxpayer had thereafter, established various independent units, which were stated to be operating as new units in respective years. During the year under consideration, the taxpayer had established two undertakings i.e. in Bangalore and Mumbai respectively, which commenced business after the end of the relevant year. The taxpayer claimed that the conditions laid down in Section 10A(2) of the Act were fulfilled in respect of these units and therefore, these were eligible for deduction under Section 10A of the Act. The AO held that, the aforesaid units were formed by splitting and reconstruction of the existing business and therefore, it was not eligible to claim deduction under Section 10A of the Act. The CIT(A) held the decision in favour of the taxpayer.

The Pune Tribunal held that Section 10A(2)(iii) of the Act prohibits formation of new units by way of transfer of previously used plant and machinery to a new unit. However, the explanatory memorandum for the said Section does not express additional objective of employment generation. There is no legal requirement of having certain percentage of new employees in the new unit in Section 10A of the Act. However, the CBDT has clarified vide Circular No.14/2014, dated 8 October 2014 that transfer or re-deployment of technical manpower from the existing units to the new units located at a Special Economic Zone (SEZ) in the first year of commencement of business, shall not construe as splitting up or reconstruction of the existing business, provided the number of technical manpower so transferred at the end of the FY does not exceed 50 per cent of the total technical manpower actually engaged in the development of software or IT enabled projects in the new unit.

The Tribunal observed that in the new unit at Bangalore, the new employees employed were 289 and the transferred employees were 112 i.e. total employees 401, and hence the percentage of transferred employees to the total employees was 27.93 per cent. In respect of Mumbai unit, the new employees totaled to 65 along with transferred employees of 6, resulting in a total of 71 employees and the percentage of transferred employees was 8.45 per cent. Hence, for both the units the transferred employees are well within the parameters laid down by the CBDT Circular No.14/2014. Accordingly, the transfer of old employees to the new units cannot be construed as splitting up or re-construction of existing business.

Further, the taxpayer had also furnished on record the investment made in plant and machinery in both the undertakings where both the units have complied with the conditions prescribed under Section 10A of the Act and are independent and separate undertakings working from different locations with new plant and machinery, having an adequately skilled staff to carry out its operations and are independently viable undertakings earning profits/losses, which are attributable to the business carried on by the taxpayer in the separate units. The said units are eligible to claim deduction under Section 10A of the Act since the same were not formed by splitting up or reconstruction of business already in existence.

iGATE Computers Systems Ltd. v. ACIT (ITA No.2504/PN/2012, ITA No.342/PN/2013; AY 2005-06)

Two enterprises treated as AEs without satisfaction of the deeming fiction set out under Section 92A(2) of the Act

The taxpayer had received service charges/commission charges for making purchase of textile, yarns, etc. on behalf of Kaybee Exim Pte Limited, Singapore (Kaybee, Singapore). During the course of assessment proceedings, the AO observed that the taxpayer and Kaybee, Singapore had a common director, who was also a shareholder of the taxpayer and held a key position i.e. Chief Operating Officer in the management of Kaybee, Singapore. Based on the common directorship and participation in management of both the enterprises, the AO held that the taxpayer and Kaybee, Singapore are AEs. The CIT(A) confirmed the action of the AO; and the taxpayer carried the matter in an appeal before the Tribunal.

The Tribunal observed that the language of Section 92A(1) is unambiguous and does not leave any scope for importing any meaning to the expression ‘AE’. While addressing as to whether the meaning of the expression ‘AE’ as per Section 92A(1) had to be read in conjunction with clauses (a) to (m) of Section 92A(2), the Tribunal held that if the condition provided in clause (a) and (b) of Section 92A(1) are independently satisfied, then the two enterprises for the purpose of Section 92B to 92E of the Act will be treated as AEs. The Tribunal further observed that, sub-section (1) does not begin with a subjective clause i.e. subject to sub-section (2). The Tribunal held that since the said companies had a common director who was also a major shareholder in the taxpayer’s company and held a key position in the management of the other enterprise, the condition of participation in management or control or capital as prescribed under Section 92A(1) was satisfied. Therefore, the said companies qualified as AEs as per the provisions of Section 92(A) of the Act.

Kaybee Private Limited v. ITO (I.T.A. No. 3749/Mum/2014)

Issue of shares is an ‘international transaction’ but not an ‘income chargeable to tax’ warranting the

substitution of such income with income determined on the basis of its arm's length price

During the year, the taxpayer reported an international transactions viz. issue of share capital and applied the Comparable Uncontrolled Price method and concluded that to be at ALP. Having observed that the book value of a share was higher than the issue price per share, the TPO held that such undercharging of the share price would tantamount to a deemed loan for which the taxpayer ought to have been compensated with an appropriate interest by its AEs. The TPO applied the benchmark interest rate of 14 percent on such deemed loan and made a TP adjustment, which was affirmed by the first appellate authority.

The Tribunal observed and held as under:

- To compute the income arising from an international transaction having regard to the ALP, the following two conditions should be satisfied cumulatively: (i) There should be an international transaction; and (ii) Such international transaction should result into income chargeable to tax.

- Based on the provisions of Chapter X of the Act and relying on the judgments of the Bombay High Court in the case of Vodafone India Services Private Limited v. ACIT [2014] 368 ITR 1 (Bom) and Shell India Markets Pvt. Ltd. v. ACIT and Others [2014] 369 ITR 516 (Bom), the Tribunal held that:

  - The transaction of issue of share is an international transaction under Section 92B of the Act, as the same has bearing on the assets of the taxpayer.

  - If an international transaction with its determined ALP does not lead to the generation of any income chargeable to tax, then the provisions of Section 92(1) of the Act are not attracted.

  - Chapter X of the Act does not contain any charging provisions but is a machinery provision and does not change the character of the receipt but only permits re-quantification of income independent of the relationship between the AEs.

  - Since the definition of income does not specifically include any capital receipt arising on issue of share capital, the issue of shares at par or premium is a transaction of capital nature, which would not have an impact on the income of a company.

- An international transaction of capital nature may not lead to generation of any income itself but the resultant transaction may have an impact on the income of the taxpayer which, if is not at arm's length, would invoke and need to satisfy the provisions of Chapter X of the Act.

First Blue Home Finance Ltd.v. ACIT (ITA No. 5460/Del/2011)

Notification & Circulars

The CBDT relaxes norms for wealth-tax refund on 'urban land' post retrospective amendment

Before the amendment of the Finance Act, 2013, Section 2(ea) of the Wealth tax Act

1957, provided that urban land was liable to wealth-tax. This included the land situated in any area which is comprised within the jurisdiction of a municipality or a cantonment board and which has a population of not less than ten thousand or land situated in any area within such distance not being more than eight kilometers from local limits of any municipality or cantonment board as the Central Government may, having regard to specify in the official gazette.

Vide the amendment made in the Finance Act, 2013, the term 'urban land' does not include the land classified as agricultural land in the records of the government and used for agricultural purposes. Accordingly such land stands exempt from wealth tax. This amendment has given effect from 1 April 1993.

With a view to avoid genuine hardship and in exercise of the powers conferred under Section 10(2)(b) of the Wealth tax Act, the CBDT authorizes a Principal Commissioner/Commissioner of Wealth-tax to admit the application for revision from taxpayers seeking a refund due to the aforesaid amendment after the expiry of the period specified under the said section. The Principal Commissioner/ Commissioner of Wealth-tax shall dispose of such application within one year from the end of the FY in which the application is received. However, the Principal Commissioner/Commissioner of Wealth-tax shall not set-aside any order. While disposing the application, the Principal Commissioner/Commissioner of Wealth-tax may for deciding the matter call a report from the AO and seek relevant information from the taxpayer. In case such an order results in a refund, the taxpayer shall be entitled to interest on such a refund at the rate specified in the Act.

The application of refund shall be made within one year from date of issue of this order. After expiry of the said period, no claim shall be admitted.

CBDT Circular No. 11/2015, dated 11 June 2015

BEPS Action Plan 8: Discussion Draft on hard-to-value Intangibles

This Discussion Draft responds to the requirement under Action 8 of the Base Erosion and Profit Shifting (BEPS) Action Plan to develop an approach to determine the ALP of hard-to-value intangibles (HTVI). It explains the difficulties faced by tax administrations in verifying the arm's length basis on which pricing was determined by taxpayers for transactions involving HTVI. The Discussion Draft includes an approach based on the determination of the arm's length pricing arrangements, including any contingent pricing arrangements that would have been made between independent enterprises at the time of the transaction. It specifies conditions that are to be met before the tax administration can make a pricing adjustment to transactions involving transfer of intangibles or rights in intangibles.

As per the discussion draft, the term HTVI are intangibles or rights in intangibles for which, at the time of their transfer in a transaction between AEs (i) no sufficiently reliable comparables exist, and (ii) there is a lack of reliable projections of future cash flows or income expected to be derived from the transferred intangible, or the assumptions used in valuing the intangible are highly uncertain. The discussion draft also lays down certain features that HTVI may exhibit.

The discussion draft states that pricing adjustments may be made to the value of intangibles or rights in intangibles in case of HTVI, except where the taxpayer (i) provides full details of its ex-ante projections used at the time of the transfer to determine the pricing arrangements; and (ii) provides satisfactory evidence that any significant difference between the financial projections and actual outcomes is due to unforeseeable or extraordinary developments or events occurring after the determination of the price that could not have been anticipated by the AEs at the time of the transaction.

As a result, although the ex post evidence about financial outcomes provides relevant information for tax administrations to consider the appropriateness of the ex-ante pricing arrangements, in certain circumstances where the taxpayer can satisfactorily demonstrate that the developments leading to the difference between the projections and outcomes arose from unforeseeable events, no adjustment to the ex-ante pricing arrangements based on these special considerations would be justified.

OECD/G20 BEPS Action 8: Public Discussion Draft on BEPS Action 8: Hard-to-value intangibles

BEPS Action Plan 13: Country-by-Country Reporting Implementation Package

In September 2014, OECD under its BEPS Action Plan released a report under Action Point 13 on Transfer Pricing documentation and proposed a 3-tier documentation consisting of Master-file, Local-file and Country-by-Country (CbyC) Report. The CbyC report provides a template for Multinational Enterprises (MNEs) to report annually for each tax jurisdiction in which they do business, the information set out therein. OECD acknowledged that developing countries may require support for the effective implementation of CbyC reporting. In order to provide such support an Implementation Package on CbyC Reporting (CbyC Implementation Package) has been issued on 8 June 2015, that consists of:

Model legislation which could be adopted by countries that require the Ultimate Parent Entity of an MNE group to file the CbyC Report in its jurisdiction of residence including backup filing requirements. The Model legislation provides important definitions; description of the filing obligations; information to be captured in the CbyC report; time limit for filing of the CbyC report; provisions relating to the use and the confidentially of information provided in the CbyC report by the tax administrations; penalties proposed to be prescribed and effective date of the CbyC reporting standard. The Model legislation shall be made effective in all countries post 1 January 2016 (i.e. from the tax year starting on or after 1 January 2016).

Three model Competent Authority Agreements (CAAs) that could be used to facilitate implementation of the exchange of CbyC Reports, respectively based on the a) Multilateral Convention on Administrative Assistance in tax matters, b) bilateral tax conventions and c) Tax Information Exchange Agreements (TIEAs). A template for each of the aforesaid agreement has been provided which may serve as a basis for countries to draft the respective agreements for automatic exchange of information with the other country.

OECD/G20 BEPS Action 13: Country-by-Country Reporting Implementation Package

CBDT issues FAQs on APA Rollback Provisions

The CBDT introduced the rollback rules under the Advance Pricing Agreement (APA) programme on 14 March 2015. On 10 June 2015, the CBDT issued Frequently Asked Questions (FAQs) on the APA rollback provisions clarifying certain issues. Some important clarifications have been briefly explained herein below:

Return of income - Rollback provisions will be available for APA applicants who have revised their returns but will not be available in case of belated returns.

Same international transaction - The term 'same international transaction' implies that the transaction in the rollback year has to be of the same nature and undertaken with the same AEs, as proposed to be undertaken in the future years and in respect of which APA has been reached. Rollback provisions would apply only if the FAR analysis of the rollback year does not differ materially from the FAR validated for the purpose of reaching an APA in respect of international transactions to be undertaken in the future years.

Rollback years - The applicant has to either apply for a rollback for all the four years or not apply at all. An APA applicant does not have the option to choose any specific year/s for rollback. However, if the covered international transaction/s did not exist or there is some other disqualification due to which rollback cannot be claimed, then the applicant can apply for rollback for less than four years.

Appeal before the tax authorities - The rollback provisions would not be applicable for an international transaction for which the Tribunal passed an order disposing of an appeal. However, if the Tribunal has only set aside the order for fresh consideration by the lower authorities with 'full discretion' at their disposal, the matter shall not be treated as one having reached finality and rollback provisions would be applicable.

Cancellation of APA - If the applicant does not carry out any actions prescribed under rollback rules for any of the rollback years, the entire APA shall be cancelled.

Mutual Agreement Procedure (MAP) applications - If MAP has been concluded for any of the international transactions in any of the rollback year under APA, rollback provisions would not be allowed for those international transactions for that year but could be allowed for other years or for other international transactions for that year, subject to fulfillment of prescribed conditions. However, if MAP request is pending for any of the rollback years under APA, the APA applicant can exercise an option, to pursue MAP or the rollback application.

Determination of ALP - The manner of determination of ALP has to be the same and in line with the APA signed by the taxpayer in all years, however the ALP may be different.

Withdrawal of rollback application - The applicant has an option to withdraw its roll back application even while maintaining the main APA application for the future years. However, it is not possible to accept the rollback results without accepting the APA for the future years.

CBDT Circular No. 10/2015 issued by CBDT

Employees' Provident Fund Organisation to deduct income tax on Provident Fund withdrawals

The Finance Act, 2015 has inserted a new provision (Section 192A) on payment of Provident Fund (PF) accumulation due to an employee. Consequently, the Employees' Provident Fund Organisation (EPFO) has now issued a circular to its field officials for deducting tax at the time of payment of accumulated provident fund balance due to an employee.

As per the new provisions, income tax will be deducted at source at the time of withdrawal of accumulated PF balance, where the withdrawal amount is more than or equal to INR30, 000 and the services are for a period of less than five years:

- TDS will be at the rate of 10 per cent if a Permanent Account Number (PAN) is submitted. No TDS in case Form 15G or 15H is submitted with PAN by the member.
- TDS will be at the maximum marginal rate if a member fails to submit PAN. As per the EPFO circular, tax at source will not be deducted in respect of the following cases:
    - Transfer of PF from one account to another PF account.
    - Termination of service due to ill health of a member, discontinuation/ contraction of business by employer, completion of project or other cause beyond the control of the member.
    - If employee withdraws PF after a period of five years of continuous service, including service with former employer.
    - If PF withdrawal is less than INR30,000.
    - If member submits Form 15G/15H along with their PAN.

The amendment in relation to PF withdrawals is expected to have significant implications for employees (including International Workers) who are withdrawing their provident fund balance. TDS will be levied by the PF office unless documents/details are provided to prove otherwise.

Source: www.epfindia.com

Simplified income tax return forms proposed for assessment year 2015-16

The Government of India (GOI) has proposed to simplify the Income Tax Return (ITR) forms for the tax year 2014-15 (AY 2015-16) which were earlier notified by CBDT on 15 April 2015.

In view of various representations, the ITR forms were kept on hold. Having considered the responses received from various stakeholders, these forms are proposed to be simplified. Some of the key changes are as follows:

- Individuals having exempt income without any ceiling (other than agricultural income exceeding INR5,000) can now file ITR-1 (Sahaj). Similar simplification is also proposed for individuals/HUF in respect of ITR-4S (Sugam).

- A new ITR-2A is proposed which can be filed by an individual or HUF having income from more than one house property but who does not have capital gains, income from business/ profession or foreign asset/foreign income.

- In lieu of foreign travel details, it is now proposed that only passport number would be required to be given in ITR-2 and ITR-2A. The details of foreign trips or expenditure thereon are not required to be furnished.

- Only the IFSC code and account number of all the current/savings account which were held at any time during the previous year will be required to be filled up. The details of dormant accounts which were not operational during the last three years are not required to be furnished.

- An individual who is not an Indian citizen and is in India on a business, employment or student visa (expatriate), would not mandatorily be required to report the foreign assets acquired by him/her during the previous years in which he was a non-resident, if no income is derived from such assets during the relevant previous year.

- The time limit for filing these returns is also proposed to be extended to 31 August, 2015 and a separate notification will be issued for the same.

Source: www.incometaxindia.gov.in

II. SERVICE TAX

Recent Case laws

High Court Decision

Applicability of mandatory pre-deposit of 7.5 per cent to the adjudication order passed before the date of amendment of Section 35F

In the present case, the Tribunal had rejected the appeal and stay application, on the ground that the taxpayer had not made a deposit equivalent to 7.5 per cent of the confirmed duty liability even though the appeal was filed after the amendment of Section 35F of the Central Excise Act, 1944. Aggrieved by the same, the taxpayer filed a writ petition before the High Court.

The Ahmedabad High Court mentioned that the taxpayer needs to comply with the amended provisions since, the amended provisions would apply to all the appeals which are filed, after the amended Act coming into force and the appeal of the taxpayer before the Tribunal would not be maintainable in the absence of a deposit of an amount equivalent to 7.5 per cent of the confirmed amount of duty liability. Hence, the writ petition was dismissed.

Premier Polyspin Pvt Ltd v. UOI (2015-TIOL-1265-HC-AHM-CX)

Seismic survey for oil company pure 'service'; not 'works contract', in absence of equipment transfer

In the present case, the taxpayer had entered into a contract with Jubilant Oil and Gas Pvt. Ltd. (Jubilant), which is engaged in oil exploration, to provide 2D seismic data acquisition and basic processing services in the state of Tripura. The sales tax registration certificate granted to the taxpayer described the nature of business as works contract. Consequently, treating the contract as a works contract, Jubilant had made deductions from the payments made to the taxpayer. The taxpayer demanded a refund of tax wrongly deducted by Jubilant as they were paying service tax on this activity considering the same as pure service but the same was rejected by the sales tax authorities. Aggrieved by the same, the taxpayer filed a writ before the High Court of Tripura.

The issue before the High Court was whether the services rendered by the taxpayer were in the nature of works contract and whether the equipment brought in by the taxpayer to carry out the surveys had been transferred to Jubilant, resulting in 'sale'.

The High Court observed that as per the contract, there was no transfer of any property. Further, the taxpayer remained in exclusive possession and control of the equipment and all the resources supplied. The High Court also, contended that the Revenue had also failed to point out any stipulation in the contract which indicated that there was any transfer of right to use property. Hence, it is apparent that the contract is not in nature of a works contract as only a survey was carried out and there has been no transfer of any property.

Given the above, the High Court concluded that the taxpayer was only rendering services and accordingly, the writ petition was allowed.

Asian Oilfield Services & Others v. the State of Tripura & Others [TS-264-HC-2015(TRI)-VAT]

Tribunal Decision

Web-based services of storing photographs and images for viewing and downloading for commercial use qualifies as online database and access retrieval services

In the instant case, the issue was whether the activity of allowing free-of-cost viewing of photographs and images on the monitor and downloading the same for further commercial use, would be covered under the service category of 'Online information and data base access or retrieval service'.

The Mumbai Tribunal held that the activity of the taxpayer qualifies as 'online information and data base access or retrieval services' since the main activity was to make digital content (i.e. images) available for retrieval and the copyright on the said images was incidental. The Tribunal has placed reliance on the decision of the Delhi High Court in ITA v. Alcatel Lucent Canada decided on 27 February 2015 and mentioned that the large collection of photographs may be copyrightable but the consideration is paid for access and retrieval to such photographs by the customer.

Photo library India Pvt. Ltd. v. Commissioner of Service Tax (2015-VIL-259-CESTAT-MUM-ST)

Amount retained as payment of royalty for use of brand name and technical knowhow in a job-work arrangement (for manufacture of Indian Made Foreign Liquor) is not liable to service tax

In the instant case, the issue was whether service tax is payable on the amount retained by the taxpayer as consideration paid by the job-worker for using the brand name and technical know-how of the taxpayer in the process of manufacture and sale of Indian Made Foreign Liquor (IMFL). The Delhi Tribunal held that mere inclusion of the clause on royalty in the agreement of manufacture and sale of IMFL does not mean that the taxpayer had been given the right to use its brand name to the job-worker for their use. The taxpayer is the brand owner of IMFL and the job worker manufactured IMFL on behalf of the taxpayer and the amount retained by the taxpayer is the business profit and therefore, the same would not be liable to service tax.

BDA Pvt. Ltd. v. Commissioner of Central Excise (2015-VIL-288-CESTAT-DEL-ST)

Permission for storage of goods outside the factory premises for exceptional circumstances only

In the present case, under Rule 4(4) of Central Excise Rules, 2002 [Rule 4(4)], the taxpayer requested to grant permission to store excisable goods outside the factory premises without payment of duty. The Commissioner after considering various submissions, rejected the request on the ground that the period for which taxpayer was asking for storing the goods is not a few days or a few months but a period of two years. It was further submitted that the said Rule 4(4) covers the situation of exceptional nature. Rule 4(4) cannot be used to create the depot outside the factory and store the goods without payment of duty.

In this regard, the Mumbai Tribunal observed that exceptional circumstances undoubtedly would imply a temporary and brief period and upheld the reasoning given by the Commissioner and rejected the request.

GKN Sinter Metals P Ltd v. CCE (2015-TIOL-990-CESTATMUM)

VAT is not leviable on an element of service tax charged in the invoices

The taxpayer, hoteliers, running business in restaurants, convention centre and banquet hall paid tax on sale of food, liquor, etc. The Assistant Commissioner passed an order confirming levy of VAT on service tax collected and on sale of liquor. The taxpayer preferred an appeal before the Appellate Deputy Commissioner, which was partly remanded and partly the appeal was dismissed. Aggrieved by the same, the taxpayer filed an appeal before the Tribunal.

The Tribunal contended that the payment of service tax as well as VAT are mutually exclusive. Both the levies should be applicable having regard to the respective parameters of service and sale as envisaged in a contract. Also, the service charges collected under the Finance Act and paid to the respective department under statutory obligation, neither do they form a part of the turnover and nor does it constitute the turnover. Further, the Tribunal placed reliance on various judicial pronouncements wherein it has been held that the service tax collected on value of services rendered relatable to value of goods is eligible for deduction for quantifying the liability of VAT.

In view of the above, the Tribunal allowed the appeal filed by the taxpayer and set aside the levy of VAT on service tax collection.

Cyberabad Convention Centre Pvt. Ltd. v. The State of Andhra Pradesh [T.A. No. 139/2013]

Notification & Circulars

Services tax exemption to services provided under the Power System Development Fund Scheme of the Ministry of Power

Services provided by way of re-gasification of liquefied natural gas imported by the Gas Authority of India Limited and transportation of the incremental re-gasified liquefied natural gas to specified power generating companies or plants under the Power System Development Fund Scheme of the Ministry of Power, have been exempted from service tax (subject to fulfillment of prescribed conditions).

Notification No.17/2015-ST, dated 19 May 2015

Rate of service tax clarified on restaurant service

The Central Board of Excise and Customs (CBEC) has clarified that with the increase in the service tax rate from 12.36 to 14 per cent, the effective rate of service tax on services provided in relation to serving of food or beverages by a restaurant, eating joint or a mess, having the facility of air-conditioning or central air-heating in any part of the establishment, has increased to 5.6 per cent (i.e.14 per cent of 40 per cent) of the total amount charged.

Further, the service tax exemption on services provided in relation to serving of food or beverages by a restaurant, eating joint or a mess, other than those having the facility of air-conditioning or central air-heating in any part of the establishment, would continue.

Circular No. 184/3/2015-ST, dated 3 June 2015

Exempted services – in regard to CENVAT credit reversal amount payable hiked to 7 per cent

With effect from 1 June 2015, under Rule 6(3)(i) of CENVAT Credit Rules, 2004 in situations, where the manufacturer of goods or the provider of output service, does not opt to maintain separate accounts, the reversal rate has been increased from 6 to 7 per cent.

Notification 14/2015 – CE (NT) dated 19 May 2015

Dispensing with Statutory Declaration Form (SDF) form

For the purpose to enhance the ease of doing business, the Reserve Bank of India (RBI) has recently dispensed with the SDF in case of exports taking place through the Electronic Data Interchange (EDI) ports. Consequently, RBI has desired that the declaration of Foreign Exchange remittance may be made as a part of Shipping Bill.

Board has issued Notification 46/2015-Customs (N.T.), dated 18 May 2015 to incorporate the following declaration -'I/ We undertake to abide by provisions of Foreign Exchange Management Act, 1999, as amended from time to time, including realisation/repatriation of foreign exchange to/from India.' in lieu of SDF Form in the Shipping Bill.