

TAX SCOUT

A quarterly update on recent developments in Taxation Law

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FOREWORD

We are delighted to present to you, the latest issue of the *Tax Scout*, our quarterly update on recent developments in the field of direct and indirect tax laws for the quarter ending March 2016.

The taxation of e-commerce transactions has been a cause of concern for several countries across the globe due to difficulties in characterizing the nature of payments, establishing a nexus or link between a taxable transaction and taxing jurisdiction etc. In the Budget 2016-17, Equalization Levy on e-commerce payments for specified services made to non-residents not having a permanent establishment in India was introduced. Thereafter, during the last quarter, the Central Board of Direct Taxes (“**CBDT**”) released a report on the proposal to impose the said levy wherein the CBDT recognised the challenges surrounding digital transactions and made suggestions and recommendations to facilitate implementation of the said levy in India. Currently, specified services means online advertisement, any provision for digital advertising space or any other facility or service for the purpose of online advertisement and includes any other service as may be notified by the Central Government in this behalf.

In this issue of *Tax Scout*, we have discussed at length, as part of our Cover Story, the various aspects of Equalization Levy such as the issues and challenges from the tax perspective on account of the digital space transactions, the Base Erosion and Profit Sharing Report on Action 1 that discusses the challenges of the digital economy and the measures to resolve them and the aforesaid CBDT report, the constitutional validity of the Equalization Levy and so on.

Additionally, we have also analyzed some of the important rulings by the Indian judiciary and certain key changes brought about by way of circulars and notifications in the direct and indirect tax regimes during the March quarter.

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

Regards,

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COVER STORY

THE HUNT FOR EQUALITY IN THE 'EQUALIZATION LEVY'

INTRODUCTION

E-commerce trade has now become a way of life. While one can avail a bundle of services or undertake a number of business transactions at the click of a button, it also enables a foreign entity to carry out revenue generating business activities in a particular jurisdiction without having any physical presence there.¹ The digital economy platforms comprise of trade and business, cloud computing, data warehousing, music, movies, digital advertising, etc. Most of the companies operating in this field would be able to undertake almost all their business activities through the internet without establishing any physical presence.

Thus, from a tax perspective, one of the concerns is whether the income generated from India by these e-commerce companies could be taxed in India under the current taxation laws in India read with the relevant DTAAs, if any. In a number of situations, mere digital platforms may not result in the formation of a 'permanent establishment'. When it is proposed to tax digital transactions wherein the transacting party does not have any physical presence in the relevant jurisdiction, it would be essential to determine the jurisdiction from where revenues are being earned. The jurisdiction where the activities are being performed will also have to be ascertained i.e. server location, etc. Thereafter, an appropriate methodology shall have to be ascertained to attribute income to each of the jurisdictions so that the same can be offered to tax. The tax issues relating to e-commerce transactions include characterization of payments (either as 'royalty' or 'fees for technical services'), establishing a nexus or link with the source jurisdiction, the place of actual execution, apportionment of revenue or profits among various jurisdictions that have the footprint, etc. These transactions have resulted in several tax challenges which the existing tax laws could not appropriately address. The challenges arising on account of digital transactions include parking of profits by e-commerce enterprises in low tax jurisdictions while significant proportion of profits ought to have been attributable to jurisdictions whose resources and people are utilized on account of the limitations under the prevailing tax laws.

The OECD by way of its BEPS initiative has attempted to address the tax challenges of the digital economy ("Action 1"). Based on the recommendations in the BEPS Report, India has now become the first country to tax digital levy by introducing equalization levy ("EL") on certain specified transactions. Immediately after Action 1 was published by the OECD, the CBDT constituted Committee on Taxation of E-Commerce ("CTE")

1. Technological development has led to the creation of online marketplaces which cater to the needs of many in terms of shopping, advertising, trading, socializing, etc.

to provide its recommendations regarding taxation of digital transactions under different business models.

GENERAL BACKGROUND

As per the IT Act, non-residents are taxed in India in respect of all incomes derived which are received or deemed to be received in India or accrue or are deemed to accrue in India.² The IT Act also provides for income that is deemed to accrue or arise in India in respect of a non-resident.³ Business income of a non-resident entity can be taxed in India only if such non-resident has a BC as per the IT Act and / or a PE in India as per the concerned DTAA. In case the payment is not towards a business income, the nature of such income has to be examined carefully in order to ascertain the taxability of such income.

SALIENT FEATURES OF THE OECD BEPS INITIATIVE UNDER ACTION 1

- Recommends several options to tackle the direct tax challenges and provides countries with the options to introduce safeguards so long as they respect existing treaty obligations.
- Highlights issues in relation to nexus⁴ and characterization⁵ with respect to digital economy transactions.
- Focuses on development and analysis of the possible options that can be adopted to address the aforesaid tax challenges arising from the digital economy. It provides three options i.e. (i) a new nexus based on 'significant economic presence'⁶; (ii) withholding tax on digital transactions⁷; and (iii) equalization levy⁸.
- It also provides that implementation of these proposals may not be required at this stage since adopting them would require substantial changes to key international tax standards and would require further work. However, countries could introduce any of the options in their domestic laws as additional safeguards against BEPS, provided they respect the existing treaty obligations or in their bilateral tax treaties.

2. Section 5 of the IT Act

3. Section 9 of the IT Act

4. Paragraphs 253 to 261 of the BEPS Report on Action 1

5. Paragraphs 268 to 272 of the BEPS Report on Action 1

6. A non-resident would have a significant economic presence in a country on the basis of factors that evidence a purposeful and sustained interaction with the economy of that country via technology and other automated tools. (Paragraphs 278, 279, 280 of the BEPS Report on Action 1)

7. A final withholding tax can be imposed on the gross amount of payments in case of specified B2B transactions as an effective means of collecting tax. This can also be combined with the concept of significant economic presence. (Paragraph 298 to 292 of the BEPS Report on Action 1)

8. This approach has been used by some countries to ensure equal treatment of foreign and domestic suppliers. (Paragraphs 302 to 308 of the BEPS Report on Action 1)

9. *Pinstorm Technologies (P) Ltd. v. ITO* (2013) 154 TTJ 173 (Mumbai ITAT)

10. *Yahoo India (P) Ltd. v. DCIT* (2011) 140 TTJ 195 (Mumbai ITAT)

11. *ITO v. Rights Florists (P) Ltd.* (2013) 143 ITD 445 (Kolkata ITAT)

12. Specified services have been defined to mean online advertisement, provision of digital advertising space or any other facility of service for the purpose of online advertisement

INDIAN JUDICIAL PRECEDENTS ON THIS ASPECT

- In the case of *Pinstorm Technologies*⁹, the Mumbai ITAT held that the amount paid by the assessee to Google Ireland with respect to the advertising services was in the nature of business profits and in the absence of a PE, the amount was held to be non taxable in India.
- In the case of *Yahoo India*¹⁰, the Mumbai ITAT held that the payments made by Yahoo India to YHHL for the services rendered in relation to advertising on its web portal were not in the nature of 'royalty' but in the nature of 'business profits' and in the absence of a PE, the income from services was not chargeable to tax in India.
- In the case of *Rights Florists*¹¹, the Kolkata ITAT held that Google Ireland and Yahoo USA's presence in India through their websites could not be said to constitute a PE in India and accordingly, no profits could be said to have accrued to either of the entities in India. It also held that such payments would not fall within the ambit of either 'royalty' or 'fees for technical services' under the IT Act.

SALIENT FEATURES OF EL AS PROPOSED BY THE FINANCE BILL, 2016

- The Finance Bill, 2016 proposes to introduce EL at the rate of 6% on the gross payments being made towards specified services¹² either by a resident and a non-resident that has a PE in India, to non-residents who do not have any PE in India. This EL shall be leviable only if the aggregate amount of consideration for the specified services availed during any tax year exceeds INR 0.1 million.
- The Central Government could notify any other service for aforesaid purposes.
- This levy would be applicable only in case of B2B transactions.

- It would not be levied in certain exceptional situations.
- Any income arising on account of specified services provided on which EL is chargeable shall be excluded from the total income of the assessee.
- It provides that the expenses incurred by the assessee towards specified services shall not be allowed as a deduction if appropriate withholding obligations are not met.¹³
- Some of the aforesaid payments could either be royalty or fees for technical services, the effective rate of tax would be reduced from 10%²⁰ to 6%-8%.
- The option of getting EL deducted by the person making the payment would place compliance burden on the payers in India. In some cases, the beneficial owner may insist for receiving the full payment, the payer may have to bear the tax burden as well.

CONCLUSIONS AND RECOMMENDATIONS OF THE CTE REPORT

- The only option that appears to be feasible and can be resorted to, without violating the obligations under a DTAA is 'EL'.
- EL should be separated from the income tax laws in India and, therefore, should be imposed through the statutory provisions of the Finance Act just like securities transaction tax¹⁴ and service tax.¹⁵
- The EL on gross amounts of payments made for digital services appears to be in accordance with the entries at serial number 92C¹⁶ and 97¹⁷ of the Union List of the Seventh Schedule of the Constitution of India and, therefore, its constitutionality can not be challenged.
- It would be preferable to restrict the application of EL to B2B transactions only.
- The rate of EL may be set between 6%-8% of the gross payments.
- Incomes on which EL has been paid should be exempt under section 10¹⁸ of the IT Act.
- Certain payments may also be subjected to EL such as online¹⁹ advertising or any services, rights or use of software for online advertising, including advertising on radio or television; digital advertising space; designing, creating, hosting or maintenance of website; etc.
- Such transaction could be given a label by the parties which is not included in the aforesaid list of specified services, and, therefore, it should be specified that these services would be subject to EL, irrespective of whatever nomenclature provided by the parties. Also, payments could also be made by a third party outside India (to avoid EL), which could be subsequently reimbursed by the actual user with a claim that no EL is payable on reimbursements. The Committee has recommended that EL should also be payable on payments made by a payer in India for reimbursement of expenses incurred by a third party outside India in respect of services covered under this levy.
- It would be essential to clarify that EL will become applicable once the payment is either credited or paid; whichever is earlier, to the beneficial owner in the books of accounts, irrespective of when and how the actual payment is made.
- The payments subjected to EL should be notified under section 195(7)²¹ of the IT Act.
- It is recommended that the definition of 'business connection' under section 9 of the IT Act may be expanded to include the concept of significant economic presence.

POSSIBLE GROUNDS OF CRITICISM ADDRESSED BY THE CTE

- EL being an additional tax over and above all other taxes that are already in place could affect the ease and cost of doing business in India: It is explained by the CTE that the aim and objective of EL is to ensure that unfair tax

13. Amendment proposed vide Finance Bill, 2016 by inserting section 40(a)(ib)

14. Imposed by Chapter VII of the Finance (No. 2) Act, 2004

15. Imposed by Finance Act, 1994

16. Taxes on services

17. Any other matter not enumerated in List II or List III including any tax not mentioned in either of those Lists

18. Amendment proposed vide Finance Bill, 2016 by inserting section 10(50)

19. The CTE has clarified that for the purposes of these services, 'online' means a facility or service or right or benefit or access that is obtained through the internet or any other form of digital or telecommunication network

20. Rate of tax (exclusive of surcharge and education cess) on royalty and fees for technical services under the IT Act

21. Notwithstanding anything contained in sub-section (1) and sub-section (2), the CBDT may, by notification in the Official Gazette, specify a class of persons or cases, where the person responsible for paying to a non-resident, not being a company, or to a foreign company, any sum, chargeable under the provisions of this Act, shall make an application to the Assessing Officer to determine, by general or special order, the appropriate proportion of sum chargeable, and upon such determination, tax shall be deducted under sub-section (1) on that proportion of the sum which is so chargeable

advantage to multinational companies is minimised thereby improving competitiveness of the businesses in India. By bringing greater clarity in tax obligations in respect of digital business, EL will stabilise the tax environment in India and facilitate businesses in India.

- The burden of EL is likely to fall on the Indian businesses and, therefore, would be detrimental to them: The CTE is of the view that the payer in India would be in a better situation to assess the tax and negotiate with the foreign beneficial owner. Even in cases where the economic burden of tax deducted falls on the Indian businesses, the lower rate of 6%-8% would provide a significant relief to them.
- The imposition of the EL may be a violation of the international tax practices: The CTE is of the view that the concept of EL is identified by the G-20 and OECD as a possible option that countries can adopt in their domestic tax laws and hence, the introduction is in accordance with the consensus view accepted by the G-20 and the OECD.
- Why such a levy should be imposed when it is not imposed in any other country: The CTE has discussed that India is not the only country²² to have imposed a levy to address the concerns arising from the ability of digital multinational enterprises to avoid paying taxes in the jurisdiction from where they are earning their income. The CTE remarks that all these instances along with the fact that the G-20 and OECD countries now agree on the rights of every country to impose any of the options identified in the BEPS Report is a clear indication that countries across the world are thinking about it.
- Non-availability of foreign tax credit: It is remarked that there is nothing to prevent the country of which the taxpayer is a resident from granting relief to the taxpayer under its own domestic laws to avoid double taxation. It is always possible for a taxpayer to have a PE in India and get taxed only on its net income attributable in India while creating disincentives against artificial arrangements to avoid paying taxes on income arising from India by exploiting the systematic weaknesses in the existing international taxation rules.
- Adverse effect on the competitiveness of Indian digital enterprises: The existing tax advantage that is being enjoyed by foreign enterprises over their Indian counterparts creates strong incentives for Indian enterprises to locate outside India and thereby poses a

strong challenge for the growth and expansion of the Indian digital industry. The EL aims at neutralising this disincentive and facilitating an environment where Indian digital enterprises can compete with their foreign competitors without having to locate outside India.

ISSUES FOR CONSIDERATION

IS EL A TAX AND WILL FOREIGN TAX CREDIT BE AVAILABLE?

The proposed definition of EL means tax leviable on consideration received or receivable for any specified service under the provisions of Chapter VII of the proposed Finance Bill, 2016. As per the provisions of the IT Act, tax means income tax chargeable under the provisions²³ of the IT Act. Therefore, in effect, it is proposed to levy 'income tax' under the garb of 'EL' on payments made for specified services as discussed above.

If the nature of 'EL' is not 'income tax', it would cause great difficulty to residents of a jurisdiction other than India to claim foreign tax credit in relation to the same. Hence, non-residents may charge a higher mark up to that extent or demand grossing up of such fees such that the Indian businesses have to bear the levy on account of EL. This could potentially increase the cost of the domestic businesses and may not lead to a level playing field for foreign and domestic e-commerce companies since the burden of EL would fall on the domestic players.

TREATY OVERRIDE

It seems that the Government has not considered the recommendations of the OECD BEPS Report on Action 1 in its entirety. The options suggested (i.e. including the option of EL) as measures to combat the challenges of the digital economy were recommendatory in nature which could be adopted by countries only if such a levy does not compromise the existing treaty obligations.

By introducing the EL by way of a unilateral act into the domestic tax laws of India, it is indirectly sought to override the existing tax treaties which may not be well accepted by several countries across the globe.

The issue that requires examination is whether a country can unilaterally amend the domestic tax laws that could override the provisions of the concerned tax treaties. Article 18 of the Vienna Convention²⁴ provides that a State, which is a party to a treaty, is obliged to refrain from acts, which would defeat the object and purpose of the treaty. Article 26 of the Vienna Convention provides the principle *pacta sunt servanda* i.e.

22. UK has imposed "Diverted Profit Tax" from April 1, 2015 to address these concerns. Australia has imposed a "Multinational Anti Avoidance Law" from January 1, 2016. Italy is reported to be considering a new "Digital Tax" consisting of 25% withholding tax on payments. Some countries, like Brazil, already impose withholding tax on such payments

23. Section 2(42) of the IT Act

24. Tax Treaties are governed by the Vienna Convention. India has not yet signed the Vienna Convention and therefore, it is not binding in nature. However, it certainly provides guidance for interpretation

every treaty in force is binding upon the parties and must be performed in good faith. Thus, any unilateral act by a country that leads to an amendment of the domestic tax laws could lead to a violation of the aforesaid Articles.

Article 27 (without prejudice to Article 46) of the Vienna Convention provides that a party may not invoke the provisions of its internal law as justification for its failure to perform its obligations under a treaty. Article 46 provides that a State may not invoke the fact that its consent to be bound by a treaty has been expressed in violation of a provision of its internal law regarding competence to conclude treaties as invalidating its consent unless that violation was manifest and was related to a rule of its internal law of fundamental importance. When India negotiated the tax treaties, the domestic tax laws did not provide for any statutory obligation stating that a tax treaty could be unilaterally overridden by subsequent amendment to the domestic tax laws. Therefore, one can conclude that any unilateral act on the part of Parliament would lead to a contravention of Article 27 and 46 of the Vienna Convention.

CONSTITUTIONAL VALIDITY

The CTE is of the view that imposition of EL is constitutionally valid (as discussed above). It is pertinent to note that as per List II, Entry 55 of the Constitution of India, only the State Government is empowered to levy 'taxes on advertisements other than advertisements published in newspapers and advertisements broadcast by radio or television'. Similarly, Entry 92C of List I of the Constitution of India provides for 'Taxes on Services' which could include all services on which taxes can be levied by the Centre. However, since Entry 55 of List II is extremely specific in terms of granting powers to the State for taxes on advertisements, the constitutional validity of this levy by the central Government could be challenged because the State has got the specific power to levy taxes on advertisements.

Conclusion

The CTE, after examining a wide variety of aspects, has touched various crucial aspects of the introduction of EL such as constitutional validity, review of the rate of levy and an upward escalation of the same on a going forward basis, analyzing and recommending other services on which EL could be imposed, etc. The CTE has also granted the flexibility to the Government to notify any other services on which EL can be levied.

It can be alleged that by amending the domestic tax laws only to tax certain services is a case of treaty override. Constitutional validity could still be challenged. Instead of introducing this levy, it would have been far more appropriate if India waited to ascertain how other OECD member countries are responding to this Report. We also need to analyze this aspect in greater detail taking into consideration the broader challenges and perspectives from an Indian standpoint. The consequences of such a levy would have to be examined from an Indian market perspective and how it would impact the recently much promoted concept of 'Start-up India/ Digital India/Ease of Doing Business in India'.

CASE LAW UPDATES

Direct Tax

PROJECT OFFICE FOR INSTALLATION OF PETROLEUM PLATFORMS AND PIPELINES NOT A PE IN INDIA

In *National Petroleum Construction Company*²⁵, the Delhi HC held that the activities of a UAE resident's project office ("PO") fell within the exclusionary clause of Article (5)(3)(e) of the India-UAE DTAA. Further, since the project activities were for a duration of less than 9 months, the UAE entity did not have an installation PE and in the absence of a dependent agent of the UAE entity in India, there could be no dependent agent PE.

FACTS

National Petroleum Construction Company ("**Assessee**") was incorporated and was a tax resident in the UAE. Assessee was, *inter alia*, engaged in the fabrication of petroleum platforms, pipelines and other equipment. In addition, the Assessee also undertook installation of petroleum platforms, submarine pipelines and pipeline coating. The Assessee had entered into a contract with ONGC for the installation of petroleum platforms and submarine pipelines. The contract comprised of various activities among which those relating to survey, installation and commissioning were undertaken in India while the platforms were designed, engineered and fabricated overseas.

The Assessee computed income under the IT Act on a presumptive basis by taxing the gross receipts pertaining to activities in India, as reduced by the verifiable expenses at the rate of 10% and receipts pertaining to activities outside India at 1%. Though the Assessee had been following this basis for tax computation since AY 1999-00, the AO did not accept the methodology during AYs 2007-08 and 2008-09.

For AY 2007-08, the AO passed a draft assessment order holding that the Assessee had a fixed place PE in India in the form of its PO in Mumbai. Further, the AO also held that its agent i.e. M/s Arcadia Shipping Ltd. ("**ASL**"), was a dependent agent of the Assessee which constituted its Dependent Agent PE ("**DAPE**") in India. The AO also concluded that the Assessee had formed an Installation/Construction PE in India.

Additionally, rejecting the Assessee's submission that the fabricated material was sold to ONGC outside India, the AO held that the contract was a turnkey composite contract which was indivisible. Accordingly, the contractual receipts of the activities performed outside India were also taxable in India. The consideration received by the Assessee for design and engineering was in the nature of Fee for Technical Services. In the absence of separate books of accounts for the contract, the AO estimated Assessee's profit to be 25% of the consideration received from ONGC. AO also rejected the Assessee's contentions that the provisions of section 44BB of IT Act should be applied to it.

Assessee filed its objections to the draft assessment order before the DRP. The DRP rejected the Assessee's arguments and concurred with the observations of the draft assessment order. The AO passed an assessment order without any changes from the draft.

The Assessee then preferred an appeal before the ITAT. The ITAT concurred with the views of the AO and held that the Assessee had a fixed place PE, DAPE and Installation PE in India. However, Assessee's contention that the contract in question could be segregated into offshore and onshore activities

25. National Petroleum Construction Company v. Director of Income-tax (2016) 66 taxmann.com 16 (Delhi)

was accepted. Accordingly, the income from activities carried out outside India could not be attributed to its PE in India. As a result, the profits attributable to design, procurement of material and fabrication could not be taxed in India. The ITAT neither accepted the Assessee's contention that tax should be computed on presumptive basis, nor accepted the Assessee's contention that section 44BB of the IT Act was applicable.

Aggrieved by the ITAT order, the Assessee preferred an appeal before the Delhi HC.

ISSUES

1. Whether the Assessee's PO constituted a fixed place PE, DAPE or an Installation PE in India;
2. Whether the turnkey contract was divisible into offshore and onshore components;
3. Whether the presumptive basis of taxation adopted by the Assessee was correct;

ARGUMENTS/ANALYSIS

The IRA contended that the Assessee had filed a return admitting that it had a PE in India and a contrary claim cannot be made at the time of assessment. Further, drawing inference from the definition of "PO" under the exchange control regulations, they also argued that a PO has been defined as a place of business to represent the interest of the foreign company executing a project in India and accordingly, could be construed as a fixed place of business. It was also contended that the Assessee's Installation PE would also commence with the commencement of the contract. The third party agent i.e. ASL was appointed as the sole and exclusive agent and under the terms of the consultancy agreement, had agreed not to represent a competitor of the Assessee or act in a manner detrimental to the Assessee's interest, had participated in the pre-bid meeting, had no discretionary powers and was acting as per the instructions of the Assessee. It was also argued that since the contracts in question were composite contracts and all activities were closely linked, the contract could not be split between the activities carried out overseas and activities carried out in India. Accordingly, the ownership of the platforms and other material could be transferred to ONGC only upon ONGC issuing a certificate of completion and acceptance of work. Thus, the Assessee's contention of the income from activities conducted in relation to design, procurement of material and fabrication of the platforms, was not attributable to the PE in India, was erroneous.

The Assessee, on the other hand, submitted that it had established the PO only to comply with contractual requirements and exchange control regulations. The PO was merely a communication channel between the Assessee and ONGC. In the past too, the addresses of the POs were

different and had been established only for the contracts entered into. Accordingly the AO had erred in holding that the Assessee had carried its business in India through a PE. Further, the installation and commissioning of platforms carried out by the Assessee in India was carried out by its employees at the offshore site, with the help of barges. Pre-engineering and pre-construction surveys were conducted by independent third party service providers, on a principal-to-principal basis. The PO was not involved in pre-bid meetings, surveys, kick-off or review meetings. Further, the Assessee contended that in terms of article 5(2)(h) of the DTAA, the Installation PE would come into existence only if the construction or assembling activity continued for a period of 9 months or more in India. Assessee also argued that the activities of the independent sub-contractor could not be included for calculating the period of 9 months under Article 5(2)(h) of the DTAA. The Assessee also disputed the finding that ASL was a DAPE of the Assessee in India as ASL was an independent entity and carried out substantial business activities other than those related to the Assessee. It relied on the SC decision in *Hyundai Heavy Industries*²⁶ to support its contention that a profit margin of 10% was appropriate for installation and commissioning of platforms in India. The Assessee also argued that it had estimated its taxable income on a consistent basis and had been accepted by the AO in the past and there was no material on record which would justify a departure from the consistent methodology accepted earlier. It also argued that the computation of presumptive profit was based on CBDT Instruction No.1767 and principles which were approved by the Supreme Court in *Hyundai Heavy Industries* and, thus, had a sound legal basis.

DECISION

The Delhi HC held that it is clear from the expression 'Permanent Establishment' there is (a) a fixed place of business; and (b) business of the enterprise being carried on wholly or partially through the said fixed place of business. These two conditions must be satisfied. In addition, the word permanent in the term 'permanent establishment' indicates that there should be some permanency attached to the fixed place of business i.e. a place which is not temporary, interim, short-lived or transitory.

Article 5(2) of the DTAA provides for an inclusive definition of the term "PE" and specifically lists out places of business that fall within the meaning of that expression. The use of the word 'especially' underscores the intention of removing any doubts that only such places listed in sub-paragraphs (a) to (i) fall within the definition of 'PE'. If read in the context of the other provisions of Article 5, paragraph 2 clearly indicates that it has been used as an explanatory provision to include certain places of business that would constitute a PE of an enterprise. Thus, all classes of PEs as specified in various sub-paragraphs of paragraph 2 of Article 5 of the DTAA would be construed as a PE, subject to the essential conditions of paragraph 1 of Article 5 being met. Insofar as sub-paragraphs (h) and (i) of paragraph 2 of Article 5 are concerned, the test of

26. CIT v. Hyundai Heavy Industries Co. Ltd. (2007) 291 ITR 482 (SC)

permanence as required under paragraph 1 of Article 5 is substituted by a specified minimum period of 9 months. Thus, places of business as specified under sub-para (h) and (i) of paragraph 2 of Article 5, cannot be construed as a PE of an enterprise unless they exist for a period of at least 9 months.

Article 5(3) is an exclusionary clause and is intended to exclude certain places of business from the scope of PE. Paragraph 3 begins with a non-obstante clause—“Notwithstanding the preceding provisions of this Article”. Thus, the exclusions provided under paragraph 3 would override the provisions of paragraph 1 and 2 of Article 5 of the DTAA. In other words, even if a place of business squarely falls within the definition of paragraph 1 of Article 5 and is specifically listed in paragraph 2 of the said Article, the same would, nonetheless, not be construed as a PE of an enterprise, if it falls within any of the exclusionary clauses contained in sub-para (a) to (e) of paragraph 3 of Article 5 of the DTAA.

Article 5(4) of the DTAA provides for a legal fiction to include an agent (other than an agent of an independent status) to be a PE of the principal enterprise. Paragraph 4 also begins with a non-obstante clause. Thus, even though an agent may not, in the strict sense, fall within the definition of a ‘PE’ as defined under paragraph 1 and/or paragraph 2 of Article 5 of the DTAA, it would be deemed that a PE of an enterprise exists if the business of an enterprise is carried on through an agent. Paragraph 5 of Article 5 provides for an exclusion to the application of paragraph 4 and the agents of a principal enterprise as described in paragraph 5 of the DTAA would be excluded from the scope of paragraph 4 of Article 5 of the DTAA.

Even though the Assessee’s PO established in Mumbai falls within the definition of PE in terms of paragraph 1 and 2 of Article of DTAA, it would still have to be seen whether it stands excluded under paragraph 3 of Article 5 of the DTAA. Clause (e) of paragraph 3 of Article 5 expressly provides that notwithstanding the provisions of paragraph 1 and paragraph 2 of Article 5, a PE would not include “maintenance of a fixed place of business solely for the purposes of carrying on, for the enterprise any other activity of a preparatory or auxiliary character”. The Assessee contends that its PO falls within this exclusionary clause. Further, its office at Mumbai was opened only to comply with contractual requirements and the exchange control regulations. It was only as a communication channel and not for the execution of the Contracts. The PO was only used for the purposes of correspondence and as a communication channel; apart from that, the PO had no role to play in the execution of the activities under the contracts and no other business of the Assessee was carried on through the PO. Further, there is no material to suggest that the employees of the PO had participated in review of the engineering documents done in Mumbai or had participated in the discussions or approval of the designs submitted to ONGC. In absence of any material evidence to controvert the Assessee’s claim that its PO was only used as a communication channel, the same has to be accepted.



Installation PE:

As per Article 5(2)(h), an installation PE is constituted by a building site or a construction or an assembly project, when activities relating to the project or site are commenced. The said clause is also to be read harmoniously with paragraph 1 of Article 5 of the DTAA which provides for a fixed place PE. An activity which may be related or incidental to the project but which is not carried out at the site in the source country would clearly not be construed as a PE as it would not comply with the essential conditions as stated in Article 5(1) of the DTAA. A building site or a construction assembly project does not necessarily require an attendant office; the site or the attendant office in respect of the site/project itself would constitute a fixed place of business once an Assessee commences its work at site. For Article 5(2)(h) to be applicable, it is essential that the work at site or the project commences – it is not relevant whether the work relates to planning or actual execution of construction works or assembly activities. Preparatory work at site such as construction of a site office, a planning office or preparing the site itself would also be counted towards the minimum duration of an installation PE. However, a building site or a construction could be construed as a PE only if the business of the enterprise is carried on for a minimum period of 9 months. Where an enterprise is not granted access to the site for a long duration and carries on no activity at site during that period, the site will not be a fixed place of business of an Assessee during that period. While the duration of the project itself exceeded 9 months, a careful reading of Article 5(2)(h) of DTAA indicates that it is necessary that the ‘site, project or activity continues for a period of more than 9 months’. It is an implicit condition that the enterprise should be involved at the site or involved in the assembly project in the source country. In the present case, the installation activities lasted much less than the minimum period of 9 months.

Even if the time spent by ASL in conducting the pre-engineering, pre- design survey is included, the duration of the project activities in India would not exceed 9 months. The Assessee’s PO was inextricably linked to the project. Therefore, if the duration of the project activities in India was less than 9 months, it cannot be held that the Assessee had a PE in India under Article 5(2)(h) of the DTAA.

DAPE:

Based on facts, it is apparent that ASL's activities were not limited to providing services to the Assessee but extended to various other activities. ASL also provided logistics and consultancy support to various companies other than the Assessee. The Director's Report also clearly indicates that the activity of providing offshore marketing/technical consultancy and offshore fabrication and installation work were amongst the regular activities carried on by ASL. Further, the consultancy agreement entered into between the Assessee and ASL, while it says that ASL will act as 'sole and exclusive' consultant for the Assessee in India, nowhere did it fetter ASL to carry on its regular activities including providing consultancy services to persons other than the Assessee's competitors. Further, ASL had acted on behalf of the Assessee in its normal course of business. Therefore, ASL could not be construed to be working wholly and exclusively for the Assessee. Further, presence of ASL employees in the pre-bid meeting will not per se result in ASL constituting a DAPE. Additionally, there is material to support that the Assessee would bid and execute contracts in its name. The consultancy agreement does not authorise ASL to conclude contracts on behalf of the Assessee. Hence, ASL cannot be regarded as the DAPE of the Assessee in India.

Presumptive taxation under section 44BB:

Although, the Assessee had claimed that section 44BB and the CBDT Instruction No.1767 provided the legal basis for the method of computation of taxable income adopted by the Assessee, the same is clearly erroneous. Section 44BB of the IT Act provides for levying tax on a presumptive basis and 10% of the receipts are presumed to be the profits of a foreign company rendering the services specified therein. There is no scope for allowing any deduction while computing tax on a presumptive basis. The method of computation as adopted by the Assessee was also not supported by the CBDT Instruction No. 1767.

Profit attribution:

Since the Assessee does not have a PE in India, the question of splitting the business profits of the Assessee arising from the contract into profits attributable to India and profits attributable to the Assessee overseas does not arise. However, the HC, for the sake of completeness examined the attribution aspect. Under Article 5, only such income as is attributable to a UAE based Assessee's PE in India can be taxed. In *Hyundai Heavy Industries (supra)*, the SC explained that the only way to ascertain the profits arising in India would be by treating the Assessee's PE in India as a separate profit centre viz-a-viz the foreign enterprise. In the present case, the consideration for various activities has been specified in the contracts in question. Invoices raised by the Assessee specifically mentioned the work done outside India as well as in India. Thus, even though the contracts in

question may be turnkey contracts, the value of the work done outside India is ascertainable. There is no dispute that the values ascribed to the activities under the contracts are not at arm's length. There is also no material to indicate that the work done outside India included any input from the Assessee's PE in India. The HC agreed with the view of the ITAT that since the consideration for various activities such as design and engineering, material procurement, fabrication, transportation, installation and commissioning had been separately specified, the consideration for the activities carried on overseas could not be attributed to the Assessee's PE in India.

SIGNIFICANT TAKEAWAYS

This ruling is significant in as much as holding that a PO providing auxiliary and ancillary activities cannot be a PE. Further, the principle laid down by previous rulings that the date of commencement of the contract ought to be from the preparatory activities leading to the actual performance of the contract. Further, this judgement also assumes significance in clarifying that for the purpose of counting the number of days spent, long interruptions leading to suspension of the work should not be considered. Also, if the subcontractor has worked independently on the site, then the time spent by the sub-contractor should be excluded while determining the duration of the PE of the contractor.

The decision, to a large extent, reinforces the principles laid down by the SC in the *Ishikawajima Harima*²⁷ case in differentiating between the offshore and onshore activities and taxability of incomes from such activities in India. This decision reinforces that principle that if the consideration for each of the activities in a turnkey contract are identifiable, then the contract is divisible, and income from activities performed outside India will not be liable to tax in India.

27. *Ishikawajima-Harima Heavy Industries Ltd. v. DIT* (2007) 288 ITR 408 (SC)

TRANSFER OF ENTIRE SHAREHOLDING IN A SUBSIDIARY COMPANY NOT 'SLUMP SALE'

In *UTV Software Communications Ltd.*²⁸, the Mumbai ITAT held that transfer of entire shareholding in a subsidiary company does not amount to 'slump sale' but a mere transfer of shares as the consideration was received by the 'shareholder' and not by the 'subsidiary'.

FACTS

UTV Software Communications Ltd. ("**Assessee**") was in the business of production of television programs, air time sales, movie production and distribution of films. During the assessment year 2007-08, the Assessee had transferred its entire shareholding in its 100% subsidiary company, United Home Entertaining Ltd. ("**UHEL**") to a third party and worked out capital gains under section 48 of the IT Act.

The AO was of the belief that the transactions amount to slump sale of an undertaking and computed the capital gains in regards to section 50B of the IT Act. The CIT(A) upheld the order of the AO and thus, the Assessee preferred the instant appeal before the ITAT.

ISSUES

Whether sale of shares in a subsidiary company in its entirety to a third party would be construed as transfer of undertaking and thus, capital gains has to be computed under section 50B of the IT Act instead of section 48 of the IT Act?

ARGUMENTS/ANALYSIS

The primary contention of the Assessee was that it had only sold the shares of UHEL and that the same would not fall under the definition of 'slump sale' under section 2(42C) of the IT Act as there was no transfer of an 'undertaking'.

It was further contended that the shareholders do not have any rights over the assets of the company and therefore, by analogy, when the shares were transferred, it cannot be said that the assets of the company were transferred. Moreover, UHEL was still in existence even after its shares were transferred. Thus, it cannot be said that the Assessee had transferred any 'undertaking' which would come within the purview of slump sale as given under section 2(42C) of the IT Act.

DECISION

The ITAT held that a conjoint reading of section 50B, 2(42C) and explanation 1 to section 2(19AA) of the IT Act would result in a conclusion that transfer of shares would not result in the transfer of an undertaking resulting in a slump sale under section 50B of the IT Act.

The ITAT further held that in case of a slump sale, the company which is transferring its assets (i.e. UHEL) ought to have received consideration as the company is a distinct legal entity. However, this was not the case in the instant matter since the shares were transferred by the Assessee (shareholder) and the Assessee received the sale consideration.

28. *UTV Software Communications Ltd. v. ACIT (2016) 65 taxmann.com 161 (Mumbai ITAT)*

The ITAT relied on the following decisions to hold that transfer of shares cannot be considered as slump sale of an undertaking for the purpose of section 50B read with section 2(42C) of the IT Act:

- (i) *Mrs. Bacha F. Guzdar*²⁹ wherein it was held that although shareholders are entitled to the profits of the company, they do not have any right over the assets of the company nor have any share in the property of the company. The company is a juristic person and distinct from the shareholders and, therefore, it is the company which owns the property and not the shareholders.
- (ii) *Vodafone International Holdings B.V.*³⁰ wherein it was held that the controlling interest in a company is not an identifiable or distinct capital asset, independent of holding of shares. The right of a shareholder may assume the character of a controlling interest where the extent of the shareholding enables the shareholder to control the management. The tax consequences of a share sale would be different from the tax consequences of an asset sale. A slump sale would involve tax consequences which would be different from the tax consequences of sale of assets on itemized basis.
- (iii) *Bhoruka Engineering Indus Ltd.*³¹ wherein it was held that if the shareholder chooses to transfer the lands and part with the land to the purchaser of shares, it would be a valid transaction in law and merely because they were able to avoid payment of tax, it cannot be said to be colourable device or a sham or an unreal transaction.

On these premises, the ITAT held that the assessing authority had committed serious error in proceeding on the assumption that the effect of transfer of share is the transfer of immovable property, and, therefore, the corporate veil can be lifted. The ITAT agreed with the Assessee that the subject transaction involved transfer of shares and cannot be equated with the transfer of an undertaking.

SIGNIFICANT TAKEAWAYS

Recharacterisation of a transaction is often adopted by the IRA to levy or increase the taxes to be paid by an assessee. Whilst the Courts have consistently discouraged such practice and allowed recharacterisation only in certain exceptional situations, the IRA continues to play truant!

This decision is important from a corporate restructuring perspective in as much as it reiterates the fact that the transfer of shares does not amount to a slump sale. It must be recalled that in the case of *VST Industries v. ACIT*³² the Hyderabad ITAT had, in a case where the taxpayer had sold 99% of its subsidiary's shares along with all its assets and liabilities, including but not limited to, all licences, permits, approvals, registration, contracts, employees and other contingent liabilities also for a lumpsum consideration, held it to be a slump sale and this has created certain doubts regarding the characterisation of transactions involving sale of shares. It is hoped that this decision should put at rest any attempts by the IRA to recharacterise transactions involving mere transfer of shares as slump sale.

29. *Mrs. Bacha F. Guzdar v. CIT* (1955) 27 ITR 1 (SC)

30. *Vodafone International Holdings B.V. v. Union of India* (2013) 341 ITR 1 (SC)

31. *Bhoruka Engineering Indus Ltd. v. DCIT* (2013) 356 ITR 25 (Karnataka)

32. *VST Industries v. ACIT* (2010) 41 SOT 415 (Hyderabad)

NO SET-OFF OF BUSINESS LOSS ON CHANGE IN SHAREHOLDING EVEN IF ULTIMATE HOLDING COMPANY SAME

In **Yum Restaurants**³³, carry forward and set-off of business loss was denied under section 79 on change in 100% shareholding of the Assessee even though the ultimate holding company remained the same.

FACTS

Yum Restaurants (India) Private Limited ("**Assessee**") was part of the Yum Restaurants Group with its ultimate holding company being Yum Brands Inc. USA (Yum USA). In FY 2008-09, 99.99% of shares of the Assessee were transferred by Yum Asia to Yum Singapore pursuant to a restructuring within the group.

The AO observed that the parent company of the Assessee as on 31st March 2008 was the equitable owner of the shares but not as on 31st March 2009. Accordingly, the AO held that the Assessee was not permitted to set off the carry forward business losses incurred till 31st March 2008.

The CIT(A) and the ITAT upheld the position taken by the AO and held that the fact that Yum Asia and Yum Singapore were subsidiaries of the ultimate holding company, Yum USA, did not mean that there was no change in the beneficial ownership.

ISSUES

Whether carry forward and set-off of business loss can be denied under section 79 on the change in more than 49% shareholding of the Assessee even though the ultimate holding company remains the same?

DECISION

The Delhi HC took note of the ITAT's decision which held that there was a change of the beneficial ownership of shares since the predecessor company (i.e. Yum Asia) and the successor company (i.e. Yum Singapore) were distinct entities. The fact that they were subsidiaries of the ultimate holding company, Yum USA, did not mean that there was no change in the beneficial ownership. Unless the Assessee was able to show that notwithstanding shares having been registered in the name of Yum Asia or Yum Singapore, the beneficial owner was Yum USA, there could not be a presumption in that behalf.

Based on the above, the Delhi HC held that there was indeed a change of ownership of 100% shares of Yum India from Yum Asia to Yum Singapore, both of which were distinct entities. Although they might be associated enterprises of Yum USA, there was nothing to show that there was any agreement or arrangement that the beneficial owner of such shares would be the holding company, Yum USA. The question of 'piercing the veil' at the instance of the Assessee does not arise. In the circumstances, it was rightly concluded by the ITAT that in terms of Section 79 of the Act, the Assessee cannot be permitted to set off the carry forward accumulated business losses of the earlier years.

33. Yum Restaurants (India) (P.) Ltd. v. Income-tax Officer (2016) 66 taxmann.com 47 (Delhi)

SIGNIFICANT TAKEAWAYS

In the instant case, the HC has given a literal interpretation to section 79 of the IT Act and resorted to the assumption that the corporate veil cannot be lifted to treat the ultimate holding company as the beneficial owner and, therefore, the actual owner of the shares should be treated as the beneficial owner. It must be noted here that this issue has been debatable and there have been rulings supporting both viewpoints on this issue.

The Delhi ITAT in the case of *Select Holiday Resorts Pvt. Ltd.*³⁴, had held that where a parent company merged with its subsidiary, the benefit of carry forward and set off of losses could not be disallowed on the ground that there was a change in the shareholding of more than 51% of the share capital of the subsidiary company, since there was no change in control and management of the amalgamated company pre and post merger.

On the other hand, along the lines of this decision of Delhi HC, in *Just Lifestyle Pvt. Ltd.*³⁵ involving a similar situation, the Mumbai ITAT held that a company is a distinct legal entity and denied the benefit of carry forward and set off of business losses. This was on the ground that even if shares of up to 51% voting power remained within the same group, if there was a change in ownership of shares, section 79 would be attracted. The same conclusion was drawn in the case of *Tainwala Trading and Investments Co. Ltd.*³⁶, wherein the Mumbai ITAT observed that “A person is said to be a beneficial owner of shares when they are held by someone else on his behalf, meaning thereby that the registered owner is different from the actual or the beneficial owner. Where the shares are not so held by one for and on behalf of another, the concept of beneficial ownership cannot be invoked.” It must be noted that Section 79 refers to “voting power being beneficially held by persons...” The term “beneficially held” has not been defined under the IT Act. International commentaries³⁷ have defined the term “beneficial owner” as follows:

“The beneficial owner is he who is free to decide (1) Whether or not the capital or other assets should be used or made available for use by others, or (2) how the yields therefrom should be used, or (3) both”

The “beneficial owner” of dividends is the person who receives the dividends for his or her own use and enjoyment, and assumes the risk and control of the dividend he or she receives.

In view of the above uncertainty, it might be helpful for the corporate taxpayers if the Government comes up with a clarification defining what constitutes “beneficial holding” so that the uncertainty can be taken care of.

34. DCIT v. Select Holiday Resorts Pvt. Ltd. (2012) 49 SOT 20 (Delhi ITAT)

35. Just Lifestyle Pvt. Ltd. v. DCIT (2013) TS 562 (Mumbai ITAT)

36. Tainwala Trading and Investments Co. Ltd. v. ACIT (2012) 22 taxmann.com 68 (Mumbai ITAT)

37. Klaus Vogel on Double Taxation Conventions (Kluwer law International, 4th edn., 2012)

TRANSFER OF SHAREHOLDING FROM MAURITIAN TO SINGAPORE COMPANY FOR OPERATIONAL -EXCELLENCE NOT A TAX- AVOIDANCE SCHEME

In *Dow Agrosciences Agricultural Products Ltd*³⁸, the AAR held that transfer of shares of an Indian company by a Mauritius company, which it held for more than 20 years, to a Singapore company driven by geographical re-organisation of the group and "operational-excellence" motive cannot be a scheme to avoid taxes and would not be taxable under Indo-Mauritius DTAA in absence of a PE of the Mauritius company in India.

FACTS

Dow Agrosciences Agricultural Products Ltd ("**Applicant**") was a company incorporated in Mauritius holding a Tax Residency Certificate ("**TRC**") and was engaged in manufacturing and trading of pesticides and insecticides. The Applicant was part of the multi-national group of companies ("**Dow Group**") which was divided into various areas based on their geographical locations namely, North America, South America, Europe, Asia Pacific and India, Middle East and Africa group ("**IMEA**"). Between 1995 to 2005, the Applicant had acquired approximately 99.99% of the shares in Dow Agrosciences India Private Limited ("**DAS India**"), which was then a part of the India, Middle East and Africa group ("**IMEA**").

In FY 2009-10, the IMEA group was dismantled and the countries therein were realigned to other regions as per geographical convenience whereby India was made part of Asia Pacific region and DAS India was proposed to be shifted to an entity which falls in Asia Pacific Region viz., Dow Singapore from an entity which falls in Europe Region viz., the Applicant ("**Proposed Transfer**"). The Applicant claimed that the objective for the Proposed Transfer was to achieve 'operational excellence and administrative convenience' as well as 'better control' and that the Dow Group believes that the proposed transfer would help Dow Group to focus on customer service including support for new product launches, strong compliance culture, commitment to health, safety and the environment etc.

The Proposed Transfer was to be carried out by way of contribution of shares of DAS India by the Applicant to DAS Singapore as its capital whereby the Applicant would hold 100% of DAS Singapore which in turn would hold close to 100% in DAS India. The value of DAS Singapore's shares recorded in the books of the Applicant was proposed to taken as the sale consideration for transfer of shares of DAS India.

ISSUES

The questions for consideration before the AAR inter alia included the following -

1. Whether the investment of the Applicant in DAS India would be considered as a capital asset under section 2(14) of the IT Act?
2. Whether capital gains arising from the Proposed Transfer would be subject to tax in India under the IT Act?
3. Whether the gains arising to Applicant from the Proposed Transfer would be taxable in India in the absence of a PE of the Applicant in India under the Indo-Mauritius DTAA?
4. Whether the Applicant would be liable to pay MAT under the provisions of section 115JB of the IT Act?

38. Dow Agro Sciences Agricultural Products Ltd., In re (2016) 65 taxmann.com 245 (AAR)

5. Whether the provisions of section 92 to section 92F of the IT Act relating to transfer pricing would be applicable if the Proposed Transfer is not taxable?
6. Whether the Applicant is required to file any return of income in India under section 139 of the IT Act if the Proposed Transfer is not taxable?

ARGUMENTS/ANALYSIS

The IRA contended that the Applicant is a shell company and whole scheme of transfer of shares to a Singapore entity amounted to a scheme to avoid payment of taxes. The IRA also contended that DAS India has not declared and distributed dividend since 2004 and therefore, to the extent of accumulated profits, the sale proceeds should have to be assessed in India.

On the other hand, the Applicant pleaded that the transfer is proposed with the objective of the group re-organization to reduce complexities, improve efficiency and reduce costs for the Dow Group. The Applicant on the basis of the TRC issued by the Mauritius authorities contended that it is neither an Indian company nor the control and management of its affairs is situated in India. Further, the Applicant relied on the accounting test, intention test, quantum test and various judgements³⁹ to contend that the shares held in DAS should be considered as capital asset and not stock in trade. As regards the taxability, the Applicant contended that the capital gains from the Proposed Transfer would not be taxable in India under section 9(1)(i) of the IT Act read with Article 13(4) of Indo-Mauritius DTAA and also placed reliance *inter alia* on the SC decision in the case of Azadi Bachao Andolan⁴⁰, to contend that where the provisions of DTAA are more beneficial, the same would apply to an assessee and also that treaty shopping is not taboo. In the absence of Applicant's PE in India, capital gains from the proposed transfer would not be taxable in India under Article 13(2) of the India-Mauritius DTAA.

Also, the Applicant stated that the shares of DAS were acquired for the first time almost 20 years back and thereafter, over a period of 10 years from 1995 to 2005 at a cost of about INR 61 crore. The Applicant relied on the SC

ruling in the Vodafone case⁴¹ to contend that the setting up of wholly owned subsidiary in Mauritius by genuine substantial long term FDI in India from/through Mauritius, pursuant to DTAA and Circular 789 can never be considered to be set up for tax evasion.

The IRA also made detailed submissions to demonstrate the transactions/ relationship between DAS India and DAS US which is the parent company of the Applicant to state that the DAS India is controlled by DAS US. Also, the IRA contended that the DAS US should be considered as the owner of shares of DAS India and capital gains should be computed in the hands of DAS US and that the Applicant has no substantive real and independent identity.



RULING OF THE AAR

On the first issue, relying on the various submissions of the Applicant stated above and the fact that no transaction of the shares of DAS India has taken place other than the Proposed Transaction, the AAR agreed that the shares of DAS India are a capital asset and not stock in trade in the hands of the Applicant.

As regards second and third issues, the AAR observed that the acquisition of shares of DAS India was over a period of 10 years from 1995 to 2005 for a substantial cost of about INR 61 crore and the investment was made after obtaining prior approval of the Department of Industrial Policy and Promotion ("DIPP") and the RBI. Further, all this exercise was also more than 5 years old from the date of the last acquisition of the shares of DAS. Therefore, the AAR was of the view that the transaction could not have been a scheme to avoid payment of taxes in India. Also, the AAR agreed with the business objective for shifting of DAS India from the European region to the Asia-Pacific pursuant to the dismantling of the IMEA Group in 2010. The AAR also took note of various judicial precedents⁴² relied by the Applicant which have dealt with the issue of entitlement of the Indo-Mauritius DTAA and *inter alia* held that that the setting-up of a Mauritius Company with an eye on the DTAA, by itself will not make it a tax avoidance arrangement.

39. G.Venkata Swami Naidu and Company v. CIT (1959) 35 ITR 594 (SC); Raja Bahadur Kamakhya Narain Singh v. CIT (1970) 77 ITR 253 (SC); Praxair Pacific Ltd. v. Director of Income Tax (International Taxation) (2010) 326 ITR 276 (AAR)

40. UOI vs. Azadi Bachao Andolan (2003) 263 ITR 706 (SC)

41. Vodafone International Holdings BV v. Union of India and Anr. (2012) 341 ITR 1(SC)

42. UOI vs. Azadi Bachao Andolan (2003) 263 ITR 706 (SC); E Trade Mauritius Ltd., In re. (2010) 324 ITR 1 (AAR); Sanofi Pasteur Holding SA v. Department of Revenue (2013) 354 ITR 316 (AP), Castleton Investment Ltd., In re. (2012) 348 ITR 537 (AAR), Deere & Co., In re. (2011) 337 ITR 277 (AAR); Ardex Investment Mauritius Ltd., In re. (2012) 340 ITR 272 (AAR), Armstrong World Industries Mauritius Multiconsult Ltd., In re. (2012) 349 ITR 303 (AAR)

43. Castleton Investment Ltd. v. DCIT (2015) 379 ITR 363(SC)

44. Instruction 9/2015 dated September 2, 2015

The AAR also dismissed the IRA's argument of non-payment of dividend. Based on all of the above, the AAR concluded that there was no scheme for tax avoidance.

Further, the AAR held that there was no basis to the IRA's argument on DAS US being the owner of shares of DAS India.

As regards the fourth issue, the AAR relied on SC decision in the case of *Castleton Investments*⁴³, and held that in the absence of a PE in India, the MAT provisions in section 115JB would not be applicable to the applicant, a foreign company incorporated in Mauritius. The SC in *Castleton Investments* had relied on the Government's Instruction to the IRA dated September 2, 2015⁴⁴ initially extending the non-applicability of MAT to FPIs/FILs from April 1, 2001, and the later Press Release dated September 15, 2015 extending the same to all foreign companies not having a PE in India, provided they were not required to seek registration under section 592 of the Companies Act, 1956 or section 380 of the Companies Act, 1956.

Addressing the fifth issue, the AAR observed that section 92 is not an independent charging section and is applicable only if there is any chargeable income arising from the international transaction. Thus, transfer pricing provisions under section 92 would not be applicable to the Applicant in the absence of chargeable capital gains.

With regard to the sixth issue, the AAR disagreed with the AAR ruling in *Castleton Investments*⁴⁵ and relied on the earlier rulings in *FactSet Research Systems*⁴⁶ and *Vanenburg Group*⁴⁷ to hold that the provisions governing filing of tax returns are not applicable if there is no income chargeable to tax in India.

The AAR relied on these abovementioned rulings instead of *Castleton Investments* because in case of *Castleton Investments*, the AAR did not consider the binding decision of the Federal Court in the case of *Chatturam v. CIT*⁴⁸.

SIGNIFICANT TAKEAWAYS

Mauritius has been one of the most popular FDI jurisdiction for Indian companies, as Mauritius based foreign investors are not liable to pay tax by virtue of the provisions of the Indo-Mauritius DTAA. Entitlement to Indo-Mauritius DTAA has always been subject matter of litigation. Further, as per information available in the public domain, it seems that Indian government has been in negotiations with Mauritian government for the past few years to amend the Indo-Mauritius DTAA, which could include limitation of benefit clause in order to avail the DTAA benefits. This judgment would be particularly important from the perspective of investors incorporated in Mauritius who might want to transfer their investments in India to an entity in Singapore or some other jurisdiction in anticipation of the amendments to the Indo-Mauritius DTAA. The tax-free transfer of any investment from one jurisdiction to another would have to fulfil the test of 'operational-excellence' or business consideration, though it may have to be determined on a case-to-case basis.

The longstanding issue regarding applicability of MAT to foreign companies not having a PE in India has since been decided by the SC in the case of *Castleton Investments* (supra) as well as through certain legislative amendments introduced recently. While the AAR had held in the case of *Castleton Investments* (supra) that the provisions of 115JB are applicable to foreign companies not having a PE in India, the same has since been reversed by the SC due to the Government deciding to exempt foreign companies who do not have a PE in India from the applicability of the provisions of section 115JB of the IT Act.

Separately, it should be noted that the AAR's ruling on the obligation to file tax returns stands on shaky ground in light of the 2013 amendment to the Income tax rules⁴⁹ that make e-filing of tax returns mandatory for non-residents who are availing benefits of tax treaties under sections 90, 90A and provisions of section 91 of the IT Act. There have been certain contradictory decisions on this issue⁵⁰ and the same is yet to be decided by the SC.

45. *Castleton Investment Ltd.*, In re. (2012) 348 ITR 537 (AAR)

46. *FactSet Research Systems Inc.*, In re. (2009) 317 ITR 169 (AAR)

47. *Vanenburg Group BV*, In re. (2007) 289 ITR 464 (AAR)

48. *Chatturam v. CIT* (1947) 15 ITR 302 (FC)

49. CBDT Notification No. 42/2013, dated June 11, 2013

50. *VNU International B.V.*, In re. (2011) 334 ITR 56 (AAR); *Deere & Co.*, In re. (2011) 337 ITR 277 (AAR); *Ardex Investment Mauritius Ltd.*, In re. (2012) 340 ITR 272 (AAR)

PRO-RATA CREDIT OF TDS, MAT PAID ALLOWED TO RESULTING COMPANY ON DEMERGER

In *Adani Gas Limited*⁵¹, the Ahmedabad ITAT has held that the pro-rata credit of TDS, MAT and advance tax paid by the demerged company is allowable in the hands of resulting company.

FACTS

The gas distribution division of Adani Energy Limited was demerged into Adani Gas Limited (“Assessee”) by virtue of a scheme of demerger approved by the Gujarat HC vide order dated November 19, 2009 with the appointed date for the demerger as January 01, 2007.

Upon completion of the demerger, the demerged company and the Assessee filed a revised return of income. The Assessee in its return of income claimed pro-rata credit of TDS, MAT and advance tax paid by the demerged company. This was rejected by the AO and the CIT(A) on the ground that the demerger scheme did not contain any provision with respect to bifurcation of the various tax credits between the demerged and the resulting company and therefore, entire credit would be available to the demerged company.

ISSUES

Whether credit for taxes paid by the demerged company is allowable in the hands of resulting company i.e Assessee?

ARGUMENTS/ANALYSIS

It was the contention of the Assessee that the entire demerger scheme was tax neutral and hence, both the companies should be given credit for taxes paid on total income by the respective companies in such a way that the total refund claimed by both the demerging and resulting companies should not be less than the relief as per the original return of income filed before the demerger.

It was further contended that the impugned taxes pertained to the demerged undertaking; therefore, credit on such taxes should be allowable in the hands of the resulting company (i.e., Assessee) proportionately. Further, in terms of Section 199 and 200 of the IT Act, when the tax deducted has been deposited to the credit of the government and the deductor has issued the requisite certificate, the AO should grant due credit of TDS to the Assessee on the basis of original TDS certificates produced before him.

DECISION

The ITAT interpreted Section 2(19AA) of the IT Act and observed that since the demerger involves transfer of all properties of the demerged undertaking to the resulting company, along with all possible benefits including deferred tax benefits, tax credits should be permissible in the hands of the resulting company.

The ITAT relied on the SC judgement in the case of *Marshall Sons and Company*⁵² wherein it was held that the date of amalgamation/transfer is the date specified in the demerger scheme as the ‘transfer date’ as approved by the court and held that once the demerged company ceased to exist with effect from the appointed date as mentioned in the demerger scheme, the resulting company is entitled for the credits on MAT, TDS and advance tax of

51. Adani Gas Limited v. ACIT (2016) (ITA Nos. 2241 and 2516/Ahd/2011)

52. Marshall Sons & Company India Ltd. v. ITO (1997) 223 ITR 809 (SC)

the demerged undertaking on pro-rata basis since the demerged company is deemed to have carried out its business from the appointed date on behalf of the resulting company.

The ITAT also drew support from the decision of *Torrent Private Limited*⁵³ wherein the dividend distribution tax paid by the demerged company to the resulting company, before the demerger, was held to be refundable in the hands of resulting company as there cannot be payment of dividend during that period by the parent company to its own self.

It also relied on the decision of *Cadila Healthcare Ltd.*⁵⁴ wherein it was held that the transaction between the transferor company and the transferee company cannot be regarded as transaction between two different entities but would be treated as branch transfers and the tax paid on sales during the interim period are liable to be refunded to the taxpayer.

On the aforesaid premise, the ITAT concluded that the Assessee company is eligible for pro-rata credit of MAT, TDS and advance tax paid by the demerged company with effect from appointed date.

SIGNIFICANT TAKEAWAYS

This decision reiterates the position that pro-rata tax credit is available to resulting company pursuant to a demerger irrespective of whether or not the same is mentioned in the scheme of demerger.

As regards MAT credit, section 115JAA of the IT Act states that credit can be availed by the assessee in respect of MAT paid under Section 115JB of the IT Act. However, the said section is silent on the aspect of whether the amalgamated company or the resulting company can carry forward and set-off the MAT credit of the amalgamating or demerging company.

The IRA in many cases has disallowed the MAT credit claimed by the resulting company or amalgamating company on the basis that Section 115 JAA of the IT Act does not specifically allow for extension of benefit to amalgamated or resulting company unlike the provisions pertaining to tax holiday entitlement viz. Section 10A/ 10B, carry forward of losses viz. section 72A/ 72AA and other provisions like Section 35D on amortisation of preliminary expenses wherein the IT Act has specifically extended such benefit to the amalgamated/ resulting company. This decision would now further strengthen the taxpayers' contention in availing pro-rata tax credits by the amalgamated or resulting company pursuant to a scheme of amalgamation or demerger.

53. *Torrent (P.) Ltd v. CIT* (2013) 217 Taxman 149 (Gujarat)

54. *Cadila Healthcare Ltd.* (2012) 37 STT 259 (Gujarat)

NO TAX WITHHOLDING ON FTS PAYMENTS BY FOREIGN BRANCHES FOR BUSINESS OUTSIDE INDIA

In **NEC HCL Systems**⁵⁵, the Delhi ITAT *inter alia* held that payments made by the Japanese branch office of Indian taxpayer to another Japanese company for certain software development work does not require tax to be withheld as it is an expense borne by Japanese branch office for earning income outside India.

FACTS

NEC HCL System Technologies (“**Assessee**”), a joint venture between HCL Technologies Ltd., India, NEC System Technologies Ltd., Japan and NEC Corporation, Japan, was incorporated in India in October 2005 with a view to provide offshore centric software engineering services and solutions to NEC Group and its subsidiaries. The Assessee established a branch office in Japan (“**Japan BO**”) for undertaking extensive sales and marketing activities for the Assessee within and outside Japan. The Japan BO was empowered to undertake any and all activities on its own. The Assessee entered into an agreement in June 2006 with HCL Japan Ltd. (“**HCL Japan**”), for the purpose of subcontracting software development work obtained by Japan BO from NEC to HCL Japan.

HCL Japan raised invoices on Japan BO for the subcontracted work. Japan BO accounted for the payments made as outsourcing costs and accordingly debited in the profit and loss account of the Japan BO which was then consolidated with the audited financial statements of the Assessee. No tax was withheld on the outsourcing payments made to HCL Japan as the Assessee believed that the payment was covered by the exception carved out under section 9(1)(vii)(b) of the IT Act, being fees paid in respect of its business carried on by the Assessee through Japan BO outside India.

The AO took the view that the Japan BO did not have an independent identity and the Indian company was carrying out the outsourcing activities. The AO disallowed the outsourcing expense amounting to INR 16,66,37,966/- in accordance with the provisions of section 40(a)(i) on account of the fact that tax had not been withheld on the said payment. On appeal, the CIT(A) deleted the disallowance, taking the view that the Japan BO, being an independent entity, was a PE of the Assessee and any expenses borne by the Japanese BO for business activities in Japan would only be taxed in Japan. Therefore, the case of the Assessee was covered under the exclusion in section 9(1)(vii)(b) and the Assessee was not liable to withhold tax under section 195 of the IT Act.

ISSUES

1. Whether the outsourcing cost of payment made by the Assessee to HCL Japan is deemed income within the meaning of section 9(1)(vii) of the IT Act as the Japan BO neither has an independent identity nor any business activity of its own.
2. Whether tax was required to be withheld on such payments as per the requirement of section 195 of the IT Act, as the Assessee has incurred outsourcing expenses in the nature of fees for technical services and since the income is chargeable to tax in India within the meaning of Sec. 40(a) (i) of the IT Act.

55. *NEC HCL Systems v. ACIT TS 28 ITAT 2016 (ITAT Delhi)*

ARGUMENTS/ANALYSIS

The IRA contended that exception carved out under section 9(1)(vii)(b) of the IT Act was not applicable to the Assessee as the Japan BO did not carry out any work independently to earn income in Japan; hence this income will be deemed to accrue or arise in India. It further submitted that all services were rendered in India as the Japan BO's staff was not capable of doing the technical work.

The Assessee reiterated the facts put forth before the AO and the CIT(A) in support of its contention that the payments were made by Japan BO for services rendered in Japan and, therefore, under section 9(1)(vii)(b) of the IT Act the income of the recipient is not deemed to accrue or arise in India. The Assessee further contended that the Delhi HC decision in the case of *Lufthansa cargo*⁵⁶, which discussed the 'source rule' reflected in section 9(1)(vii)(b), i.e. income of the recipient to be charged or chargeable in the country where the source of payment or the payer, is located, was applicable. As the operations of the Assessee for which the expenses were made were carried on abroad, the same were covered under the exception carved out in the latter part of section 9(1)(vii)(b).

DECISION

The ITAT took note of the facts proved by the Assessee before the CIT(A) to hold that the Japan BO was a PE of the Assessee in Japan carrying out business in Japan independently. Certain key facts noted by the ITAT including the following:

- i. the Japan BO had its own employees carrying out the business development work of the BO in Japan
- ii. the AO had not appreciated the fact that the Japan BO had outsourced the technical work to HCL Japan Limited and only the sales and marketing work was done by the Japan BO's employees, which they were capable of performing
- iii. the Japan BO rendered services in Japan, as project costs were debited to its profits and loss account and bills were raised for the work carried out outside India
- iv. income was offered to tax in Japan by the Japan BO and return of income was filed in Japan

The ITAT observed that when the Assessee was carrying on the business outside India through its Japan BO, merely because the financial statements of the Japan BO were required to be consolidated into the financial statements of the Assessee, it did not mean that the outsourcing expenses were borne by the Assessee in India. The ITAT agreed with the Assessee's reliance placed on the Delhi HC decision in *Lufthansa cargo (supra)*. Thus, the outsourcing expenses, being borne by the Japan BO of the Assessee for earning income outside India, no income was chargeable to tax in India as per the provisions

section 9(1)(vii)(b) of the IT Act. In the absence of taxability under the IT Act, no tax was required to be withheld under section 195 of the IT Act.

SIGNIFICANT TAKEAWAYS

This judgement employs the 'source rule' as laid out by the courts in various cases and recently discussed by the SC in the case of *GVK Industries*⁵⁷. The SC interpreted section 9(1)(vii)(b) to be laying down the principle of the source rule, i.e., income of the recipient to be charged or chargeable in the country where the source of payment is located.

In a similar factual situation, the Mumbai ITAT in the case of *Motech Software (P.) Ltd*⁵⁸ had held that the payments for software development expenses etc made by the assessee's branches abroad were not taxable in India as the payments fell under exception to clause (b) of section 9(1)(vii) and the recipients of the amounts did not have a PE in India. Consequently section 195 had no application to such payments.

In this case, the ITAT relied on the fact that the Japan BO was bearing the expenses for the outsourced work to come to the conclusion that the expenses were made outside India for carrying on the business outside India. Thus, to establish that the 'source' of payment under section 9(1)(vii)(b) is located outside India, the fact situation needs to clearly show that the Assessee carried out an independent business outside India and had recognised the revenue realised from such activities in the books of its overseas branch on which it may have also been liable to taxation as per the local laws of the relevant jurisdiction.

56. DIT v. Lufthansa Cargo India (2015) 375 ITR 85 (Delhi)

57. GVK Industries Ltd. v. ITO (2015) 371 ITR 453(SC)

58. DCIT v. Motech Software (P.) Ltd (2014) 43 taxmann.com 122 (ITAT Mum)

INDIAN PARENT NOT A PE OF OVERSEAS WOS IN ABSENCE OF MANAGEMENT/CONTROL FROM INDIA

In *Forbes Container Line Pte. Ltd.*⁵⁹, the Mumbai ITAT held that the Indian parent of a wholly owned subsidiary (“WOS”) abroad shall not constitute a PE of the WOS in the absence of management/control from India.

FACTS

Forbes Container Line Pte. Ltd. (“Assessee”) was incorporated in Singapore and operated ships in international traffic across Asia and Middle East. It was a WOS of Forbes and Co. Ltd. (“FCL”), which was incorporated in India. FCL appointed M/s.Volkart Flemming Co. and Services Ltd. (“VFSSL”), another WOS of FCL, as its agent in India in 2007.

Pursuant to filing of a ‘nil’ income return in 2009, the AO completed the assessment, determining the income of the Assessee at INR 2.97 crores on the following grounds –

1. Being a Non-Vessel Operating Common Carrier (“NVOCC”) the Assessee could not claim exemption under Article 8 of DTAA.
2. The Assessee carried out business through a fixed place PE and an agency PE in India as it was managed from India by its parent company. It was a 100% subsidiary of FCL and had a common director with FCL permanently residing in India, who looked after the policy matters of the Assessee, constituting a common control mechanism between the two.
3. Income of the Assessee arising out of operation of ships in International traffic, arising / accruing in India was taxable in India as per the provisions of section 5(2) of the IT Act, and Section 44B of the IT Act⁶⁰ was applicable to the same.

CIT(A) upheld the order of the AO.

ISSUES

Whether the Assessee had a PE in India by virtue of it being a WOS of FCL, an Indian company?

ARGUMENTS/ANALYSIS

The Assessee contended that it did not have a fixed place of business in India nor was it holding any bank account in India. Further, only 2.29 % of its revenue was received from FCL. Additionally, the Assessee was an independent entity, and FCL had no role in its decision making. Moreover, the Assessee had not sought the benefit of Article 8 of the DTAA between India and Singapore and had stated that it did not carry out shipping operations.

DECISION

The ITAT after taking into account the following facts, held that the IRA could not establish that effective management and control of affairs of the company was in India:

1. Assessee’s books of accounts were maintained in Singapore and that it was maintaining a bank account in Singapore and all banking transactions were made from that account only.

59. Forbes Container Line Pte. Ltd., v ACIT TS 126 ITAT 2016 (ITAT Mumbai)

60. Special provision for computing profits and gains of shipping business in the case of non-residents

2. Assessee derived substantial portion of its income from the operations carried out in Middle East and other countries.
3. The business of the Assessee was proved to be carried out of the Singapore office with the help of emails.
4. IRA could not prove the existence of a bank account of the Assessee in India.

Upon factoring all of the above, the ITAT held that the IRA could not establish that effective management and control of affairs of the company was in India. Factors like staying of one of the directors in India or holding of only one meeting during the relevant year in Singapore or the location of the parent company in India would not decide the residential status of the Assessee.

The ITAT also held that section 44B would not be applicable as the Assessee had only provided container services to its clients. The Assessee had not claimed the exemption under Article 8 of the DTAA as it was not in the shipping business. The income of the Assessee had to be assessed as per the provisions of tax treaty dealing with business income. Considering the above discussion, the ITAT held that the income of the Assessee was liable to be taxed as business income and that in absence of a PE, no income was taxable in India.

SIGNIFICANT TAKEAWAYS

The ITAT in this case seems to have erroneously used the concepts of PE and tax residency interchangeably in places. While the question was whether there existed a PE of the Assessee in India in accordance with Article 5 of the India Singapore DTAA, the ITAT has observed that factors like parent company in India, one director being placed in India would not decide the 'residential status' of the Assessee.

A comprehensive analysis of all the factors needs to be undertaken to determine whether a non-resident has effective control and management located in India, thereby constituting a PE of the non-resident in India. The mere fact of a holding-subsidiary relationship, common directors, etc. would not lead to a PE in India. Under the India-Singapore DTAA, the existence of a place of management could also lead to the constitution of a PE.

It is also pertinent to note that the recently introduced tax residency criteria of place of effective management ("POEM") in the IT Act to determine residential status of a foreign company in India and the draft guidelines issued by the CBDT for the determination of POEM ("**Guidelines**") also prescribe certain criteria for determination of a place of effective management. The Guidelines place emphasis on the place where decisions are made, rather than where they are implemented. The ITAT's position on the determination of place of effective management in this case falls in line with the Guidelines for the determination of POEM in India. However, it is pertinent to note that while presence of place of management leads to the constitution of a PE, presence of POEM would lead to the concerned foreign entity being construed as a tax resident of India. It is very important to note a tax resident of India is liable to pay tax in India on its global income whereas a foreign entity having its PE in India is required to pay tax only on the income attributable to the activities carried out by the PE in India. Thus, the threshold for establishment of POEM should be far higher than those for establishing a PE.

It would have been advisable for the ITAT to deal with the concepts of place of management and POEM separately so that taxpayers could have received invaluable guidance in terms of carrying out their business activities, especially in light of lack of clarity on this issue.

SHARE TRANSACTIONS BETWEEN GROUP ENTITIES WITHOUT COMMERCIAL RATIONALE AND CONSIDERABLE TAX ADVANTAGE TREATED AS COLOURABLE DEVICE

In *Abhinandan Investment Ltd*⁶¹, the Delhi HC held that incestuous conversion of stock-in-trade into investments to treat the income received on sale as capital gains followed by transaction between group entities at substantially lower than market price was a colourable device for tax avoidance and therefore, the same ought to be disregarded.

FACTS

During the year 1983-84, Abhinandan Investments Ltd. ("**Assessee**"), a company belonging to the Jindal group acquired shares and debentures of its group companies namely, JSL and JISCO and disclosed the same as stock-in-trade and valued the same on the principle of cost or market value, whichever is less. In the year 1991-92, the Assessee passed a board resolution for treating all its securities as capital assets as they were intended to be retained for long-term basis.

Thereafter, in the same year, the Assessee sold 60,000 equity shares of JSL and declared capital gains of INR 91.31 Lakhs. Further, the Assessee renounced its entitlement to subscribe to Partly Convertible Debentures ("**PCDs**") of JISCO in favour of JSL at a consideration of INR 30 per PCD and declared capital loss of INR 1.68 crore. The cost of acquisition of one PCD was determined at INR 200 by relying on the SC decision in the case of *Dhun Dadabhoy Kapadia*⁶². The Assessee set-off capital gains of INR 91.31 lakhs (arising on sale of equity shares of JSL) with the capital loss of INR 1.68 crores incurred on renunciation of PCDs in favour of JSL.

The AO observed that the price of a PCD ranges from INR 260 to 280 as per the stock exchange rates and thus, sale at INR 30 was much below market price. He further observed that the entire transaction was sham in nature so as to purchase capital losses and thus, treated the same as income from business.

The CIT(A) upheld the order of the AO and further held that the principle laid down by the SC in the case of *McDowell & Co*⁶³ was fully applicable to the facts of the case. However, the ITAT Delhi allowed the appeal of the Assessee and held that profits made on sale of shares of JSL should be treated as capital gains. Aggrieved by the same, the IRA appealed before the ITAT Delhi.

ISSUES

- a) Whether income from sale of shares of JSL and the rights entitlement of the PCDs is chargeable as capital gains or as income from business or profession.
- b) Whether the Assessee's claim that it has incurred a loss on the sale of its rights to subscribe to the PCDs of JISCO was a colourable device to contrive an artificial loss?

ARGUMENTS/ANALYSIS

The Assessee contented that its intention was always to hold the investment on a long-term basis and further that the transfer of stock-in-trade was not relevant for the purposes of claiming loss on the renunciation of right to subscribe to the PCDs of JISCO. It relied on the Bombay HC decision in the case of *K.A.Patch*⁶⁴ in support of its contention that the method of calculation

61. CIT v. Abhinandan Investment Ltd. (2016) 282 CTR 466 (Delhi)

62. Miss Dhun Dadabhoy Kapadia v. CIT (1967) 63 ITR 651 (SC)

63. McDowell & Co v. CIT (1985) 154 ITR 148 (SC)

64. CIT v. K.A. Patch (1971) 81 ITR 413 (Bombay)

of loss on renunciation of rights would remain the same even in a case where the rights in favour of the Assessee are held as stock-in-trade.

In respect of adopting the cost of acquisition of PCDs as INR 200, which is the difference between cum-right price (INR 625) and an ex-right price of shares (INR 425), it relied on the SC judgement in the case of *Dhun Dadabhoy Kapadia (supra)*. Therefore, it was argued on behalf of the Assessee that it was at liberty to arrange its tax affairs in a manner so as to mitigate its tax liability.

DECISION

The HC, while addressing the issue of whether impugned transactions fall in the category of business income or capital gains, has held that none of the Assessee's actions indicate that its intention was to hold the shares as investments and that the ITAT failed to appreciate that the Assessee had consciously held itself out as a company engaged in sale and purchase of shares. The Court further noted that the Assessee had been consistently assessed on the income earned from business and deductions were also given on account of business expenses incurred. Therefore, the shares in question were, concededly, held as stock-in-trade. All that happened in the year in question was that the Assessee sold substantial number of shares and renounced rights to subscribe to PCDs contrary to its stated intention of holding the same on a long-term basis. In view of the above, the income received on sale of shares and the renunciation of rights to subscribe to the PCDs of JISCO was rightly held by the AO as business income and not capital gains.

In respect of the second question of law, the HC observed that the PCDs were concededly sold at a price (INR 30) which is significantly lower than the market price (INR 260 to 280, the price quoted at stock exchange) and held that if it was the business purpose of the Assessee's to sell one of its assets, it should have done so at the best possible price and terms. Thus, it is apparent that the transfer of rights was not for a business purpose.

It had also noted that the Assessee had not incurred any real loss as the original cost of acquisition of shares was less than INR 10 per share and it continued to retain the holding, besides being entitled for INR 30 per right to subscribe to the PCDs. Thus, the instant loss could at best be considered as notional loss. The transaction of renunciation of rights in favour of JSL ensured that right to subscribe remained within the 'J' group.

It quoted the judgement in the case of *McDowell (supra)* and distinguished the judgements in the case of *Azadi Bachao Andolan*⁶⁵ and *Vodafone*⁶⁶ by holding that the instant transaction would fall within the ambit of 'colourable device' or a 'sham' transaction as the transactions have been so executed to ensure that the rights remained within the 'J'

group and the AO had rightly found that the rights to subscribe the PCDs have been sold to purchase losses for the purposes of evading tax.

In respect of the alternate argument raised by the Assessee, the HC had dissented with the proposition laid down by the Bombay HC in the case of *K.A.Patch (supra)* wherein it was held that the principle laid down by the SC in the case of *Dhun Dadabhoy Kapadia (supra)* is applicable even when the shares are held by the Assessee as stock-in-trade and further held that the same method of computation should be followed.

The HC dissented with the decision in the case of *K.A. Patch (supra)* on the reasoning that when shares are held as stock-in-trade, they will form part of the trading account and the closing stock of the trading account will subsume any such loss incurred on the reduction as the closing stock is valued at the cost price or market price, whichever is lower. Therefore, there is no need for providing any notional loss which is neither incurred by the Assessee nor rerecorded in the books of accounts. If the Assessee felt it was necessary to reduce the value of shares of JISCO owing to alienation of rights of entitlement, an appropriate proportionate amount could be reduced from the closing stock.



65. UOI v. Azadi Bachao Andolan (2003) 263 ITR 706 (SC)

66. Vodafone International Holdings B.V. v. Union of India (2012) 341 ITR 1 (SC)

67. AAA Portfolios Pvt. Ltd v. DCIT (2014) 33 ITR(Trib) 23 (Delhi ITAT)

SIGNIFICANT TAKEAWAYS

It may be noted that the position in regards to determination of cost of acquisition of renouncement of right to subscribe to any financial asset has now been specifically provided under the IT Act by the insertion of Section 55(2)(aa) into the IT Act *vide* Finance Act, 1995 wherein it is stated that cost of acquisition of renunciation of rights to subscribe to any financial asset is to be taken at NIL. The judgement in the instant case is in respect of an AY prior to the insertion of the aforesaid provisions into the IT Act. Therefore, to the extent of the manner of calculating the price of rights entitlement, this decision would no longer be valid on a going forward basis.

On a separate note, it is pertinent to highlight that the IRA is increasingly scrutinising the transactions between group entities and depending on the facts and circumstances of the case, the Courts could treat such transactions as a sham and colourable devices to evade taxes. Recently, the Delhi ITAT in the case of *AAA Polios Pvt. Ltd.*⁶⁷ has held that sale of shares between group companies at a rate lower than the market rate cannot be accepted as genuine. Therefore, the transaction was held to be a sham transaction to book losses.

Similarly, in the case of *Leading Line Merchant Traders Pvt. Ltd.*⁶⁸, the ITAT ruled that purchasing the shares of a group company and then selling the same to its own group company at a throw away price of INR 10 paise is not genuine and the Assessee is not entitled to long-term capital loss on sale of shares, especially when both the transactions were carried out as off market transactions since they were unlisted.

It would also be apt to note here that the Gujarat HC in the case of *Biraj Investment Pvt. Ltd.*⁶⁹ had held that if it's not the contention of the IRA that the shares were sold between group concerns at a price lesser than the market price, then it cannot be stated that the transaction is a 'colourable device' as there is no provision in the IT Act to restrict transfer of shares between group concerns and as long as the stipulated conditions of Section 2(47) of the IT Act are satisfied, gains or loss arising on such transaction is allowable. Group company transactions have been given a clean-chit in several other cases.

Thus, intra-group transactions undertaken at a value different than their fair market value could be examined carefully by the IRA. Moreover, with General Anti-Avoidance Rule ("GAAR") coming into effect from the financial year 2017-18, the risk of transactions involving transfer of shares of group concerns and between the group concerns could be construed by the IRA as 'impermissible avoidance arrangement', especially if they are taken at a value significantly different than the fair market value unless a strong commercial rationale can be demonstrated.

68. DCIT v. Leading Line Merchant Traders P. Ltd. (2015) 155 ITD 614 (Delhi ITAT)

69. CIT v. Biraj Investment Pvt. Ltd. (2012) 210 Taxman 418 (Gujarat)

MERE FILING OF RETURN IS NOT A BAR FOR ADMISSION OF AAR APPLICATION

In *Hyosung Corporation*⁷⁰, the Delhi HC held that neither filing of return nor receipt of notice under section 143(2) prior to filing of an AAR application will tantamount to the question raised in the application being already pending before the income-tax authorities. However, receipt of notice under section 142(1) raising specific questions prior to filing of an AAR application will be treated to be a question already pending before the income-tax authorities.

FACTS

Hyosung Corporation (“**Petitioner**”) was incorporated and was a tax resident in South Korea. It was a comprehensive energy solution provider and manufactured transformers, motors, etc. Further, it has been engaged in several projects in India and is regularly assessed to tax in India. In 2011-12, it filed several AAR applications seeking a ruling on the issue of taxability of profits from offshore supplies in respect of different AYS.

The IRA raised an objection before the AAR for not entertaining the application as the question involved in the AAR was already pending before the AO as per ‘proviso to section 245R(2) of the IT Act’⁷¹ (“**245R**”). The IRA contended that prior to filing of the AAR application, either (a) the return of income was already filed by the Petitioner or (b) notice under section 143(2) was already issued or (c) notice under section 142(1) was already issued. The Petitioner contended that as the bar makes a distinction between resident and non-residents, the said bar under the said 245R is violative of the Article 14 of the Constitution as well as Article 25 on non-discrimination of Indo-Korea DTAA.

The AAR rejected the applications as non-maintainable by holding that even though mere filing of return may not make the application non-maintainable on account of restrictions imposed under 245R, once notice under section 143(2) is issued, the returns filed by the Petitioner would be pending for adjudication before the AO and, therefore, the bar imposed under 245R comes into effect. Further, the AAR was of the view that it had no jurisdiction to deal with the question of discrimination. The Petitioner subsequently filed a writ petition challenging the rejection order of the AAR.

ISSUES

1. Whether the bar under 245R is violative of the Article 14 of the Constitution and Article 25 on non-discrimination of Indo-Korea DTAA?
2. Whether the question raised in the application can be said to be already pending before the income-tax authorities under 245R in the following cases -
 - a. filing of return prior to filing of the AAR application
 - b. receipt of notice under section 143(2) prior to filing of the AAR application

70. *Hyosung Corporation v. AAR* [2016] 66 taxmann.com 217 (Delhi)

71. Section 245R(2) reads as below -

“The Authority may, after examining the application and the records called for, by order, either allow or reject the application :

Provided that the Authority shall not allow the application where the question raised in the application,-

(i) is already pending before any income-tax authority or Appellate Tribunal [except in the case of a resident applicant falling in sub-clause (iii) of clause (b) of section 245N] or any court... ..”

Section 245N reads as below -

“(b) “applicant” means any person who -

(iii) is a resident falling within any such class or category of persons as the Central Government may, by notification in the Official Gazette, specify in this behalf... ..”

- c. receipt of notice under section 142(1) prior to filing of the AAR application

ARGUMENTS/ANALYSIS

The Petitioner urged that the provisions of 245R were, on the face of it, discriminatory in nature, since they exempted Public Sector Undertakings (“PSU”) from the bar imposed by the said provisions which restricted filing of an AAR application in respect of a question which was already pending before the IRA. Therefore, the Petitioner urged that the aforesaid benefit to residents should be extended to non-residents applicants like the Petitioner. Further, it was also submitted that as per section 90 of the IT Act, notwithstanding the discriminatory provision, the beneficial provisions under the DTAA would apply. On the issue of pendency before IRA, the Petitioner submitted that the notice under section 143(2) were issued in a pre-printed format and did not specify the questions on which information was being sought by the AO. However, in respect of the notice under section 142(1), the Petitioner did not dispute that the notice was accompanied by a detailed questionnaire and therefore, in such cases, only AAR applications pertaining to those AYs which were filed prior to the issuance of the notice, may be accepted.

Countering the above submissions, the IRA contended that the classification made between PSUs and non-resident applicants was a reasonable one and had nexus to the implied object of not having two adjudication proceedings on parallel basis on the same issue. A conscious decision has been made by the Government to exempt PSUs from maintaining the application notwithstanding the pendency of such question before the IRA. Further, the IRA submitted that a question which is pending for one AY should be taken as pending for any subsequent AY and accordingly, AAR applications pertaining to all AYs should be rejected.

DECISION

Constitutional Validity and Non-discrimination under DTAA

The Delhi HC analysed the relevant provisions and agreed that there was no doubt that 245R makes a distinction between resident and non-resident applicants as the PSUs notified by the Central Government can submit an application for advance ruling notwithstanding that the question raised in the application is already pending before the income tax authorities whereas a non-resident applicant cannot, in the same circumstances, maintain such an application. The HC stated that the object behind the said provision was to ensure that parallel proceedings do not take place simultaneously before two different fora in respect of the same question and, therefore, the proviso is per se not irrational. Further, the Delhi HC noted that the remedy which the Petitioner is seeking is not merely a declaration of the invalidity of the discriminatory part of the provisions but that a reading into the said provision to the effect that even non-

resident applicants would be exempt from the bar. To this, the HC held that while the Court cannot possibly re-write the statute, extending the exemption from the applicability of the said provision to non-residents would render the entire proviso otiose and defeat the very object of its insertion.

The Delhi HC then examined the issue from the point of view of section 90 of the IT Act and Indo-Korea DTAA which mandates that the Petitioner as a South Korean entity should not be subject to any taxation requirement which is more burdensome than the requirement to which an Indian entity is subject. The HC stated that it was not understandable as to how the provision can be said to be more beneficial to the Petitioner even if the discriminatory portion is invalidated. Even if the offending portion was invalidated, the result would be that the bar would apply equally to both a resident and a non-resident and thereby, become equally burdensome to both. Consequently, Article 25 of the DTAA could not come to the aid of the Petitioner. Due to the aforesaid reasons, the Delhi HC declined to pronounce on the validity of the said provision.

Whether question pending before the income-tax authorities

On the interpretation of ‘pending before the income-tax authorities’, the Delhi HC agreed with the AAR view that mere filing of return to claim refund of tax deducted at source, will not tantamount to the question raised in the applications before the AAR being pending before the income-tax authorities and the same has been upheld by the SC in the case of *Sin Oceanic Shipping ASA v AAR*⁷².

As regards the issue of notice under section 143(2), the HC observed that the notice can be issued by the AO where he has reason to believe that any claim of such exemption, deduction, allowance or relief made in return is inadmissible and the notice should specify the said particulars which has not been done in the instant case and it was a standard pre-printed format which merely states that “there are certain points in connection with the return of income on which the AO would like some further information”. In any event the question raised in the applications by the Petitioner before the AAR do not appear to be forming the subject matter of the notices under Section 143(2) of the Act. Consequently, the Delhi HC held that the mere fact that a notice under section 143(2) was issued prior to the filing of the AAR application will not constitute a bar on the AAR entertaining the applications.

As regards the issue of notice under section 142(1), the HC observed specific notices which sought information and questions in respect of overseas supply contracts. Based on the said notices, the HC held that in as much as, the notices under Section 142(1) raising the very questions that form subject matter of the AAR applications pertaining to specific AYs were issued prior to the filing of the applications, the bar under section 245R(2) of the Act stood attracted and, therefore, the rejection by the AAR of the said applications

72. *Sin Oceanic Shipping ASA v AAR* (2014) 223 taxmann 102 (SC)

was not erroneous. However, as far as the notices issued after the AAR application pertaining to another AY, the HC held that only if on the date of filing of the AAR application, the question raised therein was already the subject matter of proceedings pending before the income tax authorities, the bar contained in 245R would apply but would not be applicable if the notice is issued thereafter. The HC also placed reliance on another AAR decision in case of *Monte Harris v CIT*⁷³ which clarified that the words 'already pending' in 245R should be interpreted to mean 'already pending as on the date of the application and not with reference to any future date'.

SIGNIFICANT TAKEAWAYS

The issue of maintainability of an AAR application in view of the restriction under 245R that the question should not be 'pending before the income-tax authorities' has been subject matter of litigation for quite sometime. This issue is very important for taxpayers who are contemplating to seek a remedy from the AAR because they need to ensure that the application is maintainable in the first place before examining the merits of such application. The Delhi HC in this decision has succinctly analysed various stages at which the pendency before the tax authorities could be claimed namely, filing of tax return - not a case of pendency, receipt of notice under section 143(2) - not a case of pendency and receipt of notice under section 142(1) with the list of queries seeking information pertaining issues being raised in the application - case of pendency. However, in the past, in few cases, AAR applications had been rejected⁷⁴ when the returns of income were filed and/ or notices under section 143(2) were issued whereas in few other cases, the AAR applications were admitted⁷⁵. In fact, the Delhi HC in another case⁷⁶ held that where a return had been filed, the bar under section 245R would apply and the AAR application would not be admissible. However, the SC in *Sin Oceanic* (supra) set aside the said Delhi HC decision taking note of a subsequent AAR ruling which allowed the application post filing of return. Further, the Delhi HC in this case has broadly held the 245R provision to be rational and non-discriminatory under the DTAA though it has not explicitly ruled on the constitutional validity of the bar.

73. *Monte Harris v CIT* (1996) 218 ITR 413 (AAR)

74. *J & P Coats Ltd., In re* [2014] 41 taxmann.com 210 (AAR), *Mitsubishi Corporation, Japan, In re* [2013] 40 taxmann.com 335 (AAR)

75. *Aircom International Ltd., United Kingdom, In re* [2014] 41 taxmann.com 207 (AAR)

76. *Net App BV and Sin Oceanic Shipping ASA v AAR* (2013) 357 ITR 102 (Del)

Indirect Tax

CENVAT CREDIT OF EXCISE DUTY PAID ON TELECOM TOWERS AND PRE-FABRICATED SHELTERS NOT AVAILABLE

In *Tower Vision India Private Limited*⁷⁷, the Larger Bench of the CESTAT held that CENVAT credit of excise duty paid on MS Steel Angles/telecom towers, shelters and parts shall not be available, even while providing passive infrastructural services in the nature of Business Auxiliary Service (“BAS”) or Support Services of Business or Commerce (“BSS”) to telecommunication companies.

FACTS

In this case, the Tower Vision India Private Limited (“Assessee”) was providers of output services of BAS or BSS to telecommunication companies. It provided telecom towers, pre-fabricated shelters and their parts to telecom service providers on lease basis for which it claimed CENVAT credit of excise duty paid by them.

The Division Bench of the CESTAT recorded a difference of opinion on the availability of CENVAT credit on towers and shelters where the output service of the Assessee is BSS or BAS. The Member (Judicial) was of the view that the Assessee was eligible for credit of duty, whereas, the Member (Technical) opposed this view by placing reliance on the judgment of the Bombay HC in *Bharti Airtel Limited*⁷⁸ where it was held that the telecom service providers cannot claim credit of towers and shelters while providing telecommunication services.

ISSUE

Whether Assessee is entitled to avail CENVAT credit of excise duty paid on MS Steel Angles/telecom towers, shelters and parts thereof for payment of service tax on the provision of taxable services of BAS or BSS, as the case may be, to telecom service providers?

ARGUMENTS/ANALYSIS

The Assessee contended that, firstly, Towers, Shelters and Tower materials are all parts of Base Transmission System (“BTS”) classifiable under Tariff Heading 8517 and, hence, all components, spares and accessories thereof would qualify as capital goods in terms of Rule 2 (a) (A) (iii) of the CCR. Secondly, credit on towers and shelters and other materials cannot be denied on the ground of immovability because as per Rule 3 of CCR, credit is admissible on all inputs and capital goods which are received in the premises of service provider and in the present case, towers and shelters are received in the premises of service providers. Thus, even if later the towers are embedded to earth, the eligibility of credit will not change. Thirdly, towers and shelters are to be considered as ‘accessories’ to capital goods because without the tower, the active infrastructure, namely the antenna, cannot be placed. Alternatively, the Assessee submitted that the Towers and Shelters would qualify as ‘inputs’ under Rule 2(k) of the CCR, since sub-rule (ii) of Rule 2(k) does not provide a bar to indicate that goods which do not fall under the category of capital goods would not qualify as inputs.

The IRA contended that the items on which credit is claimed by the Assessee have no direct nexus to the output service of either telecommunication service or BSS or BAS, as the case may be. They further contended that, it was clarified⁷⁹ by the CBEC that credit of service tax can be availed only if the output is a service liable to service tax or goods is liable to excise duty. Since

77. Tower Vision India Pvt. Ltd. & Ors. v. CCE, 2016-TIOL-539-CESTAT-DEL-LB

78. Bharti Airtel Limited v. CCE, Pune-III, 2014 (35) STR 86

79. Circular No. 98/1/2008-S.T., dated January 4, 2008

immovable property is neither goods nor service, thus no credit can be taken. Reliance was placed on the decision of the Bombay HC in *Bharti Airtel Limited (supra)*, wherein it was held that towers and shelters are immovable property and whether they are treated as components, parts or accessories, credit cannot be availed.

DECISION

The CESTAT held that since the towers and shelters are erected and fixed at the desired site they become part of the overall infrastructure created at site. The BTS electronic equipment is also brought and installed at the site however; it cannot be identified as capital goods. Thus, the tower and shelter cannot be termed as an accessory of BTS because they are installed as permanent structures and are used for installing/housing the telecom equipment and hence cannot be termed as an accessory of capital goods.⁸⁰ The CESTAT further relying on the judgment in *Bharti Airtel (supra)* held that Towers and their components are immovable.⁸¹

In addition, the CESTAT further went on to clarify that the admitted basic requirement for eligibility of any duty credit is that the goods on which duty is paid (credit of which is claimed) should have a connection or nexus to the output service. However, in the present case the telecommunication service is provided by using erected and fixed towers and shelters. The inputs like MS Angles and Channels are involved in the making of such towers which in turn are used for providing infrastructure support service/telecom service. Such far remote linkages are not within the scope of the term “used for” in the definition of input. Therefore, the inputs which suffered duty like MS angles and pre-fabricated shelters, *per se*, were not used for providing output service.

Thus, the Assessee was not entitled to avail CENVAT credit of excise duty paid on MS Steel Angles/telecom towers, shelters and their parts thereof. The CESTAT held that this position would stand the same regardless of the fact that the duty paid is being used by infrastructure companies for providing BSS to telecom companies or for providing telecom service by telecom operators.

SIGNIFICANT TAKEAWAYS

This is a significant decision since coordinate benches of the CESTAT, post the *Bharti Airtel (supra)* judgment had been holding that for provision of BSS or BAS, credit of towers and shelters would be allowed, even though credit was disallowed by the Bombay HC for the provision of telecommunication services. The Larger Bench of the CESTAT has clarified this position by effectively stating that CENVAT credit on towers and shelters shall not be available, regardless of whether the output service is telecommunication service or BSS or BAS. This shall come as a blow to the telecommunication industry, for both telecommunication service providers and the companies solely concerned with providing passive infrastructural services.

Further, the CESTAT has also clarified that the eligibility of any item for credit is to be decided as per provisions of the CCR and mere classification of a product and paying of duty under a particular heading, does not give rise to an automatic claim for credit for that item. Such restrictive interpretation of the CCR by the CESTAT is in line with the decision of *Vandana Global*⁸² and the long line of decisions arising out of the issue of availability of credit on structural items. In addition, the CESTAT followed the decisions in *Bharti Airtel (supra)* and *Vodafone India Limited (supra)* which held that towers and shelters and parts are immovable property and accordingly no credit can be availed.

80. See, *Saraswati Sugar Mills v. CCE, Delhi-III, 2011 (270) ELT. 465 (SC)*

81. See also *CCE, Mumbai-IV v. Hutchison Max Telecom Private Limited, 2008 (224) ELT 191 (Bombay)*

82. *Vandana Global Limited v. CCE, 2010 (253) ELT 440 (Tri. - LB)*

FOR ASSOCIATED ENTERPRISE TRANSACTIONS, THE POINT OF TAXATION SHALL BE THE FIRST DATE ON WHICH AN ENTRY HAS BEEN MADE IN THE BOOKS OF THE ASSESSEE

In *Deutsche Asset Management (I) Pvt. Ltd.*⁸³, the CESTAT held that there is no distinction in service tax law between provisional entry and final entry made in the books of accounts of the Assessee. Therefore, the point of taxation for such transactions shall be the first date on which an entry has been in the books of the Assessee, i.e. a provisional entry. Accordingly, the date of payment of service tax shall be determined from this point of taxation.

FACTS

The Deutsche Asset Management (India) Private Limited (“Assessee”) is engaged in providing services of Banking and other Financial Services (“BFS”) falling under Section 65(12) of the FA. During the course of audit proceedings, it was found that the Assessee acted as an Investment Manager to M/s. Deutsche Mutual Fund (“DMF”) and paid service tax on the fees received from them. The financial statement of the Assessee revealed that the investment fees received from DMF were in the nature of a related party transaction. The said investment fees were credited/paid to the account of Assessee not later than the last day of the respective months. The Assessee had shown the amount as received in the following month. In the show cause notice, it was alleged that though these were associate enterprise transactions, the Assessee had not accounted for the fees in the respective months itself as per Section 67 of the FA and Rule 6(2)(a) of the ST Rules, as amended. Thus, it was alleged that there was a delay of one month in payment of service tax from May 2008 onwards on which interest was payable.

ISSUE

Whether the point of taxation should be the date of provisional entries of the transaction in the books of account or the date of final entry and invoice made by the Assessee?

ARGUMENTS/ANALYSIS

The IRA submitted that the fact that the Assessee is an “Associate Enterprise” in terms of Section 92A of the IT Act has not been disputed during the adjudication proceedings. Therefore at this stage, the Assessee could not dispute the status of them being an Associate Enterprise of DMF. It was further contended that Section 67 and its explanation make it very clear that if the entry of transaction is made even on provisional basis, then also it shall be taken as the point of taxation and service tax shall be due according to the date of such entries. Therefore, there was a delay in payment of service tax and interest was rightly demanded and so was the imposition of penalties.

The Assessee submitted that it does not fall under the definition of “Associate Enterprise”. Moreover, the entries of transaction made during the month were provisional and was only for the purpose of management of the information system. The final entries were made in the next month, according to which the invoices were raised. Moreover, the amount mentioned in the final entry and amount of the invoices were varying with the amounts as mentioned in the provisional entries. Therefore, there is no significance of provisional entries and the same cannot be considered for the purpose of determining the point of taxation.

DECISION

The CESTAT held that on the basis of definition provided under Section 92A of the IT Act, the Assessee is an associate enterprise of the service recipient i.e.

83. CST, Mumbai-I v. Deutsche Asset Management (I) Pvt. Ltd., 2016-VIL-203-CESTAT-MUM-ST

DMF. This position was never in dispute by the Assessee, and therefore at this stage it cannot be disputed, specifically considering that there has been no change in factual situation.

The CESTAT further held that the explanation (c) of Section 67 does not make any distinction between provisional entries in the books of accounts and final entries made. As per the plain reading of the explanation, the moment any entry is made, irrespective of whether it is provisional or final, the same will be covered as a debit entry for the purpose of the explanation. Therefore, the said explanation did not provide any scope for differential treatment to a provisional entry.

Thus, it was held, service tax became due in accordance with the date of provisional entries made by the Assessee in its books of account, since the point of taxation for the relevant period arises on the date of making payment (which for associated enterprises is on the date of making entry in the books of accounts as per the said explanation to Section 67 of the FA).⁸⁴ Therefore, the delay in payment of service tax, as alleged by the IRA, shall correctly attract interest. However, penalties under Section 76 & 77 of the FA were not imposable because this was not a case of non-payment or short payment of service tax. Penalties under these sections are only imposable when there is a case for non-payment or short payment of service tax and the present case involved a demand for interest only. Accordingly, no penalty is imposable.

SIGNIFICANT TAKEAWAYS

The above decision has provided clarity on associated enterprise transactions. In this regard, for the purposes of determining the date of payment between associated enterprises, it was clarified by the CESTAT that by way of the explanation to Section 67 of the FA, the date of payment was to be determined as the date on which entries have been made in the books of accounts of the Assessee.⁸⁵ The present judgment further rules that the first entry in the books of accounts of the Assessee shall be taken as the date of payment, since there is no distinction between provisional and final entry as per the FA.

This judgment shall impact transactions between associated enterprises. Assessee should be careful before booking entries in their books of accounts, as the date of first booking of amount in the books shall be the date from which the date of payment of service tax shall be determined regardless of whether such entry is provisional or final.

84. Rule 3, Point of Taxation Rules, 2011

85. General Motors (I) Pvt. Ltd. vs. CCE, 2015 (40) STR 962 (Tri-Mumbai)

REGARDLESS OF ANY ADDITIONAL FEATURES, MULTIMEDIA SPEAKERS ARE ALL CLASSIFIED UNDER CHAPTER HEADING 8518

In *Logic India Trading Co.*⁸⁶, the CESTAT has held that the principal function of a 'multimedia speaker' is amplification of sound. Additional features such as USB port or FM radio introduced to such speakers would not change its main and principal function. Accordingly, the CESTAT has concluded that 'multimedia speaker' would be classifiable under Chapter Heading 8518 22 00 of the CTA.

FACTS

Logic India Trading Co. ("**Assessee**"), was a trader engaged in the import of 3 types of multimedia speaker viz-a-viz speakers without any USB port or a FM radio; speakers with USB port playback; and speakers with USB port playback and FM radio. The IRA had alleged that these three types of speakers would be classified under the Customs Tariff Headings 8518 22 00, 8519 81 00 and 8527 99 19, respectively. The Basic Customs Duty in respect of the contending entries is same, however there was a difference of Countervailing Duty resulting in an additional demand of Customs Duty by the IRA from the Assessee.

ISSUE

Whether the multimedia speakers having additional features would still be classifiable as speakers under Customs Tariff Heading 8518 22 00?

ARGUMENTS/ANALYSIS

The Assessee argued that the prime and utmost function of the product imported by them is a speaker which amplifies the sound signals received by it. As a technological advancement, some additional features are introduced in the speakers to have an inbuilt technology to receive sound through a pen drive or FM radio to amplify the sound. However, such inbuilt facilities would not convert the multimedia speakers into a sound reproducing apparatus or an FM radio for classification under the Customs Tariff Headings 8519 81 00 and 8527 99 19, respectively. The essential function of the multimedia speakers would remain the amplification of sound signals. Accordingly, it should be classified under the Customs Tariff Headings 8518 22 00. The Assessee further relied on Circular of the CBEC⁸⁷ wherein the smart phones/mobile phones having additional features of touch screen, internet, sending and receiving emails, video/ still camera were said to be classified as phones as the essential feature of smart phones is to communicate. Further, the Assessee relied on another Circular of the CBEC⁸⁸ relating to classification of tablet computer having additional facility of voice calling which adhered to similar principles. The CBEC clarified that since the essential feature of the tablet computer is to act as input output device for data processing, tablet computer with voice calling would not be classified as a phone. Accordingly, the multimedia speakers should be classified as speakers only.

The IRA argued that the goods imported by the appellant are not speakers. It was contended that since the goods contain additional feature such as a USB port with playback function and radio facility, they could not be classified as speakers falling under the Customs Tariff Headings 8518 22 00. When a speaker is fitted with the radio, the principal function of the speaker would be converted from merely amplifying the sound received by it to a radio. The IRA further relied on the Circular of the CBEC⁸⁹ wherein the issue was discussed in the Conference of Chief Commissioners and as per their opinion, the speakers

86. *Logic India Trading Co. v. Commissioner*, 2016-VIL-175-CESTAT-BLR-CU

87. Circular No. 17/2007-Cus dated April 19, 2007

88. Circular No. 20/2013-Cus dated May 14, 2013

89. Circular No. 27/2013-Cus dated August 01, 2013

having USB port or radio are required to be classified under the Customs Tariff Headings 8519 81 00 and 8527 99 19, respectively, as held by the lower authorities.

DECISION

The CESTAT held that going by the Interpretative Rules and the Section notes to the HSN, the criteria for classifying the product is the principal and the main function it performs, which in the present case remains that of a speaker. Accordingly the goods in question are properly classifiable under the Customs Tariff Heading 8518 22 00.

Further, the CESTAT observed that the Circulars of the Revenue Department⁹⁰ while determining the classification of smart phones and tablet computers, had classified the products according to their principal and essential function by relying on the Interpretative Rules and Section Note 3 to Section XVI of the HSN. However, the opinion expressed by the CBEC in respect of multifunctional speaker system⁹¹ is diagonally opposite to the opinion expressed by the CBEC in the other two circulars based on the same Interpretative Rules and Section Note 3 to Section XVI of the HSN. Accordingly, the CBEC Circular in respect of multifunctional speaker systems does not lay down the correct classification.

Accordingly, relying on the decision of the SC in the matter of *Xerox India Ltd.*⁹², the goods shall be classifiable as speakers.

SIGNIFICANT TAKEAWAYS

The above judgment reiterates that the classification of goods should be based on their primary or main function. There was confusion in the industry relating to this principle with the introduction of the CBEC Circular⁹³ relating to multifunction speaker systems. However, the present order re-examines the said Circular and upholds the principle as laid down in *Xerox India Ltd. (supra)* and the HSN. The same principle was upheld in the recent AAR ruling in *Samsung India Electronics Private Limited*⁹⁴ on the issue of classification of the Samsung Galaxy K Zoom (which was essentially a mobile phone with a top of the line camera). In this ruling, the AAR applied the same principle of classification to hold that the product is principally and essentially a mobile phone and not a camera.

Further, the classification of products under the CTA are *pari materia* to the entries in CETA. Therefore, 'multimedia speaker' would be classifiable under the Chapter Heading 8518 22 00 of the CETA.

The judgment would also resolve disputes under VAT legislations of various States which borrow the classification of products as per the CTA or the CETA.

90. Circular No. 17/2007-Cus dated April 19, 2007; Circular No. 20/2013-Cus dated May 14, 2013

91. Circular No. 27/2013-Cus dated August 01, 2013

92. *Xerox India Ltd. v. CCE, 2010 (260) ELT 161 (SC)*

93. Circular No. 27/2013-Cus dated August 01, 2013

94. *Samsung India Electronics Private Limited vs. Commissioner of Customs, New Delhi, 2016-VIL-07-ARA*

NO SERVICE TAX ON PROFITS SHARED BETWEEN PARTIES TO A BOOT CONTRACT DURING THE BOOT PERIOD

In *Sahastronics Controls Pvt. Ltd.*⁹⁵, the CESTAT held that amount shared between the Assessee and NMC as operating profit, during the Build, own, operate and transfer (“BOOT”) period in a BOOT agreement, was not liable to be taxed under the category of Maintenance, Management or Repair services.

FACTS

The Sahastronics Controls Pvt. Ltd. (“Assessee”), entered into a contract with Nashik Municipal Corporation (“NMC”) for the activity of design & drawing, manufacture, supply and installation, testing and successful commissioning of micro-processor based energy saving devices and the maintenance thereof. The nature of the agreement was a BOOT (Build, own, operate and transfer) contract. The term of the contract was five years. The IRA was of the view that the amount which had been shared between the Assessee and NMC as operating profit was liable to be taxed under the category of Maintenance, Management or Repair services.

ISSUE

Whether the amount shared between the Assessee and NMC as operating profit, during the BOOT period, was liable to be taxed under the category of Maintenance, Management or Repair services?

ARGUMENTS/ANALYSIS

The IRA argued that the agreement on BOOT basis was not solely for Built own operate & transfer but was also for periodical and systematic plan for recovery of cost of the project as well as services rendered and to be rendered by Assessee. The Assessee was a commercial concern and any activity undertaken by it was for earning profit. The earnings could be categorized as cost of equipment manufactured and the earnings from the functioning of the equipment i.e. in the form of energy saved during the BOOT period. The Assessee relied on the order of the lower authorities in stating that in a BOOT contract the profits are shared between the parties, and the share of profits is essentially a service to self. Accordingly, no service tax is liable.

DECISION

The CESTAT concurred with the findings of the first appellate authority. The lower authorities had concluded that under a BOOT contract, profit/savings are shared between the parties. In the present case, savings in energy cost were shared between NMC and the Assessee for a period of five years. Reference was had to Para 9B and 10 of the contract and it was observed that the whole contract was principally based on the concept of energy saving and that the Assessee was to be paid through energy cost saved in percentage basis for a period of five years. Moreover, if the equipment was not functioning optimally, they were bound to lose their remuneration/earnings. Thus, it is the responsibility of the Assessee and in his interest to maintain and ensure proper functioning of the equipment installed so as to ensure that maximum energy was saved, because remuneration /consideration is directly dependent on the energy saved which can only be ensured only through proper maintenance.

Therefore, to categorize the services rendered by the Assessee during the BOOT period and remuneration received, solely on account of maintenance and repair services rendered to NMC is without any basis, grounds or evidence.

95. CCE v. Sahastronics Controls Pvt. Ltd., 2016 (41) STR 454 (Tri. - Mumbai)

It was further held by the lower authorities that the contract clearly mentions that the ownership of the equipment will be with the Assessee. Thus, it was held that to maintain one's own equipment, to optimize the usefulness, by maintenance and repair, in the BOOT period, was certainly not liable to Service tax as services rendered to self cannot be taxed as under Section 68(1) r/w Section 65(105)(zzg) of the FA.

SIGNIFICANT TAKEAWAYS

This case highlights the principle that service to self is not taxable and applies it to BOOT contracts. The CESTAT has analysed that any profit sharing arrangement during the BOOT period, where assets are owned by the service provider, any activity of profit sharing at that time shall essentially be a service to self and shall not be taxable under service tax. This highlights the principle that for the purposes of service tax, the service needs to be provided to two distinct entities.

LEASE TRANSACTION ENTERED BY CUSTOMER POST IMPORTATION OF GOODS NOT ELIGIBLE TO BENEFIT OF EXEMPTION AS LEASE IN THE COURSE OF IMPORT

In **Hewlett Packard Financial Services India Private Limited**⁹⁶, the Karnataka HC has upheld the judgment of the VAT tribunal, wherein the Tribunal had held that exemption under section 5(2) of the CST Act is not available to the Lessor, in case of a lease in the course of import, as the ownership of goods at the time of import vests with the Lessee and not the Lessor.

FACTS

Hewlett Packard Financial Services India Private Limited ("**Assessee / Lessor**") entered into a Master Lease Agreements ("**MLA**") with its customers ("**Lessee**") for procuring goods from outside India. The *modus operandi* of the said arrangement was as follows:

- The purchase order was placed directly by the Lessee on the foreign vendors.
- The goods were shipped to the Lessee but the invoice was raised in the name of the Lessor.
- The shipping authorization letter was issued by the Lessor to the vendors and the invoice were issued in the name of the Lessor.
- The bill of entry was filed by the Lessee at the time of clearing the goods. Thereafter, the acceptance certificate was issued by the Lessee. Post the delivery of the goods and their unconditional acceptance by the Lessee, the novation notice, as per the MLA, was issued by the Lessee, confirming that the purchased documents shall now remain with the Lessor.
- Thereafter, the lease schedule was signed by the parties specifying the goods under lease as per terms and conditions of Master Rental and Finance Agreement.

ISSUE

Whether in the present case the Lessor i.e. the Assessee was entitled to exemption under section 5(2) of the CST Act in relation to lease in the course of import?

ARGUMENTS/ANALYSIS

The Assessee contended that the VAT Tribunal failed to appreciate all the facts and therefore arrived at a flawed conclusion. To that effect, the Assessee produced further lease agreements between itself and various other lessees, claiming that in the said transaction structure, the Lessor was infact the owner of the goods at all times.

In addition, the Assessee contended that the relevant aspect for availing the said exemption was that after the goods crossed the customs frontier of the country, the acceptance of the products and the ownership of the goods imported *vide* the purchase order were re-entrusted by the Lessee in favour of the Lessor, and it was only thereafter that the master rental and financing agreement was entered into between the Lessor and Lessee. Thereafter, on account of the novation of the contract, the ownership was entrusted by the Lessee to the Lessor and then the rental lease agreement was entered into.

96. Hewlett Packard Financial Services India Private Limited v. State of Karnataka, 2016-VIL-142-KAR

The IRA reiterated the findings of the VAT Tribunal that stated that section 5(2) of the CST Act has two prongs; the first prong envisages the sale or purchase in the course of import if such sale or purchase occasions import. The second prong envisages that the sale or purchase is in the course of import when it is effected by transfer of documents of title to the goods before the goods have crossed the customs frontiers of India. The second prong is not fulfilled as the transfer of documents of title to the goods has not taken place on the high seas.

The IRA further reiterated leading case laws⁹⁷ of the SC to list the conditions that need to be satisfied to claim exemption under section 5(2) of the CST Act and submitted that if the transactions between the foreign exporter and the local user in India get transmitted through an independent canalizing import agency which enters into back to back contracts and there is no direct linkage or causal connection between the export by foreign exporter and the receipt of the imported goods in India by the local users, the integrity of the entire transaction would be disrupted and would be substituted by two independent transactions. In such a case, the sale by the canalizing agency to the local users would be because of or by the import, which would not be covered by the exemption provision of section 5(2) of the CST Act.

The IRA further submitted that the right on the goods lies with the end customer till the acceptance certificate is issued followed by the novation notice. By virtue of acceptance certificate and novation notice, the rights on the goods gets transferred to the Assessee and till then the rights over the goods vest with the end customer only. The Lessor stands as a financial guarantor only.

DECISION

The Karnataka HC emphasized two aspects of this case; firstly, that in the bill of entry, the Lessee is shown as the importer on record; and secondly, the Lessee had claimed concession under the Customs Act since the goods were to be used for a 100% Export Oriented Unit (“EOU”). The aforesaid two aspects show that, in so far as the Customs Act is concerned, the Lessee is the person who is to claim benefit of exemption from duty or concessional rate of duty, as if the Lessee is the owner of the goods and he has to utilize the goods in an EOU. The Lessee may not be entitled for the benefit of the scheme if the Lessee is not the owner of the goods.

The HC further observed that even if one proceeded on the basis that the MLA was executed in the absence of any advance payment made or any part consideration paid, then also, as far as the Customs Act is concerned, the relationship is severed in as much as, the Lessee is shown as the owner and only the payee of the consideration is shown as the Lessor. Consequently, the HC observed that in this case, the

novation of the contract for transfer of ownership from the Lessee to the Lessor only takes place post importation, as rightly noted by the VAT Tribunal.

The HC proceeded to distinguish the instant case from the decision in *Karnataka Bank Limited*⁹⁸ rendered by the Madras HC on the facts that the Madras HC in that case had no occasion to consider the division of the relationship and the link between the assessee and the customer when the goods were imported. The Madras HC also had no occasion to consider the aspects of entrustment of the ownership by novation of the contract as in the present case.

Accordingly, the HC agreed with the broad reasons provided by the VAT Tribunal and observed that the decision of the Tribunal was a mixed question of law and fact which cannot be interfered with at this stage.

SIGNIFICANT TAKEAWAYS

In the peculiar facts and circumstances of the case, it can be seen that the present MLA contemplated the novation of the contract post importation and not on the high seas. Therefore, the lease transaction had come into effect in India, and therefore, the transaction attracted the levy of sales tax.

In this regard, while structuring similar transactions, care must be taken while wording the contract, in so far as it unambiguously brings out the intention of the parties to pass on the property in goods, in the high seas, in order to occasion sale/lease in the course of import. This would mitigate the risk of the Indian sales tax authorities demanding sales tax on such back to back transactions.

97. *Cashew Corporation of India vs. State of Karnataka*, (1997) 105 STC 580 (SC)

98. *State of Tamil Nadu vs. Karnataka Bank Limited*, (2012) 50 VST 93 (Madras)

PACKAGING AND RELATED ACTIVITIES PERFORMED PRIOR TO DELIVERY OF GOODS BY E-COMMERCE PLATFORM DOES NOT AMOUNT TO MANUFACTURE

In the Advance Ruling of *Amazon Seller Services Private Limited*⁹⁹, the AAR held that activities relating to spectacles and frames (placing in case, tightening screws on eyewear) and activities such as tagging and inserting freebies, placing the product in original box / pack, etc, carried out by an online platform in relation to the products of the sellers using the online platform for trading, prior to the delivery of the goods would not amount to manufacture or deemed manufacture under section 2(f) of the CEA.

FACTS

Amazon Seller Services Private Limited (“**Applicant**”) was an operator of an online marketplace portal available at www.amazon.in (“**Website**”) that enables customers from any location in India to purchase products listed on the Website (“**Product(s)**”) at the price indicated therein, from the sellers who have listed their Products on the Website (“**Seller(s)**”). The Applicant proposed to provide an additional facility in the nature of fulfillment services; namely, inspection, testing and installing batteries, cleaning, lint brushing and deodorizing, touching up and re-stitching, filing, de-bundling and jewellery correction, activities related to spectacles and frames, folding, hanging and ironing, polishing, shinning and coating, tagging, freebies, protective stickering, placing the products in original box, inserting warranty card, inserting moisture absorbing tablets, inserting books mark, replacing shoe laces; through its fulfilment centers. the fulfilment centers would either be the warehouses owned and operators or the warehouses operated by third parties on behalf of the Applicant.

ISSUE

Whether the aforesaid activities proposed to be undertaken by the Applicant would be regarded as manufacture or deemed manufacture under section 2(f) of the CEA?

ARGUMENTS/ ANALYSIS

The Applicant primarily submitted that the proposed activities would not alter the primary packaging or labeling on the Products which is done by the Seller. Further, as envisaged by section 2(f) of the CEA, the proposed activities would not involve affixation, alteration or change in the Maximum Retail Price (“**MRP**”) or Retail Sale Price (“**RSP**”) of the Products. The intent to undertake the activities is to facilitate the sale of Products to the customers of the Sellers. Since, there is no value addition on the Product, these activities would not amount to manufacture or deemed manufacture.

In response to the application, the IRA replied that the activities other than the following will not constitute manufacture:

- (a) Activities relating to spectacles and frames;
- (b) Tagging; and
- (c) Provision of freebies.

The specific arguments made by the Applicant and the IRA in relation to the aforesaid activities are as follows:

99. In Re, Amazon Seller Service Private Limited, Bangalore, 2016-VIL-05-ARA

(a) Activities relating to spectacles

Under this activity, the Applicant proposed to place the spectacles and sunglasses received from the Sellers in their matching cases. Along with the placing of spectacles, the Applicant proposed to tighten the screw at the temples and hinges on the spectacles wherever required owing to storage and customer returns.

The Applicant relied on the decision of the Calcutta HC in the case of *Bholanath Sreemony*¹⁰⁰ wherein it was held that the activity of assembling of frames and fitting in of glasses based on prescription does not create a new and distinct article. Hence, such activities would not amount of manufacture as no new distinct Product is emerging out of the performance of the proposed activities by the Applicant.

The IRA submitted that the proposed activities are to be carried out to render the Products marketable.

(b) Tagging

The Applicant proposed to re-apply the loosened out or displaced tags on the Products. The activity would have also involved placing the Applicant's tag on jewellery while placing it in the box to prevent return of counterfeit item.

The Applicant argued that primarily the activity does not involve applying Applicant's additional tag on the Products. In case of the jewelry, tags are placed on the boxes of the unbranded jewelry and would not amount to manufacture. The Applicant relied on Circular of the CBEC¹⁰¹, wherein it was clarified that if the brand name is not affixed or embossed on the jewelry but only appears on the packing of the jewelry, such a jewelry would not be treated as a branded jewelry and thus will not be liable to excise duty.

The IRA submitted that tags contained the names of the brands which are to be attached to the jewelry before dispatching. The Applicant has not provided the sample jewelry to ascertain whether the brand names are already embossed on the jewelry and such brand names are registered.

(c) Freebies

The Applicant proposed to put freebies along with the Products to be sold either at the instruction of the Seller or on its own accord.

The Applicant argued that the activity of putting freebies on the Products would not alter the primary packaging. Since the purpose of the freebies is to offer incentives to

the customers for purchasing items on the Website, the freebies do not enhance the price of the Products. Therefore, MRP/RSP of the Products remains the same. Hence, such activity would not amount to manufacture.

The IRA submitted that if the combo packs result in additional labeling and altering the MRP of the pack, then such activity would amount to manufacture.

RULING OF THE AAR

The AAR ruled that the proposed activities in relation to spectacle and frames would not result in emergence of a new article with distinct use, name and character. Therefore, relying on the decision of the HC in the case of *Bholanath Sreemony (supra)*, the AAR ruled that such proposed activities would not amount to manufacture or deemed manufacture.

In relation to the other specifically objected activities, namely; Tagging and Freebies, the AAR observed that the facts were clear from the application that the proposed activities would not alter the MRP of the Products. Further, in relation to Tagging of jewelry, the tags were to be placed on boxes or packaging rather than on the jewelry. Therefore, such activity would not result in branding of jewelry. Accordingly, these activities would not amount to manufacture or deemed manufacture.

SIGNIFICANT TAKEAWAYS

The above ruling has provided a clarity on the issues relating to the activities undertaken by the online portals, trade facilitators, warehouse keepers and other similar service providers, on the products of the sellers or manufactures prior to the delivery. In case the activities are intended to provide sale support only and do not alter the products or its packaging or its MRP/RSP, then such activities would not amount to manufacture or deemed manufacture under section 2(f) of the CEA.

Relying on this Advance Ruling, the AAR in the matter of *Amazon Wholesale (India) Private Limited*¹⁰² has held that similar service would not amount to manufacture.

100. *Bholanath Sreemony v. Additional Commissioner of Commercial Taxes*, MANU/WB/0397/1978

101. Circular No. F. No. 354/38/2011-TRU dated March 02, 2012

102. In Re, *Amazon Wholesale (India) Private Limited*, New Delhi, 2016-VIL-06-ARA

THE DOCTRINE OF UNJUST ENRICHMENT SHALL NOT APPLY WHERE INCIDENCE OF TAX IS PASSED ONTO SELF

The CESTAT in *Usha International*¹⁰³ held that services rendered post amalgamation became service to self and consequently service tax paid during the said period was eligible for refund.

FACTS

M/s Jay Engineering Works Limited (“JEW”) was receiving royalty from M/s Usha International Ltd. (“UIL” or “Assessee”) for the use of its brand name and paid service tax on royalty so received. However, JEW merged with UIL and M/s Shree Ram Fuel Injections Ltd. with effect from April 1, 2007, being the appointed date of the merger. The new entity carried on business under the name of “Usha International Limited”.

The HC approved merger of erstwhile company UIL with JEW vide order dated May 26, 2008. Further the ROC issued the approval for change of name of “Jay Engineering Works Limited” to “Usha International Limited” on June 20, 2008. The Assessee filed refund claim on January 8, 2009 seeking refund of service tax paid for the period April 1, 2007 to March 31, 2008 on royalty paid by the erstwhile company UIL to the erstwhile company JEW.

The first appellate authority held that the ROC had only issued its approval for aforesaid change of name on June 20, 2008 and, therefore, up to that date the rendition of service could not be termed as service to self and the service tax was correctly payable / paid and so no refund was admissible.

ISSUE

Whether as a result of merger dated April 1, 2007 and approved by the order of the HC dated May 26, 2008, services rendered during impugned period of April 1, 2007 to March 31, 2008 became service to self and, therefore, no service tax was payable?

ARGUMENTS/ANALYSIS

The Assessee relied on *Marshall Sons & Co. (I) Ltd. v. ITO*¹⁰⁴ and contended that it is immaterial when the HC order was passed and when the ROC issued the letter of its approval of the change of name. It was further submitted that no CENVAT credit of impugned service tax was taken by the Assessee. It was further submitted by the Assessee that as a result of merger dated April 1, 2007, service rendered during impugned period April 1, 2007 to March 31, 2008 became service to self and, therefore, no service tax was payable, however the Assessee continued to pay the same as the order of the HC approving the merger was received only on May 28, 2008.

The IRA contended that the service tax was paid by JEW which functioned as an independent company up to June 20, 2008 and therefore service tax was payable and accordingly, was also correctly paid. Further, the onus is on the Assessee to show that the burden was not passed to the end customer. The fact that the prices of the Assessee’s final product did not go down from April 1, 2007 clearly shows that the burden was passed on to the customers.

In this regard, the Assessee submitted that the variation in price is hardly conclusive evidence with regard to passing of the burden of tax.

103. Usha International Ltd. v. CST, New Delhi, 2016-VIL-191-CESTAT-DEL-ST

104. Marshall Sons & Co. (I) Ltd. v. ITO, [1997] 2 SCC 302

DECISION

As per the arrangement between the erstwhile company JEW and the erstwhile company UIL, it is clear that pending the approval and sanction of the scheme of amalgamation by the HC, JEW carried on its business and activities for and on account of and in trust for the erstwhile company UIL. In these circumstances, the only inescapable conclusion which emerges is that the amalgamation was effective from April 1, 2007, even if its approval by the HC and the letter of ROC approving change of name were issued later. This view is clearly supported by the SC judgment in the case of *Marshall Sons & Co. (I) Ltd. (supra)*. Therefore, the date of amalgamation is to be held to be April 1, 2007 and not June 20, 2008.

It is pertinent to note that the refund in the instant case is arising on account of the fact that the effective date of merger/amalgamation is to be treated as April 1, 2007, which makes the service rendered during the relevant period as service to self.

As the service was rendered to self and service tax was paid thereon, burden can only be passed on to self and passing on the burden to self is not tantamount to passing it to any other person. In other words, the Assessee is not hit by the doctrine of unjust enrichment.

SIGNIFICANT TAKEAWAYS

This judgment applies settled law in *Marshall Sons & Co. (I) Ltd. v. ITO (supra)* to state that the merger has taken place on the date of the scheme of the arrangement and not the date of approval from the HC or the date of approval for change in name. In this regard, the HC highlighted an important proposition regarding unjust enrichment. In cases of service to self, there is no scope of passing on the incidence of tax to self, hence unjust enrichment shall not apply.

Therefore, significantly in such cases of service to self where refund is claimed, the logical conclusion is that the Assessee does not have to fulfill the burden of showing that the incidence of tax has not been passed onto the customer.

SERVICES IN RELATION TO BRANDING, OFFLINE MARKETING, MARKETING, ETC. ON A PRINCIPAL TO PRINCIPAL BASIS IS NOT AN “INTERMEDIARY SERVICE”

The AAR in the decision of *In, Re: GoDaddy India Web Services Private Ltd.*¹⁰⁵ held that the bundled activities of support services provided in India by the Applicant to GoDaddy.com, LLC (“GDUS”) would qualify as the main service and not an intermediary service. Accordingly, the place of provision of service would be outside India.

FACTS

GoDaddy India Web Services Private Ltd. (“Applicant”) entered into a service contract with GDUS to provide specific services in an integrated manner to assist GDUS in developing its brand in India and to carry out its operations efficiently. The support services included marketing and promotion services wherein the Applicant would advise GDUS about the prevailing market conditions in India, the suitable time for rolling out campaigns in India. However, all advertisements would be prepared by GDUS. The Applicant would assist GDUS in development of GDUS’s brand in India wherein it would advise on various events taking place in India for possible advertisement placements. Further, the Applicant would take part in conferences, talk shows, webcasts, and road shows to spread awareness regarding GDUS’s brand. The Applicant may sponsor certain events too. Further, the Applicant would supervise the functioning of GDUS’s customer care centre in India, which would be run by a third party. Further, the Applicant would provide GDUS payment processing services wherein the Indian customers would be able to pay in INR to the Applicant, who would then remit the amount to GDUS in United States Dollar (“USD”).

The Applicant would charge a fee in USD for rendering these services which would be equal to the costs incurred plus a mark-up of 13% on such cost.

ISSUE

Whether the above captioned services amount to export services under Rule 6A of the ST Rules?

ARGUMENTS/ANALYSIS

The Applicant submitted that these aforementioned services would be provided in an integrated manner – a bundle of services which are naturally bundled in the ordinary course of business. This bundle would be in the nature of support services in relation to marketing, branding, quality oversight of third party customer care unit and payment processing on a principle to principle basis. The payment for these support services would be one consolidated amount. Accordingly, the definition of intermediary would not be applicable in the present case because the Applicant would be providing the main service itself i.e. “business support services” to GDUS. Therefore, it was put forth that the place of provision of service would be determined according to Rule 3 of the POP Rules and not Rule 9(c) as contended by the IRA. As per Rule 3, the place of provision of service would be outside India. Further, the Applicant contended that the services would qualify as an export of service under Rule 6A of the ST Rules

The IRA submitted that various services, i.e., marketing, event management services and collection of money from customer on behalf of GDUS, etc. that are proposed to be provided by the Applicant to GDUS are not a bundle of services. Consequently, these services so provided are covered as ‘intermediary services’, under Rule 9(c) of POP Rules. Therefore, as per section 66F(2) of FA, for the purpose of classification of service, the more

105. In Re, GoDaddy India Web Services Private Ltd., 2016-VIL-08-ARA

specific description shall be preferred over a more general description. Therefore, the IRA contended that in view of subsection (3) of section 66F, such service would not be taxed as a bundled service, if the same can be termed as an 'intermediary service'. Thus, the place of provision of service would be in India as per Rule 9 of the POP Rules, and would be taxable in India. Therefore, as per the IRA, these services would not qualify as export as they are taxable in India.

RULING OF THE AAR

The AAR held that the definition of "intermediary" as envisaged under Rule 2(f) of the POP Rules does not include a person who provides the main service on his own account. In the present case, the Applicant was providing main service, i.e., all these services to GDUS and on his own account. Therefore, it was held that these services are a "bundle of services" which are naturally bundled in the ordinary course of business and not an intermediary service. Accordingly, the AAR held that the services are covered under Rule 3 of POP Rules which *inter alia* envisages that place of provision of service is the location of the recipient of service. In the present case, that was outside India.

Further, the AAR held that these services would be treated as export services fulfilling all the criteria laid down under Rule 6A of the ST Rules, namely, *first*, the provider of service is located in the taxable territory, *second*, the recipient of service is located outside India, *third*, the service is not a service specified in the section 66D of the FA, *fourth*, the place of provision of the service is outside India, *fifth*, the payment for such service has been received by the provider of service in convertible foreign exchange and *lastly*, the Applicant and GDUS were separate entities for the purposes of service tax and not mere branch offices of each other. Therefore, these services qualify as export of service and accordingly, the benefits for export would apply to these services.

SIGNIFICANT TAKEAWAYS

This ruling shall provide major relief to entities that provide marketing and promotion services to overseas entities on a principal to principal basis. In this regard, due may be placed on the decision in *Paul Merchants*¹⁰⁶, which stated that service tax is a destination based consumption tax. Accordingly, the POP Rules are framed keeping that principle in mind.

In this case, the AAR has concluded that the services in the present case are provided on a principal to principal basis and are consumed entirely by a foreign entity. Therefore, services provided by the Applicant are the main service and not in the nature of providing services in the nature of facilitation or arrangement of a provision of another service (i.e. an intermediary service). Assesseees must take care to structure such transactions on a principal to principal basis and not as an agent arranging a provision of services or goods, as in the latter case, the transaction shall be taxable in India.

In light of this ruling the companies need to evaluate the applicability of the AAR ruling looking at the rationale laid down by the AAR. Though it applies only to the parties in question, it may have persuasive authority before other forums.

106. Paul Merchants Ltd. v. Commissioner of Central Excise, Chandigarh, 2013 (29) STR 257 (Tri.-Delhi)

THE AMOUNT CHARGED BY THE EMPLOYER FROM ITS EMPLOYEES FOR THE USE OF VEHICLES UNDER CAR LEASE SCHEME, IS NOT EXIGIBLE TO SERVICE TAX UNDER SECTION 66B OF THE FINANCE ACT, 1994

In *J.P. Morgan Services India Private Limited*¹⁰⁷, the AAR held that service tax is not payable on the amount recovered by the employer from the employee for the use of vehicles under a car lease scheme.

FACTS

In this case, the J.P. Morgan Services India Private Limited (“**Applicant**”), as part of an employee retainment program, sought to provide vehicles to its employees during their employment, under a scheme wherein, the Applicant would hire cars from the car leasing companies and such cars would be made available to the employees who accept the option to have the car for their personal as well as official use. In lieu of this, the Applicant would charge the said employees the same amount which the Applicant shall be paying to the car leasing company from whom the cars would be hired.

The service which would be provided by the car leasing company to the Applicant was proposed to be taxed under service tax by the IRA.

ISSUE

Whether the amount charged by the Applicant to its employees for use of the said vehicles is subject to service tax?

ARGUMENTS/ANALYSIS

The Applicants contended that, the said activity was covered under the exception created to the definition of ‘service’ by section 65B(44)(b) of the FA for services provided by an employee to the employer in the course of employment. The Applicant was merely making available a car for the use of the employees during the course of their employment for which it was charging only the car rent which the Applicant was paying to the car leasing company from which it has hired the car.

The IRA contended that the car was being made available to the employee both for official and personal use. Therefore, on this basis, the said activity would attract the levy of service tax.

RULING OF THE AAR

The AAR held that the Applicant was providing the service of making the car available to its employee. In this context, both the conditions in clause (b) of section 65B (44), were required to be fulfilled in order to be covered within the exception to the definition of service are satisfied. Firstly, it was held by the AAR that the activity was in the course of the employment because the agreement between the Applicant and employee clearly suggested that it would be *during the course of his employment* only. Secondly, since the service was being provided during the course of employment in as much as the employee was part of the service and in that sense the service became *in relation* to his employment.

In addition, it has been held by the AAR that the car being given for official use or personal use or for both, would not make any difference in so far as the service still fell within the ambit of the exception to the definition of service under the FA.

107. In Re, J.P. Morgan Services India Private Limited, Ruling No. AAR/ST/16/2015 dated December 04, 2015

Accordingly, the AAR held that the amounts collected by the Applicant from its employees in respect of the car leasing scheme were not exigible to service tax.

SIGNIFICANT TAKEAWAYS

In the present case, the AAR has extended the meaning of the terms '*in course of or in relation to employment*' under section 65B(44)(b) of the FA by interpreting it to include both personal and official use of such a services provided by the employer. In this regard, the exception provided under the definition of service already excluded services of an employee to the employer. Additionally, as per this decision amounts collected by the employer in the course or in relation to employment of the employee shall also not be included under the definition of service and therefore shall not be liable to service tax.

SMS TERMINATION SERVICE IS A CONTINUOUS SUPPLY OF SERVICE, AND POINT OF TAXATION IS TO BE DETERMINED ACCORDINGLY

In **Vodafone Cellular Ltd**¹⁰⁸ the CESTAT held that the fee paid by the originating telecom operator, whose subscriber subscribes to the Short Messaging Service (“SMS”), to the terminating telecom operator (in whose network the SMS is delivered or terminated) (“**Termination Charges**”) are amenable to service tax and the point of taxation for such services shall be determined as a continuous supply of service. Accordingly, service tax is chargeable every time an invoice is raised for providing continuous supply of service.

FACTS

The Termination Charges are governed by the guidelines issued by the Telecom Regulatory Authority of India (“**TRAI**”). The actual charge of SMS termination service between telecom operators began with effect from April 1, 2011 where the Telecom Disputes Settlement & Appellate Tribunal (“**TDSAT**”) had ordered to collect five paise per SMS.

In this regard, proceeding against the Vodafone Cellular Limited (“**Assessee**”) was initiated for not paying service tax on the Termination Charges provided by them. Proceedings culminated in the impugned order confirming the demand of service tax of INR 4,28,05,261/-

ISSUE

Whether, under the POT Rules, service tax is payable as a continuous supply of service on the regular raising of invoice on the SMS termination service rendered by the Assessee to other telecom operators with whom neither a contract for service has been signed nor any consideration has been received?

ARGUMENTS/ANALYSIS

The Assessee submitted that telecom service is notified as a continuous supply service under Notification No. 38/2012-ST dated June 20, 2012 in terms of Rule 2(c) of the POT Rules. Therefore, in terms of proviso to Rule 3(b) of the POT Rules, in the case of continuous supply of service, the point of taxation arises on completion of events specified in the contract which requires receiver of service to make the payment to the service providers. In their case, the event had not arisen because neither there was a contract nor had there been a payment of consideration. Therefore, the service tax was not yet payable as the point of taxation had not arisen yet. The Assessee relied on the Circular of the CBEC¹⁰⁹ which clarifies that in case of continuous supply service, the invoice is to be issued within a period of fourteen days from the date of completion of the service.

The IRA contended that Rule 2(c) of the POT Rule categorizes "continuous supply of service" in two categories. Under the second category, in case of a service, such as the service in question, the point of taxation is governed by Rule 6 (as it stood during the relevant period) of the POT Rules. It was put forth by the IRA that Rule 6 provides that the point of taxation shall be the time when the invoice is issued or if the invoice is not issued within fourteen days of the completion of the service, the point of taxation shall be the date of such completion. In this regard, the IRA submitted that the periodic demand letters issued by the Assessee for payment of Termination Charges, to other telecom service providers (“**Demand Letter(s)**”) shall constitute an invoice under the ST Rules and accordingly, service tax is liable to be paid as the invoice has been raised.

108. Vodafone Cellular Ltd v. Commissioner of Central Excise, Pune, 2016-VIL-164-CESTAT-MUM-ST

109. Circular No. 144/13/2011-ST dated July 18, 2011

DECISION

The CESTAT held that as there is no such contract requiring service receiver to make any payment, the point of taxation is to be determined in terms of Rule 6(a) of the POT Rules. Under Rule 6(a), where a continuous supply of a notified service is provided under a contract, the determining point is date of issue of invoice.

The CESTAT also observed that that it is inescapable fact that service was provided under a contract. The absence of a consideration clause in the contract does not come in the way of determining the point of taxation under Rule 6 (a). Therefore, in the present case the service is provided when the invoice is issued. Where invoices were not issued within fourteen days of the completion of the service, the point of taxation was to be the date of such completion.

The CESTAT further held that the Demand Letters issued by the Assessee to various telecom operators contained all the details required in an invoice under Rule 4A of the ST Rules. The Demand Letters provided the name and address of the service provider as well as the name and address of the service recipients. The description and value of service provided is also mentioned by the Assessee in the Demand Letter. The Demand Letters complied with the substantive provisions of Rule 4A and therefore, may be considered as invoices. Accordingly, invoice had been issued by the Assessee periodically by way of issue of the Demand Letters. Accordingly, for every invoice raised, the point of taxation has arisen for continuous supply of service and accordingly, service tax shall be payable.

SIGNIFICANT TAKEAWAYS

This decision significantly holds that any document complying in substance with the provisions of Rule 4A of the ST Rules shall be held to be an invoice and accordingly, the point of taxation for continuous supply of service for each such invoice shall arise. In this regard, care must be taken to ensure that where an invoice is raised for any service fees, the point of taxation shall arise, and service tax needs to be paid on the amount mentioned in the invoice as service fee, on the dates as specified. This places emphasis on the mechanism of the POT Rules which has made the basis of payment of service tax on an accrual basis rather than on receipt basis, as was in existence prior to April 1, 2011.

NON-JUDICIAL UPDATES

Direct Tax

1. Tests for characterisation of gains on sale of securities

The determination of the character of a particular investment in shares or other securities, whether the same is in the nature of a capital asset or stock in trade, is essentially a fact specific determination and has, over the years, led to a lot of uncertainty and litigation. The reason why it has become a controversial issue is because the tax implications vary to a great extent on these transactions, being treated either as capital gains or business income. Courts have laid down various parameters for drawing a line of difference between capital investments and stock-in-trade. The CBDT had *vide* Instruction no. 1827 dated August 31, 1989 and Circular no. 4 of 2007 dated June 15, 2007 summarised the principles laid down by several Courts for the guidance of the AOs.

While partially modifying the earlier Circulars, the CBDT *vide* Circular No.6 of 2016 instructs that the AOs in holding whether surplus generated from sale of listed shares or other securities would be treated as capital gains or business income, shall take into account the following:

- (a) Where the assessee itself, irrespective of the period of holding of the listed shares and securities, opts to treat them as stock-in-trade, the income arising from the transfer of such shares/ securities would be treated as business income.
- (b) In respect of listed shares and securities held for a period of more than 12 months immediately preceding the date of transfer, if the assessee desires to treat the income arising from the transfer thereof as capital gains, the same shall not be put to dispute by the AO. However, this stand, once taken by the assessee in a particular AY shall remain applicable in the subsequent AYs also and the taxpayers shall not be allowed to adopt a different/ contrary stand in this regard in the subsequent years.
- (c) In all other cases, the nature of transactions (i.e. whether the same is in the nature of capital gains or business income) shall continue to be decided considering the view provided in aforesaid CBDT Circulars.

- (d) It is, however, clarified that the above principles shall not apply for transactions in securities, where the genuineness of the transaction itself is questionable. To illustrate, bogus claims of long term capital gains/ short term capital gains or any other sham transaction.

The CBDT has reiterated that the aforesaid principles are formulated with the sole objective of reducing litigation and maintaining consistency in approach on the issue of treatment of income derived from transfer of securities.

It would be noted that the Easwar Committee had recommended that gains on transfer of shares and securities held for a period of more than 12 months should be taxable as capital gains, unless they are treated as stock-in-trade by the taxpayer itself.

2. AOP test for EPC consortium contractors

Large infrastructure and turnkey projects demand several domestic as well as foreign parties to come together so as to form a pool of expertise in various segments, facilitate co-ordination amongst each other, execute different phases of tasks, etc. A question arises as to whether such consortiums would form an association of persons ("AOP"¹¹⁰), a separate taxable entity and be taxed accordingly. Further, if the consortium is treated as an AOP, there may be number of issues, like income being taxed at the maximum marginal rate, inability to set off losses of other projects, non-availability of tax credit for non-residents, etc.

The AAR in the case of *Linde AG*¹¹¹, *Alstom Transport*¹¹², *Roxar Maximum Reservoir Performance WLL*¹¹³ ruled that on the facts, there was an AOP in cases of consortium. However, the Delhi HC has recently struck down the ruling of the AAR in the case of *Linde AG* (supra), though based on specific facts of the case, and laid down several principles under which consortium can be treated as an AOP, such as common scope of work, revenue sharing arrangements, joint participation, joint management and control of work, bearing of all risks, etc.

110. AOP has not been specifically defined under the IT Act. However, there are certain judicial decisions, which lay down certain criteria for formation of AOP

111. *Linde AG, Linde Engineering Division v.DDIT* (2014) 44 taxmann.com 244 (Delhi HC); An SLP has been filed with the SC against this decision and is pending for hearing

112. *Alstom Transport SA, In re* (2012) 349 ITR 292 (AAR)

113. *Roxar Maximum Reservoir Performance WLL, In re* (2012) 349 ITR 189 (AAR)

In order to terminate this contentious issue and avoid tax disputes, the CBDT, vide Circular No. 7/2016 dated March 7, 2016, has clarified that a consortium arrangement for executing turnkey/EPC contracts which has the following attributes may not be treated as an AOP:

- (a) Each member is independently responsible for executing its part of work through its own resources and also bears the risk of its scope of work, i.e. there is a clear demarcation in the work and costs between the consortium members and each member incurs expenditure only in its specified area of work;
- (b) Each member earns profits or incurs losses, based on performance of the contract falling strictly within its scope of work. However, the consortium members may share contract price at gross level only to facilitate convenience in billing;
- (c) The men and materials used for any area of work are under the risk and control of the respective consortium members;
- (d) The control and management of the consortium is not unified and common management is only for the inter-se co-ordination between the consortium members for administrative convenience.

It has also been clarified that there may be additional factors also which may justify that consortium is not an AOP and the same shall depend on the facts and circumstances of each particular case which needs to be taken into consideration while taking a view in the matter.

It is further clarified that this Circular shall not be applicable where all or some of the members of the consortium are associated enterprises within the meaning of section 92A of the IT Act and in such cases, the AO will decide whether an AOP is formed or not keeping in mind the relevant provisions of the IT Act and the judicial jurisprudence on this issue.

The issuance of this Circular is a welcome move and it would help in reducing the litigation surrounding the taxation of EPC contracts. However, in many cases, the non-resident party executes an Indian project with the assistance of its Indian subsidiary or its affiliates and, therefore, it would be interesting to see how the IRA deals with such situations!

3. Holding period of convertible bonds/debentures

Under the IT Act, there is no provision specifically providing to include the pre-conversion holding period of convertible bonds/debentures while computing the holding period of the converted securities. Accordingly, this aspect became ambiguous and a subject matter of litigation¹¹⁴. In the absence of any specific provision, the IRA used to contend that the holding period of converted securities should not include the pre-conversion period, relying upon the clause (f) of Explanation 1¹¹⁵ of section 2 (42A) of the IT Act.

In order to combat this uncertainty, the CBDT through Notification dated March 17, 2016 has inserted Rule 8AA into the IT Rules to provide that in case of capital assets, being shares or debentures of a company, which become the property of an assessee in the circumstances under section 47(x) of the IT Act (i.e. non-taxable transfers, being conversion of debentures into shares or conversion of bonds into debentures, etc.), the period for which such capital assets were held prior to conversion shall also be taken into account for the purpose of determining the holding period of such assets on subsequent sale/transfers.

4. Benefit of Indo- UK DTAA to UK partnership firms

Article 4 of the Indo-UK DTAA was amended¹¹⁶ to specifically deal with partnership firms. However, the issue which still existed was whether a 'partnership firm' which does not fall within the scope of the word 'person' as per paragraph 2 of Article 3 of the Indo-UK DTAA, would be eligible to be a resident of a contracting state and claim the benefits of the Indo-UK DTAA.

To put an end to the controversy and provide the much needed clarity, the CBDT has vide Circular No. 02/2016 dated February 25, 2016, clarified that the provisions of the Indo-UK DTAA would be applicable to a partnership firm that is a resident of either India or UK, to the extent that the income derived by such partnership, estate or trust is subject to tax in that state as the income of a resident, either in its own hands or in the hands of its partners or beneficiaries.

It is pertinent to note that the Calcutta HC in the case of *P&O Nelloyd Ltd. & Ors*¹¹⁷ has held that even though a partnership firm is not a taxable unit in UK, it is a 'person'

114. CIT v. Naveen Bhatia (ITA no. 153 of 2008) (Punjab & Haryana High Court) and Smt. Roda v. ITO (ITA No. 1069/AHD/96) (Ahmedabad ITAT)

115. In case of a capital asset, being a financial asset, allotted without any payment and on the basis of holding of any other financial asset, the period shall be reckoned from the date of allotment of such financial asset

116. Notification No. 10/2014 dated February 10, 2014 with effect from December 27, 2013

117. *P&O Nelloyd & Ors v. ADIT* (2014) 52 taxmann.com 468 (Calcutta HC)

under section 2(31) of the IT Act, thereby fall within the ambit of paragraph 2 of Article 3 of the Indo-UK DTAA.

5. Clarification regarding nature of share buy-back transactions under the IT Act

The Finance Act, 2013 introduced section 115QA to provide that any amount of distributed income by a company on buyback of unlisted shares shall be charged to tax and the company so distributing the income shall be liable to pay additional income tax at the rate of 20% (“**buyback tax**”) of such distributed income.

However, the CBDT realized that the provisions of buyback of shares, since the introduction of dividend distribution tax (“**DDT**”) were being interpreted in a conflicting manner thereby giving rise to disputes. It has been contended that subsequent to the introduction of section 115QA in the IT Act and placing reliance on a decision of the AAR in the case of XYZ India¹¹⁸, the IRA has sought to recharacterise the amounts received on buyback of shares, undertaken prior to June 1, 2013, as dividend (as against capital gains), and accordingly, were subjecting the amounts so distributed to DDT. The AAR in the aforesaid case, while dealing with the issue of taxation on buyback of shares ruled that the buyback of shares held by the Mauritian shareholder was a colorable device to evade the payment of DDT (capital gains was not taxable by virtue of the benefit under the Indo-Mauritius DTAA), which would have otherwise been payable on distribution of dividend under section 115-0 of the IT Act. However, in the case of *Goldman Sachs (India) Securities Private Limited*¹¹⁹, the Mumbai ITAT held that the buyback of shares cannot be recharacterised as dividend and the profits arising out of the buyback of shares should be taxed as ‘capital gains’. It further held that the provisions of buyback tax have been introduced with effect from June 1, 2013 and since the relevant year under consideration was before such amendment, the issue was to be decided as per the law prevailing prior to such an amendment.

The CBDT has *vide* Circular No. 03/2016 dated February 26, 2016 clarifies that the consideration received on buyback of shares between the period April 1, 2000 till May 31, 2013, would be treated as capital gains in the hands of the recipient in accordance with section 46A of the IT Act and no such amount shall be treated as dividend in view of the provisions of section 2(22)(iv) of the IT Act.

Indirect Tax

1. Taxable services used beyond the place of removal of the factory or other premises shall be eligible for rebate by way of refund

The CBEC, vide Notification No. 01/2016, dated February 03, 2016 has made amendments in Notification No. 41/2012-ST dated June 29, 2012. As per the amendments, definition of ‘place of removal’ has been omitted and taxable services used beyond the factory of production or any other premises of manufacture have been specified as services for which rebate by way of refund will be admissible. Prior to this amendment, specified services in case of excisable goods were defined as taxable services that have been used beyond the place of removal, for the export of the said goods. Also vide this Notification, the rate at which the rebate is calculated has been increased in certain cases.

2. Refund of Swachh Bharat Cess

The CBEC, vide Notification No. 02/2016, dated February 03, 2016 has made amendments in the Notification No. 12/2013-Service Tax, dated July 01, 2013. In the said notification, in paragraph 3, in sub-paragraph (III), after clause (b), the clause (ba) is inserted to provide that the SEZ Unit or the Developer shall be entitled to-

- (a) refund of the Swachh Bharat Cess paid on the specified services on which *ab-initio* exemption is admissible but not claimed; and
- (b) the refund of amount as determined by multiplying total service tax distributed to it in terms of clause (a) by effective rate of Swachh Bharat Cess and dividing the product by rate of service tax specified in section 66B of the Finance Act, 1994.

118. In Re, XYZ India (2012) 206 Taxman 631 (AAR)

119. Goldman Sachs (India) Securities Private Ltd. v. ITO (2015) 56 taxmann.com 130 (ITAT Mum)

GLOSSARY

ABBREVIATION	MEANING
AAR	Hon'ble Authority for Advance Rulings
ACIT	Learned Assistant Commissioner of Income Tax
AO	Learned Assessing Officer
APA	Advance Pricing Agreement
AY	Assessment Year
B2B	Business to Business
BC	Business Connection
BEPS	Base Erosion and Profit Shifting
CA	Companies Act, 1956
Customs Act	Customs Act, 1962
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
CIT	Learned Commissioner of Income Tax
CIT(A)	Learned Commissioner of Income Tax(Appeal)
CST	Central Sales Tax
CST Act	Central Sales Tax Act, 1956
CTA	Custom Tariff Act, 1975
DCIT	Learned Deputy Commissioner of Income Tax
DDIT/ DIT	Deputy Director of Income Tax
DRP	Dispute Resolution Panel
DTAA	Double Taxation Avoidance Agreement
EOU	Export Oriented Unit
EPC	Engineering , Procurement and Construction
FA	The Finance Act, 1994
FM	Hon'ble Finance Minister
FTS	Fees for Technical Services
FY	Financial Year
HC	Hon'ble High Court
HSN	Harmonised System of Nomenclature
INR	Indian Rupee
IRA	Indian Revenue Authorities
IT Act	Income Tax Act, 1961

GLOSSARY

ABBREVIATION	MEANING
ITO	Income Tax Officer
IT Rules	Income Tax Rules, 1962
ITAT	Hon'ble Income Tax Appellate ITAT
Ltd.	Limited
MAT	Minimum Alternate Tax
OECD	Organisation for Economic Co-operation and Development
PE	Permanent Establishment
POP Rules	Place of Provision of Service Rules, 2012
POT Rules	Point of Taxation Rules, 2011
Pvt.	Private
ROC	Registrar of Companies
SC	Hon'ble Supreme Court
SLP	Special Leave Petition
ST Rules	Service Tax Rules, 1994
TDS	Tax Deducted at Source
TPO	Transfer Pricing Officer
TRC	Tax Residency Certificate
UAE	United Arab Emirates
UK	United Kingdom
USA	United States of America
VAT	Value Added Tax
VAT Tribunal	Hon'ble VAT Tribunal



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