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tax scout

Tax Scout | July - September, 2020

Main Stories

Dear Readers,

We are back with our regular update on direct and indirect taxes, detailing key decisions and legislative changes that took place in the quarter ending September 30, 2020.

Though the COVID-19 pandemic continues to spread across the country, the Centre as well as the States have now lifted most of the restrictions, allowing businesses to start operations at sub-optimal capacities. To enable businesses to overcome this unprecedented crisis, several concessions and relaxations have been granted to them. However, with the end of this crisis nowhere in sight, everybody is cautiously treading the path.

In the cover story of this edition of Tax Scout, we have discussed an extremely significant and momentous decision by the Government involving the introduction of faceless assessments and faceless appeal system. While the proof of the pudding shall be in the eating, both tax administrators as well as the taxpayers have to transform into their new improved versions to do justice to a very significant decision aimed at reducing corruption and increase efficiency among the tax administration. With both assessment and appellate system becoming faceless, it is going to be extremely challenging for both sides to come up with their own points of view and justifications. One hopes that this decision will herald a new mindset among tax administrators to view the situation objectively. If the exercise is undertaken every year by different officers, who may not be willing to follow the same path as their predecessors, it may help reduce the volume of pending litigations. Our cover story attempts to bring out some of these pertinent facts.

In addition, we have also dealt with other important developments and judicial precedents in the field of taxation.

We hope you find the newsletter informative and insightful. Please do send us your comments and feedback at cam.publications@cyrilshroff.com.

Regards,
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India's leading law firm

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NO NEED TO FACE TAX AUTHORITIES - WELCOME TO THE FACELESS REGIME

The Modi Government 2.0 has been striving to move towards a non-adversarial tax regime. Time and again the Hon'ble Prime Minister has outlined the intention to move towards a transparent taxation system and a non-adversarial tax regime. Towards this end, to reduce the physical interaction between the taxpayer and the IRA, the transparent taxation portal and faceless assessment scheme ("**Scheme**") was launched on August 14, 2020 via video conferencing. It is trite to mention that assessment proceedings undertaken by IRA under the IT Act form an important part of the overall taxation system as it helps to ensure that assessees have not understated their income and their respective tax liabilities have been correctly determined in their income tax returns and discharged by way of advance tax , TDS and self-assessment tax. Even though only a select number of cases are picked up for scrutiny by the IRA each year, it is important that such proceedings are carried out as efficiently as possible. Thus, the introduction of the Scheme marks a phenomenal overhaul to the process of conducting the assessment proceedings under the IT Act. The optimum utilisation of the limited resources by the IRA and completion of the assessment proceedings efficiently has also been at the centre of the Scheme introduced recently. This was emphasised in the speech of the Hon'ble FM, Ms. Sitharaman, where she upheld the dynamic jurisdiction, team-centric assessments and speedy completion of the proceedings. In this cover story, we trace the history of the efforts made by the Government to move towards a faceless transparent taxation system and discuss the features of the schemes announced in relation to conduct of various procedures under the IT Act through the transparent taxation portal.

Key initiatives for improvement in conduct of assessment proceedings

A valuable step in this direction was taken when a pilot project for *Paperless Assessment Proceedings*[1] was launched in select metro cities on October 19, 2015 for non-corporate assessees, thus allowing email correspondence to become the new mode of interaction between the AOs and the assessees for conducting the assessment proceedings. This pilot project was allowed only on voluntary basis i.e. with the consent of the assessees. Later in May 2016, the project was extended to two more cities (i.e. Hyderabad and Kolkata). In 2018, the CBDT extended the pilot project to few other cities and issued various guidelines to ensure secured transmission of electronic communication and interaction between the IRA and the assessees.

The erstwhile Hon'ble Finance Minister, Mr. Arun Jaitley, made a significant announcement in the budget speech for 2018 that e-assessment proceedings would be rolled out across the country to eliminate person to person contact. The Finance Act 2018 brought about amendments to the provisions of the IT Act by inserting three new sub-sections in Section 143 of IT Act, enabling the Government to notify a scheme for this purpose. The provisions of Section 143 (3A) of the IT Act thus paved way for notifying any scheme for assessment to impact greater transparency, efficiency and accountability by: (a) eliminating interactions between the taxpayer and the IRA in the course of the proceeding to the extent technologically feasible; (b) optimising utilisation of the resources through economies of scale and functional specialisations; and (c) introducing a team-based assessment with dynamic jurisdiction.

Further, the CBDT *vide* Instruction[2] dated August 20, 2018, made it mandatory to conduct the assessment proceedings for the FY 2018-19 under Section 143(3) of IT Act electronically. Until this point, this process was voluntary, subject to certain exceptions

1 CBDT F No. 225/267/2015-ITA-II dated October 19, 2015.
2 CBDT Instruction No. 3/ 2018 dated August 20, 2018.

such as in case of set-aside assessments, search and seizure cases, etc.

Thereafter, the announcement to launch a scheme for faceless assessment *vide* electronic medium was done during the 2019 budget speech. Finally, on September 12, 2019, the CBDT introduced the *E-Assessment Scheme, 2019 vide* a separate notification,[3] which contained elaborate provisions as to how the assessment proceedings would be carried out under the faceless regime.

E-Assessment Scheme 2019

As per the said scheme, all communications with the assessee had to be routed through a communication centre which would allot cases to various assessment units *via* an automated allocation system (determined by artificial intelligence and machine learning-based advanced algorithm). For this purpose, the E-Assessment Scheme 2019 envisaged the setting up of:

a. A National e-Assessment Centre ("**NeAC**") at New Delhi to serve as a Central cell for communication and allocation of cases, and

b. Regional e-Assessment Centre(s) ("**ReAC**") which are basically regional centres containing various units to undertake different functions such as:

Assessment units ("AU"): for undertaking the assessment proceedings including identifying issues for determination of liability and seeking information and clarification on the basis of material shared by the assessee

- **Verification units ("VU"):** for conducting enquiries or verification or examination of books of accounts or witnesses etc
- **Technical units ("TU"):** for providing technical assistance including from a legal, accounting, forensic, information technology, valuation, transfer pricing, data analytics, management or from any other technical perspective
- **Review units ("RU"):** for conducting review of draft assessment orders including identifying whether the relevant and material evidence has been brought on record; whether the relevant points of fact and law have been duly incorporated in the draft order; whether the draft order had discussed issues on which addition or disallowance should be made; whether the applicable judicial decisions have been considered and dealt with in the draft order; checking for arithmetical correctness of modifications proposed basis material available on record and applicable laws.

It may be noted that the aforesaid scheme has now been named as *Faceless Assessment Scheme, 2019* with effect from August 13, 2020 vide CBDT Notification of same date and some changes were also brought in the scheme *vide* aforesaid notification.

Proceedings covered under the Faceless Assessment Scheme 2019 (erstwhile E-assessment Scheme 2019)

As per CBDT notification dated September 12, 2019[4] *vide* which *e-E-Assessment Scheme, 2019* was first introduced, it was only meant to cover assessment of total income or loss of the assessee under Section 143(3) of IT Act.

Thereafter, when the scheme was modified w.e.f. August 13, 2020, it was also made applicable to best judgment assessments under Section 144 of IT Act. In this regard, it may be noted that the Scheme, as modified, stipulates that in case an assessee fails to comply with a notice issued by NeAC for furnishing any information/ documents/evidence, or a notice issued under Section 142(1) to furnish return of income or such other documents as may be required, or with a direction issued under Section 142(2A) of IT Act to get its accounts audited by an accountant as specified in the IT Act, the NeAC shall serve a notice to the assessee under Section 144, providing an opportunity to show cause why proceedings should not be completed to the best of its judgment. In case an assessee fails to respond to such notice, NeAC shall intimate such failure to the relevant AU, which would proceed to pass an order to the best of its judgment.

Further, the modified E-assessment Scheme also provides an option to an assessee or any other person, to whom a notice is issued by NeAC, to furnish any information/ documents/ evidence or under Section 144 of IT Act for best judgment assessment or to show cause where modification is proposed by RU, to apply for extension of time in furnishing of reply to NeAC by filing an application with NeAC in this regard.

Also, under the initial scheme, NeAC could at any stage of the assessment, if considered necessary, transfer a case to the AO having a jurisdiction over it. But under the modified scheme, it is the Principal Chief Commissioner or the Principal Director General in charge of NeAC who can transfer a case to the jurisdictional AO with the prior approval of the CBDT.

It may be noted that on August 13, 2020, the CBDT had passed an order under Section 119 of IT Act saying all assessment orders would henceforth be passed by NeAC except for central charges (such as search and seizure cases) and international tax matters; and orders not passed in accordance with the Scheme would be considered null and *void ab initio*.

Scope of faceless proceedings further expanded vide Taxation and Other Laws (Relaxation and Amendment of Certain Provisions) Act 2020

Subsequent to the above, it may be noted that Taxation and Other Laws (Relaxation and Amendment of Certain Provisions) Act, 2020 ("**Amendment Act, 2020**") received the assent of the President and was enacted on September 29, 2020. The Amendment Act, 2020 has further extended the overall scope of

3 CBDT Notification No. 61/ 2019 dated September 12, 2019.
4 CBDT Notification No. 61/ 2019 dated September 12, 2019.

carrying out faceless proceedings to other processes under the IT Act as well.

Under the amended provisions, the Government has been empowered to notify a scheme so that IRA may carry on its various functions or exercise its powers under the IT Act in a faceless manner such that it can collect information under Sections 133, 133B or 133C or exercise its powers to inspect or conduct an enquiry under Sections 134 or 135 or make reference to a Valuation Officer under Section 142A or issue notice under Section 148 or carry out reassessment proceedings under Section 147 or rectification proceedings under Section 154 or perform its functions for collection or recovery of taxes such as nil/low withholding tax certificate under Section 197 or assess in-default proceedings under Section 201 or 206C etc., or conduct revision proceedings under Section 263 or 264 of IT Act. The wide powers conferred on the Government also enables it to notify a scheme for granting any approval or registration under the provisions of IT Act in a faceless manner.

In addition, *vide* Amendment Act, 2020, the Government has also been empowered to notify a faceless scheme so that the proceedings before the TPO under Section 92CA for the purposes of determination of arm's length price may be carried out in a faceless manner. The power to notify the scheme for conduct of proceedings in faceless manner has also been extended to proceedings before DRP, enabling it to issue directions under Section 144C[5] of IT Act in a faceless manner.

The Amendment Act, 2020, has also introduced a new Section 144B in the IT Act to administer the Scheme. As per Section 144B(2) of IT Act, faceless assessment would be applicable in respect of such territorial area, or persons or class of persons, or incomes or class of incomes, or cases or class of cases as may be specified by the CBDT, though these are yet to be notified. Section 144B(9) of IT Act also provides that any assessment under Section 143(3) or Section 144 of IT Act covered under Section 144B(2) of IT Act after March 31, 2021 shall be considered non-est if not made in accordance with this provision.

It may be appreciated that the provisions herein cover the proceedings before the DRP as well. The directions passed by the DRP after adjudicating the objections raised before it shall be forwarded by National Faceless Assessment Centre to the concerned AU. The AU will then pass draft assessment order in accordance with the DRP's directions and send it to National Faceless Assessment Centre, which will send it to the assessee.

Procedure for conduct of faceless assessment proceedings

1. NeAC shall issue notice on assessee under Section 143(2) specifying the issues for selection of its case for assessment.

2. Assessee may file response with NeAC within 15 days from receipt of notice.

3. NeAC shall assignt the case to a specific AU in a ReAC through an automated allocation system.

ReAC may request the NeAC for:
a. obtaining further information/ documents/ evidence from assessee or any other person, or
b. conducting enquiry or verification through VU, or
c. seeking technical assistance from TU.

4. **In response to the above, NeAC shall:**
a. issue notice to assessee or any other person for obtaining information requisitioned by AU and share response received with AU. In case no response is received, NeAC shall issue notice under section 144 of IT Act for best judgement assessment and intimate the ReAC if still no response is received, or
b. assign a VU in a ReAC through an automated allocation system and share its report with AU, or
c. assign a TU in a ReAC through an automated allocation system and share its report with AU.

5. Basis material on record, AU shall prepare draft assessment order or order to the best of its judgement in case no reply is received, under Section 144 of IT Act, and send the order to NeAC along-with details for initation of penalty proceedings, if any

6. **NeAC shall analyse the draft order using automated examination tools and it may:**
   a. serve the final order on assessee, or
   b. In case modification is proposed in draft order, issue show cause notice ("SCN") to assessee and serve final order on assessee basis revised draft assessment order of AU, passed after considering assessee's response to SCN. In case no response received, NeAC shall follow step a above, or
   c. Assign the case to a RU in a ReAC through an automated allocation system who will either concur with draft order, or suggest modifications to NeAC. In case RU suggests a modification, NeAC will assign the case to another AU (other than present AU) who will consider the modification and send final draft order to NeAC. In either case, NeAC will then follow step a or b above, as applicable.

7. NeAC shall transfer all electronic records to jurisidctional AO after completion of assessment.

It may be noted that in case modification is proposed in the revised draft assessment order of AU referred to in point b in step 6 above, based on assessee's response to SCN, and if such order is prejudicial to the interest of the assessee, NeAC shall provide an opportunity to the assessee to file a response by serving a SCN to him and the AU shall prepare the revised draft assessment order, basis response received from the assessee. It may also be noted that the procedure as specified in point c of step 6 above, with respect to assigning of case to another AU (other than the present AU), which will consider the modification proposed by RU and prepare the final draft order, was made part of the Scheme w.e.f. August 13, 2020.

Also, an appeal against an assessment order passed by NeAC shall lie before the CIT(A) having jurisdiction over the jurisdictional AO.

Appraisal of the scheme

Brings in transparency

As the assessment cases would get allocated to the respective AUs through an automated allocation system, the present Scheme is a marked improvement from the earlier paperless assessment scheme where the concerned AO remained the same and only the proceedings were conducted online.

Faceless assessment seeks to make the entire process transparent and convenient for the assessees with the use of latest technologies. It reduces the possibilities of any undue demands or harassment of honest assessees by the IRA.

Brings in an efficient regime for collection of taxes and curbs corrupt practices

Under the conventional assessment system, it would sometimes happen that hearings in a proceeding would be fixed at frequent intervals as a routine, even though there was no relevant discussion or any progress being made during the course of such hearings. The new scheme would curtail the scope of any such practices and save the precious time and resources of the assessee and the IRA making the assessment process more efficient. It would also prevent any corrupt practices from being employed by the AO or the assessee, and the assessment proceedings would be carried on as fairly and objectively as they should be.

Proper implementation is key to success of the new scheme

1. *Tax officers need proper training and guidance*

   While it is easier to look at only the bright side of the new scheme, it is important to realise that proper implementation is the key to the success of such kind of initiative. For this purpose, it is very important that adequate training and continuous guidance be provided to the tax officials carrying out the assessment proceedings.

   A face to face assessment, as was carried on under the previous regime, allowed a tax officer to interact directly with the concerned representative of an assessee, and it helped him to gain useful insight into the case and understand the complex functioning and the voluminous book-keeping or documents of various assessees in comparatively short amount of time.

Therefore, an assessment or an addition/disallowance was usually made on the basis of a proper understanding of the facts of the case. However, a faceless assessment might prove to be a bit challenging as the AOs would need to allocate proper time in order to understand a particular case. In some cases, the AO may not be able to understand the entire factual position by merely perusing the submissions. The IRA would need to ensure that the units are adequately trained to go through the submission online, without having to interact with the taxpayer directly.

2. *Submissions filed before AO need to be clear, concise and systematically arranged*

   In the absence of any face to face interaction, the AO has to completely rely on the submissions filed by the assessee to understand a particular matter before him. Going forward, a lot will depend on the quality of the legal and factual submissions filed by the assessees before the IRA. Hence, it is advisable that submissions that need to be filed before the IRA be made clearer and adequately elaborate to convey the strength of the merits of the case to the IRA. If a reference is drawn from the annexed documents for any point, such point should be clearly marked and highlighted in the relevant documents as well.

3. *Difficulty in explaining the complex issues to the AO and TPO*

   It will be difficult for the taxpayer as well as the AOs and TPOs to understand the complex structure and background in specific situations without any face to face meetings. Hence, it is hoped that the authorities would be more pragmatic, abandon the typical conservative approach and recommend additions where they are unable to understand the purpose of the transactions. It may also be difficult for the taxpayer to submit appropriate documentary evidence in the later stages as with every level, the ability to bring out additional evidences would become limited.

4. *Inability to produce appropriate documents electronically*

   It must be kept in mind that the information technology infrastructure ("**IT Infrastructure**") of the Government, though generally very good, is prone to a lot of challenges. It is possible that a lot of taxpayers may face difficulties to upload their respective documents through the IT Infrastructure within the limited timeframe due to technical issues. It is, therefore, advisable that the AO and the TPO be sensitive to the glitches faced by the taxpayers.

Faceless Appeal Scheme, 2020

While an appeal before the first appellate level i.e. at the CIT(A) level was already being filed online through the official income tax portal, the hearings in such matter were being conducted physically. The government in a bid to take the faceless regime forward, announced in the Budget speech on February 1, 2020 that a system of faceless appeal would also be introduced. Amendments to it were also brought by Finance Act 2020, by inserting three new sub-sections in Section 250 of IT Act, enabling the CG to notify a proper scheme for this purpose.

The CBDT has, *vide* a detailed notification[6] dated September 25, 2020, specified the manner in which appeal proceedings before the CIT(A) would be conducted in a faceless manner. The overall mechanism is similar to that of faceless assessment proceedings and has been discussed in detail below.

Under the Faceless Appeal Scheme, 2020, National Faceless Appeal Centre ("**NFAC**") would serve as a central point of communication for all appeals, and it would be responsible for assigning the appeals to specific Appeal Units in Regional Faceless Appeal Centres ("**RFAC**") through an automated allocation system. Hence, there would be no direct interaction of the concerned CIT(A) adjudicating a particular appeal with the appellant or even with the concerned AO/NeAC, from whom any information is sought by him for the adjudication of the appeal.

Procedure for conduct of proceedings under faceless appeal scheme

1. ***For admission or rejection of appeal***

Where appellant has filed a delayed appeal or applied for exemption under section 249(4b) of IT Act w.r.t. non-payment of advance tax.

↓

The Appeal Unit will decide whether there is sufficient cause for condoning delay or whether exemption under section 249(4)(b) of IT Act should be allowed.

↓

The Appeal Unit will intimate the NFAC about its decision of admission or rejection of appeal and NFAC would intimate the appellant.

↓

6 CBDT notification no. 77/2020 dated September 25, 2020.

2. ***For obtaining information from appellant***

The Appeal Unit would need to approach the NFAC.

↓

NFAC would serve a notice either upon the appellant or the NeAC/ AO, as the case may be, as follows:
a. to obtain further information/ documents/ evidence from the appellant.
b. to obtain a report from NeAC/ AO on information filed by the appellant.
c. to direct the NeAC/ AO to make further enquiry u/s 250(4) and file a report.

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Appellant shall furnish his response within specified date and time as referred in the notice or as extended by NFAC on an application being made, which response NFAC would send to the Appeal unit or it would intimate it in case no response is received.

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3. ***In case additional ground of appeal or additional evidence is filed by appellant before NFAC***

NFAC shall send it to NeAC/ AO for providing comments/ its report within the specified time period, which would be shared with the Appeal Unit.

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Appeal Unit shall decide whether omission of additional ground from appeal was wilful or not or whether additional evidence is admissible under Rule 46A of IT Rules.

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In case such additional evidence is admitted, the Appeal Unit shall send a notice to NFAC for issuing notice to NeAC/AO to provide them an opportunity to examine/ cross -examine the evidence filed. Any report of NeAC/AO in this regard would be shared with the Appeal Unit by the NFAC.

↓

In case NeAC/ AO request the NFAC to direct the production of any document or evidence by the appellant or examination of any witness, NFAC shall send such request to Appeal Unit for approval and once approved, Appeal Unit will prepare notice for this purpose and send it to NFAC who will serve it on the appellant.

↓

4. ***In case Appeal Unit intends to enhance an assessment or a penalty or reduce the amount of refund:***

Appeal Unit needs to prepare SCN containing reasons for such enahncement and send it to NFAC who will serve it on the appellant and the response filed by appellant with NFAC would be sent to the Appeal Unit.

↓

Appeal unit shall prepare draft order after taking into account the response received from appellant or any report furnished by NeAC/AO and send it to NFAC along-with details of initiation of penalty proceedings, if any

↓

If disputed amount is more than a specified amount, NFAC shall send draft order for review to an Appeal Unit (other than the one which drafted the order). Else, NFAC would examine the draft order as per automated examination tools and basis this it would either finalise the draft order or send it for review to an Appeal Unit (other than one which drafted the order).

↓

Upon review, the Appeal Unit may either concur with the draft order, in which case NFAC will finalise the order, or it would suggest variations to NFAC in which case it would send order to an Appeal Unit (other than the one who drafted it or reviewed it).

↓

In case suggestion pertained to increase in liability, aforesaid Appeal Unit would issue a SCN to appellant through the NFAC and prepare draft order considering the assessee's response. Else, it would prepare a draft order taking into account all the material on record.

↓

5. ***Rectification Application***

An application for rectification may be filed by appellant/ Appeal Unit/ NeAC/ AO as the case may be, with NFAC.

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Application is assigned by NFAC, to a Appeal Unit in any RFAC through an automated allocation system.

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Apppeal Unit shall prepare notice to grant opportunity to appellant/ Appeal Unit/ NeAC/ AO as the case may be and send notice to NFAC.

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NFAC shall serve the notice to the above, as required, and send the response received or intimate non-receipt of response to the Appeal Unit.

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Appeal Unit shall consider the response and pass orders for rectification or rejection of application and send it to NFAC who will communicate it to the person who applied for it and also to the NeAC/ AO for relevant action.

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An appeal against an order passed by the NFAC shall lie before the ITAT having jurisdiction over the jurisdictional AO.

Appraisal of the scheme

The First Appellate authority i.e. the CIT(A) is a very crucial level amongst the various appellate levels before which an appeal can be filed by the appellant. It is here that an assessee gets an opportunity to explain the facts in great detail and the concerned CIT(A) adjudicating the appeal has sufficient opportunity to understand and discuss the entire set of facts over a course of a number of hearings. Subsequent to the CIT(A), appeals are heard by the ITAT where the entire matter may have to be argued and presented in a very limited time frame

Further, it should be appreciated that since the powers of CIT(A) are co-terminus with that of the AO, he has the power to enhance the assessment or penalty or reduce the refund if he deems it necessary as per his analysis of the facts of a particular case. Hence, it becomes all the more crucial that the facts are clearly laid out and explained at the CIT(A) level.

While a faceless appeal system for adjudication of appeals at CIT(A) level is a welcome step as it helps in reducing the possibilities of any corruption and brings in the much-needed transparency, fairness and efficiency in the system, it cannot be overlooked that any miscommunication or incomplete understanding of facts at this stage could have disastrous effects as the CIT(A) also has the powers to enhance the tax liability of an appellant.

Request for a Personal hearing

It should be appreciated that both in case of faceless assessment and faceless appeal, the assessee/appellant has the option to request for a personal hearing (that would be carried on through video conferencing). If SCN is issued to the assessee or an appeal is being adjudicated by a CIT(A), the request needs to be approved by the Chief Commissioner or Director General in-charge of concerned ReAC/ RFAC. The said requirement of obtaining approval from the Chief Commissioner or Director General has been introduced in the Scheme w.e.f. August 13, 2020 and did not form part of the initial scheme introduced vide CBDT notification dated September 12, 2019.

In respect of the above option of a personal hearing made available to an assessee, it is important that at least in the initial phases of implementation of these schemes, any requests for a personal hearing are allowed liberally to avoid chances of any miscommunication and to instil confidence in the new system in the minds of the taxpayers.

Conclusion

One must stay mindful that robust documentation including the rationale of the transaction being structured in a particular manner, need for undertaking the transaction etc., is half the battle won. Hence the documentation will be the most critical step going forward. Due to the limited time available for the assessment proceedings, it is critical that India-Inc has adequate preparedness for maintaining proper documentation that can be made available to IRA during the online conduct of the assessment proceedings in a faceless manner. It is also vital to note that the scope of the faceless proceedings would include the assessee in default proceedings, revisionary proceedings, issuance of lower/nil deduction certificates;, hence the ease of obtaining certificates from IRA for the purpose of the compliances for the transaction could be increased. As regards the transfer pricing disputes, it would become more important than ever that taxpayers don't produce a lengthy and verbose transfer pricing study. An improved quality of the transfer pricing study would include all the relevant rationale for benchmarking it. It is critical that the functions, assets and risk-analysis is lucid and is undertaken in the report with commercial justification included in the documentation as well as the facts of each case. In case of intra group transactions such as financing and services, it is critical that the rationale for adopting the method of ALP determination is well explained along with the relevant comparables. Thus, to be better prepared for the assessment, going forward the role of the tax lawyer is bound to increase manifold for it will entail ensuring documentation submissions are in line with the facts of each case and the taxpayers are better prepared to achieve a successful order in conduct of the assessment and various other procedures which are to be carried out in faceless manner.

It is also important that the CBDT upgrade their IT Infrastructure and limit chances of any damage to it. It is also equally important to ensure that confidentiality of the assessment and appellate proceedings are maintained at all cost.

It would be advisable for both the taxpayers and the tax administrations to embrace the new system wholeheartedly, but with a lot of empathy towards the taxpayers who will not have the options to plead their cases in face-to-face meetings. It is also important that the tax administration set up a data centre so that all records, which in their now reduced form occupy less space electronically, can be stored easily since the process of completion of assessment and appellate proceedings are getting smaller by the day. It may also be advisable for the tax administration to allow taxpayers an opportunity to address their views in face-to-face meetings, to the extent possible, so that the risk of any mis-communication is minimized and the taxpayer should not be able to complain any lack of opportunity in the subsequent stages.

It is indeed a revolutionary change to the tax assessment and appellate proceedings and one sincerely hopes that the Scheme is successful so that India does not have to defend her position to be one of the most notorious and litigation-friendly jurisdictions in the global community any further!

CASE LAW UPDATES- DIRECT TAX

INTERNATIONAL TAX

Project office of a foreign enterprise engaged in preparatory and auxiliary activities not a PE in India

In the case of ***Samsung Heavy Industries Co. Ltd.***[7]**,** the SC held that a project office of a foreign enterprise engaged solely in preparatory and auxiliary activities shall not constitute a PE of the foreign enterprise in India.

Facts

Samsung Heavy Industries Co. Ltd., a Korean entity ("**Assessee**"), along with Larsen & Toubro Ltd. ("**L&T**"), had entered into an agreement in February 2006 with Oil and Natural Gas Company ("**ONGC**") as a consortium, for carrying out certain work, i.e. conducting surveys (pre-engineering, preconstruction/pre-installation and post construction), design, engineering, procurement, fabrication, installation, modifications at existing facilities, start up and commissioning of entire facilities, etc. covered under 'Vasai East Development Project' ("**Project**"). The Project was a turnkey project under the agreement entered between the Assessee, L&T and ONGC whereby pre-engineering, survey, engineering, procurement and fabrication activities took place abroad by the Assessee, and were later brought in India at the project site. For the purposes of this Project, the Assessee established a project office ("**PO**") in India in May 2006 with the permission of the RBI, which, as per the Assessee, was to act as "a communication channel" between the Assessee and ONGC in respect of the Project.

For AY 2007-08, the Assessee filed its return of income in India showing loss of INR 23.5 lacs in relation to the activities of its PO in India. However, during the assessment proceedings, the AO took the view that the project was a single indivisible "turnkey" project, whereby ONGC was to take over the Project that had been completed in India. The AO did not agree with the submissions of the Assessee that the PO was used merely for communication and coordination purpose, which is a preparatory and auxiliary activity and held that PO of the Assessee constituted a PE in India and consequently, profits arising from successful commissioning of the Project would also arise only in India. Accordingly, the AO passed a draft assessment order attributing 25% of the revenues from the Project (i.e. INR 113 crore approx.) as being the income of the Assessee liable to tax in India.

The DRP observed that if the Assessee intended to perform only preparatory and auxiliary activities, it could have opened an liaison office ("**LO**") in India and the fact that a PO was opened indicates that the Assessee was doing something more than an LO. Thus, the DRP confirmed the finding of the AO as per draft assessment order that the agreement was a "turnkey" project, which could not be split up and as a result of which the profits earned from the project would be earned within and shall be taxable in India.

The Assessee went on appeal to ITAT wherein it argued that the PO had only two employees, neither of whom had technical qualification. The PO had no role in execution of the contract such as conducting pre-survey activities, all of which were done by separate contractors and the activities performed by the PO were only preparatory and auxiliary in nature and accordingly, it would fall under the exemption provided in Article 5(4)(e) of India-Korea DTAA and that PO did not constitute a fixed place PE in India.

However, the ITAT held that the PO of the Assessee constituted a PE in India, on following grounds:

i. The contract obtained by Assessee from ONGC was indivisible;

ii. The resolution and minutes of the meeting of the Board of Directors expressly stated that the PO was opened for co-ordination and execution of the Project in India;

7 Director of Income Tax-ii (International Taxation) New Delhi & Anr. v. M/s Samsung Heavy Industries Co. Ltd. Civil Appeal No. 12183 of 2016.

iii. The approval of the RBI did not impose any restriction on the activities of the PO;

iv. The documents on record proved that all the activities to be carried out by the Assessee under the Project were routed through the PO only.

v. The Assessee had taken insurance with respect to the entire project in India and it received the major payment from the insurance company in that year itself. The said policy was not restricted only to the activities carried outside India by the Assessee;

vi. The onus is on the Assessee to prove that the PO only undertook preparatory and auxiliary activities and no material has been brought on record by the Assessee to prove the same; and

vii. Due to lack of material to ascertain as to what extent activities of the business were carried on by the Assessee through the PO, attribution of 25% by the AO was considered suitable and hence, the addition was confirmed by the ITAT.

The Assessee went on appeal before the HC, which reversed the decision of the ITAT and deleted the addition of 25% of profits attributed to the PO of the Assessee in India, after making the following observations:

i. In terms of paragraph 1 of Article 5, the Assessee would acquire its tax identity in India only when it carries on business in India through a PE situated in India;

ii. There was no finding on record that the revenue has been earned or said to have been on account of India activity of the PO; and

iii. Neither the AO nor the ITAT established or had made any effort to bring on record any evidence to justify that the business was actually carried out by the PO and that 25% of the gross revenue is attributable to such PO.

Thereafter, the IRA went on to appeal before the SC.

Issue

Whether the activities of the PO of the Assessee constituted a PE of the Assessee in India?

Arguments

The IRA argued that the Project, being a "turnkey" one, was one and indivisible, and the entire revenue earned by the Assessee would, therefore, be taxable in India. The IRA argued that it would be completely incorrect to state that there was no finding that 25% of the gross revenue of the Assessee was attributable to the business carried out by the PO of the Assessee. On the contrary, the IRA referred to all the documents that ITAT had looked at, to show that the PO was not a mere LO, but was vitally connected with the core business of the Assessee and, in the absence of figures given by the Assessee, a "best-judgment" assessment had to be made in respect of profits attributable to such PE.

On the other hand, the Assessee argued that the PO consisted of only two employees, neither of whom had any technical qualification whatsoever. Secondly, the accounts that were produced would show that the PO had not incurred any expenditure on execution of the Project. The Assessee also argued that the burden of establishing that a foreign assessee has a PE in India is on the IRA, which burden had not been discharged on the facts of the present case. Further, the Assessee also argued that even assuming that there is a permanent establishment in India through which the core business activity of the Assessee was carried out, no taxable income can be attributed to it, as audited accounts that were produced showed that the Project did not yield any profit, but in fact resulted in only losses.

Decision

The SC made following observations in the case:

i. In order to constitute a 'fixed place PE' the condition precedent for applicability of Article 5(1) of the DTAA is that there should be an establishment 'through which the business of the enterprise' is wholly or partly carried on in India. Further, the profits of a foreign enterprise were taxable in India only if the enterprise carried on its core business activities through such PE;

ii. Maintenance of a fixed place of business solely for the purpose of preparatory or auxiliary character in the trade or business of the enterprise would not be construed a PE. Even if a PE is constituted, only so much profits of the foreign enterprise would be taxed in the other contracting state as are attributable to the activities of the PE;

iii. The Board Resolution submitted to RBI for registration of the PO showed that the PO was established to co-ordinate and execute "*delivery of documents in connection with construction of offshore platform modification of existing facilities for ONGC*". However, the ITAT only relied upon the first paragraph of the Board Resolution and held that the PO was for co-ordination and execution of the project itself. Thus, the finding of the ITAT that the PO was not merely an LO, but was engaged in the core activities of execution of the project itself was incorrect and perverse;

iv. The conclusion of the ITAT that financial statements of the PO did not show any expenditure incurred relating to the execution of the Project as preparation of such accounts are in the hands of the tax payer and mere mode of maintaining accounts alone cannot determine the character of PE, are perverse and should be set aside;

v. The finding of the ITAT that the onus is on the tax payer and not on the Tax Authorities to display that PO does not constitute PE was against the decision in case of *E-Funds IT Solution Inc.*[8] delivered by the SC;

8 Asst. Director of Income Tax, New Delhi v. E-Funds IT Solution Inc., (2018) 13 SCC 294.

vi. The ITAT had ignored the fact that there were only two persons working in the PO and neither of whom was qualified to perform any core activity of the Assessee;

vii. The activities of the PO of Assessee would fall within exception provided under Article 5(4)(e) of the DTAA, as the PO was solely involved in auxiliary activities i.e. acting as LO between the Assessee and ONGC.

Accordingly, the SC held that the PO of the Assessee did not constitute a PE in India, as it was not carrying any core business activities in India.

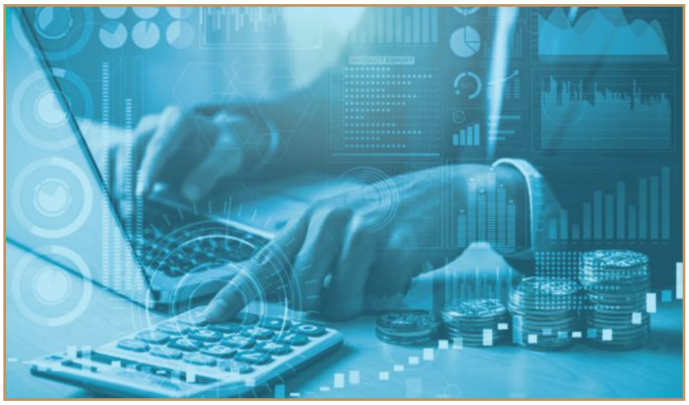
Significant Takeaways

The SC had arrived at its decision after analysing certain key judicial precedents of the various HCs and of its own on the subject such as rulings in the case of ***Morgan Stanley & Co.***[9], ***Ishikawajima-Harima Heavy Industries Ltd.***[10], ***E-Funds IT Solution Inc.***[11], ***Hyundai Heavy Industries Co.***[12].

One of the key takeaways from the ruling of the SC is the focus on the activities undertaken by the fixed place in India rather than the nature of the entity of the foreign enterprise set up in India. As per the RBI regulations, the PO may be permitted to undertake a much wider set of activities than an LO. The ruling of DRP as well as ITAT in this case, concluding that the Assessee had a PE in India, largely stemmed from the fact that the Assessee was granted an approval from the RBI to operate as a PO and was thus, allowed to undertake a larger set of activities as against mere preparatory and auxiliary activities that are usually undertaken by an LO. Thus, the ITAT and DRP relied more on the perception created by the RBI approval than on the reality of what the PO was actually doing and whether any income could be attributed to the activities undertaken by the PO.

Having said so, the SC could have also considered analysing the applicability of Article 5(4)(f) of the India-Korea DTAA which provides for an anti-abuse provision for artificial avoidance of PE, which is similarly worded as Article 13 of the MLI. The relevant Article 5(4)(f) of the India-Korea DTAA states:

> *"Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include:*
>
> > *(f) The maintenance of fixed place of business solely for combination of activities mentioned in sub-paragraphs (a) to (e), <u>provided that overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.</u>"*



The essential condition under this clause is wherein a combination of activities, which are otherwise individually exempt from the definition of PE, are being performed by a fixed place, it has to be ensured that the overall activity from such combination of activities is also of preparatory or auxiliary character.

It would have been pertinent had SC also looked at the applicability of the above clause in the present case. This is so because MLI in India has become effective from April 01, 2020 and many Indian DTAAs, which are Covered Tax Agreements ("**CTAs**"), have been impacted post applicability of MLI. Article 13 of MLI provides two options i.e. 'Option A' and 'Option B' to deal with the artificial avoidance of PE through specific activity exemptions i.e. activities which are preparatory or auxiliary in nature. India has opted for 'Option A', which continues with the existing list of exempted activities from (a) to (e) in Article 5(3)/(4), but has added one more sub-clause (f) (similar to India-Korea DTAA discussed above) mandating that all the activities mentioned in sub-clauses (a) to (e) activities or combination of these activities must be preparatory or auxiliary in nature to qualify as exempt activities.

The applicability of this condition given in MLI and in Article 5(4)(f) could have set a precedent towards future interpretation of India's DTAAs which are CTAs impacted by the MLI.

" PO of a foreign enterprise, engaged only in preparatory and auxiliary activities, does not constitute a PE in India. "

9 M/s DIT (International Taxation), Mumbai v. M/s Morgan Stanley & Co. Inc., (2007) 7 SCC 1.
10 Ishikawajma-Harima Heavy Industries Ltd. v. Director of Income Tax, Mumbai, (2007) 3 SCC 481.
11 Asst. Director of Income Tax, New Delhi v. E-Funds IT Solution Inc., (2018) 13 SCC 294.
12 Commissioner of Income Tax and Another v. Hyundai Heavy Industries Co. Ltd., (2007) 7 SCC 422.

Payment for non-resident's inspection & quality check services, not FTS

In the case of ***Jeans Knit Pvt. Ltd.***[13]***,*** Karnataka HC held that the payments made by an Indian company to a non-resident company for rendering inspection and quality check services did not amount to FTS.

Facts

Jeans knit Pvt. Ltd. ("**Assessee**") was engaged in the business of manufacturing and export of garments and 100% export-oriented undertaking. The Assessee imported accessories from other countries, especially from Europe. For the aforesaid purpose, the assessee had engaged M/s Sharp Eagle International, Hongkong ("**NR**") to render various services at the time of import such as inspection of fabrics, timely dispatch of material etc. The Assessee paid 12.5% of the import value as charges to the aforesaid NR. The Assessee made payments to NR in assessment year 2007-08 without the deduction of TDS.

During assessment proceedings, the AO held that the NR was a service provider and not an agent of the Assessee and the services rendered by NR had to be treated as technical services which were squarely covered under the scope and ambit of Section 9(1)(vii) of the IT Act. As the Assessee had failed to deduct tax at source, it was treated as a assessee-in-default case.

On appeal, the CIT(A) held that the Assessee had not been able to furnish proper and satisfactory evidence to establish that the consideration payable for services rendered by NR under the terms of the agreement was not in the nature of fee towards technical services within the meaning of Explanation 2 to Section 9(1)(vii) of the Act and dismissed the appeal.

Thereafter, the Assessee approached the ITAT. The ITAT held that the NR was not involved either in identification of the exporter or selection of material and negotiating of price. The quality of material was already determined by the Assessee and NR was only required to make physical inspection of the material to examine if it resembled the quality specified by the Assessee. Thus, it was only comparing the material with samples provided by the Assessee and for this activity, no technical knowledge or expertise was required. Accordingly, it was held that the NR was not providing any technical services and the payments made by the assessee to NR did not fall within the ambit of FTS and, therefore, provision of Section 195(1) was not attracted. In the result, the appeal filed by the assessee was allowed.

The IRA preferred a further appeal with the HCC.

Issue

Whether the payment made by the Assessee to the NR for quality check and inspection services qualified as FTS under Explanation 2 to Section 9(1)(vii) of the IT Act.?

Arguments

The IRA argued that NR had the requisite expertise in the textile sector and as per the agreement it was required to check quality, quantity and to ensure timely dispatch of materials. Such services were not technical in nature and, therefore, the NR had rendered managerial services. Alternatively, it was submitted that the services rendered by the NR amounted to consultancy services. In support of aforesaid submissions, the IRA placed reliance on decisions of the Supreme Court in ***Oberoi Hotels (India) (P.) Ltd.***[14] as well as ***GVK Industries Ltd. & anr.***[15]

On the other hand, the Assessee argued that the it got raw material from abroad and under the agreement NR was only required to inspect and ensure quality of sample approved by the Assessee and to ensure timely delivery. The Assessee highlighted that under the agreement the NR had no role in selecting samples, design, or colour, but it acted only as commission agent. The Assessee also pointed out that all the documents were presented before the AO and all the correspondences were produced before the CIT(A), however, neither the AO nor the CIT(A) took the aforesaid materials into consideration. Further, the Assessee also argued that the NR had not provided any technical or managerial or services and the ITAT's evidence on record shows that the services rendered by the NR did not amount to consultancy services, and such findings were not assailed as perverse by the IRA in their submissions.

Decision

On consideration of arguments above, the HC re-visited the definition of FTS under Explanation 2 to Section 9(1)(vii) of the IT Act. The HC observed that it was a well settled rule of interpretation of taxing statute that words not defined in the Act must be interpreted in their popular sense giving it the same meaning that people conversant with the subject matter with which statute is dealing would attribute to it. Thus, the words would have to be interpreted according to ordinary parlance and must be given a meaning, which people conversant with the commodity would ascribe to it.

Using this rule of interpretation, the HC stated that expression 'managerial', 'technical' and 'consultancy services' employed in

13 Director of Income Tax (International Taxation) v.Jeans Knit (P.) Ltd., (2020) 119 taxmann.com 305 (Karnataka HC).
14 Central Board of Direct Taxes v. Oberoi Hotels (Inida) (P.) Ltd., (1998) 97 Taxman 453 (SC).
15 GVK Industries Ltd. & ANR. v. The Income Tax Officer & Anr., [2015] 54 taxmann.com 347 (SC).

Explanation 2 to Section 9(1)(vii) of the Act have neither been defined under the IT Act nor under the General Clauses Act, 1987. Therefore, the aforesaid words have to be understood in a sense in which they are understood by the persons engaged in the business and by the common man who is aware and understands the same.

Further, the HC also relied upon the ruling of the Delhi HC case of ***Bharti Cellular Ltd.***[16] as well as ***Panalfa Autoelectrik Ltd.***[17] wherein the word 'consultancy' was understood to mean an act and advise of someone (such as a lawyer), as provided under the Black's Law Dictionary[18]. The HC further observed that for consultation service under Explanation 2 to Section 9(1)(vii), there should be a provision of service by the non-resident, who undertakes to perform it, which the acquirer may use. The service must be rendered in the form of an advice or consultation given by the non-resident to the resident Indian payer. The HC further relied on another Delhi HC ruling in the case of *Grup ISM*[19] wherein it was held that consultancy services ordinarily would not involve instances where the non-resident is acting as a link between the resident and another party, facilitating the transaction between them, or where the non-resident is directly soliciting business for the resident and generating income out of such solicitation.

Given the above, the HC held that from the agreement executed by the Assessee with the NR, it was evident that the NR was required to inspect the quality of fabric and other accessories in accordance with the sample approved by the Assessee and coordinate with the suppliers to ship the goods within the stipulated date. Under the agreement, the NR was required to ensure coordination with the suppliers, so that goods were shipped on time and ensure that correct quantity and quality of goods were shipped to Assessee. In consultation with the exporters, it identified the manufacturers as well as the quality and price of the material to be imported. The NR was nowhere involved either in identification of the exporter or in selecting the material and negotiating the price. The quality of material was also determined by the Assessee and the NR was only required to make physical inspection to see if it resembles the quality specified by the assessee. For rendering aforesaid service, no technical knowledge was required. Therefore, the services rendered by the NR would not fall within the services contemplated under Section 9(1)(vii) of the Act.

Significant Takeaways

In the absence of a definition or meaning of the words 'managerial' and 'consultancy,' there has been significant litigation to ascertain whether a payment for particular service qualifies as FTS or not. There have been multiple interpretations that have been provided by the Indian courts to the words "technical", "managerial" and "consultancy" basis the fact situation of each of the case. The HC, in the present case, has appropriately applied rules of interpretation to pave way for the manner of interpretation of these significant terms and their applicability on the facts of the case.

Previously, Courts have taken divergent views on whether payments for quality check services would not fall under the ambit of FTS. For instance, Delhi ITAT in the case of ***NQA Quality Systems***[20] held that the consideration paid by an Indian company to a foreign company for quality assurance assessment and certification activities would not be regarded as FTS. The Delhi ITAT gave the benefit of the 'make available' clause available under the India – UK DTAA. However, in the present case, the income relates to a period prior to India – Hong Kong DTAA coming into force, therefore, the question of resorting to definition under the DTAA, does not arise.

On the contrary, Delhi ITAT itself, in the case of ***Maruti Udyog Ltd.***[21] stated that carrying out impact tests on cars (to check their quality) and submitting test reports, amounted to rendition of 'technical services' and therefore, payment for such services was held as FTS under the India – France DTAA.

While divergent views do exist, since the emphasis by the IRA in the present case was on such services being categorised as 'consultancy services' hence the rationale and ruling of the Karnataka HC cannot be contested basis the above-mentioned cases.

" Payment made to foreign company for inspection and quality check services was held as not FTS. "

16 CIT v. Bharti Celluar Ltd., (2009) 319 ITR 139 (Delhi HC).
17 Director of Income Tax (Intl. Tax.)- II v. Panalfa Autoelectrik Ltd., [2014] taxmann.com 412 (Del).
18 Black's Law Dictionary, 8th Edition.
19 Commissioner of Income Tax-IV v. M/G Grup ISM P. Ltd., [2015] 57 taxmann.com 450 (Delhi).
20 NQA Quality Systems Registrar Ltd v. DCIT, (2004) 92 TTJ 946 (Delhi ITAT).
21 Maruti Udyog Ltd. v. ADIT, (2009) 130 TTJ 66 (Delhi ITAT).

Mumbai ITAT holds reimbursement of expenses incurred by non-resident agent not FTS, and not subject to withholding tax

In the case of ***Gepach International***[22]**,** the Mumbai ITAT ruled that reimbursement of sales promotion expenses to a UAE-based agent did not amount to FTS and consequently the assessee was not required to withhold tax under Section 195 of the IT Act.

Facts

Gepach International ("**Assessee**") was an Indian firm engaged in export of pharmaceutical and nutraceutical products. In respect of AY 2013-14 and AY 2014-15, the Assessee filed its ROI declaring total income of NIL.

During the assessment proceedings, the Assessee was asked to submit details of sales promotion expenses of INR 2,16,41,556 debited in its profit and loss account. The Assessee submitted that the amount was in the nature of reimbursement of expenses incurred by its sales promotion agent, M/s Pharmark Consulting FZE ("**Agent**"), resident in UAE and had not withheld taxes under Ssection 195 of the IT Act while making the payment to the Agent. The Assessee was asked to substantiate why the reimbursement should not be disallowed under Section 40(a)(i) of the IT Act for failure to withhold taxes on the said payments under Section 195 of the IT Act. The Assessee submitted the details of the payment as well as the relevant agreement under which it was made, submitting that Section 195 did not apply in its case. While the Agent was appointed on a commission basis by the Assessee, there was no dispute with the IRA on the taxability of such commission received by the Agent, and the issue pertained only to whether tax is required to be withheld on the reimbursement component.

The AO rejected the submissions of the Assessee and characterised the payment made by the Assessee to the Agent as FTS and disallowed the reimbursement of expenses under Section 40(a)(i) of the IT Act. based on the fact that the Agent was dependent on the Assessee for its decision-making – the Agent was required to take confirmation from the Assessee on the terms of sales of products and was prohibited from engaging with the Assessee's competitors.

In its appeal before the CIT(A), the Assessee submitted that the Agent had been exclusively appointed for promotion of Assessee's products, identifying new customers, liaising with governmental authorities for developmental activity relating to the Assessee's business, and carrying out marketing and sales promotion in Russia. The Assessee retained full control over all marketing activities in Russia and the Agent simply implemented the Assessee's instructions. The Agent incurs the expenses in relation to its functions on behalf of the Assessee and the Assessee makes reimbursement of the said expenses. The CIT(A) engaged in an elaborate analysis of the facts and relevant judicial precedents, concluding that, having regard to the nature of the services rendered by the Agent, the payment, therefore, does not amount to FTS. The CIT(A) also observed that the Agent was only taking instructions from the Assessee to provide market support services, while acting as an agent on commission basis. It had not provided the Assessee any managerial or technical services, payment for which could be construed as FTS. The CIT(A) went on to hold that fee payable for the purposes of making or earning income from any source outside India is not included in the ambit of taxability of FTS under Section 9(1)(vii)(b) of the IT Act. For this finding, the CIT(A) relied on a decision of the jurisdictional High Court in ***CEAT International S.A.,***[23] where export commission paid to a non-resident was held to be outside the scope of FTS, since the payee had not imparted any information concerning technical, industrial, commercial or scientific knowledge, exports or skill, nor rendered any managerial technical or consultancy services. Accordingly, as business income of the Agent, and not FTS, the reimbursement amount was held to not be taxable in India since the Agent did not have a business connection in India. Accordingly, the CIT(A) deleted the disallowance made by the AO under Section 40(a)(i) of the IT Act.

Aggrieved by the order of the CIT(A), the IRA went in appeal before the ITAT.

Issues

1. Whether the reimbursement expense amounted to FTS?
2. Whether the reimbursement was subject to withholding tax under Section 195 of the IT Act?

Arguments

Before the ITAT, the IRA pressed that the terms of the arrangement between the Assessee and the Agent alluded to a technical service being rendered by Agent to the Assessee and, therefore, payments made should be treated as FTS. On the other hand, the Assessee submitted that the IRA had read the agreement clause-wise and line-by-line and had misinterpreted the main object of the agreement. The Assessee sought to distinguish between managerial and technical services and pointed out that in the commission agency there was no requirement of technical knowledge or technical skill. The Agent had appointed staff in Russia to manage the commission business and the managerial skill is thus used by the Agent for his own business. For this purpose, the Assessee placed reliance on the judgment of Delhi HC in the case of ***Panalfa Auto Electric***.[24] The Assessee claimed that the Agent's role was non-

22 ACIT v. Gepach International, ITA No. 5942/Mum/2018 (Mumbai ITAT).
23 CEAT International S.A. v. CIT, (1999) 237 ITR 859 (Bombay High Court).
24 DIT v. Panalfa Autoelektrik, (2014) 272 CTR 117 (Delhi High Court).

technical in nature, involving mere procurement of orders and following up with customers for payment.

Decision

The ITAT observed that the Assessee had reimbursed to its Agent operating from UAE the expenses incurred by it in Russia, which were marketing support services as per marketing and promotion strategies devised by the Assessee. The ITAT also noted that the Assessee retained full control over all the marketing activities in Russia and the Agent was simply implementing the same. The ITAT further observed that there was no evidence that the Agent had rendered any managerial service to the Assessee and that the agreement indicates only services on commission basis. Thus, the ITAT upheld the reasoning and conclusion of the CIT(A) without interference. Since the Agent's functions did not constitute technical, managerial or consultancy services, the reimbursement of expenses incurred, as paid by the Assessee to the Agent, shall not amount to FTS. The reimbursement income should be treated as ordinary business income in the hands of the Agent, which is not taxable in India since the Agent did not have any business connection in India. Accordingly, it was held that the provisions of Section 195 of the IT Act are not attracted on payment of reimbursement of expenses made by the Assessee to its Agent in UAE and, therefore, the disallowance under Section 40(a)(i) of the IT Act cannot be made.

Significant Takeaways

Generally, a transaction of reimbursement of expenses (at cost without mark-up) has typically been considered as not subject to tax in the hands of the recipient.[25] Some of these judicial precedents were also relied upon by the Assessee in its submission before the CIT(A) and ITAT. Where the line seems to blur is when the reimbursement is made as consideration for seemingly technical services, such as in the Assessee's case. It has indeed been held in certain cases by higher judicial fora that sales and export promotion services rendered by group companies or outsourced to agents, cannot be considered as technical services, and hence cannot trigger taxation under Section 9(1)(vii).[26] This judgment has reinforced the principle that payments for market management services rendered for businesses carried on outside India could not be considered to be taxable as FTS in India.

Interestingly, neither the CIT(A) nor the ITAT undertook an analysis of the India-UAE DTAA for the purpose of determining taxability of the reimbursement of expenses incurred for marketing support activities. The India-UAE DTAA does not have a specific clause governing taxation of FTS, in relation to which it has been held in a number of judgments that such income shall anyway be taxed only as business profits, provided the recipient has a PE in India.[27] Therefore, based on this reasoning, even if the payment made by the Assessee to its Agent was considered as FTS, the same would have had to be taxed as business profits only in the absence of a specific clause in the India-UAE DTAA.

> **“Reimbursement of sales promotion expenses to agent is not FTS and shall not be taxed in the absence of a business connection in India.”**

25 DIT v. A. P. Moller Maersk AS (2016) 383 ITR 1 (Supreme Court); CIT v. Tejaji Farasram Kharawalla Ltd., AIR 1968 SC 200 (Supreme Court); CIT v. Siemens Aktiongesellschaft, (2009) 310 ITR 320 (Bombay High Court); CIT v. IDFC Investment Advisors Ltd., ITA No. 968 of 2014 (Bombay High Court); DIT v. WNS Global Services (UK) Ltd., ITA No. 1130 of 2012 (Bombay High Court).
26 Dr Reddy Laboratories Ltd., In re., A.A.R. No 1572 of 2014 (AAR); Cushman and Wakefield(s) Pte. Ltd., In Re., (2008) 305 ITR 208 (AAR); Le Passage to India Tours & Travel Pvt. Ltd. v. DCIT, ITA No. 210/Del/2012 (Delhi High Court).
27 ABB FZ-LLC v. ITO, ITA No.188/Bang/2016 (Bangalore ITAT).

Shipping agents in India will not constitute POEM / PE for the non-resident principal

In the case of ***Overseas Transport Company Ltd.***[28]**,** the Mumbai ITAT held that agents which do not operate exclusively for one non-resident principal, but earn income from many other principals, cannot be considered as constituting place of effective management ("**POEM**") or a PE for that non-resident in India. Accordingly, the ITAT proceeded to grant benefits of the relevant DTAA to the non-resident principal as no PE had been created in India.

Facts

Overseas Transport Co. Ltd. ("**Assessee**"), a tax resident of Mauritius, was engaged in the shipping sector. For the AY in question, the Assessee filed returns claiming exemption under Article 8 (Shipping and Air Transport) of the India-Mauritius DTAA, which *inter alia* provides that income from shipping business should be taxable in the country where the assessee's POEM is situated. During the hearings, the AO noted that the Assessee had two shareholders who were residents of UAE and most board meetings were held in UAE. Further, the Assessee's shipping business in India was conducted through two agents. Therefore, the AO alleged that the POEM of the Assessee's shipping business is in India. The AO additionally alleged that the said agents had also created a fixed place PE under Article 5(1) of the DTAA as well as a dependent agency PE under Article 5(5) of the DTAA for the Assessee in India.

The CIT(A), on appeal, reversed the assessment order, holding that the agents had their own independent business through which they received commission income from other principals or clients as well. Accordingly, there was no dependent agent PE of the Assessee that was created in India. The CIT(A) did not make any observations on the creation of a fixed place PE as held by the AO.

The IRA thus appealed against the findings of the CIT(A) to the ITAT.

Issues

1. Whether the agents constituted a POEM for the Assessee in India?
2. Whether the agents had created PE for the Assessee in India?

Arguments

The IRA argued that the agents had constituted a fixed place PE and a dependant agent PE for the non-resident in India since the entire shipping business of the Assessee in India was carried out by the agents viz., co-ordination with the parties, loading and unloading of cargo, etc. Therefore, profits arising out of such activities carried out by the agents, i.e., the PE, should be taxable in India.

The IRA further contended that to avail the benefits under Article 8 of the India-Mauritius DTAA, the Assessee should prove that its POEM is in Mauritius. In the instant case, the Assessee company only had a legal presence in Mauritius since it was managed from UAE, where all its shareholders were based and conducted board meetings through video conferencing. Therefore, it was alleged that the Assessee's POEM is not in Mauritius. Secondly, the entire shipping business of the Assessee in India was carried out through agents based out of India and, therefore, it was contended that the POEM of Assessee was also constituted in India. Accordingly, as per Article 8, the profits of the Assessee should be taxable in India.

On the other hand, the Assessee pointed out that the remuneration paid by it to the said agents constituted only a fraction of their total income i.e., during the relevant year, the two agents received mere 12.14% and 2.79% respectively, of their total receipts from all principals. In view of the same, it was contended that the agents are independent in nature and accordingly cannot constitute a dependant agent PE for the Assessee in India. Similarly, the office premises of the said agents are undoubtedly not at the disposal of the Assessee. Moreover, no business activities of Assessee was conducted at its direction. Therefore, it was contended that the agents cannot constitute fixed place PE for it in India as well.

The Assessee also contended that business activities were indeed conducted from Mauritius. Merely because it had engaged agents in India to carry out activities, it cannot be stated that key management and commercial decisions were taken by the said agents and that the Assessee's POEM was in India.

Decision

First, the ITAT chose to examine the meaning of the term 'fixed place of business' in Article 5(1) of the DTAA. The ITAT elaborated that the tests required to determine the existence of a PE under Article 5(1) are: first, there must be a business of the enterprise of one contracting State in the other contracting State; second, there must be a fixed place of business in the other contracting State; third, the place of business must be at the disposal of the enterprise; lastly, through this fixed place of business, the enterprise must either wholly or partly carry on its business. The ITAT thus concluded that the Assessee did not satisfy any of the above tests as there was no permanent infrastructure, office, supervisory staff, tangible and intangible assets in India. Further, the allegation of the AO that the directors/shareholders of the Assessee were residents of UAE bears no relevance to the creation of a fixed place PE in India.

With regard to the agents of the Assessee through which its Indian business was conducted, the ITAT noted that the agents had other clients on behalf of which they carried out activities in their ordinary course of business and the receipts of the agents from the Assessee only constituted a fraction of their total

28 DDIT v. Overseas Transport Co. Ltd., ITA No. 3129/Mum/2002 (Mumbai ITAT).

receipts. The ITAT also placed reliance on an earlier Mumbai ITAT decision in *Bay Lines,*[29] where it was decided based on an identical fact scenario that the assessee did not have a dependent agent PE in India.

Insofar as arguments regarding POEM are concerned, the ITAT held that the AO had failed to prove with substantial evidence that key management and commercial decisions were taken in India. The mere fact that board meetings were conducted in the UAE cannot lead to a conclusion that POEM of the Assessee was in India. To establish POEM in India, the AO was required to prove that key management and commercial decisions were taken in India.

In view of the foregoing reasons, the ITAT held that the Assessee neither had its POEM nor any PE in India. The agents were independent in nature and accordingly, the profits of the Assessee cannot be taxed in India.

Significant Takeaways

Most of India's DTAAs, through Article 8, state that that income from international shipping activities should be taxable in the state in which the assessee's POEM is situated. A few other DTAAs provide that such income should be taxable in the state of residence of the assessee. The legislative intent behind this clause in DTAAs was to avoid controversies arising from the creation of multiple PEs in the multitude of jurisdictions through which ships tend to transit and to provide certainty over taxability of income arising from international shipping activities. Therefore, Article 8 supersedes other clauses of the DTAA regarding PE, so as to make the income from the international shipping activities taxable in the state of the POEM and not the PE.

In the instant case, the facts reveal that while the Assessee was incorporated in Mauritius, its shareholders were based out of UAE and board meetings were conducted in UAE. Assuming that the key commercial decisions were taken in UAE, it can be stated that Assessee's POEM was neither in India nor in Mauritius, but in UAE i.e., a third country. Klaus Vogel in his commentary on DTAAs has opined that if the POEM of a shipping company is in the third state, then Article 8 cannot be applied.

In that event, the income of the shipping company should then be taxed based on the principles of PE. In the Assessee's case, the ITAT held that the agents cannot be construed to be PE of Assessee in India since the office premises of the agents were not at the disposal of the Assessee and the agents were acting in their independent capacity. In other words, even if the exemption under Article 8 cannot be granted owing to POEM being situated in a third state, the Assessee's income cannot be taxed in India since it did not have a PE in India, as was held by the ITAT's co-ordinate bench in ***Bay Lines***.[30]

> **"Agents who are not exclusively working for the assessee and are having their independent status, providing services to the assessee in the ordinary course of their business, cannot be considered as dependent agents creating a PE of the assessee."**

29 ADIT v. Bay Lines (Mauritius), ITA No. 1181/Mum/2002 (Mumbai ITAT).
30 ADIT v. Bay Lines (Mauritius), ITA No. 1181/Mum/2002 (Mumbai ITAT).

Exchange of shares in an amalgamation, held as 'stock in trade', taxable as business income

In the case of ***Nalwa Investment Ltd.***[31]**,** Delhi HC held that gains arising from exchange of shares, held as stock-in-trade by the taxpayer, in case of an amalgamation, would be taxable as business income.

Facts

Nalwa Investment Ltd. ("**Assessee**"), the promoter company of Jindal Group of companies, was holding shares of Jindal Ferro Alloy Ltd. ("**JFAL**"). In the relevant FY, JFAL, amalgamated with Jindal Strips Ltd. ("**JSL**") ("**Amalgamation**"). As a part of the Amalgamation, the Assessee transferred its shareholding in JFAL in lieu of receipt of shares of JSL. The Assessee claimed that the transaction was exempt from capital gains under Section 47(vii) of the IT Act which provides that any transfer by a shareholder, in a scheme of amalgamation, of a capital asset being shares held by him in the amalgamating company in consideration of the allotment of shares in the amalgamated company, provided that the amalgamated company is an Indian company, would not be regarded as a transfer for the purposes of computing capital gains under the IT Act.

The AO held that as the Assessee was holding the shares of JFAL as stock in trade and not as capital asset, therefore, it was not entitled to exemption under Section 47(iii) of the IT Act. Accordingly, the AO held that the difference between the market value of shares of JSL, received pursuant to the Amalgamation, and the book value of shares of JFAL was taxable as 'business income'. The CIT(A) upheld the order of AO. On further appeal, the ITAT without recording a categorial finding as to whether the shares were classifiable as 'capital asset' or 'stock in trade', held that no profit accrued to the Assessee from the receipt of shares of the amalgamated company. This order of the ITAT was assailed by the IRA before the Delhi HC.

Issue

Whether Assessee was liable to pay tax on the receipt of shares of JSL pursuant to the Amalgamation?

Arguments

The IRA contended that as the Assessee held the shares of JFAL as stock in trade, exemption under Section 47(iii) was not available. It also argued that receipt of shares of amalgamated company in lieu of shareholding the amalgamating company, constituted a 'transfer' and placed reliance on the SC judgment in the case of ***CIT v. Mrs. Grace Collis and Ors.***[32] ("**Grace Collis**"). Reliance was also placed on the decision in the case of ***Orient Trading Co. Ltd. v. CIT***[33] ("**Orient Trading**") to contend that accretion in value of shares received in exchange amounted to realisation of profit and, therefore, was taxable as business income.

It was contended on behalf of the Assessee that the shares in JFAL were held as investment and not as stock in trade. Assessee argued that even if the shares were held as stock in trade, there was no taxable income. It was asserted that only profit on realisation of stock-in- trade by way of sale thereof could be brought to tax under the head 'profit and gain of business or profession' and relied on the SC decision in the case of ***Rasiklal Maneklal***[34], to contend that receipt of shares under the scheme of amalgamation did not amount to 'exchange'. Accordingly, it was argued that since the shares of JSL were not sold during the relevant previous year, no addition for business profit could be

31 (2020) 118 taxmann.com 278 (Delhi HC).
32 (2001) 248 ITR 323 (SC).
33 (1997) 224 ITR 371 (SC).
34 (1983) 43 Taxman 259 (SC).

made in the hands of the Assessee, even if there was notional accretion in the value of shares of JSL vis-a-vis value of shares held in JFAL.

Decision

The HC followed the decision of ***Grace Collis*** to observe that extinguishment of rights of the transferor in the capital asset being shares of amalgamating company, amounted to transfer under Section 2(47) of the IT Act. The HC distinguished the decision in the case of ***Rasiklal Maneklal*** (supra) on the ground that it dealt with the scope of capital gain tax provisions under the Income-tax Act, 1922 and not of Section 2(47) under the IT Act. The HC held that such transfers, where the shares were held as capital asset, would be covered under Section 47(vii) of the IT Act and, therefore, would not be subject to tax. The HC added that, however, if the shares were held to be stock-in-trade, then the receipt of shares of the amalgamated company in lieu of shares of an amalgamating company amounts to exchange and the difference between the book value of the shares of the amalgamated company and the market value of the shares of the amalgamating company would be taxed as profits under the head of 'profits and gains from business and profession'. The Delhi HC observed that the concept of extinguishment / transfer in relation to receipt of shares of amalgamated company by Assessee in lieu of shares of amalgamating company did not lose its relevance even if the shares were characterized as stock-in-trade. The HC remanded the matter back to ITAT for determining whether the shares were held as stock- in- trade or capital asset.

Significant Takeaways

The judgment of the Delhi HC would have a bearing on all the schemes of amalgamation, wherein a shareholder holds the shares of the amalgamating company as stock-in-trade and is allotted shares of the amalgamated company. Interestingly, the Delhi HC has extended the definition of transfer under Section 2(47) of the IT Act to determine taxability under the head "profits and gains from business and profession", even though the word 'transfer' under Section 2(47) has been specifically defined in relation a capital asset. This interpretation given by HC is in sharp contrast to the literal construction of the provisions of Section 2(47) and it may be open for the taxpayers to argue that the said definition may not be relevant while examining the meaning of 'transfer' of a stock-in-trade.

It is a settled position of law that as long as the stock-in-trade remains with the trader, any appreciation or depreciation in its value is considered notional and is not subject to tax. The question of taxability arises only when such stock-in-trade is realised. The HC, in the instant case, relied on the SC decision in the case of ***Orient Trading*** to hold that receipt of shares under exchange amounts to realisation of the securities and thus, the profits are subject to tax. However, this case may be differentiated on the grounds that the SC in said case was not dealing with the receipt of shares under a scheme of amalgamation.

Separately, if as per the instant decision, receipt of shares of amalgamated company by a shareholder of the amalgamating company in lieu of its shareholding in the amalgamating company, where such shares are held by him as stock-in-trade, pursuant to a scheme of amalgamation is held to be taxable, the issue of valuation of such shares may arise. Will such shares be valued at cost as maybe prescribed under the amalgamation scheme, or will they be valued at fair market value? Can the fair market value of the shares allotted by the amalgamated company be computed under Rule 11UA of the IT Rules, 1962?

It is also pertinent to note that the taxpayers should be extremely careful in looking at the relevant assets and liabilities of the amalgamating companies and should ensure that they are complying with the relevant provisions to claim any merger related exemptions.

"Receipt of shares, held as stock-in-trade, under a scheme of amalgamation should be taxed as business income."

Business transfer for non-monetary consideration is not taxable as slump sale

In the case of ***M/s. Areva T&D India Ltd.***[35]**,** the Madras HC held that transfer of a business for a non-monetary consideration did not qualify as slump sale under the IT Act and hence, was not taxable.

Facts

Areva T&D India Ltd. ("**Assessee**"), during the relevant year had transferred its non-transmission and distribution business ("**Business**") to its subsidiary company, Alstom Industrial Products Limited ("**AIPL**") under a scheme approved by the Calcutta HC, for a total consideration of INR 413 million, being the fair value of the Business. This consideration was to be discharged by issuance of 39,00,000 equity shares of AIPL.

The Assessee, in its income tax return, characterised the sale of its Business as a slump sale and computed capital gains from such sale. However, the Assessee did not pay the capital gain tax as the capital gains were to be invested in tax savings bonds as notified under Section 54EC of the IT Act. Subsequently, during the assessment proceedings before the AO, the Assessee raised an alternative plea that the transfer of Business did not constitute slump sale and hence, was not taxable.

Rejecting the contention of the Assessee, the AO held that since it had itself said that the transaction was a slump sale while filing original and revised return, it was estopped from raising the alternate plea that transfer of Business undertaking was not a slump sale. The order of the AO was upheld by CIT(A) or the ITAT. Aggrieved by the order of the ITAT, the Assessee preferred an appeal before the Madras HC.

Issues

Whether the transfer of Business by the Assessee to AIPL, under the scheme of arrangement approved by the HC, constituted a slump sale under the IT Act?

Arguments

The Assessee argued that since Business was transferred vide a court approved scheme for a non-monetary consideration, such transfer could not be regarded as sale. Accordingly, it was argued that the transfer of Business to AIPL did not qualify as slump sale under the IT Act. The Assessee, in this regard, placed reliance on the case of ***Avaya Global Connect Ltd.***[36]

The IRA argued that since the Assessee did not raise the argument saying the transfer of Business to AIPL did not qualify as slump sale under the IT Act while filing original and revised return of income, it was estopped from raising the plea that the transfer was not a slump sale. Additionally, the IRA also argued that the impugned transaction was in nature of an exchange, therefore, it was covered under the expression 'transfer of capital asset' and 'slump sale' as defined under the IT Act.

Decision

The HC placed reliance on ***CIT v. Bharath General Reinsurance Co. Ltd.***[37] and held that there is no estoppel in taxation law and, therefore, the Assessee was not estopped from raising the plea that the transfer of Business did not constitute slump sale.

With regard to the substantial issue, the HC noted that the word 'sale' was not defined in the IT Act and therefore, referred to Section 54 of Transfer of Property Act, 1882 which defines 'sale' to mean a transfer of ownership in exchange of a price paid or promised or part paid or part promised. The HC also noted that the term 'price' was defined in Sale of Goods Act, 1930 to mean money consideration for sale of goods. Thus, the HC held that in order to constitute slump sale under the IT Act, the sale should have been by way of transfer of ownership in exchange of price paid or promised or part paid and part promised and the price ought to have been by way of a monetary consideration. If no monetary consideration was involved, then the transaction could not be covered within the ambit of slump sale. The HC held that since the for transfer of Business undertaking was done without monetary consideration, the transfer did not constitute slump sale.

While passing the judgment, the HC placed reliance on the Bombay HC judgment in case of ***Bharat Bijlee***[38] wherein the Bombay HC had held that where preference shares and bonds were issued in consideration for a transfer of an undertaking and there was no monetary consideration involved, it amounted to exchange and not slump sale. The Court also relied on the SC judgment in ***State of Madras v. Gannon Dunkerly & Co. (Madras) Ltd.***[39] and held that a transfer, pursuant to a court approved scheme of arrangement, is not a contractual transfer, but a statutory transfer, which cannot be covered within the definition of word 'sale'.

Significant Takeaways

The issue of taxability of transfer of business undertaking in lieu of securities by the transferee entity, has been a subject matter of litigation. The ruling reinforces the distinction carved out between slump sale and slump exchange by the Madras HC in the case of ***Bharat Bijlee***. In this case, the HC held that issue of

35 (2020) 119 taxmann.com 171 (Madras HC).
36 (2008) 26 SOT 397 (Mumbai ITAT).
37 (1971) 81 ITR 303 (Delhi HC).
38 CIT v. Bharat Bijlee Ltd., (2014) 365 ITR 258 (Bombay HC).
39 1959 SCR 379 (SC).

shares in lieu of transfer of business undertaking does not constitute slump sale but a slump exchange. However, it is to be noted that the appeal against the decision of ***Bharat Bijlee*** is pending before the SC, and thus, cannot be said that the issue has attained finality.

One may also rely on the decision of the SC in case of ***CIT v. B.C. Srinivasa Shetty,***[40] wherein it was held that where the computation machinery fails, no tax could be levied on the concerned income. Further, the issue of valuation may still arise while recording the transaction and at the time of subsequent transfer; whether the cost of acquisition of the undertaking would be taken at Nil, at the fair value or the price at which the initial transferor acquired it, could be a matter that require resolution.

The issue of non-taxation may still be challenged by the tax authorities by invoking GAAR. In case the parties are unable to establish the commercial rationale behind the transaction, the tax authorities may contend that the principal purpose of the slump exchange was to avail tax benefits. If GAAR is invoked, it could have various consequences including, *inter-alia*, recharacterisation of the transaction.

“ Monetary consideration is necessary to constitute a slump sale under the IT Act. ”

40 AIR 1981 SC 972 (SC).

Deduction of indexed cost of acquisition available on sale of long-term capital asset while computing MAT liability

In the case of ***Best Trading and Agencies Ltd.***[41]**,** the Karnataka HC upheld the eligibility of indexed cost of acquisition on the sale of long-term capital asset while computing MAT liability. The HC also allowed the deduction of interest paid under Section 57(iii) of the IT Act against the interest earned on deposits.

Facts

Best Trading and Agencies Ltd. ("**Assessee**") is a company formed with the purpose of being utilised as a special purpose vehicle ("**SPV**") for restructuring of another company (Kirloskar Electric Company Ltd. ("**Kirloskar**") under a scheme approved by the Karnataka HC. Under the restructuring scheme, a surplus of non-manufacturing and liquid assets (including real estate, capital asset and land) together with certain liabilities were transferred to the Assessee for disbursement of liabilities.

The lenders and bankers were shareholders of the Assessee holding 88% of the equity. The Assessee had taken over the loans of erstwhile company and the interest payable to the term lenders was a part and parcel of the loan, which was outstanding. During AY 2005-06 and 2006-07, the Assessee earned interest from fixed deposits consisting of surplus from restructuring process. Against the said income, it claimed deduction for interest paid to the term lenders and creditors under Section 57(iii) of the IT Act. The Assessee also declared a long-term capital loss on sale of land being a capital asset.

During the assessment proceedings, the AO disallowed the interest claimed as deduction under Section 57 of the IT Act holding that and there is no direct nexus between the interest paid to term lenders and the interest earned from other sources. The AO also invoked MAT provisions under Section 115JB of the IT Act and assessed the Assessee on the book profits without giving a benefit of indexation on the cost of capital asset sold during the year.

The CIT(A) held that there was a close nexus between the interest earned on the fixed deposits and the interest earned on the fixed deposits and the interest paid to the lenders and the creditors. Accordingly, the claim of deduction under Section 57 of the IT Act was allowed. Further, the CIT(A) held that the Assessee was eligible to claim indexed cost of acquisition on sale of capital asset while computing MAT liability under Section 115JB of the IT Act.

However, the ITAT observed that there was no nexus between interest income and interest expenditure claimed under Section 57 of the IT Act. Therefore, such interest claimed under Section 57 of the IT Act should not be allowed. The ITAT also observed that the Assessee was not eligible to claim the benefit of indexation on the cost of capital asset sold during the year while computing the MAT liability.

The Assessee, therefore, appealed before the Karnataka HC.

Issue

i. Whether the Assessee was allowed to claim deduction under Section 57 of the IT Act against the interest earned on deposits?

ii. Whether the indexation benefit on cost of acquisition should be allowed on sale of capital asset for computing the MAT liability?

Arguments

The Assessee submitted that it acted as a conduit and was formed for the sole purpose of restructuring of Kirloskar under the scheme approved by Karnataka HC; the interest was paid to the term lenders and creditors. The Assessee submitted that the interest income accrued from the fixed deposits and nexus between deposit, interest earned and interest paid was directly established as the Assessee did not have any other activities in the relevant AY. The Assessee invited the attention of the HC to Section 57(iii) of the IT Act to state that the interest paid to the lenders and creditors was an allowable expenditure to be deducted from the income under other sources. The Assessee also submitted that the CIT(A) had recorded a finding that the interest was not taxable on the principles of diversion of overriding title, which was not considered by the ITAT.

The Assessee argued that there was no provision under the IT Act which prevented the Assessee from claiming the indexed cost of acquisition on sale of asset in a case where the Assessee is subjected to provisions of Section 115JB of the IT Act. It was argued that in view of Section 115JB(5) of the IT Act which provides that all other provisions of the IT Act apply, the indexed cost of acquisition has to be considered for the purpose of computation of book profit under Section 115JB of the IT Act. Section 115JB of the IT Act was not applicable in the case of the Assessee as it does not have book profits and has also not declared any dividends. In this regard the Assessee placed reliance on CBDT Circular No. 762 dated 18 February, 1998 ("**Circular**"), wherein the intent of introducing the provisions of

41 Best Trading and Agencies Ltd. v. DCIT ITA No. 191/2011.

MAT has been laid out. As per the Circular, the intent behind the introduction of MAT was to target companies which have earned substantial book profits and have paid handsome dividends but no tax has been paid by them to the exchequer. In this regard, the Assessee placed reliance on the decision of the SC in the case of ***Shoorji Vallabh Das and Co.***[42] and several other decisions by various courts.

On the other hand, the IRA submitted that there were no details as to how the restructuring scheme was framed. It was further submitted that in the absence of the scheme, it could not be held that the Assessee was holding funds as conduit. Therefore, the matter deserved to be remitted to the ITAT for decision afresh. The IRA also submitted that the Assessee was not entitled to deduction under Section 57(iii) of the IT Act in the facts of the case as there was no finding that the source of deposits which were placed under fixed deposits by the Assessee was the restructuring scheme framed/ approved by the Karnataka HC and no nexus had been proved between the funds deposited in the fixed deposits and the amount payable to the lenders and the creditors.

The IRA submitted that since the Assessee was not excluded from the ambit of Section 115J(1) of the IT Act, therefore, the submission of the Assessee that Section 115JB of the IT Act was not applicable to the facts of the case cannot be accepted. The IRA further submitted that Section 115JA(4) and Section 115JB(5) of the IT Act dealt with post determination of the profit under the Companies Act, 2013 (and erstwhile Companies Act, 1956). It was further submitted that if the contention of the Assessee that Section 115JB of the IT Act does not apply to the fact situation of the case is accepted, it would amount to rewriting the provision. Reliance was made to a number of judgments[43] regarding the applicability of MAT in various scenarios.

Decision

Rejecting the contention of the IRA that the matter needs to be considered afresh as no details of the framing of the scheme have been provided and Assessee could not be considered as a conduit in absence of the scheme, the HC ruled that both the AO and CIT(A) had taken note of the scheme and held that the Assessee was utilised as a special purpose vehicle for the purposes of distribution of surplus, if any, after clearance of debts of Kirloskar.

On eligibility of indexed cost of acquisition while computing MAT liability

The HC observed that the legislative history of introducing the MAT provisions shows that the intent of introducing the MAT provisions was to tackle companies which were making profits and declaring dividends without paying any taxes. Considering

42 CIT v. Shoorji Vallabh Das and Co., (1962) 46 ITR 144 (SC).
43 Tuticorin Alkali Chemicals & Fertilizers Ltd. v. Commissioner Of Income-Tax, (1997) 93 Taxman 502 (SC); Apollo Tyres Ltd. v. Commissioner Of Income-Tax, (2002) 122 Taxman 562 (SC); Joint Commissioner of Income-Tax v. Rolta India Ltd., (2011) 330 ITR 470 (SC); and M/S Yokogawa India Ltd. v. The Deputy Commissioner Of Income-Tax, ITA NO.87/2012 dated 04.06.2020.

this intent, the MAT provisions were held to be not applicable in the present case as the Assessee had not declared any dividend.

Further, the HC relied on a catena of judgments wherein it was held that while computing capital gains, benefit of indexed cost of acquisition was to be considered for computing MAT liability under Section 115JB of the IT Act. The HC held that on the invocation of Section 115JB(5) of the IT Act, the application of other provisions of the IT Act was open unless specifically barred by the applicable sections itself. The indexed cost of acquisition was a claim allowed under Section 48 to arrive at the income from capital gains. The difference between the sale consideration and the indexed cost of acquisition represents the actual cost of the Assessee. The Assessee was allowed to take the benefit of indexed cost of acquisition as denying the same would have resulted in taxing income other than actual/real income. The HC also observed that there was no provision in the IT Act to prevent the Assessee from claiming indexed cost of acquisition on the sale of an asset where the Assessee is subject to the provisions of MAT under Section 115JB of the IT Act. Section 112 of the IT Act which taxes long term capital gains cannot be denied on application of general provisions of MAT under Section 115JB of the IT Act. Therefore, the Assessee was eligible to claim the benefit of indexed cost of acquisition.

Allowability of interest paid to the creditors

The HC observed that the purpose of expenditure was relevant in determining the applicability of Section 57(iii) of the IT Act and the purpose must be 'making or earning of income'. The Assessee had, in order to cover the cost of interest payable to the creditors for the unpaid period, invested the surplus in the fixed deposits and earned interest on such deposits. The amount earned by way of interest was paid to the lenders and creditors. Thus, there was a close nexus between the interest paid to the creditors and interest earned on the deposits. The interest expenditure was incurred wholly and exclusively for the purpose of earning the interest income and, therefore, the Assessee was entitled to deduction of interest paid to creditors, from the interest income under Section 57(iii) of the IT Act.

Significant Takeaways

The issue of eligibility of indexation and other benefits available under the capital gains provisions while computing MAT has been a subject matter of debate before the Courts.

The Madras HC in the case of ***Metal & Chromium Plater Pvt. Ltd.***[44] held that the allowance or otherwise of the claim of deduction under Section 54EC of the IT Act has to be seen in the context of the provisions of Section 115JB of the IT Act, which is a self-contained code of assessment. The levy of tax is on the book profits after effecting various upward and downward adjustments as set out in terms of the Explanation to Section 115JB of the IT Act. The provisions of Section 115JB(5) of the IT Act open the assessment to the application of all other provisions contained in the IT Act except if specifically barred by the relevant section itself.

Similarly, Mumbai ITAT in the case of ***Savannah Real Estate Pvt. Ltd.***[45] held that the benefit of indexation under Section 48 of the IT Act should be allowed while computing capital gains to be added to the book profits under the provisions of MAT.

However, in the case of ***Dharmayug Investments Ltd.***[46], Mumbai ITAT held that only amount on sale of shares will be taken into account while computing book profits under Section 115JB and the amount of long-term capital gain cannot be imported while computing book profits under Section 115JB of the IT Act.

The HC in the present case also held that the Assessee was entitled to the benefit of indexed cost of acquisition on the sale of long-term capital asset while computing MAT liability under Section 115JB of the IT Act. Thus, this decision reinforces the position that MAT is a general code of taxability and it cannot determine the manner of application of provisions on other specific provisions of the IT Act.

> **“ Karnataka HC grants indexation benefit on capital gains while computing MAT liability. ”**

44 CIT v. Metal & Chromium Plater Pvt. Ltd., (2019) 415 ITR 123 (Madras HC).
45 ITO v. Savannah Real Estate Pvt. Ltd., ITA No. 6310/Mum/2017.
46 Dharmayug Investments Ltd. v. ACIT, ITA No. 1284/Mum/2013.

Depreciation on goodwill is available on acquisition of business operations of a company

In the case of ***Geodis Overseas Pvt. Ltd.,***[47] the Delhi ITAT reiterated that goodwill is a depreciable asset and is allowed to an assessee who had acquired it through the acquisition of inhouse shipping and logistics operations of a global corporation to claim depreciation on the goodwill of the acquired business.

Facts

Geodis Overseas Pvt. Ltd. ("**Assessee**") is an Indian company engaged in domestic and international transportation of time-sensitive documents and cargo. It is a wholly owned subsidiary of a Geodis SA, incorporated in France ("**Geodis**"), which is also engaged in similar businesses. In 2009, Geodis acquired the internal global logistics and freight forwarding operations of IBM Corporation, USA ("**IBM**") at a global level. Pursuant to the same, the Assessee acquired the internal logistics business from IBM India Pvt. Ltd., Network Solutions Pvt. Ltd and IBM Daksh Business Process Services Pvt. Ltd (collectively known as "**IBM India**") for a consideration of USD 2.7 million, exclusive of transfer taxes. As a part of the acquisition, the Assessee received supplier contracts, including the right to provide logistics services to IBM for up to 15 years, with an option to extend it for another seven years, along with employees and certain tangible assets (comprising of laptops). The Assessee showed an addition in the assets in goodwill at INR 147,293,773 and claimed depreciation at 25% amounting to INR 36,823,443. However, the AO as well as the DRP disallowed Assessee's claim of depreciation on the goodwill acquired as above. Being aggrieved by the order of the AO and DRP, the Assessee preferred an appeal before the ITAT.

Issue

Whether claim for depreciation on goodwill was allowable?

Arguments

The Assessee justified its claim of depreciation on goodwill on the basis that by virtue of acquisition of IBM India's logistic business, it became the sole logistic service provider to the entire IBM group in India, the expertise of its workforce also increased significantly by the addition of trained workforce from IBM India, market reputation of IBM India and all third-party contracts already existed with IBM India. The Assessee further relied on the landmark decision of the SC in ***Smifs Securities***,[48] wherein it was held that goodwill was an asset under Explanation 3(b) to section 32(1) of the IT Act and, therefore, was eligible for depreciation. The Assessee also cited ***Areva T&D India Ltd.,***[49] where the jurisdictional HC had held that business contracts, business information, skilled employees etc., acquired as part of a slump sale could constitute 'goodwill' for the purpose of claiming depreciation.

In terms of the valuation, the Assessee submitted that the business transfer agreement specifically mentioned that the purchase consideration was inclusive of goodwill and that out of the total consideration, laptops and other tangible assets were valued for a meagre sum of INR 5 lakh and the remainder of the consideration amounting to NR 14.8 crores approximately represented the goodwill value of the transferor viz. (i) the transferred workforce; (ii) supplier contracts, including the contract for being the sole service provider of IBM group; and (iii) market reputation of the transferor company.

It was contended on behalf of the IRA that *prima facie* no depreciation was allowable on goodwill as per the legislative intent of section 32 of the IT Act. According to the AO, the expression "or any other business or commercial rights of similar nature" in section 32 of the IT Act was restricted to intangible assets of a 'similar nature' akin to business and commercial rights and did not cover goodwill.

The IRA additionally contended that goodwill was not been defined in the agreement between the Assessee and IBM India and no separate valuation was made. Therefore, the IRA contended that the Assessee was unable to demonstrate that the amount paid to IBM India reflected as goodwill, was in fact paid to IBM India for acquiring certain business and commercial rights, as part of the purchase consideration. Moreover, it was alleged that since the Assessee had not become the sole service provider for IBM India, it did not transfer its brand name, commercial knowledge or technical know-how to the Assessee and the third party contracts that were acquired had expired soon after the acquisition, no goodwill was thereby acquired.

Decision

Without delving into an elaborate analysis, the Delhi ITAT, relying entirely on ***Smifs Securities*** and ***Areva T&D*** held that the Assessee was entitled to depreciation on goodwill and, therefore, allowed the appeal of the Assessee. The ITAT noted that these earlier decisions had applied the principle of ejusdem generis to establish that the legislature did not intend to provide for depreciation only in respect of the intangible assets specified in Section 32 of the IT Act, but also other categories of intangible assets of like nature. It had been held that "business or commercial rights" cannot be restricted only to the specified six categories of assets, i.e., knowhow, patents, trademarks, copyrights, licences or franchises. Business claims, information, records, contracts, employees, and knowhow are assets that are

47 DDIT v. Overseas Transport Co. Ltd., ITA No. 3129/Mum/2002 (Mumbai ITAT).
48 CIT v. Smifs Securities Ltd., (2012) 348 ITR 302 (SC).
49 Areva T&D India Ltd. v. DCIT, (2012) 345 ITR 421 (Delhi HC).

invaluable to the business. They are intangible assets comparable to a licence to carry on the relevant business. Without acquiring the same, the taxpayer would have had to commence the business from scratch and had to undergo a gestation period, which is not needed in case of acquisition of an up and running business.

Therefore, applying the rationale adopted in the above-mentioned decisions, the ITAT proceeded to allow the Assessee's claim, while overturning the decision of the AO.

Significant Takeaways

The issue of whether goodwill constitutes a depreciable asset is almost *res integra*, with multiple fora at higher levels having decided in favour of the taxpayer, including the SC in the case of ***Smifs Securities***[50]***,*** wherein it was held that the goodwill being the difference between the amount paid and cost of shares in the amalgamation scheme was an asset eligible for depreciation under Section 32 of the IT Act. Despite the same, depreciation claims on goodwill continue to be litigated by the IRA, such as in the case of the Assessee.

In the instant case, the IRA disallowed the depreciation on the goodwill on the grounds that the components of goodwill had not been identified and valued by the Assessee. further, the submissions made by the Assessee on the supplier contracts were disregarded on frivolous contentions such as the Assessee did not become sole service provider to IBM. It is worthwhile to highlight that out of the total sale consideration, only INR 500,000 was allocated towards the tangible assets (consisting of laptops, etc.) and the remainder was not allocated for any other specific assets. Ttherefore, the said remaining part of the consideration should automatically be construed as goodwill of the acquired business since the only other benefit (apart from laptops) accruing to the Assessee was the supplier contracts, employees, etc, which ought to have been classified as goodwill. Moreover, the transaction had taken place between third parties and thus, the question of manipulation of value was also ruled out. Therefore, disallowing the claim of depreciation on the ground that the taxpayer had failed to identify and value ofevery component of goodwill was against the principles established by the SC.

> **“ Assessee acquiring operations of an existing company is entitled to claim depreciation on goodwill if the operations acquired. ”**

50 B. Raveendran Pillai v. CIT, 332 ITR 531 (2011) (Kerala HC); CIT v. Hindustan Coca Cola Beverages Pvt. Ltd., 331 ITR 192 (2011) (Delhi HC).

CASE LAW UPDATES- DIRECT TAX

MISCELLANEOUS

Mumbai ITAT upholds the addition of unaccounted money stashed in bank account in HSBC, Switzerland

In the case of ***Renu T Tharani***[51], Mumbai ITAT ruled that a sum of INR 196 crore held by HSBC Switzerland in the name of Tharani Family Trust, of which Renu Tharani was a beneficiary, was assessable as undisclosed income of the Assessee.

Facts

Renu Tharani (“**Assessee**”), a lady in her late eighties, filed return of income (“**ROI**”) for AY 2006-07 on July 29, 2006 disclosing returned income of INR 0.17 million and disclosing herself as a resident in India for taxation purposes. No scrutiny was made in respect of the said ROI. However, based on the information received from the investigation wing of IRA, the assessment was reopened on October 31, 2014, under Sction 148 of the IT Act. The reasons recorded for reopening the assessment was information received by AO regarding her bank account with HSBC Geneva, Switzerland (“**HSBC**” or “**bank**”) which was alleged to have had a peak balance of USD 39.74 million (INR 1.96 billion) during the relevant AY 2006-07. Since this peak balance was not considered in the ROI of the Assessee, the AO concluded that the said income had escaped assessment.

The Assessee filed her objections to the reopening of assessment wherein she stated that the information obtained by the AO was erroneous and she did not hold any bank account with HSBC. The Assessee also claimed that she was a non-resident in India for taxation purposes during AY 2006-07 and thus, any income accruing or arising outside India was not liable to be taxed in India. In support of her claim, the assessee also submitted her copy of passport and travel details to prove that she was a non-resident in India during AY 2006-07.

The AO rejected the objections and proceeded to assess the income of the Assessee. The Assessee filed an appeal before the CIT(A) submitting that the reassessment proceedings were bad in law and against the addition made by the AO. However, the CIT(A) upheld the validity of reassessment proceedings and declined to interfere in the matter. Aggrieved, the Assessee filed an appeal before the ITAT challenging the validity of reopening the assessment proceedings as well as the addition made by AO.

Issues

i. Whether, basis information received from investigation wing of the IRA, the AO was justified in re-opening the assessment for AY 2006-07?

ii. Whether the AO was justified in making the addition of peak balance in HSBC to the total taxable income of the Assessee?

Arguments

The Assessee argued that she was residing in USA since March 23, 2004 and hence, was a non-resident for the relevant AY. She submitted relevant documentary evidence i.e. passport and travel details to substantiate her claim. Thus, she was not required to disclose the income accrued outside India in foreign bank account. Basis this, the Assessee also argued that there was a lack of direct nexus between the information coming to notice of AO and formation of belief of escapement of income, which was a necessary condition to be satisfied for reopening the assessment proceedings.

Further, the Assessee argued that the information received was not in respect of a bank account, but investment account held by GWU Investments Ltd. (“**GWU**”), a company incorporated in Cayman Islands. The Assessee got a written clarification from HSBC that GWU was the settlor of Tharani Family Trust (“**Trust**”)

51 Renu T Tharani v. DCIT, ITA No. 2333/Mum/2018.

and had given funds to GWU. Further, the clarification from HSBC stated that the Assessee was only a discretionary beneficiary of the Trust. She also submitted that she was not aware of GWU's source of funds.

The Assessee also submitted a written clarification from HSBC, which stated that eventually the Trust was terminated and none of the assets of the Trust deposited with HSBC was distributed to the Assessee. Thus, according to the Assessee, the taxability in her hands ought to have been confined to the monies actually received by her from the Trust. Since the Assessee did not receive anything from the Trust, and nothing remains in the investment account as the same had since been closed, she would not be liable to pay any tax. She relied on the wealth tax related decision of the SC in the case of ***Estate of HMM Vikramsinhji of Gonda***[52].

On the contrary, the IRA argued that the claim of the Assessee being a non-resident (even though it was mentioned as 'Resident' while filing ROI) was made only after the reopening of assessment was initiated. Notwithstanding the same, even if the claim was to be accepted that the Assessee was not residing in India since March 23, 2004, the huge funds to the tune of peak balance in the HSBC bank account abroad could not have been earned by the Assessee in a short span of one year i.e. after becoming a non-resident.

The IRA argued that the unaccounted monies in the HSBC bank account is usually not deposited by taxpayers in their own names, but through a complex web of layering, nominee directors and trusts, etc. Hence, there cannot be any other possible reason for an entity set up in a tax haven to leave such a huge sum for the Assessee as a beneficiary.

The ITAT relied on the ruling of co-ordinate bench of ITAT Mumbai in the case of ***Mohan Manoj Dhupelia***[53], wherein the facts were similar to the case of the Assessee at hand. In that case, the ITAT had held that discretionary trusts are created for the benefit of particular persons and those persons need not necessarily control the affairs of the trust. Thus, the bank account of the trust represented unaccounted money of the beneficiaries, even if no benefits were transferred to them. As per the IRA, in the case of the Assessee also, the Assessee was an Indian resident having interest and assets in India and in absence of showing a source of money, it would be inferred that the amounts deposited were unaccounted deposits sourced from India and, therefore, were taxable in India.

Decision

With respect to the re-opening of assessment, the ITAT observed that the ROI of the Assessee clearly showed that the Assessee had marked herself as a 'resident' for the relevant AY. Further, the peak credit at her disposal, as per the details of HSBC Switzerland bank account, was over 11,500 times her annual income. The ITAT observed that the AO had to record his satisfaction for initiating the income escaping assessment based on the material in his possession. A subsequent claim may be made during the proceedings by the Assessee about being a non-resident in relevant AY, which would have to be examined separately on merits in the re-assessment proceedings and adjudicated accordingly. This subsequent claim cannot be the reason for holding the reassessment proceedings as invalid.

Further, the ITAT observed that when the Assessee herself was making an incorrect claim in the ROI (by claiming her residential status as Resident in ROI, and subsequently submitting that she is a non-resident), because the AO believed in the claim and took initial steps of initiating reassessment proceedings on that basis, the Assessee could not claim that the AO was in error in considering her as a resident. Further, the ITAT re-emphasised on the fact that it was wholly unrealistic to assume that the money at her disposal in the Swiss Bank account reflected income earned outside India in such a short period of one year since she became a non-resident.

The ITAT observed that at the time of issuance of notice, the AO was only required to form a prima-facie view and not look for sufficiency of the reasons. For this, the ITAT relied on the judgments of Bombay HC in the case of ***Multi Commodity Exchange of India Ltd.***[54] ***and Multiscreen Media Pvt Ltd.***[55]

Based on the above, the ITAT held that the correctness of reopening of the assessment proceedings cannot be challenged and confirmed the action of the AO.

With respect to the merits of the case, the ITAT conducted its *suo moto* research on the HSBC Swiss leaks and reproduced the BBC news links on the same. The ITAT also recorded the stringent manner in which HSBC's role in tax evasion by unscrupulous taxpayers had been seen by law enforcement agencies in the world for which HSBC had to face criminal investigation and ultimately ended up in paying hefty settlements amounts in certain jurisdictions e.g. the US. The ITAT referred to the website of HSBC wherein HSBC was offering trust services as per which it was evident that trust structures were being employed to enable the settlor to transfer the legal ownership of settlor's assets (which then become the trust assets) to the trustee, who manages and holds the assets for the benefit of the beneficiaries (e.g. settlor and his family). The ITAT further noted that it is a common knowledge that trustees are often corporate entities based in the jurisdictions in which secrecy laws are very strict like in Cayman Islands.

The ITAT also noted that the Assessee had refused to sign the *consent waiver form*. This form would have enabled the AO to seek information from HSBC directly. Thus, the AO was deprived

52 Commissioner of Wealth Tax, Rajkot v. Estate of HMM Vikramsinhji of Gonda, (2014) 45 taxmann.com 552 (SC).
53 Mohan Manoj Dhupelia and other ITA no. 3544/Mum/ 2011 (ITAT Mumbai).
54 Multi Commodity Exchange of India Ltd v. DCIT, (2018) 91 taxmann.com 265 (Bombay HC) [SLP dismissed as reported in (2019) 101 taxmann.com 13 (SC).
55 Multiscreen Media Pvt. Ltd. v. CIT, (2010) 324 ITR 54 (Bombay HC).

of the opportunity to seek relevant information from HSBC in respect of Assessee's bank account. The ITAT categorically stated that if the Assessee had nothing to hide, there was no reason for not signing the consent waiver form. Hence, not signing the consent waiver form was considered as non-cooperation by the Assessee which made the ITAT conclude that she had something to hide. This conclusion was supported by the judgment of Bombay HC in the case of ***Soignee R Kothari***.[56]

The ITAT also noted that within a short time of information being received by India regarding Swiss leaks, the said investment account was closed, and assets were transferred back to GWU and it was almost impossible to find out beneficial owners of the company incorporated in Cayman Islands. In addition, within a short time thereafter, GWU's name was also struck off from the Registrar of Companies, Cayman Islands. Further, the Trust also stood terminated and no information was available about the Trust now. The ITAT questioned the timing of the closure of the account, the striking off of GWU's name and the termination of trust.

The ITAT noted that being the final fact-finding authority, its job was onerous and demanding and required it to take a holistic view keeping in mind the surrounding circumstances, preponderance of probabilities and ground realities and that it could not be swayed by the not so convincing, but apparently in order, statements and letters given by the Assessee.

In conclusion, the ITAT stated that the Assessee was not a public personality like Mother Teresa, that some unknown person with complete anonymity will settle a trust with her as a beneficiary of an amount as high as USD 39.74 million. Also, Cayman Islands is not known for philanthropists. It is, in-fact, known for an atmosphere conducive to hiding unaccounted wealth and money laundering.

Thus, considering the overall scheme of things, the ITAT confirmed the additions of INR 1.96 billion made by the AO and upheld by the CIT(A) and declined to interfere in the matter.

Significant Takeaways

While the IRA placed heavy reliance on the ruling of the co-ordinate ITAT bench in the case of Mohan ***Manoj Dhupeila***, which was affirmed by the ITAT. However, the ITAT did not consider the ruling of its co-ordinate bench in 2018 in another case of ***Deepak Shah,***[57] wherein on very similar facts and circumstances, the Mumbai ITAT had deleted the AO's addition of unaccounted money in an offshore account of HSBC Bank due to lack of substantial evidence. In the case of *Deepak Shah*, just as in the present case, the Assessee was asked to sign a consent waiver, which was duly refused by the assessee in that case. However, non-signing of the consent waiver form was not regarded as non-cooperation from the Assessee's end and was, therefore, not used as a ground to make an addition. In the instant case, the ITAT failed to appreciate the reasoning given by the Assessee for non-signing of the consent waiver form. As per the Assessee, she could not have signed a consent waiver for a bank account that belonged to GWU, not her.

Further, the ITAT's confirmation of addition made by the AO was based less on the actual facts of the case, but more on its own research done on the Swiss leaks and involvement of HSBC and the BBC reports. Further, the ITAT made certain assumptions in this case such as corporate entities are often set up in Cayman Islands with the intention of creating subterfuge structures to evade taxes, and accordingly, considered GWU as a shell entity. Further, the ITAT seems to have invalidated the trust structure and have assumed that the beneficiary should be aware of the contributor to the corpus of the trust. It may be said that the ITAT may not be entirely wrong in making such assumptions, as other factors like closure of the bank account, GWU and the Trust were all important factors. However, ITAT being the final fact-finding authority, ought to have probed into the matter in greater detail before upholding the addition made by the AO.

Notwithstanding the above, this judgment is an important one in terms of the comprehensive analysis. The independent research made by the ITAT proves it had not restricted itself by relying on reasoning/documents submitted by the assessee and the IRA. The fact that the issue involved black money stashed abroad made it all the more important for the ITAT to not take any lenient stance or give benefit of doubt to the assessee. Further, the assessee's submission that she was not aware of details of the settlor of the trust with a huge corpus, and in which she was a discretionary beneficiary, and her conduct in not letting the IRA obtain details directly from HSBC also worked against her. With such limited information and resources available with the ITAT, the approach and the judgment of the ITAT in this case may be considered to be a significant step and which may be followed in future in cases involving black money stashed abroad.

> **"ITAT upholds the addition of unaccounted money stashed in bank account with HSBC Switzerland, condemns the approach of Assessee as "Run with the hare and hunting with the hounds"."**

56 Soignee R Kothari v. DCIT, (2016) 386 ITR 466 (Bombay HC).
57 Deepak B Shah v. ACIT 16(2) Mumbai, (2018) 100 taxmann.com 43 (Mumbai ITAT).

No supremacy in the water fall mechanism to capital gains on sale of assets under IBC

The Allahabad bench of National Company Law Tribunal ("**NCLT**") in the case of **LML Limited**[58] has held that capital gains on sale of assets at the time of liquidation under the Insolvency and Bankruptcy Code ("**IBC**") would not form part of the liquidation cost, and therefore, would not get any priority in the waterfall mechanism prescribed under Section 53 of the IBC. As per the waterfall mechanism, liquidation cost falls at the top of the chart, followed by debts owed to secured creditors (who have relinquished their security) and Government dues.

Facts

In the matter pertaining to liquidation of LML Limited, the liquidator conducted various auctions in relation to the assets and realised a sum of INR 1.13 billion. The liquidator filed an application before NCLT seeking directions as to whether the capital gains tax was to be paid on proceeds received from sale of assets of the corporate debtor and if such tax was to be included in the liquidation cost or was to be distributed as Government dues as part of waterfall mechanism.

Issue

Whether capital gains tax liability arising out of sale of liquidation assets under IBC should be treated as liquidation costs so as to give priority over other dues?

Arguments

Liquidator submitted that as per Section 52 of IBC, at the time of liquidation, secured creditors have an option to either relinquish their security interest to the liquidation estate and receive proceeds from the sale of assets by the liquidator as part of the waterfall mechanism, or realise their security interest on their own as per the prescribed manner.[59] Where the secured creditors choose the latter option to realise their security interest on their own, they are entitled to first appropriate entire sale proceeds towards their dues without making any liability to pay the capital gains tax. Liquidator argued that if under the first option, capital gains were to be treated as a part of liquidation cost, then this would lead to an anomalous situation where secured creditors would realise less amount as compared to the amount they would have realised had they enforced their security on their own. Further, liquidator relied on Section 238 of IBC and Section 178 of IT Act to argue that waterfall mechanism prescribed under IBC prevailed over the provisions of IT Act.

Income tax department, on the other hand, argued that provisions of IBC prevailed over IT Act only in case of an inconsistency. As in the present case, there was no inconsistency with respect to chargeability of capital gains tax under IBC and IT Act, provisions of IT Act were applicable and capital gains was liable to be discharged.

Decision

The NCLT held that the capital gains cannot be considered as liquidation costs and can only be considered as Government dues under the waterfall mechanism. Liquidation cost means any cost incurred by the liquidator during the period of liquidation such as fee or remuneration payable to the liquidator, costs incurred by the liquidator for preserving and protecting the assets, properties, costs incurred by the liquidator in carrying on the business of the corporate debtor, etc. The bench accepted the contention that provisions of IBC prevailed over the provisions of IT Act, and therefore, any dues to the income tax department formed part of Government dues and could not be ranked above the debts owed to security creditors who had opted to relinquish their security.

The NCLT relied on the SC ruling in the case of ***Principal Commissioner of Income Tax v. Monnet Ispat and Energy Ltd.***[60] to state that the waterfall mechanism provided under Section 53 of IBC prevailed over provisions of IT Act and thus, capital gains cannot be considered as a part of the liquidation cost.

Significant Takeaways

This is a welcome ruling as it reinforces the principle that capital gains on proceeds from sale of assets at the time of liquidation would not be discharged as a government due under the waterfall mechanism. The SC in the case of ***Commissioner of Income Tax v. KTC Tyres (India) Ltd.***[61]**,** in the context of the water fall mechanism prescribed under the Companies Act, 1956 held that capital gain tax cannot be treated as liquidation expenses and liability towards workmen's dues; and debts owed to secured creditors had to be paid in priority to all other debts, including taxes due to the revenue. Similarly, in the context of IBC, NCLT Delhi in the case of ***M/s Shree Ram Lime Products Pvt. Ltd. v. Gee Ispat Pvt. Ltd.***[62] held that capital gains payable on sale proceeds, cannot be considered as a part of liquidation cost.

58 LML Limited (under liquidation) v. Commissioner of Income Tax, CA No. 389 of 2019 in CP(IB) No. 55/ALD/2017.

59 Secured creditors can enforce their security interest as per Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016 or Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("SARFAESI"), as applicable.

60 (2018) 211 Comp Cas 99 (SC).

61 (2014) 185 Comp Cas 17 (SC).

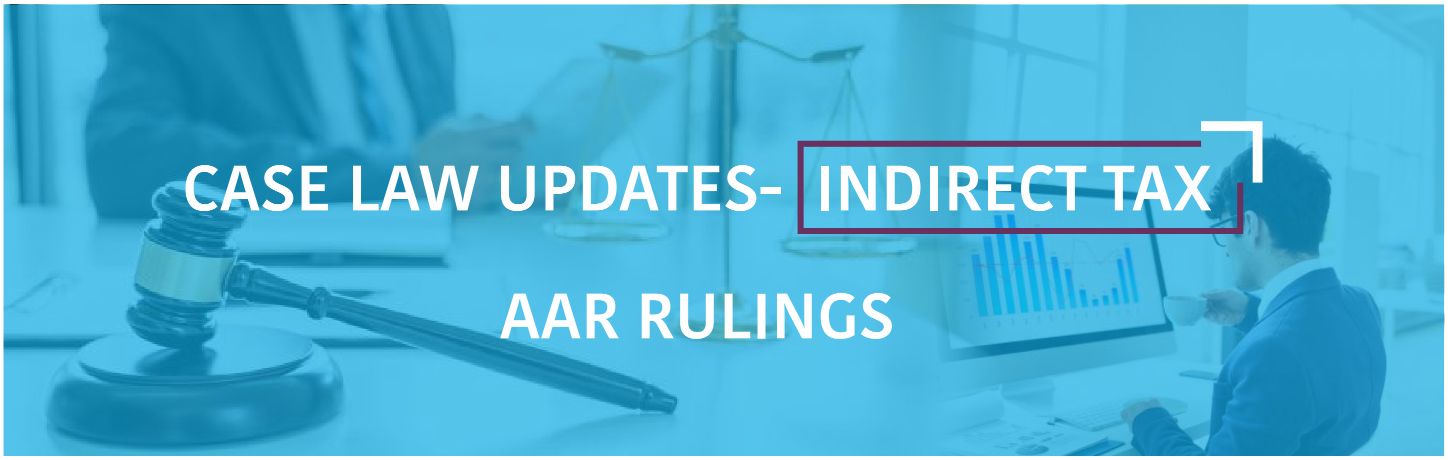
Notably, this NLCT Delhi decision has been referred in the Circular[63] issued by the Insolvency and Bankruptcy Board of India to apprise insolvency professionals and other stakeholders of the liquidation process of the significant orders and observations concerning liquidation process.

The income tax authorities consistently raise a plea to get preference for the tax dues over the secured creditors primarily because the income tax liabilities are given preference over the claims of secured creditors under the general liquidation proceedings (as against liquidation proceedings carried out through IBC) as per Section 178 of the IT Act. However, Section 53 of IBC starts with an non-obstante clause overriding all other existing laws viz. *"Notwithstanding anything to the contrary contained in any law enacted by the Parliament or any State Legislature for the time being in force,..."* and thereafter, provides a waterfall mechanism wherein interest of the secured creditors were given preference over the Government dues. It is also worthwhile to highlight that provisions of the IT Act had been amended to provide that Section 178 will not apply to proceedings covered under IBC. Therefore, it can be stated that there is no conflict between the provisions of IT Act and the provisions of IBC and the plea of the IRA that its dues should be given priority over the claims of secured creditors does not have any legal support, insofar as the liquidation proceedings carried out under the IBC are concerned.

This decision confirms the legal understanding and provide certainty to the stakeholders that the secured creditors would have a preferential right over the government dues, including tax, over the sale proceeds.

"Capital gains on sale of assets do not form part of liquidation cost."

62 CA -666 / 2019 in (IB) – 250(ND)/ 2017.
63 Circular No. Facilitation/002/2020, dated August 5, 2020.



Exemption under GST to educational institutions would not be available to coaching institutions

In the case of ***M/s Logic Management Training Institutes Private Limited***[64]**,** the AAR held that unapproved institutions, such as coaching classes, would not be covered under the exemption given to 'educational institutions' and services rendered by them would be exigible to GST.

Facts

M/s Logic Management Training Institutes Pvt Limited ("**Applicant**") was engaged in providing education by conducting classes for students to obtain legally recognised professional qualifications like Chartered Accountancy, Cost Accountancy, Company Secretary, etc. The Applicant was not a recognised institute, but offered qualification recognised by law. To do so, it followed the curriculum of certain legally constituted and recognised universities and provided lectures as well as notes specified by such universities. The Applicant also collected exam fees from the students and remitted the same to the respective exam bodies. Further, the Applicant provided other ancillary supplies to its students such as accommodation, food, selling textbooks etc.

Issue

1. Whether the Applicant would be entitled to the exemption under Notification No. 12/2017 Central Tax (Rate) dated June 28, 2017 ("**Exemption Notification**")?
2. Whether ancillary supplies made to students such as collection of exam fees, provision of hostel facility, selling of books etc. would be exigible to GST?

Arguments

The Applicant contended that it was imparting education on the basis of lectures and notes formulated as per the curriculum published by government-recognised institutions like ACCA[65], IMA USA[66] etc. The Applicant claimed that educational qualifications issued by foreign universities and recognised by the Government of India were to be treated as "certificate recognized by law"[67]. Therefore, it was not liable to discharge GST on such services as offering education as a part of a curriculum to obtain a qualification recognised by the law was exempt under the Exemption Notification. The Applicant also contended that it was collecting exam fees without any profit motive to help students who had no technical expertise, in making online payment. Therefore, such service was undertaken in its capacity as a pure agent. Additionally, it was contended by the Applicant that as the cost of hostel accommodation provided to students was less than INR 1000 per day, it was entitled to be exempted from the levy of GST as per entry 14 of the Exemption Notification, which provided a nil rate of tax on accommodation services where value of supply of a unit of accommodation was below or equal to INR 1000 per day. The Applicant concluded its arguments by stating that the sale of textbooks was undertaken with only a slight margin and it would also be exempted from the levy of GST.

64 AAR No. KER/76/2019 (Kerala AAR).
65 Association of Chartered Certified Accountants, the UK
66 Institute of Management Accountants, the USA
67 ITM International Pvt. Ltd v. Commissioner of Service Tax, Delhi [2017 (7) G.S.T.L 448 (Tri-Del)] (CESTAT Delhi).

Decision

The AAR took a strict interpretation of the term 'educational institutions' and held that the Applicant was not recognised or approved by bodies such as Institute of Chartered Accountants of India or Institute of Company Secretaries of India to conduct coaching as per the curriculum provided by such institutions to obtain a qualification granted by these institutions. Therefore, the Applicant would not fall under the definition of 'educational institutions' and its services would not be exempt from the levy of GST under the Exemption Notification. The AAR held that institutes providing coaching or training classes without issuing a certificate were classifiable as establishments providing commercial training or coaching under the service code 999293.

In relation to the taxability of exam fees collected by the Applicant, the AAR noted that in terms of Rule 33, subject to satisfaction of the conditions, any cost incurred by a pure agent would be excluded from the value of supply if the pure agent *inter alia* received only the actual amount incurred for procuring goods and/or services on behalf of the recipient. Therefore, it held that if the Applicant satisfied the conditions mentioned in Rule 33 of the CGST Rules while collecting the examination fees, the same would be excluded from the value of supply.

The AAR observed that the hostel accommodation provided by the Applicant was at a rate of less than INR 1000 per day, thereby satisfying the condition under the Exemption Notification. However, when the Applicant provided such accommodation services to students who also availed the coaching offered by the Applicant, the entire supply would be treated as composite supply with the coaching service being the principal supply. Therefore, supply of commercial training and coaching services along with the accommodation services would be taxable at the rate applicable to supply of the principal supply i.e. coaching services. The AAR concluded its findings by holding that no exemption would be available to sale of textbooks and they would be chargeable to GST at the notified rates.

Significant Takeaways

The ruling by AAR provides a very comprehensive view on the classification of various services involved in imparting education. In order to avail the benefit under the Exemption Notification, an institute needs to satisfy the dual conditions of imparting educational services as well as being an educational institution conferring a qualification recognised by law. This is in line with various AAR decisions[68] which held that the exemption for educational institutions would not be available to coaching institutions as they do not provide a qualification recognised by law. Therefore, coaching institutions, tuition classes, unaffiliated colleges would not be entitled to the benefit of exemption.

Further, denial of exemption to the accommodation services being a composite supply affords guidance to various institutions and establishments to structure their supplies. The ruling is a welcome relief from the ambiguity under the service tax regime for many educational institutions as it categorically clarifies that hostel facility provided to students will be exempt from GST. Separately, other institutions would benefit from splitting the provision of education service and accommodation service, by delinking the supplies and raising separate invoices to avail the benefit of exemption when the value of unit of accommodation is less than INR 1000 per day.

> **“ Institutes providing coaching, accommodation, textbooks to students would not qualify as educational institutions and would be liable to discharge GST. ”**

68 In re Simple Rajendra Shukla ST-ARA-06/2017/B-05; 09/03/2018 (Maharashtra AAR); In re Master Minds AAR No. 08/AP/GST/2020 (Andhra Pradesh AAR).

Sale of TDR and FSI leviable to GST

In the case of ***Vilas Chandanmal Gandhi***[69], the Maharashtra AAAR affirmed the AAR's ruling and held that GST was leviable on sale of Transferable Development Rights ("**TDR**") or Floor Space Index ("**FSI**") received as consideration for surrendering the joint rights.

Facts

Mr. Vilas Chandanmal Gandhi ("**Appellant**"), was an owner of the land situated within the limits of Pune Municipal Corporation ("**PMC**"). The Appellant entered into a Joint Development Agreement ("**JDA**") with M/s. Amar Builders and Developers ("**Developer**") under which the development rights in land were assigned/transferred to the Developer for a consideration in the form of 45% of the sale proceeds of the developed projects.

The underlying land for which JDA was entered into was held under reservation by the PMC. Upon realising that vacation/removal of reservation may not be possible, the Appellant and the Developer surrendered their respective rights in the said land in favour of PMC against which PMC awarded them TDR/Additional FSI as compensation by issuance of Development Right Certificates ("**DRCs**").

Subsequently, the Appellant entered into an agreement/deed of assignment to sell the proportionate TDR /Additional FSI awarded by PMC to Vamona Developers Pvt. Ltd. ("**VDPL**") and shared the sale proceeds in the agreed ratio.

The Appellant sought an advance ruling on the issue of leviability of GST on the transaction of sale of TDR/ FSI received as consideration for surrendering the joint rights in land. The AAR ruled that GST at the rate of 18% was leviable on sale of TDR/ FSI and the said transaction would fall under HSN 9972 i.e. Sr. No. 16, entry no. (iii) of the Notification No. 11/ 2017-C.T. (Rate) dated June 28, 2017 ("**Notification**").

Accordingly, the Appellant being aggrieved by the order of the AAR filed an appeal before the AAAR.

Issue

1. Whether GST was leviable on sale of TDR/ FSI received as consideration for surrendering the joint rights in land?
2. If yes, what would be the classification and the applicable rate of tax under GST?

Arguments

The Appellant submitted that as per the definition of 'Land' in Bombay Land Revenue Code, 1879[70], the development rights, being the benefit arising out of land, was to be construed as land only. Therefore, any transaction pertaining to a sale of TDR/FSI was in the nature of sale of land/ immovable property, which was covered under clause 5 of schedule III of the CGST Act and thus, was neither a supply of goods nor a supply of services. Hence, such transaction was outside the scope of GST.

The Appellant placed reliance on the decision of the Bombay HC in the case of ***Chedda Housing Development***[71], wherein it was held that FSI/TDR being benefits arising from the land would be considered as an immovable property.

The Appellant further submitted that the term 'service' would not include sale of immovable property in terms of the popular meaning and common parlance. It submitted that the purpose of GST was not to tax transactions of immovable property, similar to that under the erstwhile service tax, central excise and VAT laws.

The Appellant also contended that the transaction of sale of TDR/FSI would not fall under the HSN 9972 as the same was not in the nature of 'real estate services.' The Appellant also alleged that the AAR had based its ruling merely on the frequently asked questions issued by the Government which did not have any legal force.

During the course of the hearing, the Appellant made additional submissions that the scope of the term 'anything' in the definition of service needed to be understood in the context of GST scheme and would not cover all transactions.

The Appellant also contended that TDR or FSI was akin to money and that the reliance placed by the AAR on the rate/exemptions notifications was misplaced as leviability of tax would not be determined merely on the basis of entries in the rate/exemptions notifications. Lastly, the Appellant contended that the present case was not maintainable before the AAR as the subject transaction was already completed before filing of the application before the AAR.

On the other hand, the Department contended that the Appellant had entered into two separate transactions. Firstly, the Appellant had transferred the land to PMC for TDR/ FSI as consideration. Subsequently, on receipt of the TDR/FSI, the Appellant sold the said TDR/FSI in open market with a motive to earn profit. The Department also contended that the sale price of the TDR/FSI would depend on the real estate market situation at the time of sale and would vary from the value of TDR/ FSI given by PMC. Therefore, it was clear that the subsequent transaction was not related to land.

The Department also contended that the reliance placed on the decision in the case of ***Chedda Housing Development (Supra)*** was misplaced as the facts were very different.

69 In re Vilas Chandanmal Gandhi, Order No. MAH/AAAR/RS-SK/25/2020-21 (Maharashtra AAAR).
70 "Land" includes benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth, and also shares in or charges on, the revenue or rent of villages, or other defined portion of territory.
71 Chedda Housing Development v. Bibijan Shaikh Farid & Ors. [2007 (3) Mah.L.J.P. 402] (Bombay High Court).

Decision

As regards the maintainability of the case, the AAAR held that since the Appellant himself has approached the AAR for a ruling, it could not reject or question the same procedure, subsequently. Therefore, the AAAR refused to deal with the issue of maintainability.

The AAAR also rejected the contention of the Appellant that sale of the TDR would be sale of land covered under Clause 5 of Schedule III of the CGST Act, by relying on the judgment of the Hon'ble ITAT in the case of ***Shri Prem Rattan Gupta***[72], wherein it was held that TDR was not land, but a right arising out of land and hence, it was an immovable property.

The AAAR observed that Clause 5 only contained the words 'land' and 'building' and neither the CGST Act nor the schedules defined 'land'. Further, the CGST Act also made no reference to any other law while mentioning 'land' in Schedule III. Accordingly, the AAAR held that the term 'land' had to be interpreted strictly and would not be extended to cover 'benefits arising out of land' in light of the Supreme Court decision in case of ***Dilip Kumar and Company***[73], wherein it had been held that exemptions need to be interpreted strictly.

The AAAR observed that transfer of TDR made for consideration in course or furtherance of business would be considered as a supply of service as the definition of 'service' under the CGST Act was wide and would cover anything other than goods. The AAAR also stated that there was no section under the CGST Act that explicitly prohibited taxation of TDR as Schedule III to the CGST Act only mentioned 'land' to be outside the ambit of GST and not 'benefits' arising out of land.

In relation to the argument of the Appellant that the term 'anything' in the definition of service had to be read in the context, the AAAR stated that the definition had to be read in a context only to avoid absurdities and the Appellant had not pointed out any absurdity or illogicality in treating the TDR as a service.

The AAAR also stated that it did not agree with the submission of the Appellant that TDR was money; it stated that just because TDR/FSI was given in lieu of money it would not qualify as money. The AAR also held that the various notifications[74] issued by the Government revealed the intention of legislature to tax all the transactions of TDR/Additional FSI under the CGST Act.

Further, in relation to the Appellant's contention that the sale of TDR/FSI would not get covered under entry (iii) of the Heading 9972 of the Notification, the AAAR stated that the explanatory notes of the notification would not prevail over the notification itself and merely non-appearance of the service in the explanatory notes to that notification would not mean that the services were not covered under that heading.

In light of above deliberations, the AAAR upheld the AAR's ruling and held that TDR, FSI would be leviable to GST under heading 9972 at the rate of 18% as prescribed under entry No. 16(iii) of the Notification.

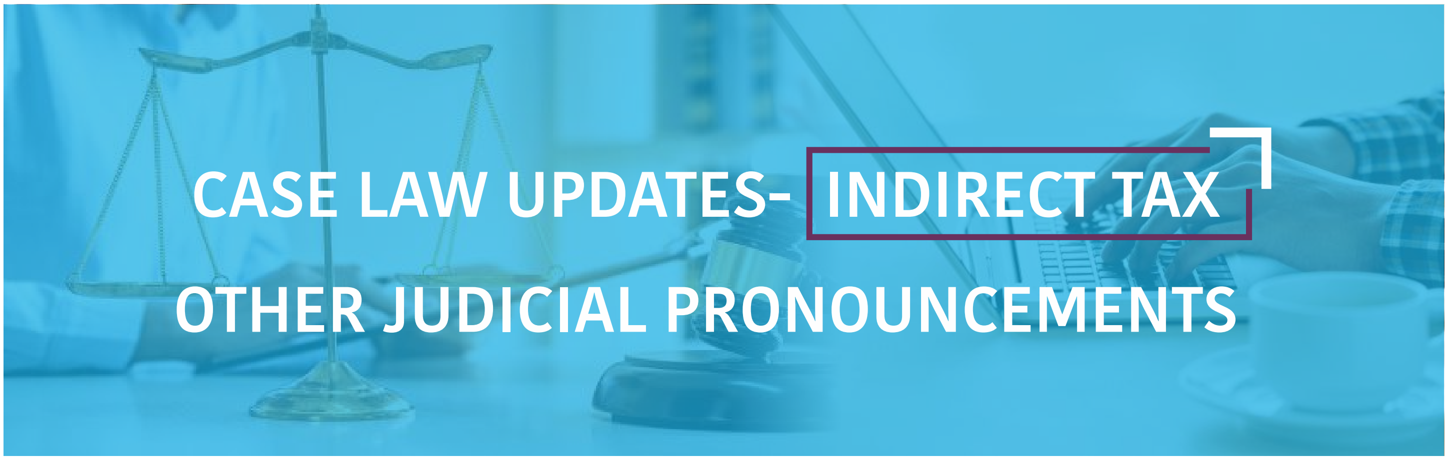
Significant Takeaways

The instant ruling confirms the GST liability on transfer of TDR/FSI on Appellant considering it to be a supply of service under the CGST Act. However, under the erstwhile service tax regime, transactions of TDR were not made liable to tax by the various judicial authorities on the ground that TDR is nothing but a benefit arising out of land and does not fall within the purview of service tax.[75]

However, the stand taken the AAR/ AAAR under the GST regimes remains to be tested before the higher forums as to whether such rights arising out of land can be regarded as an immovable property and accordingly, not liable to GST.

> **"TDR is liable to GST as it is a benefit arising out of land and not land itself."**

72 Income-tax Officer v. Shri Prem Rattan Gupta [ITA No.5803/Mum/2009] (Mumbai ITAT).
73 Commissioner of Customs (Import) Mumbai v. M/s Dilip Kumar and Company and Ors (App 3327 of 2007 dated July 30, 2018) (Supreme Court).
74 Notification No. 4/2019 -C.T. (Rate), dated March 29, 2019, Notification No. 5/2019 -C.T. (Rate), dated March 29, 2019, Notification No. 11/2017 – Central Tax (Rate), dated 28-06-2017
75 DLF Commercial Projects 2019 (27) GSTL 712 (Tri. Chan.) (Chandigarh CESTAT).



CASE LAW UPDATES- INDIRECT TAX

OTHER JUDICIAL PRONOUNCEMENTS

Taxpayer would be eligible to claim refund of Education Cess, Secondary and Higher Education Cess and the Krishi Kalyan Cess

In the case of ***Bharat Heavy Electricals Ltd***[76], the CESTAT held that where the taxpayer could not utilise the credit on account of those becoming impossible to use, he would be eligible for the cash refund. Accordingly, Education Cess, Secondary and Higher Education Cess and the Krishi Kalyan Cess ("**Cesses**") lying as CENVAT credit balance on June 30, 2017 would be eligible for the cash refund.

Facts

Bharat Heavy Electricals Ltd ("**Appellant**") was engaged in the manufacture and supply of equipment, for generation and transmission of electrical energy at ex-Thermal, Hydro, and Nuclear Power Stations. The credit of Cesses availed on procurement of indigenous inputs and inputs services was accumulated on the account of supply of products to Mega/Ultra Mega Power Projects, SEZ, EOU, etc. as they were exempt from payment of duty. The Appellants did not seek refund of unutilised credit on the expectation that they would be able to use them on domestic clearances on the basis of their past clearances. While the credit balance of service tax and central excise duty was carried over via TRAN-1 to GST regime, the balance of unutilised credit of Cesses was carried by Appellant in their ER-Returns only till the implementation of GST, i.e. upto June 30, 2017. Therefore, the Appellant filed refund claim of the unutilised Cesses with the relevant authority, which was rejected on the ground that since there was neither a provision to carry over the impugned cesses under the GST regime nor for refund of the same, leading to credit lapse. The Commissioner (Appeals) also rejected the refund on same ground. Aggrieved by the same, the Appellant filed an appeal before the CESTAT.

Issues

Whether the Appellant would be eligible to claim refund of Cesses which were not carried over in TRAN-1 to GST regime?

Arguments

The Appellant contended that the refund was admissible to the Appellants as the valid credit in their accounts on July 01, 2017 was eligible to be utilised for payment of duty on their domestic clearances. However, the same could not be utilised as the Cesses were not carried over to the GST regime due to absence of transitioning provision. In this regard, the Appellant relied on the settled position of law that where lawful credit accumulated in the accounts of a taxpayer could not be utilised due to closure of the factory or shifting of the factory to another area which was exempt from payment of duty, such valid earned credit would be refunded in cash.[77] In other words, there was no provision in the central excise legislation which would prohibit refund of such credit.

The Appellant also rebutted that the ruling in Cellular operator's case[78] was not applicable since the issue involved was different. In the instant scenario the relief claimed by the Appellant was not to allow payment of GST through Cesses. The Appellant

76 Bharat Heavy Electricals Ltd v. the Commissioner of CGST, Central Excise and Customs, 2020-VIL-402-CESTAT-DEL-CE. (Delhi CESTAT).

77 CCE Hyd. v. Apex Drugs & Intermediates Ltd. 2014 (314) E.L.T. 729 (Tri-Mumbai); Leo Oils & Lubricants v. CCE Chennai-I 2016 (343) ELT 1105 (Tri-Chennai.); Bangalore Cables P. Ltd. v. CCE Bangalore-III, 2017 (347) ELT 100 (Tri-Bangalore); CC,CE&ST Hyd.-IV Vs. Apex Drugs & Intermediates Ltd. 2015 (322) E.L.T. 834 (Tri- Andhra Pradesh); CCE v. Birla Textile Mills, 2015 (325) ELT (Tri-Delhi) Slovak India Trading Co. Pvt Ltd. 2006 (201) ELT 559 (Tri-Karnataka)

78 W.P. (C) no. 7837/2016, (Delhi High Court).

further contended that the right to credit was vested as soon as input goods/services were received.[79] Accordingly, since the balance of the Cesses constituted a valuable and substantive right, it would not be obliterated or taken away. Therefore, the exchequer was bound to refund the Cesses.

On the other hand, revenue authority contended that there was neither a provision to carry over the credit of Cesses to the GST regime nor was there any specific provision to refund the same. Hence, the credit of Cesses would lapse. In this regard, the revenue authority relied on CESTAT ruling which stated that refund was not a vested right in absence of specific provision. Therefore, refund of credits would not be granted at the time of closure of a factory as there was no law which permitted such refund. [80]

Decision

The CESTAT observed that the credit of Cesses which were available with Appellant till July 01, 2017 could be utilised as per the erstwhile legislation, however, it could not be carried to GST regime. Therefore, the Appellant was unable to utilise the same. The CESTAT relied on the judicial precedents that the credits earned were a vested right and would not automatically lapse with the change of law unless there was a specific provision which restricted the refund. The CESTAT noted that there was no provision in the newly-enacted law which stated that credit of Cesses would lapse. Further, the CESTAT drew guidance from precedents which held that refund would be available to taxpayer, if he was unable to utilise the credit due to closure of factory or shifting of factory to a non-dutiable area. Therefore, the CESTAT held that the Appellant was eligible for the cash refund of balance of Cesses available on June 30, 2017.

Significant Takeaway

The transfer of credit of Cesses through TRAN-1 into GST regime has been one of the most debated and litigated issues. With the aforementioned CESTAT ruling, a ray of hope would come to all taxpayers who were unable to transfer Cesses into GST regime or seek refund of credit of such Cesses. The CESTAT ruling has highlighted the applicability of principle that the validly earned credits were a vested right and their refund would be available to taxpayer, if the taxpayer could not utilise the credit due to closure of factory or shifting of factory to a non-dutiable area even in scenario of change in law.

> **“In case of change in law, balance of non-transitional credit could be refunded where there is no specific provision extinguishing such credits.”**

79 Eicher Motors v. UOI 1999 (106) E.L.T. 3 (Supreme Court).
80 Steel Strips v. CCE Ludhiana 2011 (269) E.L.T. 257 (Tri-LB).

Section 13(8)(b) of the IGST Act is not ultra vires to the Constitution.

IIn the case of ***Material Recycling Association v Union of India***[81], the Gujarat HC held that Section 13(8)(b) read with Section 2(13) of the IGST Act, which provided the place of provision of intermediary services to be the location of the supplier, was not *ultra vires* or unconstitutional in any manner.

Facts

Material Recycling Association ("**Petitioner**") consisted of member industries and traders ("**Members**") who were engaged in providing business promotion and marketing services to principals located outside India. The Members also facilitated sale of goods by such foreign principals to Indian customers as well as customers in non-taxable territory. The members earned commission on such sales after the proceeds were received by their clients in foreign convertible currency. They did not play any role in the actual sale or purchase of goods.

Issue

Whether Ssection 13(8)(b) of the IGST Act[82] read with Section 2(13) of the IGST Act[83] was *ultra vires* to the provisions of the Constitution as well as the principles of GST?

Arguments

The Petitioner submitted that Article 286 of the Constitution barred the States from levying a tax on supplies of goods or services which took place outside the State or were in course of import or export. However, as Section 13(8)(b) classified the location of the supplier to be the place of provision of intermediary services where either the service recipient or the supplier was located outside India, such service were treated as an intra-state supply as per Section 8(1)[84] of the IGST Act. Since, both CGST and SGST were levied on intra-state supplies, States were assumed to have the power to tax intermediary services, even where services were rendered to foreign principals. Therefore, levy of SGST by a State on a supply which was in the course of export, was in violation of Article 286 of the Constitution.

The Petitioner argued that while Parliament was authorised to determine principles for categorising any supply as either an inter-state supply or import/export, it was not empowered to artificially assign the place of supply to be in India when services were actually exported.

The Petitioner further contended that as per Section 12 of the IGST Act, where the location of the supplier and the recipient was in India, the place of provision of service ("**PPOS**") would be the location of the recipient, and the same principle would be applicable for intermediary services as well. However, under Section 13(8)(b) of the IGST Act, the PPOS for intermediary services would be the location of the supplier merely because one of the parties was located outside India. Therefore, the Petitioner contended that since Section 13(8)(b) of the IGST Act prescribed different yardsticks for determination of PPOS for the same set of services i.e. intermediary service, it was also in violation of Article 14 of the Constitution.

The Petitioner also contended that the definition of intermediary was vague and no attempts were made to define the scope of the phrase 'services provided on one's own account'. The Petitioner argued that such vague laws were liable to be struck down.[85] The Petitioner contended that Section 13(8)(b) was also in contravention to the principles of GST *inter alia* due to the following reasons:

(i) Section 13(8)(b) was an aberration from the destination-based theme of GST, as it attempted to tax basis the location of the supplier;

(ii) Section 13(8)(b) would lead to double taxation as the intermediary services would be taxed in India, being the location of the supplier as well as in the country of the service recipient, being import of service; and

(iii) The IGST Notification no. 20/2019 dated September 09, 2019 ("**Notification**") exempted the payment of tax of intermediary services when the location of the supplier and recipient of goods was outside India. Therefore, an unreasonable distinction was made between intermediary services rendered for movement of goods versus the transactions of service.

On the other hand, the Respondent argued that by virtue of Article 246A of the Constitution, the Parliament was given wide powers inter-alia to create deeming fiction under Section 13(8)(b) of the IGST Act. Since the location of the supplier of intermediary services was in the taxable territorial of India as per Section 13(8)(b) of the IGST Act, supply could not be treated as export of services[86] as defined under IGST Act. Therefore, Section 13(8)(b) of the IGST Act was not violative of Article 286 of the Constitution.

The Respondent further argued that the Parliament was in legislative competence to the right to categorise goods and

81 R/Special Civil Application Nos. 13238 and 13243 of 2018

82 Section 13 of the IGST Act determines the place of provision of service when the location of either the supplier or the recipient of service is outside India. In such a scenario, section 13(8)(b) provides that the place of provision of intermediary services would be the location of the supplier.

83 Section 2(13) of the IGST Act defines an intermediary as broker, an agent or any other person, by whatever name called, who arranges or facilitates the supply of goods or services or both, or securities, between two or more persons, but does not include a person who supplies such goods or services or both or securities on his own account

84 Supply of goods where the location of the supplier and the place of supply of goods are in the same State or same Union territory shall be treated as intra-State supply

85 Kartar Singh v.State of Punjab (1994) 3 SCC 569 (Supreme Court); Shreya Singhal v. Union of India (2015) 5 SCC 1 (Supreme Court).

86 Section 2(6) of the IGST Act.

services for the purpose of taxation in alignment with the policies of the Government and, therefore, separate place of supply for intermediary services for separate set of recipients was not violative to Article 14 of the Constitution.

The Respondent relied on the similar PPOS provisions and contended that the differential treatment to intermediary services as against the rest of services, was always there and it was neither unlawful nor a violation of the Constitution. Lastly, it contended that though the intermediaries provided their services to foreign principles, but the place of effective use and enjoyment of such service was at the location where the agent/intermediary was located, and therefore, the general rule was not the appropriate proxy for determining place of supply for intermediary service. Therefore, intermediary services were to be accorded distinctive treatment and the same would be within the contours of the GST legislations.

Decision

The Gujarat HC discussed the constitutional provisions in detail and held that Article 246(A) of the Constitution gave the Parliament the exclusive rights to frame laws for inter-state supply of goods or services.

The HC also looked into the relevant provisions under IGST Act and noted that the basic logic or inception of Section 13(8)(b) of the IGST Act was to levy CGST and SGST. Such intermediary service, therefore, would be out of the purview of IGST, irrespective if it was provided to a person in India or outside India. The HC held that only because the invoices were raised on the person outside India with regard to the commission and foreign exchange was received in India, it would not qualify to be export of services, especially when the legislature had thought it fit to consider the place of supply of services as place of person who provided such service in India.

The HC also held that there was no deeming fiction created by the Parliament, instead a stipulation was made under the GST law to consider the location of the service provider as the PPOS and consequently, such supply was not treated as 'export of services'. The position of law also existed under the service tax regime, and therefore, Section 13(8)(b) of the IGST Act had rightly considered the location of supplier of service as place of supply so as to attract CGST and SGST.

Accordingly, the HC held that Section 13(8)(b) read with Section 2(13) of the IGST Act was not ultra vires or unconstitutional in any manner. However, the HC left it open for the Respondents to consider the representation made by the Petitioner to consider the grievances.

Significant Takeaways

The HC failed to consider that in the service tax regime, there was no distinction in the place of provision of intermediary service in domestic or cross border transactions but under the GST regime separate treatment is meted out to intermediary services when both the supplier and recipient were located in India vis-à-vis the situation when either of the parties was located outside India. The HC also failed to pinpoint the fallacy of the Notification which imposes a nil rate of tax when an intermediary is facilitating a supply of goods between two foreign parties, but does not extend the benefit to intermediaries facilitating a supply of services between two foreign parties or those supplying.

However, while the HC has upheld the constitutionality of the provisions determining the PPOS of cross-border intermediary services, it has left open an opportunity for the Government to consider the representations of the intermediaries and address their grievances. Therefore, the Government should avail the opportunity by formulating unambiguous guidelines to determine the scope of intermediary services.

> **"An intermediary cannot be regarded as an exporter of services because he is only a broker who arranges and facilitates the supply of goods or services or both."**

Taxpayer would be eligible to claim refund of unutilised input tax credit for services in case of inverted duty structure

In the case of ***VKC Footsteps India Pvt. Ltd.***[87], the Gujarat HC held that the exclusion of refund of tax paid on "input service" as part of the refund of unutilised ITC in case of inverted duty structure was contrary to the provisions of Section 54(3) of the CGST Act which provided for claim of refund of "any unutilised input tax credit".

Facts

VKC Footsteps India Pvt. Ltd. ("**Petitioner**") was engaged in the manufacture and supply of footwear which attracted the levy of GST at an effective rate of 5%. The petitioner procured input services such as job work services, goods transport agency services, etc. and inputs such as synthetic leather, PU polyol, etc. for use in manufacture. Most of these inputs and input services were exigible to GST at effective rates of 12% and 18% respectively, and Petitioner availed the ITC of the same.

Since the rate of GST paid by the Petitioner on such procurements was higher than the rate of GST payable on the outward supply of footwear, there was an accumulation of unutilised ITC in the electronic credit ledger of the Petitioner.

The GST legislation provided refund of unutilised ITC in case of inverted duty structure. However, the formula prescribed for computation of the amount of refund of unutilised ITC in the CGST Rules allowed to claim the refund of unutilised ITC on inputs only. The refund of unutilised ITC on input services was not provided therein. Aggrieved by the same, the Petitioner challenged the validity of Rule 89(5) of the CGST Rules to the extent it denied refund of unutilised ITC on input services.

Issue

Whether the Rule 89(5) of the CGST Rules was ultra vires to the extent it denied refund of unutilised ITC on input services?

Arguments

The Petitioner contended that the restriction on refund of unutilised ITC on input services was contrary to the fundamental principle of GST. In this regard, the Petitioner highlighted that Section 54(3) of CGST Act used the phrase "any unutilised input tax credit". 'Input tax' was specifically defined under the CGST Act to mean tax charged on supply of goods or services or both made to a registered person. Thus, the use of the word "any" would include all ITC i.e. even ITC on input services. Therefore, 'input tax credit' used in Section 54(3) of CGST Act would include ITC on both inputs and input services.

The Petitioner also argued that Section 54(3) of CGST Act would not enable the Central Government/executive to frame/enact rules as it did not use the phrase "as may be prescribed". Therefore, any rule framed in this regard was entirely unnecessary and unwarranted. Moreover, Section 164(1) of the CGST Act conferred a general rule making power on the Government for carrying out the provisions of the CGST Act. To the extent the formula under Rule 89(5) restricted the refund of ITC to inputs only, it was not carrying out the provisions of the Act but restricting the provisions of Section 54(3) of CGST Act. Accordingly, Rule 89(5) of the CGST Rules which provided for the formula for refund and the corresponding explanation (a), which defined Net ITC to exclude ITC on input services was ultra vires the CGST Act to that extent.

The Petitioner also submitted that the formula under Rule 89(5) of CGST Rules for inverted duty structure was based on the same principle as the formula prescribed for refund in case of exports, i.e. refund of ITC in proportion to export turnover. However, even in the absence of any restriction on refund of ITC on input services under the CGST Act, it restricted such ITC. Therefore, Rule 89(5) was contrary to the CGST Act.

The Petitioner also challenged that the non-availability of refund of ITC on input services amounted to an indirect levy of tax without authority of law under Article 265 of the Constitution. The Petitioner also contended that granting refund of ITC on inputs and denying refund in respect of input services was arbitrary, irrational, discriminatory and thereby in violation of Article 14 of the Constitution.

On the other hand, the respondent contended that the CGST Rules including Rule 89(5) were not ultra vires the CGST Act as it was made pursuant to the powers conferred under Section 164 of the CGST Act. Section 164 of the CGST Act conferred the widest possible power on the Government to make rules by way of notification for carrying out the provisions of the Act on the recommendations of the GST Council.

The respondent also relied on earlier jurisprudence which had observed that ITC was a form of concession provided by the legislature and would be made available subject to conditions.[88] In another case, it was held and observed that the quantum of tax credit to be given and the circumstances in which it was to be given was a domain of the legislature.[89]

Decision

The HC held that exclusion of refund of tax paid on 'input service' as part of the refund of unutilised ITC was contrary to the provisions of Section 54(3) of the CGST Act, which provided for claim of refund of any unutilised input tax credit'. In this regard, HC observed that the term 'input service' as defined in Section

87 VKC Footsteps India Pvt. Ltd. v. UOI, 2020 (7) TMI 726 (Gujarat HC)
88 Jayam and Co. v. Assistant Commissioner and Anr., [2016] 15 SCC 125 [SC] (Supreme Court).
89 Reliance Industries Limited v. State of Gujarat, [2018] 50 GSTR 14 (SC) (Supreme Court).

2(63) meant the credit of input tax. Additionally, the term 'input tax' was defined as the tax charged on any supply of goods or services. Further, the word 'input' meant any goods other than capital goods and 'input service' meant any service used or intended to be used by a supplier. Thus, HC observed that 'input' and 'input service' were both part of the 'input tax' and 'input tax credit'. Therefore, as the legislature had provided that registered person was eligible to claim a refund of 'any unutilised input tax', the refund would not be restricted only to 'input' by excluding the 'input services' from the purview of 'input tax credit' under Rule 89(5) of the CGST Rules.

It also held that rule making power under Section 164 of the CGST Act was to be used for formulating procedure, but it was not to be used for restricting meaning of ITC as provided under the CGST Act.

Significant Takeaways

The aforementioned ruling clearly appears to rectify the differential treatment created between input, input services and capital goods. Even though the fate of ITC pertaining to capital goods has not been pronounced, the rationale will equally apply to capital goods.

Although, the aforementioned ruling had brought great relief to industries operating in inverted tax structure, as a lot of players had huge capital blockage in form of unutilised ITC of input services, the same has been disturbed again by the Madras HC ruling in ***Transtonnelstroy Afcons Joint Venture v. Union of India, 2020-VIL-459-MAD***, which upheld Rule 89(5) of CGST Rules. The Madras HC based its ruling on following points:

a) Refund was a statutory right and it is a valid exercise of power to restrict refund only to a class of taxpayer;

b) There was no necessity to adopt the interpretative device of reading down so as to save the constitutionality of Section 54(3)(ii) of the CGST Act.

c) Section 54(3)(ii) of the CGST Act was the source of restriction placed by Rule 89 (5) of the CGST Rules.

Due to two diverging rulings by two different HCs, the taxpayers are left in complete state of confusion and there is a high possibility that any refund claim filed by taxpayer would be dismissed by revenue by relying on the Madras HC ruling. Therefore, there is an urgent need of clarity on this issue to prevent flooding of HC with such refund rejections.

> **“ Rule 89(5) of the CGST Rules was ultra vires to the extent it denied refund of unutilized ITC on input services. ”**

SEZ units can claim refund of unutilised ITC distributed to it by its input service distributor

In the case of ***M/s Britannia Industries Limited***[90], the HC held that the petitioner was entitled to refund of the credit distributed by the Input Service Distributor ("**ISD**") registration as there was no specific supplier who could claim the refund under the provisions of the CGST Act.

Facts

M/s Britannia Industries Limited ("**Petitioner**"), a SEZ unit, had filed an application for refund of unutilised IGST credit received from its ISD in terms of the CGST Act, for the services provided by it.

However, a Show Cause Notice ("**SCN**") was issued by the Department ("**Respondent**"), proposing rejection of the refund application on the ground that since the services received by SEZ unit were zero rated and no GST was payable on such inward supplies, the Petitioner was not eligible for refund under Section 54 of the CGST Act that provided for refund of tax under GST. The SCN also stated that there were no circulars / notifications / relevant guidelines to provide for processing of GST refund claim of SEZ units in respect of tax paid on inward supplies.

Pursuant to a personal hearing, the Respondent passed an order rejecting the refund claim of the Petitioner. Aggrieved by the said order, the Petitioner filed the present writ petition before the Gujarat HC.

Issue

Whether a SEZ unit can claim a refund of unutilised ITC lying in its Electronic Credit Ledger, which was received from its ISD?

Arguments

The Petitioner submitted that it was eligible for refund of the unutilised ITC distributed to it by ISD, in terms of Section 16 of the CGST Act[91].

The Petitioner submitted that if the credit of service tax could be distributed to all the units by an ISD as per the manner prescribed in Notification no. 28/2012 dated June 20, 2012, then the refund of IGST credit distributed would also be refunded to the SEZ units as SEZ unit was not specifically excluded from the list of units to whom credit should be distributed.

The Petitioner argued that the refund under Section 54 of the CGST Act could not be denied to him merely on the ground that there was no express provision for processing of the refund under the CGST Act as the intention of Section 16 of the IGST Act, which provided for zero rated supply, was to avoid the cascading effect of taxation. The Petitioner also argued that the entire scheme of GST did not restrict any distribution of common credit by an ISD to an SEZ unit and on a conjoint reading of Sections 16 and 54 of the CGST Act, it was clear that a SEZ unit was entitled to get the refund of unutilised ITC lying in the Electronic Credit Ledger.

Further, the Petitioner contended that in terms of Circular No. 17 dated November 15, 2017, a refund of unutilised ITC of IGST paid and distributed by ISD, was allowed on filing of an application in FORM GST RFD-01A, post May 14, 2019.

The Petitioner also relied on ***M/s. Amit Cotton Industries***[92], wherein the HC had allowed the claim of the petitioner for refund of IGST in case of an export unit that had claimed duty drawback even though there was no specific provision for accepting the such refund claims.

On the other hand, the Respondent argued that the present writ petition was not maintainable as the Petitioner had not exhausted the alternative remedy of filing of appeal before the appellate authority available to him under Section 107 of the CGST Act.

The Respondents also contended that the Petitioner was not entitled to refund of the ITC as it was an SEZ unit and all supplies to such unit were zero rated. It further contended that only the IGST paid in relation to the supplies to SEZ unit was eligible for claim of refund as there was no provision for granting of refund to the SEZ unit in the IGST Act except the procedure prescribed under Section 16(3) of the IGST Act.

The Respondents submitted that in view of the provision of Section 54 of the CGST Act, read with Rule 89 of the CGST Rules, only a supplier of goods or services could file an application for refund and not the recipient of the services. It contended that in the facts of this case, the Petitioner was a recipient of service and hence, was not entitled to apply for refund under the provisions of the CGST Act.

The Respondents lastly also submitted that there was no circular, notification or guidelines issued by the Government or CBIC to process the ITC refund claims of the units located in the SEZ and therefore, the competent authority had rightly rejected the refund application made by the Petitioner.

Decision

The HC looked into the relevant provisions under the CGST Act and the IGST as well as the decision in ***M/s. Amit Cotton Industries (supra)*** and noted that the finding of the said decision would also answer the controversy raised in this petition as in the said decision the HC had allowed refund of IGST to export units that had claimed duty drawback even though there was no express provisions in relation to the same under the CGST Act. The HC held that instead of Rule 96 of the CGST

90 M/s Britannia Industries Limited v. Union of India (TS-728-HC-2020 (Guj.) NT) (Gujarat HC).

91 Section 16 of the CGST Act allowed claiming of credit of tax charged on any supply of goods or services or both by the supplier which are used or intended to be used in the course or furtherance of its business.

92 M/s. Amit Cotton Industries Through partner Veljibhai Virjibhai Ranipa v. Principal Commissioner of Customs (Special Civil Application No.20126/2018 on June 27, 2019) (Gujarat HC).

Rules which was applicable in the aforementioned case, Rule 89 of the CGST Act would be applicable in the present matter which pertained to refund of ITC.

The HC also rejected Respondent's contention that the Petitioner, not being a supplier, was not entitled to file refund application. The HC clarified that in the present case, ISD was an office of the supplier of goods and services that received tax invoices issued towards the receipt of input services and issued a prescribed document for the purpose of distributing the credit. Therefore, it was not possible for a supplier of such inward supply of goods and services to file a refund application in the present case. The HC held that Petitioner was entitled to claim refund of the ITC lying in the Electronic Credit Ledger, in connection to supplies made to it as there was no other specific supplier who could claim refund as the ITC was distributed by the ISD.

Accordingly, the HC allowed the claim of refund of unutilised ITC distributed by ISD and directed the Respondents to process the claim of refund of Petitioner for unutilised IGST credit lying in Electronic Credit Ledger under Section 54 of the CGST Act.

Significant Takeaways

This is a welcome judgment by the HC as it interprets the law liberally, to extend the benefit of the refund to the SEZ units for ITC distributed by an ISD even though the law is silent on the question whether the SEZ unit can claim a refund of unutilised ITC where the supplier fails to do so.

The tax department, however, has been taking a very conservative view and has been consistently denying these refunds. The judgment will help to provide the required clarity as well as relief to the SEZ units. However, amending Rule 89 of the CGST Rules and introducing provisions akin to 'deemed exports' would bring certainty to this position.

Also, the judgment allows the provisions to be interpreted in an enabling manner, thereby entitling the SEZ to claim refund in absence of any bar in law restricting the filing of such refund claims.

> **“Since it is not possible for the supplier ISD to file for a refund of the ITC distributed, the SEZ unit in turn becomes entitled to file such a refund application.”**

The Taxation and Other Laws (Relaxation and Amendment of Certain Provisions) Act, 2020 enacted on September 29, 2020

The Taxation and Other Laws (Relaxation and Amendment of Certain Provisions) Act, 2020 ("**Amendment Act**") received Presidential assent on September 29, 2020. The Amendment Act has primarily replaced the Taxation and Other Laws (Relaxation of Certain Provisions) Ordinance, 2020 (Ord. 2 of 2020) ("**March Ordinance**") that was promulgated on March 31, 2020, when the Parliament was not in session to bring in the required relaxations for the difficulties faced by taxpayers due to Covid-19 pandemic. Further, the Amendment Act has also made certain other amendments to the provisions of the IT Act. Some of the major amendments have been discussed below:

1. Residential status

The Amendment Act has added an Explanation to Section 6(1A) of the IT Act. Section 6(1A), added *vide* Finance Act, 2020, provides that an Indian citizen whose total income (excluding foreign source income), exceeds INR 1.5 million during a FY shall be deemed to be resident in India in that FY, if he is not liable to tax in any other country or territory, by reason of his domicile or residence or any other criteria of similar nature. Basis the literal interpretation of the above provision, one could argue that Section 6(1A) of the IT Act overrides Section 6(1) of the IT Act, which provides the manner for determining whether an individual is a resident in India for the purposes of IT Act. Since the provisions under Section 6(1A) of the IT Act was brought notwithstanding the Section 6(1), it was possible to interpret that an Indian citizen who is not liable to tax in any other country shall be deemed to be resident under Section 6(1A) of the IT Act, which shall further lead to categorise the said individual as an RNOR under Section 6(6) of the IT Act. This would effectively mean that those Indian citizens could not be taxed in relation to income arising outside India. In order to prevent such a view being taken and provide clarity, the Amendment Act has inserted an explanation to provide that Section 6(1A) shall not apply in case of an individual who is said to be resident in India as per Section 6(1) of the IT Act.

Further, two more clarificatory amendments have been made in relation to residential status:

(i) The Explanation 1(b) to Section 6(1) of the IT Act is that the number of days present in India has been reduced from 183 days to 120 days by way of Finance Act 2020, for a citizen of India or a person of Indian origin having a total income, other than the income from foreign sources, exceeding INR 15 lacs. The reference to the words 'the citizen or person of Indian origin' has been substituted with 'such person' as has been used in the initial part of the said Explanation. This has been made to avoid any ambiguity in relation to the meaning or reference to the individual.

(ii) The Explanation in Section 6(6) providing the meaning of the expression 'income from foreign sources' as income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India)], has been clarified by adding the words "and which is not deemed to accrue or arise in India.."

2. AIFs in IFSC

The Amendment Act has expanded the scope of Section 10(4D) of the IT Act, which granted a capital gains tax exemption to Category III Alternate Investment Funds located in International Financial Services Centre ("**IFSC**"), whose units are entirely held by non-residents (other than those held by the sponsor and manager of the AIF) ("**Specified Funds**") subject to other conditions. The ambit of the exemption was earlier restricted to capital gains income from sale of bonds, global depository receipts, rupee denominated bonds and derivatives listed on a recognised stock exchange located in the IFSC, where the consideration is paid in convertible foreign exchange. Subsequent to the Amendment Act, the exemption includes income accruing to the Category III AIF or arising from transfer of securities (other than shares in a company resident in India) or any income from securities issued by a non-resident (not being a permanent establishment of a non-resident in India) and where such income otherwise does not accrue or arise in India or any income from a securitisation trust which is chargeable under the head "profits and gains of business or profession". A corresponding amendment has been made to Section 196D of the IT Act with effect from November 01, 2020 to exempt the payer of any such income exempt under Section 10(4D) of the IT Act from the obligation to deduct TDS.

Section 10(23FBC) has been introduced in the IT Act to exempt from tax, any income received by unitholders of such Specified Funds, whether such income is received from the Specified Fund or from the transfer of units held in such Specified Fund.

Further, Specified Funds have now been included within the special regime applicable to Foreign Portfolio Investors ("**FPIs**") under Section 115AD of the IT Act. Therefore, any income, other than what is already exempt under Section 10(4D) of the IT Act, received by a Specified Fund will be subject to concessional tax rates of 10% (exclusive of educational cess and surcharge) for any income received in respect of securities, subject to the exemptions built in Section 115AD(1) of the IT Act through provisos. However, the concessional rate of 5% available to FPIs under Section 194LD of the IT Act for specified securities has not been made available to Specified Funds. It has been clarified that the above-mentioned rates for Specified Funds will be applicable only to the extent of income that is attributable to units held by non-residents (not being a PE of a non-resident in India).

The Amendment Act, through amendment in Section 196D of the IT Act with effect from November 01, 2020, also specifies a concessional withholding tax rate of 10% for interest/dividend income (except interest referred to in section 194LD) received by Specified Funds

Additionally, the Amendment Act has removed Specified Funds from the scope of provisions relating to Alternate Minimum Tax under section 115JEE of the IT Act.

3. Sovereign Wealth Funds and Pension Funds

By way of the Finance Act, 2020, eligible sovereign wealth funds ("**SWFs**") and foreign pension funds ("**FPFs**") had been granted tax exemption in respect of their dividend, interest or long-term capital gains income, so long as the investment was made on or before March 31, 2024, and was locked in for three (3) years, in specified infrastructure investee entities, subject to the satisfaction of other conditions. One of the prerequisites for availing the exemption was that the SWF or FPF is specified by the Central Government, by notification in the Official Gazette, for the purpose of the tax exemption. It has been included, as part of the Amendment Act, that such notification of each eligible SWF or FPF may specify additional conditions which the eligible entity shall be required to comply with in order to retain the tax exemption granted.

4. Approval to Charitable Institutions and Research Institutions

The Finance Act 2020, made several changes in the tax regime applicable on charitable institutions working for public religious purposes, education purposes, hospitals or institutions for specified illnesses, under Section 10(23C)(iv),(v),(vi) and (via) of the IT Act and charitable purposes registered under Section 12AA of the IT Act. Some of these major changes include, inter alia, requirement for all of such organisations to apply for fresh registration by the prescribed date, validity of such approvals was reduced from lifetime (or valid until withdrawn) to a period of five (5) years, election of one of the approvals under Section 10(23C) or Section 12AB, etc. These changes were supposed to be applicable from June 01, 2020 but on account of difficulties being faced by Covid-19 pandemic, the same were deferred to October 01, 2020. The Amendment Act has further deferred the applicability of these changes to April 01, 2021.

On similar lines, Finance Act, 2020 made changes with respect to several other institutions registered under Section 35(1)(ii), (iii) and (iia) and Section 80G(2)(a)(iv) of the IT Act i.e. which work in the field of research associations undertaking scientific, social science or statistical research and charitable purposes. The said changes *inter alia* included, the requirement to apply for fresh registration by the prescribed date which would be valid for a period of five (5) years, issue a certificate to donor certifying the amount received, provide statement regarding details of utilisation of amount, etc. The Finance Act 2020, had also proposed that any failure to comply with these obligations could entail a penalty of INR 10,000 to INR 1,00,000. While these changes were also initially supposed to be applicable from June 01, 2020, the same were deferred to October 01, 2020 on account of difficulties being faced by Covid-19 pandemic, the Amendment Act has now deferred the applicability of these changes to April 1, 2021.

5. Donations to PM Cares Fund

The Amendment Act has amended Section 10(23C) of the IT Act to provide that any income received by any person on behalf of the Prime Minister's Citizen Assistance and Relief in Emergency Situations Fund ("**PM Cares Fund**") on or after April 1, 2020 would be exempt from income tax. Further, Section 80G has also been amended to provide that any donation made by any taxpayer to PM Cares Fund, on or after April 1, 2020, would be allowed as a deduction while computing the total income of the taxpayer. These changes were a part of the March Ordinance and have now been brought into the IT Act by way of the Amendment Act.

6. **Amendments related to Faceless Assessment Scheme**

The Amendment Act has incorporated provisions to give effect to faceless assessment scheme in the IT Act. For more details on this, please refer to the ***cover story***.

7. **Reduction in TDS and TCS rates**

As a part of *Atmanirbhar Bharat Abhiyan* or Self-Reliant India Movement, the CBDT had released a Press Release dated May 13, 2020 ("**Press Release**"), reducing the TDS and TCS rates for various kinds of payments made a limited period from May 14, 2020 to March 31, 2021, to 75% of the prescribed rates. The same was done to ensure receipt of more money by the taxpayers, which could help them to face difficulties posed by Covid-19 pandemic. The Amendment Act has amended Section 197B and Section 206C(10A) of the IT Act to incorporate the announcements made vide Press Release. Notably, the reduced rates would be applicable for the payments made on or after May 14, 2020, till the end of FY 2020-21, i.e. till March 31, 2021.

8. **Capping of surcharge on dividends**

The Amendment Act has amended Section 2 of the Finance Act, 2020, to provide that while making dividend payments to every individual or HUF or association of persons or body of individuals, whether incorporated or not, or every artificial juridical person referred to in Section 2(31)(vii) of the IT Act, being a non-resident, tax shall be withheld at the following rates:

(i) 10% where the dividend income exceeds INR 5 million but is less than 10 million;

(ii) 15% where the dividend income exceeds INR 10 million.

This amendment has capped the surcharge on dividends received by such persons at 15%, which otherwise could have gone up to 37%.

9. **Extension of various deadlines**

In light of the prevailing Covid-19 pandemic situation, the Amendment Act has extended deadlines for several compliances to be undertaken as per the IT Act. A list of some of these extended deadlines has been provided below:

Compliance	Revised due date
Filing of revised and belated Income-tax return for FY 2018-19	September 30, 2020
Filing of income-tax return for all taxpayer for FY 2019-20	November 30, 2020
Due date for making investments/ payments for claiming deduction under Chapter VI A – B of the IT Act for FY 2019 – 20	July 31, 2020
Furnishing of TDS/ TCS statements and issuance of TDS/ TCS certificates pertaining to the FY 2019-20.	July 31, 2020 – for furnishing TDS/ TCS statements for quarter ending March 31, 2020 August 15, 2020 – for issuance of TDS/ TCS certificates u/s 192 for FY 2019-20
Date for making investment/ construction/ purchase for claiming roll – over benefit/ deduction in respect of capital gains under section 54 to 54 GB of the IT Act	September 30, 2020
Date of commencement of operation for the SEZ units for claiming deduction under section 10AA of the IT Act for the units which received necessary approvals by 31 March 2020	March 31, 2021
Filing of Tax Audit Report (Form 3CD) for FY 2019-20	October 31, 2020
Passing of order or issuance of notice by the authorities and various compliances under various Direct Taxes & Benami Law which are required to be passed/ issued/ made by December 31, 2020	March 31, 2021
Due date for linking Aadhar with PAN	March 31, 2021
Due date for Direct tax Vivad Se Vishwas scheme	December 31, 2020
All other compliances falling between March 20, 2020 to December 31, 2020 and after December 31, 2020 as notified	March 31, 2021

CBDT issues guidelines to clarify TDS on e-commerce transactions and TCS on sale of goods

Section 194O of IT Act was introduced by Finance Act, 2020 imposing obligation of deducting TDS on payments made by an e-commerce operator and Section 206C (1H), providing for inter alia TCS on sale of goods, has been made applicable with effect from October 1, 2020.

Section 194O of IT Act requires an e-commerce operator to deduct TDS at the rate of 1% on the gross amount of sale of goods or services or both to an e-commerce participant through its digital platform, at the time of credit or at the time of payment of the sale consideration, whichever is earlier.

Also, Section 206C(1H) of IT Act requires a seller receiving a consideration exceeding INR 50 lakh for sale of goods in a FY to collect TCS at the rate of 0.1% from the sale consideration at the time of receipt of such sum.

With respect to implementation of these provisions, various representations were received by CBDT highlighting certain issues and in order to remove the difficulties faced by taxpayers, CBDT has recently issued guidelines vide Circular dated September 29, 2020[93] as under:

1. In case of certain stock exchanges and clearing corporations when there is no one-to-one contact between the buyers and the sellers. Hence, it has been provided that the provisions of Section 194O and Section 206(1H) of IT Act would not be applicable in case of:

    a. transactions in securities and commodities traded through recognised stock exchange or cleared and settled by recogniszed clearing corporations including those located in International Financial Service Centre

    b. transactions in electricity, renewable energy certificates and energy saving certificates traded through power exchanges registered in accordance with Regulation 21 of the CERC.

    Due to the above clarification in relation to listed shares, doubts have arisen on the applicability of TCS on sale of unlisted shares, owing to the fact that the term 'goods' is not defined under the IT Act. If reliance is placed on definitions of 'goods' under the GST regime (i.e. applicable laws) or the Sale of Goods Act, 1930, both have contrasting definitions as regards inclusion of shares. While GST related enactments exclude shares from the ambit of the term /goods], Sale of Goods Act, 1930 includes shares and securities.

2. In e-commerce transactions, going by the language of the provisions, Section 194O could become applicable on both i.e. on the main e-commerce operator as well as the payment gateway through which payment is processed as it could also separately qualify as an e-commerce operator for facilitating the service. In order to remove this difficulty, it has been provided that Section 194O would not be applicable on the payment gateway if the main e-commerce operator has duly deducted the TDS and the payment gateway may take an undertaking from the e-commerce operator in this regard to ease the implementation of these provisions.

3. In case of insurance agents and insurance aggregators, it has been clarified that in the event they do not have any involvement in the transactions between the insurance company and the buyer in the years subsequent to the first year in which insurance is availed by the buyer, provisions of Section 194O would not apply to them in those subsequent years.

4. The provisions of Section 194O of IT Act are applicable if total sum credited or paid to an e-commerce participant, who is an individual or an HUF, by an e-commerce operator in a FY exceeds INR 5 lakh. The above threshold for applicability of Section 194O of IT Act would be calculated from April 1, 2020 onwards. Hence, if such provisions become applicable, TDS would be deducted under Section 194O of the IT Act in case of any sum credited or paid after October 1, 2020.

5. Provisions of Section 206C(1H) of IT Act would not apply in case of any sale consideration received prior to October 1, 2020 but on any sale consideration received after October 1, 2020 even if the sale was carried out before October 1, 2020

6. The threshold of INR 50 lakh for applicability of Section 206C(1H) of IT Act, with respect to total sale consideration received by a seller from a buyer in a FY, above which threshold such provisions would become applicable in a particular case, would be counted from April 1, 2020 onwards. The TCS needs to be collected only in respect of sale consideration received on or after October 1, 2020

7. Section 206C(1F) of IT Act is applicable in case of sale of motor vehicle for a value exceeding INR 10 lakh and is based on a single sale of a motor vehicle. Section 206C(1H) of IT Act clearly provides that its provisions would not be applicable in case of goods covered under Section 206C(1F) of IT Act and also that Section 206C(1H) of IT Act applies if receipts exceed INR 50 lakh during the FY on aggregate sale of goods. Interplay of Section 206C(1F) with Section 206C(1H) of IT Act has been explained as under:

    a. If the sale consideration from dealer is not subject to TCS under Section 206C(1F) of IT Act, Section 206C(1H) could still apply

    b. If the sale consideration received from a consumer does not exceed INR 10 lakh and hence Section 206C(1F) is not applicable, Section 206C(1H) of IT Act could still apply if aggregate sale consideration from motor vehicles during the FY exceeds INR 50 lakh.

93 Circular No. 17 of 2020 dated September 29, 2020.

c. If the sale consideration received from a consumer for a motor vehicle exceeds INR 10 lakh and Sction 206C(1F) becomes applicable, then Section 206C(1H) of IT Act would not apply.

8. For the purpose of collection of TCS as per Section 206C(1H) of IT Act, no adjustment is required to be made in respect of sales return, discount or indirect taxes including GST since the collection is to be made as per the amount of sale consideration received

9. Provisions of Section 206C(1H) of IT Act would not apply on the sale consideration received for fuel supplied to non-resident airlines at airports in India.

CBDT notifies rules introducing changes in existing rules for TCS and TDS

Reporting requirements for TCS: Section 206C of IT Act lays down elaborate provisions for collection of TCS by a seller at the time of sale of certain specified goods or services to the buyer. In this regard, Rule 31AA of IT Rules requires every seller to furnish a quarterly statement of collection of TCS under Section 206C(3) of IT Act, in the prescribed form i.e. in Form No. 27EQ. Recently, the Finance Act 2020, has expanded the applicability of provisions of Section 206C of IT Act to remittances made outside India and overseas tour packages by insertion of sub-sections (1G), (1H) (1I) and (1J) in Section 206C of IT Act w.e.f. October 1, 2020. Proviso to these sub-sections also specify certain monetary thresholds, conditions and relaxations in which case the TCS provisions would not apply or apply at a lower rate.

In this regard, Rule 31AA of IT Rules has now been amended *vide* Income Tax (17th Amendment) Rules 2020, notified vide CBDT notification dated July 24, 2020, and clause (vi) and (vii) have been newly inserted in sub-rule 4 of Rule 31AA of IT Rules w.e.f. October 1, 2020 to provide that in case the TCS provisions are not applicable due to satisfaction of certain specific condition(s) provided in the relevant provisos to Section 206(C) sub-section (1G) & (1H) of IT Act, such instances would also need to be reported in the statement of collection of TCS to be furnished in Form 27EQ. For this purpose, a revised Form 27EQ has also been prescribed in the Income Tax (17th Amendment) Rules 2020.

Relaxation from higher rate absent PAN expanded to include dividend income: Section 206AA of IT Act provides for tax deduction at source to be higher of, (i) the rate specified in the IT Act/ as per rates in force, or (ii) 20% in case a person fails to furnish his PAN to the person responsible for deduction of tax.

In this regard, Rule 37BC of IT Rules provided relaxation from deduction of TDS at a higher rate in case of a non-resident not having a PAN, receiving payments in the nature of interest, royalty, FTS or payments on transfer of any capital asset, subject to furnishing alternative documents.

However, it may be noted that dividend income has become taxable in the hands of the recipients since the abolishment of dividend distribution tax under Section 115-O of IT Act w.e.f. April 1, 2021.

Hence, in view of the changes in the taxation regime for dividend, Rule 37BC of IT Rules has now been amended vide Income Tax (17th Amendment) Rules 2020 w.e.f. July 24, 2020 to extend the benefit of relaxation from higher rate, to dividend income as well.

Due date and payment of TCS on overseas tour and foreign remittances: Rule 37CA of IT Rules specifies the due date and mode for payment of TCS to the treasury. Necessary amendments have been made in Rule 37CA of IT Act vide Income Tax (17th Amendment) Rules 2020, by deleting references to specific sub sections of Section 206C, such that said rules have now been made applicable to all sub sections, including the newly inserted sub-sections in Section 206C dealing with TCS on overseas tour packages and foreign remittances, discussed above.

Credit for TCS paid: Under Rule 37-I of IT Rules, credit for TCS was allowed for the AY for which the relevant income was assessable to tax in the hands of the person from whom tax has been collected at source. The said rule has been amended *vide* Income Tax (17th Amendment) Rules 2020 and sub-rule 2 has been newly inserted in Rule 37-I of IT Rules to provide that in respect of TCS on sale of motor vehicle, overseas tour package and foreign remittances, credit for TCS shall be allowed to the person from whom tax has been collected in the AY relevant to the FY in which tax is collected .

CBDT issues guidance on MAP

BEPS Action Plan 14 final report on ***Making Dispute Resolution*** more effective, dated October 5, 2015, had recommended that all countries which implement the BEPS package of measures must publish comprehensive MAP guidance. Subsequently, OECD released the sixth batch of peer review reports on Action Plan 14 on October 24, 2019. The said report contained the peer review of India in relation to implementation of minimum standards under Action Plan 14 and it *inter alia* recommended that India should publish a comprehensive guidance on MAP.

CBDT with a view to be fully compliant with the recommendations of the Action Plan14 and to align its approach with the best practices introduced Rule 44G of the IT Rules, *vide* Notification No. 23/2020, dated May 6, 2020, which laid down the process to be followed by the Indian Competent Authorities to resolve and implement outcomes of MAP. Following this, the CBDT, on August 7, 2020, issued a guidance on MAP, stipulating the details regarding the MAP process and guidance on technical issues pertaining to it (“**Guidance**”). The Guidance is divided into four sections: (i) introduction and basic information; (ii) access and denial of access to MAP; (iii)technical issues; and (iv) implementation of MAP outcomes.

1. **Introduction and Basic Information:** The Guidance stipulates that a MAP request may be made by a taxpayer, where it considers that the action of the tax authorities results or would result in double taxation (whether juridical or economic) or taxation not in accordance with the DTAAs. The time limit for filing such applications for MAP would be governed by the relevant article of the applicable DTAA, which generally provide for a time limit of three years from the first notification of the action giving rise to taxation not in accordance with the DTAA. The Guidance clarifies that where certain DTAAs of India provide for different timeline , the same would be amended to provide for a timeline of three years, as recommended under Action Plan 14.

   MAP process: The Guidance provides that the application for MAP request would have to be made in Form No. 34F along with all the specified information. It also provided that where an AE or a related party of an Indian taxpayer has submitted a MAP application before the Competent Authorities ("**CA**") of its country, in respect of any order/action of the tax authorities of India or of the tax authorities of such treaty partner, a copy of such MAP application would have to be provided to the CA of India having jurisdiction over the case.

   The Guidance mentions that the once a MAP application is accepted or rejected by the CA of India, it should inform the CA of the relevant treaty partner in writing of its decision/position on the application. The other CA shall also provide her views and comments on the application. Once both the treaty partners have reached a common understanding, the decision regarding the acceptance of the application would be communicated to the Indian taxpayer who filed the application. Where the application is accepted, the Guidance provides that the relevant CAs should exchange views on the issues, through exchange of position papers, in person meeting, video conferences etc and should try to reach a negotiated position. In line with the minimum standard of Action Plan 14, the Guidance provides that CAs of India should endeavour to resolve MAP cases within an average timeframe of two years.

   Further, the Guidance also provides that CAs of India may also participate in Multilateral MAPs, subject to certain conditions.

2. **Access and denial of access to MAP:** The Guidance provides that wide access to MAP would be provided taxpayer in cases/situations which result in taxation not in accordance with the relevant DTAAs including cases where the Indian tax authorities have applied domestic anti-abuse provisions or where the obligation to deduct tax at source on the payment made by an Indian entity to a non-resident entity is enforced by an order passed under Section 201 of the IT Act etc.

However, the Guidance lists down certain circumstances where the access would be granted by India, but the CAs of India would not negotiate any other outcome than what has already been achieved in therein. Such circumstances are as follows:

a. **Unilateral APA** - Where a taxpayer has entered into a unilateral APA with CBDT, , the Indian CAs would not be able to change the terms and conditions of the unilateral APA even though India would allow access to MAP. The CAs of the India would request the CAs of the treaty partners to provide correlative relief. Further, where a unilateral APA applications is under consideration and negotiation, CAs of India may accept MAP applications, however, Indian CAs would not process such MAP cases till the unilateral APA is entered.

b. **Safe harbour** – Where the taxpayer applies safe harbour provisions, as applicable on its international transactions, and the return is accepted by Indian tax authorities, then the Indian CAs may allow access to MAP but would not change the ALP of the international transactions covered under the safe harbour provisions.

c. **Orders of ITAT** – Where the taxpayer has availed the remedy under MAP and domestic law simultaneously, then where the ITAT has already passed an order in respect of the disputes being examined under MAP, then CAs would not be allowed to deviate from the orders of the ITAT and shall request the CAs of the other treaty partners to provide correlative relief.

Additionally, the Guidance also lays down certain situations where the access to MAP could be denied. Such situations are as follows:

a. **Delayed MAP applications** – Where the taxpayers do not file the MAP application within the prescribed time period under the DTAA, the CAs of India may deny the access to MAP.

b. **Taxpayer's objection not justified** - Where the CAs of India conclude that the objection raised by the taxpayer on the action taken by the tax authorities are not justified, they can deny access to MAP. However, before denying such access, the CA of India would have to discuss the matter with the taxpayer and the relevant CA.

c. **Incomplete MAP Applications / documents / information** – Where the Indian taxpayer does not furnish all the information required as per form 34F, and does not remedy the error/defects as may be pointed by the CA within a reasonable time period, access to MAP could be denied.

d. **Income-tax Settlement Commission** – Where the taxpayer has already obtained a settlement order from Settlement Commission or its settlement application has been admitted by the Settlement Commission, and such order / application covers the issues that are sought to be examined in the MAP application, the CAs of India shall not provide access to MAP to the taxpayer.

e. **AAR** – Where the taxpayer has already obtained an advance ruling from AAR or the taxpayer's application has been admitted by the AAR, and such order/application covers the issues that are sought to be examined in the MAP application, the CAs of India shall not provide access to MAP to the taxpayer.

f. **Domestic law issues** – MAP access shall not be provided in respect of issues that are purely governed by India's domestic law and arise due to the implementation of India's domestic legal provisions.

3. **Technical issues:** The Guidance has also clarified some of the technical issues as follows:

a. **Downward adjustment** - Indian CAs while negotiating a MAP case, cannot go below the returned income as it is expressly prohibited under the domestic law. However, where adjustments are made by tax authorities of the treaty partner country, the Indian CA may go below the returned income of the Indian taxpayer.

b. **Resolution of recurring issues** – While Indian CAs may resolve recurring issues on the same principles as adopted in a prior MAP resolution, they cannot resolve such issues in advance of an order by tax authorities.

c. **Interest and penalties** – The consequential issues of interest and penalty cannot be considered and negotiated by CAs of India. However, the amount of interest and penalties linked to the quantum of income shall be varied in the same proportion as the variation in the quantum of income.

d. **Secondary adjustment** – Indian CAs are required to make secondary adjustments a part of MAP resolution with respect to cases pertaining to FY 2016-17 or thereafter.

e. **Bilateral & Multilateral APAs** – With respect to the issues for which an APA application has already been filed, Indian CAs would not admit the MAP application for the same issue for the same years. However, if the APA application fails, MAP application may be accepted.

f. **Suspension of collection of taxes during the pendency of MAP** – India has entered into a Memorandum of Understanding (MoU) with certain treaty partners (USA, Sweden, etc.), wherein it is provided collection of taxes in relation to disputes that are under discussion in MAP, could be suspended during the pendency of MAP in that case. Where no such MoU exists, the domestic law of India would govern the procedure relating to suspension of collection of taxes.

g. **Adjustment of taxes paid in pursuance of orders under section 201 of IT Act** – Where MAP is resolved, payment of taxes (excluding interest) by the taxpayer pursuant to order under Section 201, may be allowed to be adjusted against the tax liability of the non-resident taxpayer (payee entity).

4. **Implementation of MAP outcomes:**

Where the CAs successfully resolve a MAP case and formulate a mutual agreement, the taxpayer can either accept or reject the MAP resolution. If the taxpayer decides to accept the MAP resolution, it has to convey its acceptance and submit evidence of withdrawal of domestic appeals to the CA, within 30 days from the date of receipt of communication from the CA. Once the AO receives the letter from the Indian CA providing details of the MAP resolution, the AO shall within a period of one month from the end of month in which such letter is received, give effect to the MAP resolution. Pursuant to giving effect to the resolution, the AO shall send a copy of the order giving effect to the MAP resolution to the Indian CA along with information regarding the amount/date of payment of taxes by the taxpayer or amount/date of issue of refund to the taxpayer (as the case may be), withdrawal of appeals filed by the tax authorities, and any other relevant details.

The CBDT asserted that India is committed to implement MAP outcomes in all cases. However, it has clarified that where an order of the ITAT (for the same assessment year that has been resolved under MAP) comes to the knowledge of the CAs of India after the MAP has been resolved or is pronounced after the MAP has been resolved but not yet implemented, MAP outcomes would not be implemented. In such cases, the CAs of India would inform their counterparts about the outcomes of the ITAT order and request them to provide correlative relief for the adjustments sustained by the ITAT, if any.

Impact

Though MAP has been a part of Indian DTAA framework for a long time now, it has not proved to be a very effective and popular means of dispute resolution among the taxpayers. In this regard, BEPS Peer Review Report noted that India met only half of the elements of the Action 14 minimum standards on an overall basis, and recommended improvements in several areas. The Guidance seeks to enforce most of these recommendations and thus, reinforces India's commitment to make dispute resolution more effective and efficient. In addition to these measures, additional resources shall be employed to make the MAP process more effective and efficient.

CBDT grants PAN exemption to NR investing in category I and II AIF located in IFSC

CBDT, *vide* notification 58 of 2020[94], dated August 10, 2020, has notified amendment of IT Rules introducing Rule 114AAB which notifies class or classes of persons to whom provisions of Section 139A which mandates obtaining PAN shall not apply.

As per the new introduced Rule 114AAB, non-residents fulfilling the following conditions shall be exempt from the applicability of Section 139A:

i. The non-resident does not earn any income in India other than income from investments in Category I or II Alternative Investment Fund ("**AIF**") registered with Securities and Exchange Board of India ("**SEBI**") and located in an International Financial Services Centre ("**IFSC**");

ii. TDS on such income is deducted by such Category I and II AIF as specified in clause (i) above in accordance with Section 194LBB of IT Act;

iii. The non-resident furnishes the following details and documents to such Category I and II AIFs specified in clause (i) above:

   a. Name, e-mail id and contact number;

   b. Address in the country or specified territory outside India;

   c. A declaration that he is a resident of a country or specified territory outside India; and

   d. Tax Identification Number in the country or specified territory of his residence and in case no such number is available, then a unique number on the basis of which the non-resident is identified by the Government of that country or the specified territory of which he claims to be a resident

Further, the notification also notifies Form 49BA under which the AIFs specified in clause (i) shall be required to furnish a quarterly statement to the IRA with details and documents of non-residents furnished in clause (iii) above.

Consequentially, the notification also amends Rule 37BC of the IT Rules, inserting clause (2) under the said rule, which states that provisions of Section 206AA (which provides for a TDS to be deducted at higher rates in case of non-furnishing of PAN) shall not apply to non-residents that are not required to obtain a PAN as per the applicability of Rule 114AAB.

Foreign Insurers eligible to apply for tax non-deduction certificate

CBDT *vide* Notification No. 75 of 2020 dated September 22, 2020 ("**Notification**") amended Rule 29B of the IT Rules to permit the foreign insurers to apply for tax non-deduction certificate under Section 195(3) of the IT Act.

Rule 29B of the IT Rules, *inter alia*, provides that any foreign banking company which carries on its operations in India through a branch that receives income by way of interest (not being interest on securities[95]) or any other sum (not being dividends) on its own account and not on behalf of its head office or any other person, then such person may make an application for a grant of certificate under Section 195(3) authorising him to receive such income without any tax deduction at source. For making this application, the concerned person has to satisfy following conditions:

1. The concerned banking company has been regularly assessed to income-tax in India and has furnished the returns of income for all assessment years which became due till the date of application,

2. The concerned person is not in default or deemed to be in default in respect of any tax, interest, penalty, fine, or any other sum payable under the Act.

The Notification has extended this provision to a foreign company engaged in re-insurance business through a branch established in India. Foreign company has been defined to mean a company or body, established or incorporated under a law of any country outside India and includes Lloyd's established under the Lloyd's Act, 1871 (United Kingdom) or any of its Members.

Such application by the foreign banking / insurance company is to be made in Form No. 15C. If the AO is satisfied that all the above conditions are met, then it would issue a certificate authorising the foreign banking/insurance company to receive income without tax deduction at source and such certificate would be valid for the period prescribed therein.

94 Notification No. 58/2020/F. No. 370133/08/2020-TPL dated August 10, 2020.
95 Other than securities prescribed in proviso to section 193, which include, *inter alia*, interest on National Development Bond, interest payable on any security of the Central or State Government, etc.

REGULATORY INDIRECT TAX UPDATES

Enforcement of certain amendments of Finance Act (No. 2) Act, 2019

Notification No. 63/2020- Central Tax dated August 25, 2020 has implemented the provision pertaining to interest liability only on the net tax liability w.e.f. September 01, 2020.

Extension of timeline

a. Completion of any action under CE Act, Customs Act, CTA and Service Tax legislation: The time limit for completion of any proceeding or issuance of any order, notice, intimation, notification or sanction or approval etc. by any authority, commission, tribunal, or filing of any appeal, reply or application or furnishing of any report, document, return or statement has been extended up to the December 31, 2020. However, this extension does not apply on delivery of arrival/import/departure/export manifest, passenger and crew arrival/departure manifest, bill of entry and clearance of goods for home consumption.[96]

b. Antiprofiteering provision: The time limit for completion or compliance of any action under the antiprofiteering provision which falls during the period from the March 20, 2020 to November 29, 2020 (which is yet to be completed), is extended up to November 30, 2020 vide Notification No. 65/2020- Central Tax dated September 01, 2020.

c. Annual Return: The time limit for filing annual return for the FY 2018-2019 has been extended to October 31, 2020 *vide* Notification No. 69/2020- Central Tax dated September 30, 2020.

d. Invoicing: The time limit for invoicing of goods sent on approval basis is six months from the date of removal. The same has been extended up to October 31, 2020 for goods sent or taken out of India on approval for sale on approval basis if its date of invoicing falls during the period March 20, 2020 – October 30, 2020, if not already complied vide Notification No. 66/2020- Central Tax dated September 21, 2020.

e. Dynamic Quick Response ("**QR**") code: QR code on invoices issued by a registered person whose aggregate turnover in any preceding financial year from 2017-18 onwards exceeds INR. 500 crore to an unregistered person (B2C invoices) to be made effective from December 01, 2020 vide Notification No. 71/2020- Central Tax dated September 30, 2020.

f. Invoice Reference Number ("**IRN**"): Relaxation has been given to taxpayers from the requirement to generate IRN in respect of e-invoices issued during the month of October 2020. In these cases, IRN for such invoices from Invoice Reference Portal can be generated within 30 days from the date of invoice vide press release dated September 30, 2020.

E-Invoicing under the GST Legislation

Notification No. 13/2020-Central Tax dated March 21, 2020 read with Notification No. 61/2020-Central Tax dated July 30, 2020 read with Notification No. 70/2020- Central Tax dated September 30, 2020 provides that registered persons having aggregate turnover exceeding INR 500 cror in any preceding financial year from 2017-2018 onwards shall issue an e-invoice w.e.f. October 01, 2020. Invoice issued in any other manner would not be treated as a valid invoice. The e-invoice can be generated on GST electronic portal by furnishing relevant information. However, the following suppliers would not be required to comply with aforesaid system:

a. SEZ unit,
b. insurer or a banking company or a financial institution, including a non-banking financial company,
c. goods transport agency supplying services in relation to transportation of goods by road in a goods carriage,
d. supplier supplying passenger transportation service,
e. supplier supplying services by way of admission to exhibition of cinematograph films in multiplex screens.

CBIC notifies Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020 ("CAROTAR")

Notification No. 81/2020- Customs (NT), dated August 21, 2020 introduced CAROTAR w.e.f. September 21, 2020 detailing the procedure regarding claim of preferential rate of duty by an importer. CAROTAR provides that details of information to be possessed by importer, the manner of furnishing information to proper officer (when requisitioned) in a specified form, timeline in which proper officer must complete his proceedings, instances where verification request can be sought from issuing authority of certificate of origin and treatment of identical goods. CAROTAR also provides instances where the claim of preferential rate of duty can be denied without verification. Mere submission of a certificate of origin shall not absolve the importer of the responsibility to exercise reasonable care to the accuracy and truthfulness of the information supplied.

Further, Circular No. 38/2020-Customs dated August 21, 2020, lays down the procedure for sending verification request to the issuing authority of certificate of origin. The Circular provides that in case an importer fails to provide information, or does not exercise reasonable care to ensure the accuracy and truthfulness of the information furnished, the Risk Management Centre of Customs must be informed through written communication for the purposes of enabling compulsory verification of assessment of all subsequent import consignments. However, the compulsory verification of assessment would be discontinued once the importer demonstrates that he has established adequate system of controls to exercise reasonable care.

CBIC notifies Faceless Assessment for customs throughout India

Circular No.40/2020-Customs dated September 04, 2020, provides that faceless or anonymised assessment, self-registration of goods by importers, automated clearances of bills of entry, digitisation of Customs documents, etc. would happen across India. This would enable exponentially faster clearance of goods, reduced interface between trade and Customs officers and enhanced ease of doing business.

Ceiling/ last date for availing MEIS benefit

Notification No. 30/2015-2020 dated September 01, 2020, provides for the following changes in MEIS:

a) The maximum total reward to be granted per IEC holder for exports [period based on Let Export Order date] made between the period September 01, 2020 and December 31, 2020 would be INR 2 crore.
b) The new IEC obtained on or after September 01, 2020 would not be eligible to claim MEIS benefit for exports made w.e.f. September 01, 2020.
c) The IEC holder who has not made any export with Let Export Order during the period September 01, 2019 to August 31, 2020, would not be eligible to claim MEIS benefit for exports made w.e.f. September 01, 2020.
d) The ceiling of the prescribed allocation of total claims under MEIS for the period September 01, 2020 to December 31, 2020 is INR 5,000 crore. Accordingly, the Government could further reduce ceiling of total rewards claimed by an IEC holder, pegged at INR 2 crore currently, to ensure the total claim limit does not exceed the prescribed allocation.
e) Benefits under MEIS shall not be available w.e.f. January 01, 2021.

GLOSSARY

ABBREVIATION	MEANING
AAR	Hon'ble Authority for Advance Rulings
AAAR	Hon'ble Appellate Authority for Advance Rulings
ACIT	Learned Assistant Commissioner of Income Tax
AE	Associated Enterprises
AO	Learned Assessing Officer
APA	Advance Pricing Agreement
AY	Assessment Year
Customs Act	Customs Act, 1962
CbC	Country by Country Reporting
CBDT	Central Board of Direct Taxes
CBEC	Central Board of Excise and Customs
CCR	CENVAT Credit Rules, 2004
CEA	Central Excise Act, 1944
CENVAT	Central Value Added Tax
CESTAT	Hon'ble Customs, Excise and Service Tax Appellate Tribunal
CETA	Central Excise Tariff Act, 1985
CGST	Central Goods and Service Tax
CGST Act	Central Goods and Service Tax Act, 2017
CGST Rules	Central Goods and Service Tax Rules, 2017
CIT	Learned Commissioner of Income Tax
CIT(A)	Learned Commissioner of Income Tax (Appeal)
CRISIL	Credit Rating Information Services of India Limited
CST	Central Sales Tax
CST Act	Central Sales Tax Act, 1956
CT Act	Custom Tariff Act, 1975
CVD	Countervailing Duty
DCIT	Learned Deputy Commissioner of Income Tax
DIT	Learned Director of Income Tax
DGFT	Directorate General of Foreign Trade

GLOSSARY

ABBREVIATION	MEANING
DRP	Dispute Resolution Panel
DTAA	Double Taxation Avoidance Agreement
EPCG	Export Promotion Capital Goods
FMV	Fair Market Value
FTP	Foreign Trade Policy
FTS	Fees for Tech nical Services
FY	Financial Year
GAAR	General Anti-Avoidance Rules
GST	Goods and Service Tax
GST Compensation Act	Goods and Services Tax (Compensation to States) Act, 2017
HC	Hon'ble High Court
IBC	Insolvency and Bankruptcy Code, 2016
IFSC	International Financial Services Centre
IGST	Integrated Goods and Services Tax
IGST Act	Integrated Goods and Services Tax Act, 2017
INR	Indian Rupees
IRA	Indian Revenue Authorities
IT Act	Income-tax Act, 1961
ITAT	Hon'ble Income Tax Appellate Tribunal
ITC	Input Tax Credit
ITO	Income Tax Officer
IT Rules	Income-tax Rules, 1962
Ltd.	Limited
MAP	Mutual Agreement Procedure
MAT	Minimum Alternate Tax
MLI	Multilateral Convention to Implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting
MoU	Memorandum of Understanding
MRP	Maximum Retail Price

GLOSSARY

ABBREVIATION	MEANING
NAA	National Anti-profiteering Authority
NCLT	National Company Law Tribunal
OECD	Organization for Economic Co-operation and Development
PAN	Permanent Account Number
PCIT	Learned Principal Commissioner of Income Tax
PE	Permanent Establishment
Pvt.	Private
PY	Previous Year
R&D	Research and Development
RBI	Reserve Bank of India
SC	Hon’ble Supreme Court
SEBI	Security Exchange Board of India
SEZ	Special Economic Zone
SGST	State Goods and Services Tax
SGST Act	State Goods and Services Tax Act, 2017
SLP	Special Leave Petition
ST Rules	Service Tax Rules, 1994
TCS	Tax Collected at Source
TDS	Tax Deducted at Source
TPO	Transfer Pricing Officer
TRC	Tax Residency Certificate
UK	United Kingdom
USA	United States of America
UTGST	Union Territory Goods and Services Tax
UTGST Act	Union Territory Goods and Services Tax Act, 2017
VAT	Value Added Tax
VAT Tribunal	Hon’ble VAT Tribunal

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