tax scout

Tax Scout | January – March, 2023

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Dear Readers,

We are delighted to present the latest issue of Tax Scout, our quarterly update on the recent developments in direct and indirect tax laws for the three months ending March 31, 2023.

In our main story, we have dealt with the benefits available to Startups in India from direct and indirect taxation perspective. In addition to the above story, we have also dealt with other important developments and judicial precedents in the field of taxation for this quarter along with analysis of the new FTP-2023 and Amendments to Finance Bill 2023.

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

Regards,
CYRIL SHROFF

Managing Partner
Cyril Amarchand Mangaldas

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Taxation of startups in India: Good times for great ideas and innovation

India's start-up boom over the course of this decade has fuelled a series of technological innovations, prompting the Hon'ble Prime Minister to call it the 'Techade' of India[1]. As per official data, India has the world's third largest startup ecosystem (after USA and China) with around 90,000 startups and 107 unicorn companies worth US$ 340 billion[2] approximately. A unicorn usually refers to any startup that has achieved a valuation of US$1 billion.

These startups have reportedly created over 900,000 jobs[3], a remarkable feat for a highly populated country like India. It benefits immensely from the rise of startups as they are expected to accelerate job creation in the country and the Government of India has been conscious of the need for a conducive environment for new and young entrepreneurs. To build a strong ecosystem for nurturing innovation, the government, launched the Startup India initiative in 2016 and has introduced several policy initiatives from time to time.

To incentivise and reduce the cost of operations for startups, the government has offered a number of crucial tax related concessions in addition to policy relaxations.

India as a HUB

India acts as a hub and serves as a home to prominent startup ventures. Instances of a few unicorn startups in India that have become very popular are Flipkart, Paytm, BharaPe, Razorpay, CRED, Urban Company, Zeta, etc. In 2022 India added around 22-23 unicorns to its hat, preceded by around 44-46 unicorns in 2021[4]. As per estimates, Indian startups raised approximately US$ 24-25 billion funding in 2022, compared to approximately US$ 37 billion in 2021.

Funding and mentorship – lifeblood of startups

While not every startup needs investment from external sources, many seek external investors when they intend to scale their business. Many startups, especially at an early stage are bootstrapped, i.e. self-funded through the founders' own savings, or through investments from friends and family. However, as they grow, it becomes vital for startups to access and tap into a global network of angel investors or high net worth individuals.

Startup incubators are highly sought after by startups as they offer much needed hand holding to build business from the ground up. These incubators are organisations that act as a springboard for early stage startups by providing them with valuable mentorship, space, networks and other resources.

Role of technology

The very essence of a startup is the innovative use of technology in various business processes. Automation and adoption of innovative technologies have improved every stage of business cycle, including internal communication, product development, inventory management, customer interface, placing of orders, delivery of product or service, client support, etc. Start-up initiative is particularly lauded for their pioneering efforts in using technology, which has led to market disruptive innovations and changed long held beliefs and habits. For

1 *https://www.business-standard.com/article/companies/this-decade-is-being-called-as-techade-of-india-pm-modi-at-startup-meet-122011500536_1.html*
2 *https://www.investindia.gov.in/indian-unicorn-landscape.*
3 *Economic Survey 2022-23.*
4 *https://techfundingnews.com/decoding-indian-tech-startup-ecosystem-10-largest-funding-rounds-of-2022/*

instance, Byju's disrupted the traditional approach to learning while Flipkart and Nykaa changed the conventional way of shopping.

Recognition as a Startup by Department for Promotion of Industry and Internal Trade ("DPIIT")

Under the Startup India initiative, eligible companies can get recognised as startups by DPIIT, which can open doors for them to be able to access a host of benefits including easier compliances under various labour laws, environment laws, fast-tracking of patent applications, tax concessions, easy winding up of company, etc.

The DPIIT *vide* a gazette notification[5] dated February 19, 2019 ("**DPIIT Notification**") laid down the following conditions to qualify as a 'startup'.

1. setup as a company or partnership firm or limited liability partnership;
2. turnover of any of the FY since incorporation does not exceed INR 1 billion[6];
3. entity is working towards:
   (a) innovation, development or improvement of products or processes or services, or
   (b) making it a scalable business model having a high potential to generate employment or create wealth
4. shall be considered as a start-up only upto ten years from date of incorporation.

The DPIIT Notification also laid down the constitution of the Inter-Ministerial Board ("**IMB**"), who have been empowered to validate startups to enable them to avail the various tax exemptions.

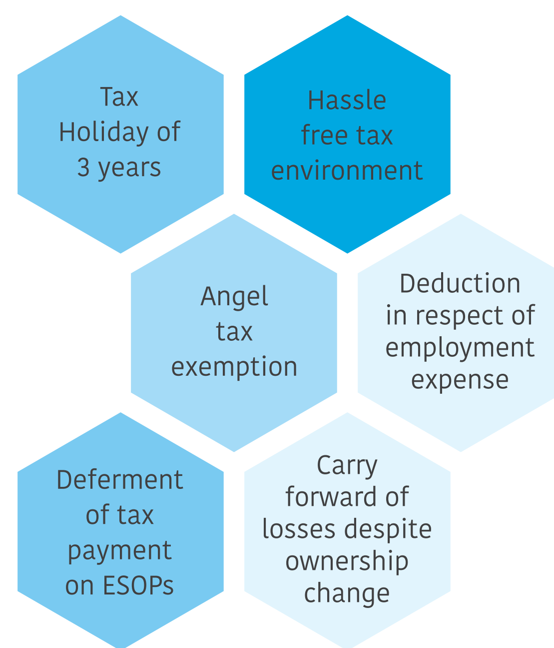
DPIIT *checklist for a startup*

- ☐ Type of entity
- ☐ Annual Turnover
- ☐ Innovative and scalable
- ☐ Age of entity

It may be noted that with each year, an increasing number of startups are getting registered with the DPIIT. The official[7] number of startups that have been recognised by the DPIIT over the previous 5-6 years is reproduced below:

Year	No. of startups
2017	5,147
2018	8,689
2019	11,328
2020	14,534
2021	20,089

Tax Benefits for Startups in India



1. ***Tax Holiday for 3 consecutive years***

   Under Section 80-IAC of IT Act, a deduction of 100% from profits is available to *"Eligible Startups"* for any three consecutive years at their option out of their initial ten years from inception. The said exemption is available to startups incorporated on or before April 1, 2024.

[5] *Notification No. G.S.R. 127(E) dated February 19, 2019*
[6] *Turnover is as defined under the Companies Act, 2013*
[7] *https://pib.gov.in/PressReleseDetailm.aspx?PRID=1881492*

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Table 1 - Criteria of a startup under section 80-IAC

Note: *Where the value of plant or machinery previously used for any purpose in India does not exceed 20% of the total value of the plant or machinery used in the startup, the condition specified in point (f) above shall be deemed to have been satisfied.*

While most of the conditions as reproduced above are similar to those laid down by DPIIT, a careful examination reveals that it excludes startups setup by partnership firms or startups whose turnover exceeds INR 1 Billion.

2. Exemption from Angel Tax

Angel tax refers to imposition of tax on the premium received by a closely-held company when issuing shares to an investor in excess of the fair market value ("**FMV**") of such shares. This provision was introduced as an anti-abuse measure to deter the use of unaccounted money and was referred to as angel tax due to its tax impact on the investments made by investors in newly set up companies.

The FMV can be determined as per book value of shares or as per valuation report of a merchant banker, whichever is higher, at the option of the company[8]. The valuation by a merchant banker is generally based on discounted value of the future cashflows of the startup which could be highly fluctuating due to a plethora of reasons. Startups, in such circumstances, are facing difficulties to justify their valuation before tax authorities, which potentially could damage their future business plans.

To provide much-needed relief to startups in this regard, the DPIIT *vide* DPIIT Notification outlined specific conditions for these to be eligible for exemption from Section 56(2)(viib) of IT Act. These conditions are enumerated below:

(a) It has been recognised by DPIIT as a "startup";

(b) Aggregate of share capital and share premium post proposed issuance of shares does not exceed INR 25 Crore. The share capital or share premium issued to a non-resident or venture capital company or venture capital fund or certain listed companies[9] shall be excluded;

(c) Startup has not invested in any of the following assets for non-business purposes for seven years from end of FY in which shares are issued at premium:

(i) Land or building;

(ii) Loans and advances;

[8] As per Rule 11UA of the IT Rules.

[9] a company whose shares are frequently traded within the meaning of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 and whose net worth on the last date of FY preceding the year in which the shares are issued exceeds INR 1 billion or its turnover for the FY preceding the year in which the shares are issued exceeds INR 2.5 billion.

(iii) Shares or securities or capital contribution in another entity;

(iv) Vehicles or other modes of transport exceeding INR 10 lakh;

(v) Jewellery; and

(vi) Drawings, paintings, sculptures, bullion, archaeological collections or any work of art.

In case of violation of any of the above conditions within such seven year period, post availment of exemption under Section 56(2)(viib) of IT Act, such exemption would get revoked with retrospective effect; and

(d) The startup shall file a self-declaration in Form 2 to DPIIT that it meets the above said conditions, which shall be forwarded by it to CBDT.

The above restrictions help to ensure that the company receiving investment is not a shell company setup solely to make use of exemption available to a startup. As per the above, a startup would also not be able to create a subsidiary company as that would entail capital contribution or investment in shares of a company that is prohibited, as above.

Pursuant to the above DPIIT Notification, the CBDT *vide* Notification[10] dated March 5, 2019 ("**CBDT Startup Notification**") reiterated that Section 56(2)(viib) shall not apply where consideration for issue of shares is received from a resident and the startup fulfils the conditions as laid down in the DPIIT Notification.

It is pertinent to note that in DPIIT Notification and CBDT Startup Notification, a Certificate of Eligible Business from IMB has not been mentioned as a pre-requisite to avail exemption from Section 56(2)(viib) of IT Act. This stance has also been confirmed by the government in answer to a question in the Lok Sabha on March 21, 2022[11] that IMB certificate is not a prerequisite for a startup to become exempt from Section 56(2)(viib) of IT Acts.

It has been observed that IMB grants a certificate of Eligible Business to qualify for various tax benefits (other than Section 56(2)(viib)) only when it is satisfied about a particular startup venture and less than 1% of the DPIIT recognised startups have IMB certification till date (discussed below). Therefore, since IMB certificate is not required to avail exemption under Section 56(2)(viib), that provides a relief to the DPIIT recognised startups.

The government, in response to a question in the Lok Sabha on March 21, 2022, revealed that the benefit of non-application of Section 56(2)(viib) were granted to around 5,476 startups that had filed declarations in Form 2 in 2021-22. .

Effect of Finance Act 2023 amendments

The government *vide* the Finance Act, 2023, has for the first time made the angel tax provisions i.e. Section 56(2)(viib) applicable in case of share issuance to a non-resident investor from FY 2023-24 onwards.

In case of startups, the provisions of erstwhile Section 56(2)(viib) (prior to amendment by Finance Act 2023) were not applicable due to the DPIIT Notification and CBDT Startup Notification, as discussed above. The DPIIT Notification does not mention 'resident' or 'non-resident' investor while notifying conditions for exemption (except for calculation of INR 25 crore threshold limit as discussed above). The subsequent CBDT Startup Notification states that Section 56(2)(viib) shall not apply in case of a resident investor where the company meets the conditions prescribed in the DPIIT Notification.

Therefore, ideally Section 56(2)(viib) shall continue to be not applicable in case of startups receiving share proceeds from a non-resident and filing the requisite declaration with DPIIT in Form 2 due to the language of Section 56(2)(viib) (as amended by Finance Act, 2023) and DPIIT Notification. However, an updated notification in this regard by the CBDT would clarify the issue.

It may be noted that startups obtain majority of their funding from foreign investors and issue shares usually at valuations higher than their market value. Furthermore, under Foreign Exchange Management Act ('**FEMA**') regulations, shares need to be valued as per any of the internationally accepted valuation methodologies and the FMV so determined denotes the minimum value at which the shares ought to be issued to non-resident investors. Whereas the provisions of Section 56(2)(viib) of IT Act prescribe an upper price limit for issue of shares to a non-resident. Valuation is a subjective exercise based on several assumptions and determining the economic worth of a business involves exercising judgment. The pricing requirements under both the regulations are in stark contrast due to which shares need to be issued to a non-resident at FMV itself, which could be a challenging task. An exemption to startups from Section 56(2)(viib) of IT Act will

[10] *Notification No. 13/2019/F. No. 370142/5/2018-TPL (Pt.)] dated March 5, 2019.*
[11] *AU2871.pdf (pqals.nic.in).*

go a long way in attracting foreign investors to Indian startups.

3. ***Carry forward of losses despite substantial change in ownership***

Under the provisions of Section 79 of IT Act, business losses from prior years cannot be carried forward and set off in the present year unless shares carrying atleast 51% of voting power are beneficially held by the same persons who held such voting power on the last day of the year of incurrence of such loss.

In this regard, there is a tax relief provided to the startups to the extent that even if there is change in shareholding beyond 51%, losses may still be carried forward and set off by them on fulfilment of following conditions:

(a) All shareholders carrying voting power at the end of FY in which loss is incurred continue to hold those shares on last day of present year; and

(b) The loss pertains to the ten[12] year period beginning from the year of incorporation of the startup.

A startup for the purpose of this provision shall imply a startup that meets the definition of *"Eligible Startup"* as per Section 80-IAC of IT Act i.e. which meets the conditions from serial no. a to d in Table 1 above.

4. ***Deferment of taxes on ESOPs***

Employee Stock Option Plans ("**ESOP**") have become a significant component of the employee compensation structure in changing times especially in case of startups. Issuance of ESOPs allows the founders of startups to employ talented staff with moderate pay packages with a major component of employee remuneration consisting of ESOPs.

The tax treatment of ESOPs at the time of exercise under the income tax provisions is as follows:

(a) As a 'Perquisite' in the hands of employee under Section 17(2)(vi) of IT Act at FMV less the exercise price; and

(b) Employer shall withhold TDS under Section 192 on such perquisite.

Tax liability arising and becoming payable at the time of exercise of options can be burdensome for an employee and even the tax outgo in cash can be a problem. There are high chances of a startup failing to develop a market and it may cease to exist on a later date in which case the tax already borne creates an unfavourable additional tax burden on the employee. At the time of exercise of the stock options, there is only a conversion of the options into shares and there are not many avenues to sell the shares of a startup at that time. Therefore, in order to address this issue, the payment of tax on ESOPs and withholding of taxes therefrom have been deferred for employees of startups such that tax will be payable within 14 days from the earlier of the following:

(i) Expiry of five years from the end of relevant FY in which options are exercised, or

(ii) Date of sale of shares by the employee, or

(iii) Date on which employee ceases to be employee of the startup.

A startup for the purpose of this provision shall imply a startup that meets the definition of *"Eligible Startup"* as per Section 80-IAC of IT Act i.e., which meets the conditions from serial no. a to d in Table 1 above.

5. ***Additional employee cost deduction for new employees***

There is an additional tax benefit recently introduced for hiring of employees in case of all assessees on whom tax audit is applicable under Section 44AB[13] of IT Act. Such tax benefit can be availed by a startup as well, which is subject to tax audit under Section 44AB of IT Act. Under the provisions of Section 80JJAA of IT Act, an additional deduction equivalent to 30% of additional employee cost can be availed for three AYs including the year in which a new employee is hired.

For this purpose, additional employee cost implies remuneration payable to to "additional employees added during the previous year. The term 'additional employees' connotes the increase in aggregate number of employees during the current year from the total headcount of employees as employed on last day of preceding year. The tax authorities have tried to ensure that additional deduction shall be available only where there is an overall increase in aggregate number of employees and not just where employees have got hired to offset the ones who leave during the year.

The new employee shall also need to meet the following criteria:

(a) salary does not exceed INR 25,000 per month; and

[12] *As amended by Finance Act, 2023.*
[13] *Where turnover from business exceeds INR 1 crore.*

(b) employed for atleast 240 days[14] in a year, failing which the person would be considered as new employee only in next year once the 240-day employment condition is met.

For instance, in the first year of a new business, emoluments payable to new employees hired shall constitute additional employee cost and shall be eligible for additional 30% deduction.

6. *Goods and Services Tax ("GST")*

While the Government has not come up with outright GST exemption for all startups, it has provided exemption to services provided by a class of startups ("Incubatee"), who are located within the premises of a technology business incubator or a science and technology entrepreneurship park ("**Incubator**") recognised by the National Science and Technology Entrepreneurship Development Board (NSTEDB) of the Department of Science and Technology, Government of India. Such Incubatee must have entered into an agreement with such Incubator to enable itself to develop and produce hi-tech and innovative products. The exemption is available when (a) the total turnover had not exceeded INR 5 Million during the preceding FY; and (b) a period of three years has not elapsed from the date of entering into the agreement.

The services provided by the Incubator or bio-incubators recognised by the Biotechnology Industry Research Assistance Council, have also been exempted.

Apart from the above, many states have also introduced their startup policy, wherein benefit in form of reimbursement of State GST has been introduced. For example, in Karnataka, the startup with a maximum annual turnover of INR 10 Million shall be eligible for 100% reimbursement of annual SGST, within first three years of it being incubated.

Government Policy Initiatives for Startups

In addition to the various tax benefits, there are also multiple policy initiatives taken by the government to support the startup ecosystem in India, some of which are captured below:

Fund of Funds for Startups (FFS) Scheme: Established in 2016 with corpus of INR 10,000 crore which funds AIFs who invest 2 times the amount in Startups.

Startup India Seed Fund Scheme (SISFS): Financial assistance to Startups for proof of concept, prototype development, trials, market entry etc; corpus of 945 cores for 4 years w.e.f April 1, 2021.

Credit Guarantee Scheme for Startups (CGSS): Notifed in 2022 for collateral free loans to Startups; 10 crore ceiling per case.

Startup India Hub: Virtual platform launched in 2017 by Government for investors, mentors, incubators, governmrnt etc to connect and engage.

National Startup Advisory Council: Setup by government in 2020 to advise the government on measures needed to build a strong ecosystem for Startups in India.

[14] *180 days in case of a company manufacturing apparel or footwear or leather products.*

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Various other states like Maharashtra, Uttar Pradesh, Gujarat, etc., have also introduced startup policies. Such state startup policy provides benefit in the form of marketing cost reimbursement, patent filing reimbursements, subject to the fulfilment of eligibility criteria. Such policy also provides for special establishment for incubation, startup funding, networking, etc. Therefore, startups may priorities setting up in a specific state for their operation in the initial years to avail additional benefits available in such policies.

Initiative by Tax Authorities:

A. *Setup of Start-up Cells*

In order to redress tax related grievances of Start-ups, a Start-up Cell i.e. a five-member special cell was constituted by the CBDT on August 30, 2019[15] consisting of various ex-officio members of the income tax department. Startup entities can also approach these cells for speedy resolution of their grievances. The Start-up Cells have been made approachable such that they can be contacted through their designated email ids[16] as well.

B. *Resolving grievances within stipulated timelines*

The CBDT *vide* office order[17] dated September 23, 2019 also laid down certain timelines for handling of grievances of DPIIT registered startups:

(a) a Preliminary Action Taken Report on grievances received shall be prepared and sent to the CBDT within one working day of being called upon to do so;

(b) a Final Action Taken Report shall be sent to CBDT within three working days of being called upon by the latter.

It has also been recommended that the Principal Chief Commissioners should constitute Startup Cells at the local level for redressal of grievances.

Challenges Faced by Start-ups

Over 95,876 entities have got registered as startups till date as per the latest figures available on government's portal[18]. Whereas by February 2022, approximately 412[19] DPIIT recognised startups were granted IMB certification for availment of tax benefits. Hence, less than 1% of the DPIIT recognised startups have IMB certification. Availment of various tax benefits for startups (with the exception of Section 56(2)(viib), as discussed above) require a startup to hold a certificate of Eligible Business from IMB. The above data shows that a large number of startups are not yet eligible for availing the tax benefits meant for startups.

There have been expectations from the government that the process of obtaining a certificate from IMB may be relaxed. However, the government has clarified *vide* its response to a question in the Lok Sabha[20] on March 21, 2022 that there is no proposal to alter the requirement for obtaining IMB certification for availing tax benefits.

On scrutiny of minutes of the meeting of the IMB, it was observed that certain startups could not furnish reliable information to be able to ascertain the possible innovation, scope of scalability and wealth generation of the product/services offered by them, leading to refusal of certification.

It may be appreciated that there is no definition of the terms 'innovation' or 'scalable' business model for employment generation or wealth generation and it is also not possible to provide generic definition with any specific criteria, quantitative or qualitative. Further, grant of any tax benefits is a largesse bestowed by the government, which should be extended to accomplished startups. However, in the same way, the government cannot be expected to extend the tax benefits of such nature indiscriminately.

It is advisable to simplify and streamline the process for IMB certification. The qualitative threshold to qualify as a startup for obtaining tax benefits may be difficult to be compromised with as its purpose is to ensure that such tax benefits are provided only in deserving cases. However, the various standards and criteria that need to be satisfied to become eligible for IMB certifications may be simplified and expressed in more clear and well defined terms so that more and more startups can make efforts to reach up to that level and make an application to IMB without any fear or suspicion.

[15] *Circular No. 22/ 2019 dated August 30, 2019.*
[16] *Startupcell.cbdt@gov.in.*
[17] *Office Order Number F. No. 173/149/2019-ITA-I, dated September 23, 2019.*
[18] *https://www.startupindia.gov.in/.*
[19] *Answer to Lok Sabha question no. 2871 on March 21, 2022.*
[20] *Answer to Lok Sabha question no. 2871 on March 21, 2022.*

Consideration paid under hire purchase agreement is not in nature of interest

Introduction

In the case of ***Muthoot Leasing and Financing Limited and another***[21], the SC held that the consideration received by a taxpayer under hire purchase agreements would not qualify as 'interest' as defined under the Interest Tax Act, 1974 (the "**Interest Act**"), and accordingly no tax was leviable. The SC also cautioned against placing reliance on precedents rendered in context of other tax enactments, disregarding the object and purposes of the relevant statutes.

Facts

The SC was apprised of a batch of matters in appeal, involving a common question, from the judgments of various HCs. The facts leading up to the appeal were that the taxpayers, ("**Assessees**") being nonbanking financing corporations (were reclassified as hire purchase finance companies) had entered into hire purchase agreements with respect to certain vehicles. Pursuant to such agreements, the Assessees were in receipt of certain hire purchase instalments.

The common question which arose in the case of the Assessees pertained to the interest component on the hire-purchase instalments -- whether such instalments should be subject to tax under the Interest Act, which, *inter alia,* seeks to tax interest received on loans and advances.

The ITAT observed that the hire-purchase agreements ---after evaluating the terms and conditions therein -- were in nature of a composite transaction i.e., it had elements of both sale and bailment. Accordingly, the ITAT ruled in favour of the Assessees and held that the hire purchase agreements were distinguishable for a pure loans and advances. Thus, the interest component of the hire purchase instalments could not be brought to tax under the Interest Act.

However, the HC reversed the order of the ITAT and observed that though the impugned transactions were styled as hire purchase agreements, they were in nature of financing arrangements. Reliance was placed on the SC decision of *Sundaram Finance Limited*[22]. The HC held that the interest component of the hire purchase instalments should be subject to tax under the Interest Act. Aggrieved of the order of the HC, the Assessees appealed before the SC.

Issue

Whether the interest component under the hire-purchase instalments can be subject to tax under the Interest Act?

Arguments

It was argued on behalf of the Assessees that 'interest' as defined under the Act, only covered interest income arising from 'loans and advances'. Accordingly, it was asserted that the hire-purchase instalments were in nature of rent, instead of interest. Thus, the provisions of the Interest Act should not be applicable.

On the other hands, the IRA placed reliance on the SC decision in the case of *Sundaram Finance Limited (supra)* and argued that the hire purchase agreements were in nature of financing arrangements. Thus, the 'finance charges' included in the hire

[21] Muthoot Leasing and Financing Limited and another v CIT, Civil Appeal No. 10201-10202 of 2010 (Supreme Court).
[22] Sundaram Finance Limited v State of Kerala and Another AIR 1966 SC 1178.

purchase instalments, being in the nature of interest, should be brough to tax under the Interest Act.

Decision

The SC at the outset, examined the scope of the term 'interest' as defined under the Interest Act and concluded that it should be narrowly interpreted to cover only interest income arising on loans and advance. The SC placed reliance on its decision in the case of *Sahara India Savings and Investment Corporation Limited*[23] *and State Bank of Patiala*[24], wherein the SC clarified that the scope of the term interest under the Interest Act, was limited to interest directly arising from loans and advances and not any other kind of interest.

Subsequently, the SC analysed the nature of the hire-purchase agreements and observed that such agreements have two essential elements, namely elements of bailment and sale, which only crystallises once the option to purchase has been exercised. Thus, even though arguably there may be an element of interest in the hire purchase instalments, such payments are essentially in the nature of rent, rather than interest. Furthermore, the SC highlighted that even if the hirer, in such transaction are recorded as the owner of a vehicle for the purposes of the Motor Vehicle Act, 1988, the same did not dilute the rights of the Assesses with respect to the title of the vehicle. Thus, the SC held that in the case at hand, the hire purchase agreement are complex transactions involving corresponding rights of the parties and cannot be regarded as simple transactions involving loans or advances.

Accordingly, the SC reversed the order of the HC and held that the hire purchase instalments cannot be regarded as interest arising from loan and advances. Thus, the same are not taxable under the Act, as interest.

Separately, the SC also distinguished its decision in the case of *Sundaram Finance Limited (supra),* which was relied upon by the HC in its judgment. In this regard, the SC clarified that in *Sundaram Finance Limited*, it had discussed the nature of hire purchase agreements in the context of Madras Sales Tax Act, 1939, which was very different in its scope as compared to the Act. The SC observed that what is sought to be brought within the tax nets of a statute depends on the language of the charging Section. Therefore, the SC cautioned that one should be very careful in placing reliance on precedent rendered in context of other tax enactments.

Significant Takeaways

While this decision has been rendered in the context of the Interest Act, which has ceased to operate with effect from March 31, 2000, this decision resolves the longstanding litigation with regards to applicability of the Act to hire purchase agreements.

One of the most relevant takeaways from this judgment is that the taxpayers (and their advisors) should be cautious while placing reliance on precedent rendered in context of other tax enactments. Pursuant to SC's *obiter*, one should give due regard to the scope of the charging section and, objectives and purposes of a statute, in the context of which judgment is rendered, before applying a judicial precedent to any other statute. For example, this decision, which deals with the scope of the term 'interest' under the Interest Act, may not be relevant to determine the scope of the same term under the IT Act, which defines interest in a very broad manner.[25]

In recent context, the SC in the case of *M/s BPL Limited*[26] had held that listed shares with transfer restrictions qualified as quoted shares, under the erstwhile gift tax regime. While this decision may impact the interpretation of the term 'unquoted shares' as used in the IT Act, caution, as enunciated by the SC, should be exercised by the taxpayer before relying on this decision in context of the IT Act.

“ Hire purchase instalments not akin to interest on loans and advances. ”

[23] CIT v. Sahara India Savings and Investment Corporation Limited (2009) 17 SCC 43.
[24] State Bank of Patiala v CIT (2015) 15 SCC 483.
[25] See State Bank of Patiala v CIT (2015) 15 SCC 483.
[26] Deputy Commissioner of Gift Tax v. M/s BPL Limited Civil Appeal No. 3256 of 2016 & Anr.

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Payroll/ Human Resource Services are not in the nature of FTS

Introduction

In the case of ***IBM India Pvt. Ltd.,***[27] the Karnataka HC held that payments made to a group entity for outsourcing of payroll/ human resource services were not in the nature of FTS.

Facts

IBM India Pvt. Ltd. ("**Assessee**" or "**IBM India**") is a company engaged in the business of providing information technology services. IBM USA had entered into a global arrangement with Procter and Gamble ("**P&G**"), USA for rendering payroll related services to P&G USA and its group companies. As a companion agreement to this, IBM India also entered into an agreement with P&G India.

The payroll related services and certain human resource services to be rendered by IBM India to P&G India were outsourced to IBM Philippines. On assessment, the IRA took the view that the payments made by the Assessee to IBM, Philippines for payroll services were in the nature of FTS and chargeable to tax in India. Since, the Assessee had made such payments to IBM Philippines without deducting TDS under section 195 of the IT Act, it was treated as 'assessee in default' under section 201 of the IT Act.

Being aggrieved, an appeal was filed before the CIT(A), who confirmed the order. Thereafter, an appeal was filed before the ITAT, Bangalore, wherein, it was held by the ITAT that the payments made by the Assessee were in the nature of business profits in the hands of IBM, Philippines and thus, were not chargeable to tax under the India-Philippines DTAA, in the absence of a permanent establishment ("**PE**") in India. Hence, no tax was required to be deducted.

The IRA decided to file the instant appeal before the Karnataka HC.

Issue

Whether the services rendered by IBM Philippines to the Assessee were in the nature of FTS?

Arguments

The IRA submitted that the services rendered by IBM Philippines fall under the category of 'managerial and consultancy services.' Data management is also one of the services rendered and it would fall in the category of 'technical services'. Therefore, they would be covered under the definition of FTS, as per Explanation 2 to section 9(1)(vii) of the IT Act. Accordingly, such income would be deemed to accrue in India as per section 5(2)(b) of the IT Act and thus, be chargeable to tax in India.

On the other hand, the Assessee maintained that IBM Philippines was not rendering any technical services to it. It was merely paying service charges to IBM Philippines for the services rendered by IBM Philippines to P&G India, on behalf of the Assessee.

Decision

The Karnataka HC noted that the Assessee made payments to IBM Philippines out of the amount it received from P&G India. The *modus operandi* made it clear that IBM Philippines was merely working as a sub-contractor under IBM India. IBM Philippines was thus, earning profit by rendering service to P&G India and not providing any technical services to the Assessee. Accordingly, the Karnataka HC held that the payments received by IBM Philippines from the Assessee were in the nature of business income. As IBM Philippines did not have a PE in India., the said income was not chargeable to tax in India under the India-Philippines DTAA.

The Karnataka HC accordingly held that the Assessee was not required to deduct TDS under section 195 of the IT Act on the said payments and thus, could not be deemed as an 'assessee in default'.

Significant Takeaways

The taxability of FTS has been a long-standing litigious issue in India. FTS has been defined under the IT Act to include any 'payments received for rendering technical, consultancy or managerial services'. However, the terms 'technical,' 'consultancy' and "managerial' have not been defined under the IT Act. The absence of a specific delineation of the boundaries between these terms has given rise to many disputes between taxpayers and tax authorities. Although many Courts and certain tribunals have tried to deal with these contentious issues in their own way, lack of unanimous application of such definitions creates unnecessary confusion.

Under India's DTAAs, business income of a non-resident taxpayer is taxable in India only if such taxpayer has a PE in India and the business income is attributable to the PE. However, payments in the nature of FTS are taxable even in the absence of a PE. While tax authorities often attempt to broaden the scope of FTS to

[27] The Director of Income-Tax, International Taxation v. IBM India Pvt. Ltd. (ITA No. 218/2014) (Karnataka HC).

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include even other support services within its ambit, Indian Courts and tribunals have maintained that the terms 'technical', 'consultancy' and 'managerial' have to be understood in their usage in common parlance by persons engaged in business.[28] When the nature services do not satisfy the ordinary meaning of these terms (such as in the instant case), the income should be taxable as business income only.

Thus, in the absence of a PE in India, it will be difficult to expect a foreign entity to pay taxes on the income earned by it. Having said that, this remains a contentious issue and more often than not, Indian payers or non-resident recipients end up in litigation with Indian tax authorities. This decision provides the much-needed clarity and reiterates the position regarding taxability of a non-resident.

> **"Payroll or human resource services are not technical services and, therefore, payment received for such services is business income and in the absence of a PE, no tax is required to be withheld in India."**

[28] *See* GVK Industries Ltd. V. ITO [2015] 371 ITR 453 (SC); Adidas Sourcing Ltd. V. ADIT(IT) [2013] 21 ITR(T) 697 (Delhi-ITAT).

Tax Residency Certificate is sufficient evidence of residence to claim benefits under a DTAA

Introduction

In the case of ***Blackstone Capital Partner (Singapore)***[29], the Delhi HC held that the IRA cannot go behind a Tax Residency Certificate ("**TRC**") issued by other jurisdictions and it would be sufficient evidence to claim tax benefits under a DTAA.

Facts

Blackstone Capital Partners (Singapore) VI FDI Three Pte. Ltd. ("**Petitioner**"), a Singapore resident, had acquired shares of Agile Sub Assembly Pvt. Ltd. ("**Agile**"), an Indian company, in the year 2013. The Petitioner sold Agile shares to various parties in AY 2016-17. While filing the return of income for AY 2016-17, the Petitioner claimed that capital gains arising from the sale of shares were not taxable in India by virtue of the benefit available under Article 13(4) of the India-Singapore DTAA (as it stood then). The Petitioner presented a valid TRC issued by authorities in Singapore to claim the benefit. Based on such disclosures, the Petitioner's return was processed under Section 143(1) of the IT Act with no demand.

In March 2021, a reassessment notice was issued to the Petitioner. Upon receiving such notice, the Petitioner requested for reasons for the reopening of assessment and filed detailed objections to the stated reasons. The IRA passed an order rejecting the objections and held that the reassessment was initiated on valid grounds. Aggrieved, the Petitioner filed a writ petition against the order before the Delhi HC.

Issues[30]

1. Whether Petitioner was a shell/conduit company?
2. Whether IRA can go behind a valid TRC issued by competent authority of a foreign jurisdiction to issue re-assessment notice to determine residency status, treaty applicability and legal ownership?

Arguments

The Respondent argued that the Petitioner was a shell company with no real nexus to Singapore. It contended that the ultimate holding company of the Petitioner, located in the USA, was the actual beneficial owner of the shares and that the Petitioner was just a conduit company set up to avail the DTAA benefits. It claimed that the India-USA DTAA provided no relief to a taxpayer with respect to capital gains and hence, the gains earned by the Petitioner shall be taxable in India. Since the Petitioner was founded with only USD 1 share capital, the Respondent relied on this information to contend that the former was indeed a shell company. The Respondent further relied on Section 90(4) of the IT Act to state that the said provision talks about TRC as an 'eligibility condition' and not as a 'sufficient evidence'.

On the other hand, the Petitioner argued that limitation of benefits ("**LOB**") clause under the India-Singapore DTAA had been satisfied, and thus, it could not be regarded as a shell/ conduit company. The Petitioner further contended that it was holding a valid TRC issued by the tax authorities of Singapore and, therefore, it was a non-resident for the purposes of IT Act and eligible to claim benefits under the India-Singapore DTAA. Under Article 13(4) of the India-Singapore DTAA (as it stood then), capital gains arising to a resident of Singapore were taxable only in Singapore. Further, no beneficial ownership requirement needed to be fulfilled to claim such benefit. The Petitioner relied on a Finance Ministry press release[31] wherein it was clarified that DTAA benefits could be claimed solely on the basis of a TRC. It further placed reliance on the case of *Azadi Bachao Andolan*[32] and *Vodafone International Holdings B.V.*[33] wherein the SC had upheld the legal position that TRC was a sufficient evidence to show residency of a non-resident in another contracting state.

Judgment

The Delhi HC noted that the India-Singapore DTAA included a LOB clause to limit the application of the DTAA to entities that are not shell/ conduit companies. The said clause provides for an objective test whereby a resident of Singapore is deemed not to be a shell/conduit company if its total annual expenditure on operations in Singapore is equal to or more than SGD 200,000, in the immediately preceding period of 24 months from the date when capital gains arise. The HC ruled that in the instant case, the Petitioner had placed enough evidence including its audited financials and a chartered accountant's certificate to show that it had satisfied the conditions imposed under the LOB clause. This had also been accepted by the authorities in Singapore.

29 Blackstone Capital Partners (Singapore) VI FDI Three Pte. Ltd. v. ACIT, [2023/DHC/000634]
30 Note: This update deals only with the substantive issues.
31 Finance Ministry's Clarification on Tax Residency Certificate, Press Release dated 01/03/2013
32 Union of India v. Azadi Bachao Andolan, [2003] 132 Taxman 373 (SC).
33 Vodafone International Holdings B.V. v. Union of India and Anr., (2012) 6 SCC 613 (SC).

Thus, the Petitioner was a genuine entity and not a shell/conduit company. Accordingly, the IRA could not claim that the Petitioner was engaged in treaty shopping.

The Delhi HC also held that the requirement of fulfilling the beneficial ownership test was only applicable to DTAA provisions in relation to interest, dividend and royalty and no such requirement has been included for capital gains. The HC further ruled that the IRA could not go behind a TRC issued by the tax authorities of another jurisdiction to check their validity. Such an attempt of the IRA is wholly contrary to the Indian government's repeated assurances to the foreign investors through press releases and legislative amendments and based on judicial precedents[34]. The HC held that TRC is an evidence of conclusive nature and is the only evidence required to be eligible for DTAA benefits. In the instant case, the tax authorities of Singapore had issued a TRC to the Petitioner after a detailed analysis and hence, the IRA could not question the validity of such TRC.

Hence, it held that there was no tax liability on the Petitioner in India *vis-à-vis* capital gains from sale of shares and hence, the re-assessment proceedings were without any jurisdiction. The reassessment notice and the order disposing the Petitioner's objections were accordingly quashed.

Significant Takeaways

Historically, India-Singapore DTAA exempted capital gains arising to Singaporean investors from the sale of shares of Indian companies, from being taxed in India. As a result, many investors used to structure their investments in India through entities incorporated in Singapore, to claim this benefit. This prompted the IRA to renegotiate its tax treaty with Singapore (and other countries), to, *inter alia*, acquire the right to tax capital gains arising from sale of shares of Indian companies and to introduce a LOB clause, which excluded any shell/conduit company to claim certain benefits under the India-Singapore DTAA. Further, a grandfathering clause was provided to provide exemption to investments made before April 1, 2017.

Despite the inclusion of grandfathering provisions, the IRA has repeatedly sought to question grandfathered transactions, alleging them to be sham or undertaken for the sole purpose of treaty shopping. This decision comes as a welcome respite to taxpayers by clarifying that the beneficial ownership test could not be read into Article 13 of the India-Singapore DTAA and the TRC was sufficient evidence for a taxpayer to be eligible to claim DTAA benefits. Similar observations were also made by the Mumbai ITAT in the case of *Blackstone Fp*[35] where the Mumbai ITAT opined that the concept of beneficial ownership was foreign to Article 13 *(Capital Gains)* of the India-Mauritius DTAA (which is similar to the India-Singapore DTAA) and if such a test was read into Article 13, it may be construed as rewriting of the DTAA provisions rather than its permissible interpretation.

This decision is also aligned with the internationally accepted principles of treaty interpretation. The HC read the provisions of the DTAA as is, to hold that the test of beneficial ownership did not apply to capital gains as it was not mentioned in the provisions of the DTAA. It also respected the provisions of DTAA and related circulars issued by the CBDT, which clarified that TRC would be a sufficient evidence and availed such treaty benefits to the Petitioner.

While the given ruling has laid down many important principles, the introduction of General Anti-Avoidance Rules ("**GAAR**") from AY 2018-19 might change Courts' stance on similar issues in the future. The GAAR provisions enable the IRA to deny DTAA benefits on transactions that were entered into to avoid paying taxes. It will be interesting to see how the Courts respond to such a situation.

" Tax Residency Certificate to serve as a conclusive evidence to claim benefits under DTAA. "

[34] Circular No. 682 dated 30/03/1994; Circular No. 789 dated 13/04/2000.
[35] Blackstone FP Capital Partners Mauritius V Ltd. v. DCIT, ITA Nos. 981 and 1725/Mum/2021. It may be noted that the interim order where the ITAT made such observations, has subsequently been recalled by the Mumbai ITAT. This matter is currently pending before the Mumbai ITAT.

Delhi HC quashes validity of assessment order passed in the name of amalgamating company after amalgamation

Introduction

In the case of ***Sony Mobile Communications India Pvt Ltd.*** (now merged with Sony India Pvt. Ltd.)[36], the Delhi HC has quashed the assessment order passed in the name of amalgamating company after amalgamation.

Facts

Sony Ericsson Mobile Communications India Pvt. Ltd. (name changed to Sony Mobile Communications India Pvt. Ltd.) ("**Assessee**" or "**Sony Mobile**") merged into Sony India Pvt. Ltd. ("**Sony India**") by virtue of scheme of amalgamation approved by Delhi HC via July 2013 order. The amalgamation was effective from April 1, 2013.

A notice under Section 143(2) of the IT Act for AY 2010-11 for the assessment proceedings was issued to Sony Mobile in August 2011. A detailed questionnaire was also issued in May 2012.

On December 06, 2013, the IRA was informed of the fact of merger along with submission of the scheme of amalgamation.

The assessment was referred to the TPO who made an upward adjustment to the taxable income filed by the Assessee and the draft assessment order was passed by the AO on March 31, 2014. The Assessee filed objections before the DRP, which were dismissed by it and hence, the final assessment order was passed with additions on December 22, 2014.

The Assessee filed an appeal before the ITAT, wherein it raised the additional ground that the assessment order has been passed on the Assessee, which does even exist in the eyes of law after the merger with Sony India. . The ITAT allowed the appeal holding that the assessment order was issued to a non-existing entity and hence, it is null and void, and that such a defect cannot be cured under Section 292B of the IT Act.

Aggrieved by the order of ITAT, the IRA filed an appeal before the Delhi HC.

Issue

Whether the assessment order passed by the AO in the name of the amalgamating company, after amalgamation should be considered valid?

Arguments

The IRA submitted that the amalgamating company dissolves upon amalgamation and its liability to tax can be determined by perusing the amalgamated company. In the scheme of amalgamation too, the liabilities of the amalgamating company had to be taken over by the amalgamated company, along with the burden of the proceedings, which had commenced against the amalgamating company.

The IRA also submitted that there was a distinction between the SC's judgment on Maruti Suzuki India Ltd. ("**Maruti Suzuki**")[37] where the notice itself was issued in the name of a non-existent company, and the instant case, where the notice was issued while the company still existed and an amalgamation had not taken place. The IRA also placed reliance on the recent judgment of SC in the case of Mahagun Realtors (P.) Ltd[38] ("**Mahagun Realtors**").

The Assessee, on the other hand, placed reliance on the judgment of *Maruti Suzuki* and also distinguished its case from *Mahagun Realtors*.

Judgment

The Delhi HC observed that the notice for initiating assessment proceedings was correctly issued in the year 2011 in the name of amalgamating company, since the amalgamation had not occurred at that time. However, even after the intimation of merger was made to the AO in the year 2013, the AO did not acknowledge the same. The Delhi HC noted that even though the DRP had also noticed the fact of amalgamation during the hearing of the objections, the AO continued to pass the assessment order in the name of non-existent entity.

The Delhi HC distinguished the instant case from *Mahagun Realtors* by pointing out certain issues, which existed in the case of *Mahagun Realtors* i.e. (a) no intimation made by the Assessee regarding amalgamation; (b) the column in the ROI regarding reorganisation was left blank; (c) representation by the representatives that the erstwhile company is in existence. All the above issues in the case of *Mahagun Realtors* had led the SC to the decision that the order passed by AO is valid.

As against the above, in the instant case, the AO was intimated regarding the amalgamation in July 2013 and a copy of amalgamation scheme was shared with him. However, he continued to issue the draft assessment order in the name of the erstwhile company. Further, even after the DRP highlighted the issue of amalgamation, the AO did not correct the error.

[36] Commissioner Of Income Tax V. Sony Mobile Communications Ind Pvt Ltd (Now merged with Sony India Pvt. Ltd.) [2023/DHC/001366] [TS-80-HC-2023(DEL)].
[37] CIT v. Maruti Suzuki India Ltd. [2019] 107 taxmann.com 375/265 Taxman 515/416 ITR 613 (SC).
[38] Principal Commissioner of Income-tax v. Mahagun Realtors (P.) Ltd. [2022] 137 taxmann.com 91 (SC).

Basis the above, the Delhi HC relied on *Maruti Suzuki* and held that the mistake committed by the AO cannot be cured under Section 292B of the IT Act. Accordingly, the assessment order passed by the AO in the name of amalgamating company, was held to be invalid.

Significant Takeaways

The Delhi HC in this case has held that the mistake committed by the AO by passing the assessment order in the name of amalgamating company cannot be cured under Section 292B of the IT Act. In doing so, the HC relied on *Maruti Suzuki*. Further, the HC also compared SC's judgment in the case of *Mahagun Realtors* and it appreciated that the precise finding in that decision cannot be applied in the instant case due to the difference in conduct and behaviour of the assesses in the two cases.

The Delhi HC has shown that the Assessee had provided true and fair disclosure to the AO in the instant case, and hence, it was not possible for the AO to take refuge by relying on *Mahagun Realtors*. The Delhi HC acknowledged the importance of variance in facts in the two cases and has provided just treatment to the Assessee. This judgment would again open doors for the other assessees who may had got disheartened after the SC's judgment in *Mahagun Realtors*.

As far as the current issue is concerned, it is relevant to mention that the controversy regarding the validity of the assessment order in case of succession has already been amended by FA 2022. Section 170(2A) has been inserted in the IT Act to clarify that in case of succession, any proceedings made or initiated on the predecessor during the course of pendency of such succession shall be deemed to have been made on the successor. Thus, this Delhi HC judgment cannot be relied upon in the future. However, it would still be relevant for the prior years.

“ Delhi HC rules that the assessment order issued on amalgamating company is invalid since the AO was informed about the amalgamation. ”

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No depreciation on toll roads and bridges for concessionaires

Introduction

In the case of ***L&T Infrastructure Development Projects Limited***[39], the Madras HC held that construction companies entering into concessionaire agreements with the Government do not have ownership over toll roads and toll bridges. Therefore, they are neither tangible nor intangible assets belonging to construction companies and accordingly, the construction companies are not eligible for depreciation.

Facts

L&T Infrastructure Development Projects Limited ("**Assessee**") entered into agreement with the Government to construct a toll bridge across the Narmada river in Gujarat on National Highway 8. The agreement was in the nature of Build, Operate and Transfer ("**BOT**") Model, wherein the Assessee was allowed to collect toll from the vehicles plying on the roads/bridges developed by them for a certain number of years and thereafter, the said roads/bridges should be transferred to the Government.

The Assessee had capitalised the cost incurred in the development of said toll bridge/road and claimed depreciation at the rate of 25% by treating it as 'plants and machinery'. The IRA characterised the toll bridges as 'buildings' and restricted the depreciation to 10%. Thereafter, Section 263 of the IT Act was invoked to hold that the Assessee was not entitled to any depreciation at all. On appeal, the ITAT, however, held that the Assessee was entitled to claim depreciation at 10% as the assets were in the natured of 'building'.

Aggrieved by the order of ITAT, the IRA and the Assessee filed cross appeals before the Madras HC.

Issue

Whether the Assessee is entitled to claim depreciation on the toll roads/bridges constructed by it?

Arguments

The Assessee submitted that the term 'owned' as occurring in Section 32(1) of the IT Act must be assigned a wider meaning. Anyone in possession of a property in his own title exercising such dominion over the property to the exclusion of others should be allowed to claim depreciation so long as that person is able to enjoy usufruct arising from such properties even though a formal deed of title may not have been executed as contemplated under the Transfer of Property Act, the Registration Act, etc. The Assessee relied on the decision of ***Podar Cements Ltd***[40] wherein the rental income from the house property was held to be 'income from house property' even though the taxpayer was not the legal owner of the property under the Transfer of Property Act.

The Assessee further submitted that the toll bridges/roads should be considered as 'plants' and not as 'buildings' by arguing that there is a difference between a premise where a business is carried out and a plant with which the business is carried out. It submitted that the Assessee was not carrying on a separate business on the toll bridges/roads but collecting toll from the bridges/roads constructed by it was its main business. It submitted that the toll roads/bridges are not just roads/bridges but are a part of the project that includes various other project assets as well. There are various constructions appended to the road and which supplement the road. It relied on the decision of Hon'ble Bombay High Court in the case of ***Warner Hindustan Ltd***[41] wherein a 'ell' dug for the purpose of carrying out the business of manufacturing pharmaceuticals was held to be 'plant.' It also relied on the decision of Hon'ble Supreme Court in the case of ***Dr. B. Venkata Rao***[42] wherein a "nursing home" equipped with a facility to sterilize surgical equipment, operation theatre, etc. was held to be a "plant". Reliance was also placed on ***Mysore Minerals Ltd***[43]***, Max India Ltd***[44]***,*** etc.

The IRA, on the other hand, submitted that the cost of construction of toll roads/bridges was borne by the Government and the remuneration for the work was in the form of collection of tolls. Such toll roads/buildings cannot be said to be the property of Assessee but that of the Government. Therefore, the Assessee cannot be entitled to depreciation under section 32(1) of the IT Act. According to the IRA, the Assessee should be legal owner of the property to claim depreciation under section 32(1) of the IT Act. The IRA relied on the decisions in the cases of ***North Karnataka Expressway Ltd***[45], ***West Gujarat Expressway Ltd***[46], etc.

[39] L&T Infrastructure Development Projects Limited v. CIT.
[40] CIT v. Podar Cements Ltd (1997) 5 SCC 482.
[41] CIT v. Warner Hindustan Ltd [1979] 117 ITR 15.
[42] CIT v. Dr. B. Venkata Rao [2000] 243 ITR 81.
[43] Mysore Minerals Ltd v. CIT [1999] 239 ITR 775 (SC).
[44] CIT v. Max India Ltd [2007] 295 ITR 282 (SC).
[45] North Karnataka Expressway Ltd v. CIT [2015] 372 ITR 145.

Decision

The Madras HC observed that under the BOT model, the construction company does not hold any rights in the project except receiver of toll fee to recoup the expenditure incurred. It referred to the ***Circular***[47] wherein the CBDT had stated that construction companies are not eligible to claim depreciation under Section 32(1) of the Act since they are not the owner of such toll bridges/roads. The Circular had also stated that the construction companies should be allowed to amortize the total cost incurred evenly over the period of concessionaire agreement. The Madras HC held that although it is not bound by the said Circular issued by the CBDT, it agrees with the position adopted in the said Circular.

It held that only specific types of 'plants and machineries' and the 'buildings' are entitled for depreciation under Section 32 of the IT Act and that toll bridges/roads do not fall within the said ambit. It held that ownership is *sine qua non* for claiming depreciation and the construction companies cannot be said to be the owners toll bridges/roads. Accordingly, they are not eligible for claiming depreciation for the toll bridges/roads constructed by them.

The Madras HC distinguished the decision of the Hon'ble SC in the case of ***Podar Cements Ltd (supra)*** by stating that ownership was deferred to a future year in the said case, whereas in case of toll bridges/roads, the construction companies will never get the ownership. It also expressly stated that it does not agree with the decisions of Hon'ble Allahabad HC in the case of ***Noida Toll Bridge Company Ltd***[48] and the Hon'ble SC in the case of ***Anand Theatres***[49] by holding that they had wrongly interpreted Part A of Appendix I to conclude that 'Toll Road' was a 'building' merely because 'building' includes roads, bridges, culverts, wells and tubewells.

Significant Takeaways

The Madras HC had directly contradicted with the decisions of other HCs and held that the construction companies are not eligible for any depreciation. It may be noted that the Hon'ble Allahabad HC decision in the case of ***Noida Toll Bridge Company Ltd (supra)*** had held that ever since the insertion of Explanation 1 into Section 32(1) of the IT Act, ownership is not a necessary criteria for claiming depreciation, which provided that a lessee would be entitled for depreciation on the constructions made under leasehold lands. The Hon'ble Madras HC, in this case, has not stated anything with respect to Explanation 1 of Section 32(1) of the IT Act.

Further, the Hon'ble SC in the case of ***Mysore Minerals Ltd (Supra)*** had held that the term 'owned' forming part of Section 32(1) of the IT Act should be given a wider meaning. It held that depreciation charge is merely the periodic operating aspect of fixed asset costs. The decision in the case of ***Podar Cements Ltd (supra)*** was also given on a similar rationale. The rationale of the decisions provided by the Hon'ble SC in the said cases have been distinguished by this decision of Madras HC on the technical grounds viz. ownership was deferred to future years.

It is now for the SC to provide clarity on this aspect due to contradictory HC decisions. With a number of new Toll Roads being built and more and more private entities getting engaged in this process, it will be extremely important for the SC to decide on this point and clarify the matter because multiple projects may be dependent on the tax treatment of similar transactions.

“ Madras HC rules that depreciation is not available to the concessionaires on toll roads and bridges. ”

[46] CIT v. West Gujarat Expressway Ltd [2017] 82 taxmann.com 224.
[47] Circular No.9/2014 [F.No.225/182/2013/ITA.II].
[48] CIT v. Noida Toll Bridge Company Ltd [2013] 213 Taxman 333 (Allahabad High Court).
[49] CIT v. Anand Theatres [2000] 244 ITR 192 (SC).

Calcutta HC upholds principle of consistency and rules beneficial circulars have retrospective effect

Introduction

In the case of ***M/s Century Plyboards (I) Ltd.***[50], the Calcutta HC held that the IRA could not deviate from its earlier position and treat shares held as investments as stock-in-trade in later years, in the absence of any material to justify the same. The Calcutta HC further held that beneficial circulars should be given retrospective effect.

Facts

Century Plyboards ("**Assessee**") was involved in the business of manufacture and sale of plywood and related products. The Assessee filed a return of income for AY 2005-06, declaring long-term and short-term capital gains from the sale of shares and units of mutual funds. During the assessment proceedings, the AO noticed a large frequency of transactions for selling and purchasing such securities and thus, treated the income from the sale of shares/ mutual funds as business profits rather than capital gains.[51] Against this order, the Assessee appealed before the CIT(A).

The CIT(A) affirmed the order of the AO. Against the order of the CIT(A), an appeal was made to the ITAT, Kolkata. The ITAT reversed the order of the AO and held in favour of the Assessee. Aggrieved, the IRA preferred an appeal before the Calcutta HC.

Issue

Whether the income arising from sale of shares and units of mutual funds is to be taxed as long-term capital gains or as business income in the hands of the Assessee?

Arguments

The IRA argued that looking at the volume and frequency of the transactions involving buying and selling of shares and other securities it was *prima facie* clear that the Assessee was transacting in shares as a business. Further, the IRA was of the opinion that the Memorandum of Association ("**MOA**") and Articles of Association ("**AOA**") of the Assessee made it clear that trading in securities as one of the main objects of the Assessee. Thus, the IRA submitted that the Assessee had carried out trading in securities in a planned, systematic and an organised manner with a view to earn profits, and thus, income arising from the disposal of such securities should be taxed as business income and not capital gains. With respect to the principle of consistency, the IRA contended that different views could be taken based on fresh material. In the instant case, the IRA believed that new facts reflected that the Assessee did not have savings or surplus funds of its own that it could invest in shares and securities.

The Assessee, on the other hand, argued that shares and securities had always been shown in its books of account as 'investments', which had been accepted by the IRA in all the preceding years. There was no justification for the AO to take a different view in the current AY. Further, during the relevant FY, the Assessee has made significantly less investments in comparison to its normal business activities, i.e., trading in plywood and related products. The Assessee further contended that mere mentioning of share trading in the objects of the company in its MOA and AOA is not sufficient to conclude that the Assessee was engaged in the business of trading of securities. Its MOA and AOA were very widely worded and allowed it to engage in the specified activities. Additionally, the Assessee argued that the mere fact of conducting activities in a systematic or organised manner, with frequency and possible profit, did not imply that these activities were undertaken in the ordinary course of business. Most prudent investments bear the same characteristics wherein genuine and legitimate investors are typically allowed to sell their holdings of securities at a premium. According to the Assessee, the determining factor was the intent of the Assessee in buying/ selling the shares, as evidenced by its books of accounts. Reliance was placed on the judgment of ***CIT v. Trishul Investments Ltd.***[52] to buttress this argument. The Assessee also presented evidence to substantiate that it had sufficient funds to invest in shares and had not used any borrowings to finance such investments. . Lastly, the Assessee relied on certain beneficial circulars issued by the CBDT, which stated that if a taxpayer holds listed securities as long-term capital assets and chooses to treat income arising from transfer of the same as capital gains, it should not be questioned by the AO. According to the Assessee, these circulars should be given retrospective effect and should apply to the AY under consideration.

Judgment

The HC observed that the long-term shares were held for a period of time and had been consistently shown as 'investment' by the Assessee in its books of account. This approach had been accepted by the IRA in all the preceding years, i.e., AY 2003-04 and 2004-05. From a perusal of the order of the CIT(A), it was evident that no fresh material or evidence was brought on record, which warranted an inquiry into the genuineness of the

[50] Commissioner of Income-tax, Kolkata-IV, Kolkata v. M/s. Century Plyboards (I) Ltd. ITA/83/2010 (Calcutta HC).

[51] It may be noted that while a beneficial rate of 10% (plus applicable surcharge and cess) is available on disposal of listed shares and securities held as long-term capital assets (subject to satisfaction of prescribed conditions), business income is taxable at 30% (plus applicable surcharge and cess) in the hands of domestic companies.

[52] CIT v. Trishul Investments Ltd., [2008] 215 CTR 96 (Madras).

transactions or for the IRA to deviate from its earlier approach. Thus, the HC held that in the absence of any doubt raised by the IRA with regard to treating the purchase of shares as 'investment' during the preceding years, a departure from the accepted approach was not justified in the instant case.

The HC further took note of Circular No. 04 of 2007[53] (which, *inter alia*, clarified that it is possible for a taxpayer to have two portfolios, i.e., investment portfolio and also a trading portfolio and such taxpayer may have income under the head capital gains as well as business income), Circular No. 06 of 2016[54] (which, *inter alia*, clarified that a taxpayer can treat income arising from disposal of listed securities as capital gains and the AO cannot dispute it, provided such taxpayer takes this approach consistently) and another circular from 2016[55] (which, *inter alia*, provided that income arising from disposal of unlisted shares should be taxed as 'capital gains' irrespective of period of holding). Basis the said circulars, the SC held that with respect to listed shares and securities held for more than 12 months, if the Assessee desires to treat the income arising thereof as capital gains, the same shall not be put to dispute by the AO. Further, in the instant case, the Assessee had consistently shown the shares and securities as 'investment' in its books of accounts, which had not been objected to earlier and thus, the Assessee or the IRA could not opt for a different treatment or take a different view, respectively, in the subsequent years. The HC further held that a reading of the circular makes it clear that it was issued to bring certainty with respect to taxability of income arising from disposal of shares and reduce litigation. It was a well settled position of law that the benefit of a circular should be extended to a taxpayer, especially when such circulars are beneficial in nature. Thus, the said circulars would have retrospective operation insofar as the clarifications/ instructions enured in favour of the Assessee.

Accordingly, the HC confirmed the order of the ITAT.

Significant Takeaways

Under the IT Act, taxation of income arising from disposal of shares may vary depending on whether such income is characterised as 'capital gains' or as 'profit or gains from business or profession' (business income).[56] Classification of income arising from the disposal of shares as capital gains or business income is dependent on whether such shares are considered to be a 'capital asset' or 'stock in trade' under the IT Act. There are no explicit provisions under the IT Act regarding characterization of transactions on capital account (and taxed under the head capital gains) vis-à-vis on trading account (and taxed under the head business income). The determination of the character of income arising from a particular investment in shares is thus, a fact-specific exercise.

Over the years, Indian courts[57] have laid down different parameters to distinguish shares held as capital assets from the shares held as stock in trade. Further, the CBDT has also issued various instructions and circulars to provide illustrative guidelines on this issue. The said instructions and circulars have been issued for evolving jurisprudence to provide the IRA and taxpayers some certainty with respect to taxation of gains arising from disposal of shares. The instant judgment of the Calcutta HC comes as a welcome respite to taxpayers who may be facing scrutiny for shares transferred prior to the issuance of the illustrative guidelines. In ***Director Of Income Tax New Delhi vs M/S S.R.M.B. Diary Farming***[58], (the case relied on by the Assessee) it was previously held by the SC that beneficial circulars shall have retrospective application placing two caveats: (i) the circular should not be applied by the HCs ipso facto when the matter had a cascading effect; and (ii) where common principles may be involved in subsequent group of matters or a large number of matters. Even as per the rules of statutory interpretation, when it may cause prejudice to the interests of any person, it is always desirable to make a beneficial interpretation of statutes requiring strict interpretation, the likes of tax statutes, when more than one interpretation is possible.[59]

> **“Consistent treatment of capital assets and stock in trade should not be questioned by the tax authorities without bringing on record any contrary evidence.”**

[53] CBDT Circular No. 04/2007 dated June 15, 2007.

[54] CBDT Circular No. 06/2016 dated February 29, 2016.

[55] F.No. 225/12/2016/ITA.II dated May 2, 2016.

[56] 'Capital asset' has been defined under section 2(14) of the IT Act to mean property of any kind held by a taxpayer, whether or not connected with its business or profession, excluding any asset held as stock in trade (i.e., business/ trading assets) and any personal effects.

[57] *See* e.g., Commissioner of Income Tax (Central), Calcutta v. Associated Industrial Development Company (P) Ltd. AIR 1972 SC 445; and Commissioner of Income Tax, Bombay v. H. Holck Larsen AIR 1986 SC 1695.

[58] Director of Income Tax v. SRMB Dairy Farming Pvt. Ltd. 2018 400 ITR Page 9 (SC).

[59] *See* CIT v. Vegetable Products Ltd. [1973] 88 ITR 192 (SC).

HC holds Tax recovery from directors only if specific findings of misconduct in company affairs

Introduction

In the case of ***Geeta P. Kamat***[60], the Bombay HC quashed the order passed by the AO under Section 179 of the IT Act, which held the director personally liable for tax dues of the company.

Facts

Geeta P. Kamat ("**Assessee**") was a director at Kaizen Automation Pvt. Ltd. ("**KAPL**"). KAPL was not traceable on the available addresses, and led to the failure to recover the entire amount of tax demand for AYs 2008-09 and 2009-10 despite attachment of its bank accounts, wherein the funds available were insufficient.

A show cause notice was issued to the Assessee on January 12, 2017 under Section 179 of the IT Act asking why recovery proceedings for an amount of INR 140 Million should not be initiated against her in her capacity as a director of KAPL. The Assesee responded negatively to the show cause on October 23, 2017 on the following grounds:

(i) As a director, she had no liberty, authorisation or independence to act in a particular manner for the benefit of KAPL and that she did not have any control over the company's affairs;

(ii) She had no authority to sign any cheque independently or take any decision on behalf of KAPL and KAPL also did not provide any operational control or space to perform her duties; and

(iii) She did not have any functional responsibility assigned to her and no one reported to her or her husband Mr. Prakash Kamat, who was also a shareholder and director in the company.

Thereafter, an order was passed under Section 179 of the IT Act holding the Assessee liable for recovery of tax dues from KAPL. According to AO, the Assessee failed to establish that she was not actively involved in the management of the company during the relevant AYs 2008-09 and 2009-10 and hence, she was liable as a director for the tax dues.

The Assessee filed a revision application under Section 264 of the IT Act, but the same was also dismissed by PCIT noting that she was a director of KAPL and hence, liable for its tax dues under Section 179 of the IT Act.

Aggrieved by the same, the Assessee filed a writ petition before the Bombay HC.

Issue

Whether the director can be held personally liable for recovery of a company's tax dues?

Arguments

The Assessee submitted that her husband was implementing a project on BOT model for railways and road transport, basis the agreement with the relevant state government companies of Maharashtra. For this purpose, huge investment was required and hence, the Company was incorporated. Khaleej Finance and Investment, a company registered in Baharain ("**KFI**") made the requisite investment in the Company, through a Mauritian company AFC System Ltd. ("**AFC**"). A joint venture agreement ("**JV Agreement**") was signed between the Assessee, Mr. Prakash Kamat, KFI, and KAPL.

The JV Agreement had clauses like auditor to be nominated by KFI and appointed by Board of Directors ("**BOD**"). Further, the management of AFC was vested with its BOD. KFI appointed six out of eight directors and also the chairman of BOD. , 6 of them . Decisions of the BOD were taken by simple majority.

It was also submitted that due to differences between the investor (KFI) and the Assessee's husband, the couple were removed from their respective positions Managing Director and director in September 2009. Accordingly, she could not be held liable for KAPL's liability which arose after her resignation.

The Assessee also contended that the AO is misplaced with regard to section 179 of the IT Act. The Assessee, placed reliance on the judgment of ***Maganbhai Hansrajbhai Patel***[61] and ***Ram Prakash Singeshwar Rungta & Ors.***[62] wherein it was held if he is able to establish that non-recovery of the tax cannot be attributed to his gross neglect, he cannot be held liable under section 179(1) of the IT Act. Further, it was also brought to the notice of the Court that the term 'gross' has been used before the word 'neglect' which reiterates and recognises the intent that each and every act of neglect of the director cannot make him responsible for the tax dues of the company, unless the neglect is of such a nature that had led to inability to collect the tax dues.

[60] Geeta P. Kamat Vs. Principal Commissioner of Income-tax, Mumbai and Others [TS-75-HC-2023(BOM)]
[61] Maganbhai Hansrajbhai Patel Vs. Assistant Commissioner of Income-tax & Anr. 1 [2013] 353 ITR 567 (Guj.)
[62] Ram Prakash Singeshwar Rungta & Ors. Vs. Income-tax Officer [2015] 370 ITR 641 (Guj.)

Countering these objections, the IRA submitted that the Assessee had failed to establish that she was not actively involved in the management of the company during the relevant AYs 2008-09 and 2009-10. Further, the IRA submitted that she had also failed to convince the Ld. AO that there was no gross neglect, malfeasance or breach of duty on her part. It was further submitted that the Assessee was actively involved in the day to day affairs of KAPL and it was normal for the core team members to have disputes with regard to operations.

Decision

Under section 179 of the IT Act, if tax dues from a private company cannot be recovered, then the same can be recovered jointly and severally from every person who was a director of a private company at any time during the relevant previous year in which the tax dues cannot be recovered. However, such a director can absolve himself if he proves that the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty in relation to the affairs of the company.

The Bombay HC observed that no material, incident, decision or action of the director was highlighted by the AO, basis which the gross negligence or breach of duty of the director can be noted with regard to affairs of the company, which may have had the potential of non-recovery of taxes due.

Basis the above, the Bombay HC sets aside the order of AO and PCIT under Section 179 of the IT Act.

Further, the Bombay HC noted that the Assessee had placed material on record, which suggested the lack of financial control and decision-making powers. With this, according to the Court, the Assessee had discharged her burden of proof in terms of Section 179 of the IT Act to absolve herself from the tax liability of KAPL. However, the AO hadn't discharged the burden of proof of negligence – a charge he levied on the Assessee with regard to the company's affairs-- by not bringing on record any evidence to establish his allegation.

Significant Takeaways

Under the provisions of Section 179 of the IT Act, the liability of the director with respect to the pending tax dues of the company is joint and several. However, the director may claim exclusion by proving that the inability to collect the pending tax dues are not attributable to specific actions of the director w.r.t. his/her gross negligence, misfeasance, breach of duty in relation to the company's affairs. It is only when the pre-requisites or the conditions of the applicability of the section are met, the liability can be fixed on the director.

In the case of ***Ashita Nilesh Patel***[63], since the IRA didn't mention the inability of collection of tax from the company and didn't provide the details of steps taken by it to recover the demand from the company, the notice was quashed by the Gujarat HC.

As against the above, in the case of ***Rajeev Behl***[64], while the IRA took actions to collect the tax dues from the company but wasn't successful due to insufficient funds, the order under Section 179 of the IT Act was considered to be valid. Then, the burden of proof to establish innocence was on the director. If he was unable to prove his innocence, the Delhi HC held that he could not claim that demand against him was not justified.

Once a director's innocence is proved, it becomes the duty and responsibility of the IRA to prove by facts and circumstances and resorting to evidences on record that the director was responsible for the payment of un-recovered tax.

> **“ Bombay HC holds that a director cannot be held liable for tax dues of the company. ”**

[63] Ashita Nilesh Patel v. Assistant Commissioner of Income-tax, Circle 4(1)(2) [2020] 115 taxmann.com 37 (Gujarat).
[64] Rajeev Behl v. Principal Commissioner of Income-tax [2021] 132 taxmann.com 283 (Delhi).

Date of last panchnama to be considered while computing limitation period for block assessments

Introduction

In the case of ***Anil Minda & Ors.***[65]***,*** the SC held that for computing the limitation period under block assessment proceedings, the date of last authorization of warrant would be irrelevant and the date on which panchnama was last drawn would be the starting point for period of limitation.

Facts

Two separate warrants authorising search and seizure operations under section 132(1) of the IT Act were issued against Mr. Anil Minda and other persons ("**Assessees**") on March 13, 2001 and March 26, 2001 respectively. During the execution of the search warrants dated March 13, 2001, the IRA got information about a bank locker belonging to the Assessees. As a result, on March 26, 2001, a second authorization for searching the locker was issued, and it was carried out on March 26, 2001. On the same date, a panchnama was drawn up. Multiples searches were conducted on different dates under the first warrant and the search was finally concluded on April 11, 2001. Accordingly, a panchnama in relation to first warrant was drawn up on April 11, 2001.

Thereafter, notices were issued on the Assessees under section 158BC of the IT Act for filing of block assessment. In reply, Assessees filed their return and assessment orders were passed in April 2003. Assessees challenged the impugned assessment orders, *inter alia*, on the ground that they were barred by limitation. While CIT(A) dismissed the appeals, ITAT, Delhi ruled in the favour of the Assessees. An appeal to the HC was preferred by the IRA wherein the Delhi HC ruled in the favour of the IRA. Aggrieved by the HC order, Assessees appealed before the SC.

Issue

Whether the period of limitation of two years for the block assessment under section 158BC/158BE would commence from the date of the Panchnama last drawn or from the date of last authorization of the search and seizure proceedings?

Arguments

Assessees argued that as per Explanation 2 of section 158BE of the IT Act, the limitation period of two years shall be computed from the date of last authorization which in the Assessees' case was of March 26, 2001. Assessees contended that based on above rationale, the assessment order passed in April 2003 was barred by limitation. They further contended that even though the panchnama in relation to the first authorization was drawn up on April 11, 2001, it was irrelevant, as the 'date of last authorization' was material for considering the starting point for the period of limitation. According to the Assessees, the date of last authorization was March 26, 2001 which shall be considered as the starting point for the 2-year limitation period.

The IRA argued that as per Explanation 2 of section 158BE of the IT Act, the period of limitation is to be computed from the date on which the last panchnama was drawn, which in the Assessees' case was April 11, 2001. It further contended that if Assessees' interpretation of Explanation 2 of section 158BE were to be upheld, then the explanation would become nugatory and redundant.

The IRA further argued that for ultimately conducting the assessment proceedings, all the material collected in various searches on different dates would be necessary as the entire material collected shall be relied on for conduction of the proceedings. Hence it contended that the date on which last search was concluded/last panchnama was drawn up has to be considered as the relevant date for limitation period. IRA placed heavy reliance on ***VLS Finance Limited & Another v. Commissioner of Income Tax & Another***[66] wherein the SC had upheld the legal position that the date on which last search was concluded was material for computing the limitation period.

Judgement

The SC heavily relied on its judgment given in the case of ***VLS Finance Ltd***[67], and reiterated its ratio and ruled that, for the calculation of limitation period, the date on which last panchnama was drawn would be relevant and not the date of last authorization. It agreed with the IRA's argument that the block assessment proceedings are conducted on the basis of the entire material collected in different searches and therefore the date of last panchnama would be relevant for computation of limitation period.

[65] Anil Minda & Anr v. Commissioner of Income-tax, [2023] 148 taxmann.com 407 (SC).
[66] VLS Finance Limited & Another v. Commissioner of Income Tax & Another (2016) 12 SCC 32.
[67] Id.

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It stated that by considering date of last authorization as the relevant date, the entire purpose of Explanation 2 to section 158BE of the IT Act would be frustrated. The SC upheld the view taken by the HC in the previous appeal and ruled in the favour of IRA.

Significant Takeaways

Limitation period in case of block assessments has been a contentious issue. A similar issue arose in the case of ***ACIT, Jodhpur v. Shree Ram Lime Products***[68] wherein the Jodhpur ITAT was called upon to interpret the meaning of panchnama under section 158BE of the IT Act and rule upon the bar by limitation. The search was essentially concluded by a panchnama dated December 21, 2002, however another panchnama was drawn on January 3, 2003, which merely revoked a restraining order. An assessment order was passed on January 31, 2005. The ITAT, while interpreting the meaning of panchnama, ruled that panchnama is just a document which records the proceedings which have taken place in the presence of the witnesses. However, the panchnama within section 158BE of the IT Act should be a panchnama which reveals that a search was carried out on the day to which it relates. If the panchnama does not reveal that a search was carried out at all, then it would not be a panchnama as referred under Explanation 2 to section 158BE of the IT Act. The ITAT therefore, ruled that the panchnama dated January 3, 2003 was not a valid panchnama and the last panchnama for computing limitation period would be the one drawn up on December 21, 2002. It finally held the assessment order to be barred by limitation as the two-year period had ended in December 2005.

In the given case of *Anil Minda (supra)*, it can be seen that the SC has tried to interpret the provisions in a way to give furtherance to the intent of the legislature. It has tried to construe the words in the provisions in a way so as to not frustrate the entire purpose of the provision.

It was noticed by the government that the block assessment proceedings were turning out to be very litigious. It was due to this reason that Finance Act, 2021 amended the re-assessment proceedings and currently the re-assessment proceedings are conducted under section 148 of the IT Act as opposed to under various provisions before the amendment.

> **" Date on which panchnama last drawn shall be relevant for computing limitation period. "**

[68] Assistant Commissioner of Income-tax, Central Circle-2, Jodhpur v. Shree Ram Lime Products Ltd., [2012] 22 taxmann.com 122 (Jodhpur) (SB)

GST Authorities incorrect in demanding GST @18% for solar power projects

Introduction

In case of ***Sterling and Wilson Private Limited***[69], the Andhra Pradesh HC set aside the demand of GST @18% on the full value for the activities of supply, installation, testing and commissioning of solar power generating system.

Facts

Sterling and Wilson Private Limited ("**Petitioner**") is engaged in supply, installation, testing and commissioning of solar power generating systems. The Petitioner entered into contracts with multiple prospective buyers for the supply and installation of solar power equipment. It also paid GST at the rates of 5% for the supply of solar equipment and 18% for the service of erection and installation of equipments generating solar power. However, the GST on the inputs procured by the Petitioner was charged at 18%. Due to this inverted duty structure, the Petitioner had accumulated ITC. Thus, it filed refund application to claim refund of INR 8,65,63,538 for period from January 2018 to March 2018. The said application was rejected by the IRA. The Petitioner filed an appeal with the Appellate Authority. While the refund appeal was still pending, the IRA issued an SCN alleging that Petitioner was engaged in works contract service and was required to discharge GST @18% for the value of both goods and services supplied. The adjudicating authority confirmed the demand along with interest and penalty. The Petitioner filed an appeal to the Appellate Authority challenging the demand. However, the Appellate Authority rejected the appeal. The IRA also initiated the recovery proceedings. Aggrieved by the same, the Petitioner filed writ petition before the Andhra Pradesh HC.

Issue

1. Whether the services provided by the Petitioner qualify as works contract services, thereby liable for GST at the rate of 18%?

Arguments

The Petitioner submitted that the supplies made by the Petitioner do not fall under the scope of works contract service, as the solar plant was not immovable, which is a pre-requisite to qualify as works contract. The Petitioner urged that they erect and commission the solar equipment for operational efficacy. The equipment could be dismantled and reassembled at any other place. The Petitioner contended that it was engaged in composite supply. In terms of Section 8(a) of the CGST Act, the supply which predominates in value must be treated as the principal supply. The Petitioner submitted that as the value of the solar equipment forms 92% of the total value of the contract, therefore as the principal supply under the contract was of supply of equipments generating solar power, which attracts GST @5%.

The Petitioner contended that the solar power project cannot be treated as immovable property because the value of supply of goods and services are differentiated through the deeming provision, which provides that 70% is supply of solar equipment and 30% is supply of construction service as per the explanation

[69] Sterling and Wilson Private Limited v. the Joint Commissioner [TS-697-HC(AP)-2022-GST]
[70] Explanation in Sl. No. 234 of Notification No. 01/2017-CT(Rate) dated June 28,2017 and Sl. No.38 of Notification No.11/2017-CT(Rate).

introduced *vide* Notification No.24/2018 dated December 31, 2018[70]. The Petitioner also argued that the order passed was against the principles of natural justice as it was done without following the procedure.

On the other hand, the IRA contended that from the perusal of the Engineering Procurement and Construction Contract the Petitioner was engaged in supply of works contract service to solar power plant developers and GST @18% was applicable on full value of services. In this regard, the IRA contended that the solar power plant has a life of 25 years. Apart from solar panels, there were several other essential items which were connected. The Petitioner was responsible for designing, engineering, civil works, land development, fixing, testing, etc. Thus, Petitioner was developing an immovable property that falls under works contract service. The argument of the Petitioner regarding deeming valuation was inapplicable for the tax periods of November 2017 to September 2018 since the deeming valuation provision was introduced with effect on January 1, 2019 and had no retrospective application.

Decision

The HC after analysing the relevant provisions of the GST legislation, drew reference from the GST Council's recommendations. The Council had clarified that the GST on renewable energy projects can be paid in terms of deeming provisions, i.e. 70:30 ratio for the supply of goods and services, for the period July 1, 2017 to December 31, 2018 in the same manner as prescribed for the period on or after January 01, 2019 *vide* Circular No.163/19/2021-GST dated October 6, 2021. However, no refund can be claimed if GST is paid more than the amount determined under the deeming provision. Therefore, in view of the aforementioned circular and notification, the HC remanded the matter back to the Appellate Authority to consider the issue afresh in terms of the Circular. The HC permitted the Petitioner to raise all objections in front of the Appellate Authority and such Appellate Authority was directed to issue a fresh order by looking at the issues from a fresh lens.

Significant Takeaways

Even after clarification from GST council that the deeming provision, i.e. 70:30 ratio for the supply of goods and services, would be applicable for the period beginning from July 1, 2017 to December 31, 2018, the GST Authority continues to take contrary position by demanding GST @18%. This decision is a step towards reconciliation and could play an important role in facilitating the energy sector in terms of ease of doing business. This decision of the HC, if accepted and implemented in toto, will prevent cash outflows from the taxpayers who may have discharged GST at lower rate of 5% for the period beginning from July 2017 to December 2018 and may have been harassed by the GST department.

> **“Deeming valuation in 70:30 ratio for the supply of goods and services would even be applicable for the period July 1, 2017 to December 31, 2018.”**

Refund cannot be denied to a taxpayer for non-compliance by a supplier's supplier

Introduction

In the case of ***M/s Choksi Exports***[71] the Gujarat HC held that the IRA cannot withhold the GST refund on the reason that the taxpayer has been tagged as a 'risky exporter' on account of purchasing goods from a supplier tagged as risky supplier.

Facts

M/s Choksi Exports ("**Petitioner**") is engaged in the business of manufacturing and exporting of organic pigments. The Petitioner had purchased certain raw material from a supplier, who, in turn, had procured goods from a supplier classified as a risky supplier in L2 category. The IRA tagged the Petitioner as a 'risky exporter' on ground of availing incorrect ITC. While the Petitioner had filed a refund claim of INR 148 Million, the same was not released on the ground that it has been marked as 'risky exporter'. In this regard, the IRA visited Petitioner's premises for physical verification on January 1, 2022. Post the verification, the Petitioner also submitted documents as required and prescribed by the Circular No. 131/1/2020- GST dated January 23, 2020. However, even after submitting details, the refund was not sanctioned.

The Petitioner filed a grievance application dated June 16, 2022, and contended that the refund was withheld violating the provisions of the GST legislations. Aggrieved by the inaction of the IRA, the Petitioner then filed a writ petition before the Gujarat HC.

Issue

1. Whether the IRA was required to pass provisional refund of 90% to the Petitioner?

Arguments

The Petitioner argued that non-refund of IGST was in violation of Section 54(6) of the CGST Act read with the Rule 91(1) of the CGST Rules, which provides that the IRA was bound to provisionally sanction 90% of the refund claimed by a registered taxpayer within seven days of the acknowledgement of the refund application, unless certain circumstances apply. The registered taxpayer has not been prosecuted for any offence under the GST legislations or any other existing law (where the amount of tax evaded exceeded INR 250 Million) during any period of immediately preceding five years, The Petitioner submitted that it has not been prosecuted under any law and has duly filed the shipping bills for all exports undertaken by it. The Petitioner relied upon the Telangana HC case of ***Bhagyanagar Copper Private Limited***[72] wherein the Telangana HC ordered refund of IGST on similar facts. contending that it has also complied with the procedure to be followed by Circular No.131/1/2020-GST dated January 23, 2020 issued by the CBIC by submitting additional documents / data pertaining to procurement, supply, turnover, bank account, financial data, income tax returns, etc.

It was also contended that refund can be withheld under GST legislations where a request has been received from jurisdictional commissioner to withhold the payment on account of the taxpayer not filing of return, non-payment of GST along with interest and penalty, non-compliance of customs legislations or where the refund proceedings were subject to appeal. In the instant case, none of the above conditions was present, but still the IRA had withheld refund without the authority of law.

The Petitioner submitted that it has reversed the disputed ITC pertaining to procurement of goods from supplier, who, in turn, had procured goods from a supplier placed in the L2 risky supplier category. It has addressed several letters to the IRA requesting to take the Petitioner off the 'risky exporter' list , but to no avail. The Petitioner highlighted that the IRA's inactivity resulted in it losing approximately INR 11 lakh per month for paying interest and other charges on its borrowings due to capital blockage on account of withheld refund.

The IRA submitted that on account of the inquiry, the Petitioner was tagged as a risky exporter. The concerned jurisdictional IRA was doing an investigation and reports were shared with the Directorate General of Analytics and Risk Management ("**DGARM**"). Once the DGRAM issues an NOC and revokes the suspension, the Customs Automated Systems will automatically disburse all the pending IGST refunds to the Petitioner. However, the Petitioner availed wrong ITC and its refund was withheld.

Decision

The Gujarat HC held that the GST legislations do not mandate that the Petitioner should verify the genuineness and legitimacy of the supplier's supplier. In other words, it was not responsible to verify whether the supplier's supplier was tagged as an L2 risky supplier. The HC observed that there are safeguards in place under the GST legislation to prevent GST leakages and recover the unpaid GST or wrongly availed ITC from taxpayer's supplier or supplier's supplier.

[71] M/s Choksi Exports v. Union of India [TS-30-HC(GUJ)-2023-GST].
[72] Bhagyanagar Copper Private Limited v. The Central Board of Indirect Tax & Customs & Ors. In W.P.No.15804.

Additionally, the HC held that the IRA was mandatorily required to sanction the 90% provisional refund as per Section 54(6) of the CGST Act. The HC acknowledged that the Petitioner had duly complied and had also reversed the disputed ITC, hence, there was no reason to withhold the refund. It also referred the Telangana HC decision in *Bhagyanagar Copper Private Limited*, which held that 90% provisional refund was provided in the GST legislation. Accordingly, it directed the IRA to grant the refund.

Significant Takeaways

The aforesaid judgment is a relief to taxpayers who have been listed as 'risky exporter' due to the fault of distant third-party suppliers. The HC observed that under the GST regime, the taxpayer isnot mandated under law to verify the credentials of supplier's supplier. The taxpayer cannot be harassed due to the fault of supplier's supplier. It is expected that IRA should be cautious and not penalise a taxpayer by withholding its refund for the faults of a distant third-party supplier..

> **“ 90% of refund amount must be granted as provided under GST legislation. ”**

GST officer does not permit seizure of cash during search proceedings

Introduction

In case of ***Arvind Goyal***[73], the Delhi HC held that the officer appointed under GST legislation does not possess the power to seize cash or deprive a taxpayer of its cash by utilising coercive methods. Such act is illegal and without any authority of law.

Facts

The IRA conducted a search operation at the residence of Arvind Goyal ("**Petitioner**") on December 4, 2020. The search was conducted pursuant to an intel received from CGST Bhopal Commissionerate, who were conducting investigation against M/s Samriddhi Enterprises, registered under GST for dealing with betel nuts. As the enquiry revealed that trading occurred without actual movement of goods, they recorded statement of the owner of such enterprise, who informed that enterprise was opened by the Petitioner. The IRA took possession of cash amounting to INR 1,22,87,000 along with mobile phone and laptop belonging to the Petitioner. However, no search memo was drawn with respect to cash. The IRA made a noting the panchnama that they took possession of cash found at the Petitioner's residence. The cash collected was deposited in a fixed deposit receipt in the name of the President of India by the Respondent. Aggrieved by the same, the Petitioner filed a writ petition before the Delhi HC.

Issue

1. Whether cash can be seized under Section 67(2) of the CGST Act?
2. Whether the IRA had authority under law to take possession of cash available at Petitioner's premises?

Arguments

The Petitioner contended that the search undertaken by the IRA was unlawful as IRA could not have any reasons to believe that any goods liable for confiscation or documents relevant to proceedings were present at the Petitioner's residence. The Petitioner contended that as per Section 67(2) of the CGST Act, the IRA has the power to seize goods which are liable for confiscation and any documents or books or things, if the same are relevant for any proceedings. The Petitioner argued that the definition of goods under GST specifically excludes money. The power under Section 67 (2) of the CGST Act to seize can be exercised only to confiscate goods. Therefore, the IRA was not authorised with the power to seize any cash. Such cash can also not be considered useful or relevant for conducting the investigation.

On the other hand, IRA argued that no cash was seized from the Petitioner. They contended as there was no seizure of cash, no seizure memo was prepared. They contended that they 'resumed' cash as noted in the panchnama, and the same cannot be equated to seizure.

Decision

The Delhi HC, after reviewing the relevant provisions under the GST legislations, held that Section 67(2) of the CGST Act provides for seizure, which was limited to goods liable for confiscation or documents or books that may be useful for any proceedings under the CGST Act. Neither cash qualify as goods nor it can be treated as a 'thing' useful or relevant for the investigation. It also noted that the action of IRA was coercive in nature. The HC held that the power of search and seizure as granted under the CGST Act are draconian in nature and should be exercised only when the underlying conditions to use such powers has been satisfied. Hence, the act of taking possession of cash found at the Petitioner's residence was without any authority of law. Accordingly, the HC directed the IRA to return the amount to the Petitioner along with interest.

Significant Takeaways

The aforementioned decision of the Delhi HC is much appreciated as it restricts the IRA from seizing the cash available with taxpayer. However, do note that the Madhya Pradesh HC ("**MP HC**"), in the case of ***Kanishka Matta***[74], widened the power of IRA and held that cash was covered under the ambit of 'things' under Section 67(2) of the CGST Act. The reasoning provided was that the term 'things' had to be given a wider meaning so that any subject matter of ownership or valuable right was covered under the same. Therefore, the MP HC held that seizure of cash under Section 67(2) was right under the law and the same was to be released when the matter is adjudicated.

Therefore, there exists contrary views of two HCs on the same issue, which may lead to the IRA taking actions differently in

[73] Arvind Goyal CA v. Union of India and Others [TS-11-HC(DEL)-2023-GST]
[74] Smt. Kanishka Matta v. Union of India and others 2020 (9) TMI 42- Madhya Pradesh HC.

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different states. From the review of the facts of the MP HC decision, it appears that any cash seized was from the sales proceeds for which GST returns were not filed may have led to the MP HC deciding against the taxpayer. While CBIC in its earlier Instruction[75] had provided that under no circumstances the taxpayer was required to deposit the requisite GST during search proceedings, it was silent regarding seizure of cash. Hence, CBIC should provide clear guidelines to avoid any ambiguity.

[75] Instruction No. 1/2022-23 [GST- Investigation] dated May 25, 2022.

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No ITC without proper document trail

Introduction

In the case of ***M/s Ecom Gill Coffee Trading Private Limited***[76], the SC held that the recipient has to bear the onus of proving the genuineness of a transaction under Karnataka Value Added Tax Act, 2003 ("**KVAT Act**"). The recipient is required to provide details in relation to physical transit of the goods, freight charges, etc., in order to claim ITC.

Facts

The Karnataka HC had passed taxpayer-friendly orders in multiple cases pertaining to interpretation of Section 70 of KVAT Act. The facts of one of the cases were as follows:

Ecom Gill Coffee Trading Pvt Ltd. ("**Respondent**") is a purchasing dealer, engaged in the business of buying green coffee beans from other dealers for the purposes of further sale in exports and in the domestic market. The IRA issued a notice to the Respondent regarding incorrect availment of ITC as certain suppliers were de-registered or had not filed their returns or claimed lower turnover or did not discharge their respective VAT obligations. Though the same was confirmed by the adjudicating authority, the Karnataka Appellate Tribunal reversed it on the ground that Purchasers could not be denied their dues for the default of the suppliers. The Karnataka HC agreed with the same. Aggrieved by the same, the IRA approached the SC.

Issue

When is the burden of proof as envisaged under Section 70 of the KVAT Act fulfilled?

Arguments

The IRA argued that as per Section 70 of the KVAT Act, the burden of proof to claim ITC is on the purchasing dealer. The burden is higher than mere production of invoice and payment challan. Sufficient documents must be made available to ensure that the transactions involved actual movement of goods and were not mere paper transactions. When the supplier's registration is cancelled and there is no evidence of payment of VAT by such supplier, the purchasing dealer is not eligible for ITC. Accordingly, the burden of proof in relation to genuineness of a transaction, i.e. actual purchase of goods, lies with the purchasing dealer.

The IRA urged that they have not recovered VAT from unregistered suppliers and other suppliers who have filed NIL returns. They also contended that the HC was incorrect in observing that the purchasing dealer cannot be held liable for non-payment of VAT by the supplier.

On the other hand, Respondents submitted that purchasing dealers have discharged their burden of proof required under Section 70 of the KVAT Act by producing copies of invoices and details of payments. They contended that post discharging this burden, ITC cannot be denied to the purchasing dealers. If VAT was not paid by the suppliers, the same must be recovered from them and the purchasing dealers must not be handicapped for suppliers' default.

The Respondent also relied on rule 27 and 29 of the Karnataka Value Added Tax Rules, 2005 ("**KVAT Rules**"), which mandates the suppliers to issue tax invoice and furnish details of invoices. The Respondents argued that neither the KVAT Act nor KVAT rules provide for any condition regarding any specific document or obligation for the purposes of claiming ITC. They also relied on previous rulings that held that ITC could be denied in cases where purchasing dealers have failed to conduct due diligence on their suppliers, specifically with regards to their registrations. Denial of ITC to purchasing dealers who have taken necessary precautions would jeopardise interests of bonafide purchasers.

Decision

The SC reviewed the relevant provision and observed that the burden of proving the ITC claim was upon the purchasing dealers. Such burden cannot be shifted to the IRA. Mere production of invoice or payment details are insufficient and would not mean the purchasing dealers have discharged their burdens of proof. The dealers claiming ITC must establish actual physical movement of goods by furnishing not only invoices or cheques, but also names and addresses of the selling dealers, details of the transport vehicles that have delivered the goods, freight charges borne, acknowledgements of deliveries, etc. Failure to produce such information would justify IRA action of rejection of ITC.

In the present scenario, the IRA had questioned genuineness of transactions backed by valid reasons and evidences such as the registration cancellations of the sellers, sales that gave rise to ITC dispute, and non-payment of VAT to the IRA. The Respondents have not produced any other documents to prove genuineness of the transactions.

The SC also observed that the argument of the Respondents in relation Rule 27 and 29 of the KVAT Rules, were of no substance

[76] State of Karnataka v. M/s Ecom Gill Coffee Trading Pvt Ltd. 2023 SCC Online SC 248.

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since they did not prove actual movement of goods. Further, the SC observed that the case of Delhi HC ***On Quest Merchandising India Pvt. Ltd.***[77] referred by the Respondents was not applicable to the instant case, since it dealt with Delhi VAT legislation and the relevant clauses are not *pari materia* with KVAT Act.

Accordingly, the SC held that the Respondents had failed to discharge the burden cast on them under Section 70 of the KVAT Act by not furnishing other documents, their burden of proof was not discharged and hence, they are not eligible to avail ITC.

Significant Takeaways

The above discussed judgement by the SC would have wide ramification leading to IRA denying benefit of ITC to recipients. The decision would also impact availment of ITC under GST legislations as it contains *pari materia* provision under Section 155 of the CGST Act. Further, the GST legislationalso provides for various conditions to avail ITC such as the supplier paying GST to the IRA, filing of GST return and payment to the supplier within 180 days. Some of the conditions have already been challenged before various HCs. For the erstwhile indirect tax regime, certain HCs have held that the IRA cannot reverse ITC already availed by the purchasing dealers on the ground that the suppliers have failed to pay the tax to the department.[78] It will be impossible for the recipients to prove that the suppliers have paid tax or not as while making the payment and thus, the Courts relaxed conditions for availment of ITC.[79] Even under the GST regime, there are instances where the HCs have held that checking whether the supplier is compliant and has deposited tax, is an onerous burden on a bonafide recipient. The taxpayer would be entitled to the refund of the ITC on goods that have been exported by it.[80] Additionally, the HCs have held if the suppliers are existing, the IRA should initiate recovery proceedings against the sellers and not against the recipients[81]. While the jurisprudence is evolving, honest taxpayers continue to face difficulty in availing the ITC due to non-compliance by the suppliers.

> **“ For claiming of ITC, genuineness of the transaction and actual movement of the goods are the sine qua non. ”**

[77] On Quest Merchandising India Pvt. Ltd. v. Government of NCT of Delhi, 2018 (10) G. S. T. L. 182 (Del.)
[78] Sri Vinayaga Agencies v. The Assistant Commissioner, CT Vadapalani, 2013 (4) TMI 215 - MADRAS HIGH COURT
[79] R.S. Infra-Transmission Ltd. v. State of Rajasthan, 2018 (4) TMI 1800 - Rajasthan High Court; Assistant Commissioner, Jaipur v. M/S Asha Oil Traders, 2022] 101 G S.T.R. 159 (Raj).
[80] M/s. Balaji Exim v. Commissioner, CGST, 2023 (3) TMI 529 - Delhi High Court.
[81] D.Y. Beathel Enterprises v State Tax Officer (Data Cell), 2021 (3) TMI 1020 - Madras High Court

Services provided by branch office of E&Y to overseas entities is not an intermediary service

Introduction

In case of ***Ernst and Young Limited*** ("**E&Y Limited**")[82] the Delhi HC allowed the refund of unutilised ITC by holding that the services rendered by it were on its own account and not as an intermediary.

Facts

M/s E&Y Limited established a branch office ("**Petitioner**") in 2008 pursuant to the approval of the RBI. The Petitioner is engaged in providing professional services. E&Y Limited entered into professional service agreements with other Ernst & Young entities like E&Y Pty Ltd. Australia, E&Y US LLP, E&Y LLP UK and E&Y Pty Ltd. New Zealand ("**EY Entities**"). In terms of the service agreements, E&Y Limited, acting through the Petitioner, was required to provide professional services including services such as assurance and business advisory; technical advice/ advice in relation to expatriate tax compliance, business tax compliance under tax laws of the United States, technical review and approval of US income tax returns, etc. The Petitioner had filed a claim of refund of ITC for the period from December 2017 to March 2020. The same was rejected by both the Adjudicating Authority as well as the Appellate Authority on the ground that the Petitioner is an intermediary and therefore, the place of supply of service shall be the location of Petitioner i.e. India and not where the recipient is located, i.e. the US. Aggrieved by the same, the Petitioner filed the writ petition before the Delhi HC.

Issue

Whether services provided by the Petitioner to the EY Entities, shall be construed as services rendered by an 'intermediary'.?

Arguments

The Petitioner submitted that the services provided by it i.e. business advisory services and technical assistance, etc., were services provided by it on its own account, The Petitioner had issued the invoices for the services rendered and consideration for the same was received directly from the foreign EY Entities. It contended that all the conditions of export of services, as specified under the extant GST legislations were met, i.e. location of supplier was in India, location of recipient was outside India, place of supply was outside India, payment was received in India and that the Petitioner was not a branch office of EY Entities. The Petitioner urged that it did not qualify as an intermediary as it was neither arranging nor facilitating any service.

On the other hand, the IRA submitted that the services provided by the Petitioner were intermediary as it has rendered service on behalf of E&Y Limited to EY Entities. Hence, such services were not on one's own account. Therefore, as the place of supply was the location of intermediary, it was not export of service and the Petitioner was not eligible for refund of unutilised ITC. The IRA has also relied on permission letter dated April 4, 2008 whereby the RBI permitted Ernst & Young Limited to establish a branch office in India to carry out services that stated *'representing the parent company in India and acting as a buying/selling agent in India'*.

Decision

The Delhi HC after analysing Section 2(13) of the IGST Act, which provides for the definition of intermediary, held that there must be facilitation or arranging of the supply of goods or services between two or more persons. Thus, any person who supplied goods or services was not an intermediary. The HC observed that the IRA had incorrectly relied on last limb of the definition, which excluded a person supplying goods or services on its own account. The HC observes that the said portion did not control the definition of intermediary. It merely restricted the applicability of definition. Hence, the HC concluded that the definition was not expansive.

The HC reiterated that the primary requirements for a service to be held as an intermediary service were; (a) involvement of a minimum of three parties i.e. one supplying the main service, the recipient of service and the one party merely arranging and facilitating the service; (b) two distinct supplies need to be present i.e. main supply of the service and ancillary supply of arranging and facilitating was required; (c) the intermediary service provider needed to have the characteristics of an agent or broker; and (d) the said intermediary service provider should not be supplying services or goods from its own account. The HC held that above-mentioned parameters were not met by the Petitioner in the instant case and hence, it could not be construed as an intermediary.

It clarified that while providing certain services, some parts may be outsourced to a third party, which should not automatically

[82] Ernst and Young Limited v Additional Commissioner CGST Appeals-II [TS-99-HC(DEL)-2023-GST].

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lead to the conclusion that it was an intermediary service. The role of an intermediary was to merely put the third party directly in touch with the service recipient and arranging / facilitating the supply. The HC also held that the Petitioner had acted as the buying/selling agent of the E&Y Limited is without any basis as the IRA had incorrectly relied on limited portion of the RBI permission letter and failed to consider other permitted activities such as export-import of goods, providing consultancy or professional services, etc. The HC observed that the definition of term 'intermediary' under the erstwhile service tax regime and GST legislation is similar.

Significant Takeaways

The aforesaid judgment clarifies that the intermediary position under the GST regime as well as IRA in many instances urged that the concept of intermediary is different under GST vis-à-vis service tax regime. The HC in the instant case has analysed the provisions of intermediary and place of supply of services. The said decision has recently been relied upon in the case of ***Ohmi Industries Asia Pvt. Ltd.***[83] in which case the Delhi HC held that the taxpayer, who was providing market research services to the affiliated entities of its parent company in Japan, was not an intermediary as it was not arranging or facilitating the services, it was instead rendering the said services. It is hoped that the IRA would take note of these decisions and not reject the refund claims of genuine taxpayers who were denied the refund.

> **"Rendering services by itself to an affiliate does not constitute intermediary services."**

[83] Ohmi Industries Asia Private Limited v. Assistant Commissioner [TS-128-HC(DEL)-2023-GST].

CBDT notifies Centralised Processing of Equalisation Levy Statement Scheme, 2023

The CBDT has notified the Centralised Processing of Equalisation Levy Statement Scheme, 2023 ("**Scheme**").[84] This Scheme is applicable in respect of the processing of the Equalisation Levy Statements ("**EL Statements**"). Some of the key features of the Scheme are as follows:

i) The CIT has been empowered to declare an EL Statement invalid on account of non-compliance or incomplete information.

ii) The Centralised Processing Centre ("**CPC**") set up under the Centralised Processing of Returns Scheme, 2011, has been given the powers to process a valid Equalisation Levy Statement.

iii) The CPC shall compute the equalization levy after adjusting for any arithmetical error in the EL Statement.

iv) Further, interest (if any) shall be computed based on the sum deductible or payable as computed in the EL Statement.

v) The sum payable by, or the amount of refund due to, the assessee shall be determined after adjustment of the amount computed under sections 166(2)(b), 166A or 170 of the IT Act, and any amount paid otherwise by way of tax or interest.

vi) No intimation shall be sent, after the expiry of one year from the end of the financial year in which the EL Statement or revised EL Statement is furnished.

vii) If a revised EL Statement is furnished, the CPC shall process only the revised EL Statement and no further action shall be taken on the original EL Statement.

viii) No assessee shall be required to appear personally or through an authorized representative before CPC in connection with any proceedings.

ix) Written or electronic communication in the format specified by CPC shall be sufficient compliance with the query or clarification received from the CPC.

x) The CPC may call for clarification, evidence, or documents as may be required for the purpose of facilitating the processing of EL Statements, and all such clarification, evidence, or documents shall be furnished electronically.

The Scheme enter into force on February 7, 2023.

CBDT notifies list of consequences that will apply to a person if his PAN becomes inoperative

CBDT *vide* its notification[85], circular[86] and press release[87] dated March 28, 2023 extended the timeline for linking Aadhar Card ("**Aadhar**") with Permanent Account Number ("**PAN**") and also amended Rule 114AAA of the IT Rules to notify the consequences for PAN becoming inoperative.

The deadline for linking of Aadhar with PAN has been extended to June 30, 2023 from the earlier mentioned deadline of March 31, 2023. No repercussions shall be attracted if the Aadhar has been linked with PAN by June 30, 2023. However, in case of a

84 CBDT Notification S.O. 614(E) [No. 03/2023/F.No.370142/1/2023-TPL], dated 7-2-2023.
85 CBDT Notification G.S.R. 227(E) [No. 15/2023/F.No. 370142/14/2022-TPL], dated March 28, 2023.
86 CBDT Circular No. 03 of 2023, dated March 28, 2023.
87 CBDT Press Release, dated March 28, 2023.

failure to link Aadhar with PAN by the given date, the PAN shall become inoperative. CBDT shall also impose the following consequences on the defaulter from the date of inoperation till the date PAN becomes operative again:

- No refund of any tax due shall be made to the person;
- No interest shall be payable on any such refund as mentioned above during the period for which the PAN becomes inoperative;
- TDS to be deducted at a higher rate in accordance with section 206AA of the IT Act; and
- TCS to be collected at a higher rate in accordance with section 206CC of the IT Act.

All these consequences shall take effect from July 1, 2023. An exemption has been provided to persons who are exempted from intimating their Aadhaar under section 139AA(3) of the IT Act.

An inoperative PAN can be made operative by intimation of Aadhar number and payment of prescribed fee/penalty. However, it shall take 30 days from the intimation of Aadhar number for the PAN to become operational again.

Withdrawal of assessment order issued under Section 62 of the CGST Act

CBIC *vide* Notification No. 6/2023-Central Tax dated March 31, 2023 notified that assessment order passed under Section 62 of the CGST Act in cases where registered person have failed to furnish a valid return from a period of 30 days from issuance of an assessment order on or before February 28, 2023 will be deemed to withdrawn, irrespective if an appeal has been filed or decided in respect of the assessment order, if the registered person:

(a) furnishes the return on or before June 30, 2023; and

(b) payment of interest due under Section 50(1) of the CGST Act and the late fee payable under Section 47 of the CGST Act.

One-time Amnesty scheme for EO defaults under the EPCG and Advance Authorisation Scheme

The DGFT *vide* public notice No. 2/2023 dated April 1, 2023 has notified the one-time amnesty scheme for defaults in fulfilment of export obligation ("**EO**") under the EPCG and Advance Authorisation Scheme.

The amnesty scheme provides that non-compliance can be regularized by payment of proportional customs duty on unfulfilled EO. The interest component for delay in payment of customs duty has been capped to 100% of the customs duty amount. However, no interest would be payable on the portion of Additional Customs Duty and Special Additional Customs Duty. The eligibility criteria and other features of scheme is as follows:

1. The authorisations issued under Advance Authorisation and EPCG Scheme provided under FTP 2014-2019 until March 31, 2015 and under FTP 2004-2009 or earlier whose EO (original or extended) was valid beyond August 12, 2013.
2. The cases which involve fraud or misdeclaration or unauthorised diversion of material or capital goods are not eligible for the benefits of the scheme. Further, cases where duty and the applicable interest has been paid in full are excluded from the availing the scheme.
3. In order to avail the benefits of the scheme, the interested person is required to submit the application by June 30, 2023 and payment of applicable customs duty and interest should be done before or on September 30, 2023.

Additionally, no refund or CENVAT credit will be available duties paid under the scheme.

Revocation of cancellation of registration

The CBIC *vide* Notification No. 03/2023-Central Tax, dated March 31, 2023, has prescribed procedure for revocation of cancellation for registered persons whose registration has been cancelled for non-furnishing of returns on or before December 31, 2022 and have failed to apply for revocation of cancellation of such registration within 30 days from the date of cancellation.

In order to avail the benefit, the taxpayer may apply up to June 30, 2023. He must have filed all due returns up to effective date of cancellation of registration along with the payment of tax dues with interest, penalty, and late fee.

The benefit may be availed even by person whose appeal against the order of cancellation of registration or order rejecting application for revocation of cancellation of registration has been rejected on ground of failure to adhere to time limit specified under Section 30(1) of CGST Act.

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Extension of time limit to issue order under Section 73(10)

The CBIC *vide* Notification No. 09/2023-Central Tax, dated 31 March, 2023, extends the time limit under Section 73(10) of the CGST Act, 2017 for issuance of order for recovery of tax not paid or short paid or of input tax credit wrongly availed or utilised for the following period:

Financial Year	Last Date
2017-18	December 31, 2023
2018-19	March 31, 2024
2019-20	June 30, 2024

Key changes in the new Foreign Trade Policy 2023

The DGFT *vide* Notification No. 1/2023 dated March 31, 2023, notified the new Foreign Trade Policy ("**FTP**"), 2023, effective from April 1, 2023. The key amendments to the policy are as follows:

Chapter 1:

1. The sunset clause for the expiry of the FTP has been removed. The new FTP does not have an expiry period and the required amendments would be made when required.
2. The FTP focuses on the sphere of ease of doing business by making most of the compliances and permissions under the FTP online and without physical interface:
   (a) for the issuance of both preferential and non-preferential Certificate of Origin (e-CoO) by designated agencies. Further, a unique number and a QR code shall be endorsed on every e-CoO for validation and authentication purposes.
   (b) digital platform for filing quality control and trade disputes and cordial resolution of trade disputes.
   (c) issuance, renewal, amendment and related process pertaining to Registration Cum Membership Certificate (RCMC)/Registration Certificate (RC).
   (d) 24X7 helpdesk facility to assist the exporters in filing applications on the DGFT portal.
3. Recognition of the AEO program on India on a reciprocal basis with counties viz. South Korea, Taiwan and the USA for faster and smoother export clearance as per Mutual Recognition Agreements. Moreover, MSMEs are also covered under the AEO program.
4. Revision in Status Holder Certification in following manner:
   (a) Earlier, for granting status, export performance was necessary in at least two out of four years. Now, export performance would be necessary in all the three preceding FYs and in all the two preceding FYs for gems and jewelry sector.
   (b) New threshold of export performance has been prescribed as stated below:

Status Category	Threshold of Export Performance (USD Million)
One Star Export House	3
Two Star Export House	15
Three Star Export House	50
Four Star Export House	200
Five Star Export House	800

   (c) The benefit of accredited clients programme has been removed.
   (d) Annual limits for Status holders to export freely exportable items revised as follows:

For exporters excluding gems and jewelry, articles of gold and precious metal).	INR 10 Million or 2% of average annual export realisation during preceding three licensing years, whichever is lower.
Export of pharma products by pharmaceutical companies.	2% of the average annual export realisation during preceding three licensing years.

Chapter 2

5. In addition to export of goods and services, now export of technology is separately recognised under the FTP, for which Import Export Code ("**IEC**") will be mandatory on the date of rendering the service to avail benefits under the FTP.
6. Any item including samples or prototypes of items, 'restricted' or 'prohibited' or is canalised through STEs under ITC HS are not permitted as part of passenger baggage except with a valid authorisation/ permission issued by the DGFT.

7. Import of refurbished/re-conditioned (second hand) spares of capital goods are now freely permitted on the condition that a chartered engineer certificate to the effect that such spares have a minimum residual life of at least 80% compared to the original spare.
8. Merchanting trade not allowed for goods/items in the CITES and SCOMET list.
9. Exports of bonafide trade and technical samples of freely exportable item now specifically allowed under the Policy without any limit.
10. Regularisation of EO default and settlement of customs duty and interest is permissible through settlement commission under customs legislations except in cases where the matter is under the purview of the NCLT.

Chapter 3

11. Introduced to promote export hubs at district levels and to accelerate trade ecosystem from the grassroot level. State and District Export Promotion Committee ("**DEPC**") will be constituted for identifying goods and services at the grassroot level and at the same time spreading awareness at district level regarding export schemes and benefits.
12. The primary function of the DEPC will be to prepare and implement district specific Export Action Plans in collaboration with all the relevant stakeholders.
13. The DEAP may be required to identify the support required from the production stage to the exporting stage by the local industry to boost their manufacturing and exports.
14. DEAP may work towards the required regulatory and operational reforms, infrastructure/utilities/logistics interventions required across the entire chain, informative material on various incentives provided by the Central and State Government, aspects of tie up of producers with exporters, import export regulatory formalities, fulfilment of destination countries standards, etc.

Chapter 4

15. The authorisation under the Special Advance Authorisation Scheme for export of 'Articles of Apparel and Clothing accessories' can be issued on self-declaration basis
16. All items with a BCD greater than 30% will be covered under the ineligible categories of import on self-declaration basis.
17. Minimum value addition criteria of 25% have been stipulated in the case of spices.
18. Criteria of pre-import condition has been removed in case of import of drugs from unregistered sources.
19. In case where ITC on input has been availed for the exported goods, a AEO certification holder has been allowed the capability of submitting a self-declaration (required at the time of filing application for EODC to RA) to the effect that the goods imported against Advance Authorisation are utilised only in the manufacture of dutiable goods either within the same factory or outside (by a supporting manufacturer).
20. Where an exporter intends to use additional inputs in the manufacturing process, eligible exporter can apply for an Advance Authorisation on self-declaration and self-ratification basis. In this regard, it has been clarified that 'additional inputs' does not refer to additionality in terms of quantity/ value of input specified in a norm, however, the said expression refers to another additional input.
21. A manufacturer cum actual user who holds the status of 2 Star or above and has already applied for grant of AEO certification, is eligible to apply under self-ratification scheme, subject to the following conditions:
    (a) submits copy of the application for grant of AEO;
    (b) Provides an undertaking to the DGFT that –
        (i) Application for grant of AEO certification has not yet been rejected;
        (ii) No case of infringement of customs and allied laws against the status holder in the current year and the previous three Fys;
        (iii) No SCN has been issued by Customs or GST authorities in the current year and last three Fys;
        (iv) has positive net current assets;
        (v) no insolvency, bankruptcy or liquidation proceedings taken against the status holder in the current year and last three Fys.
22. In the case of Advance Authorisation for free of cost and paid material, a specific endorsement by RA shall be made in the condition sheet (earlier it was to be made on the exchange control copy) of Advance Authorisation, disallowing remittances for material being supplied free of cost.
23. An Advance Authorisation is required to also specify validity period of import and EO period.

24. For Advance Authorisation or DFIA in respect of intermediate supplies, it has been stipulated that a suitable documentary evidence indicating the available quantity under Advance Authorisation shall be submitted along with the application for invalidation/ ARO. The above stated evidence is not required if invalidation is applied along with the application of Advance Authorisation.
25. No periodicity applicable for linking all exports online on the DGFT system in case of online EODC application.
26. Procedure for endorsement of copy of the Bond Waiver Certificate and EODC by RA to the Customs at the port of registration by post is done away with. Now, the same can be transmitted through EDI mode under message exchange between the DGFT and CBIC.

Chapter 5: EPCG Scheme

27. Project imports of capital goods cannot avail benefits of the EPCG Scheme.
28. The period of validity of authorisation taken under the EPCG Scheme has been increased from 18 months to 24 months
29. A Common Service Provider (CSP) is also eligible for the EPCG scheme benefits. The following amendments have been made:
    (a) CSP can also be certified by DGFT – HQ (earlier DGFT) or Prime Minister Mega Integrated Textile Region and Apparel Parks
    (b) Common utility services like providing electricity, water, gas, sanitation, sewerage, telecommunication, transportation, etc., shall not be considered for CSP benefits
    (c) Capital goods shall be installed within a Town of Export Excellence or PM MITRA
    (d) Import of capital goods shall be subject to Actual User condition until export obligation is completed and EODC is granted.
30. Conditions for fulfilment of EO has been amended to provide that the goods manufactured by the authorisation holder shall be exported as it is by the ultimate exporter (third party exporter) without further processing.
31. Export proceeds can be realised in INR towards fulfilment of EO as per amended RBI guidelines, the balances in the designated Special Vostro account of the correspondent bank of the partner country.
32. An EPCG licence holder will be entitled to only either of the following reduction in EO:
    (a) 25% less for indigenous capital goods
    (b) Early EO fulfilment i.e. 75% in three years or less)
    (c) Green Technology Products
    (d) Northeast Region and UTs of Jammu & Kashmir and Ladakh.
33. No post export EPCG Duty Scrips available now.
34. New procedure prescribed for procurement of capital goods from SEZ by making an application for authorisation for procurement of new capital goods from SEZs, the RA may issue a 'Certificate of supplies from SEZ'.

Chapter 6: EOU/ EHTP/STP/BTP

35. Export of prohibited goods by an EOU may be considered by BOA on a case-to-case basis, if the inputs (such as raw materials, intermediates, components, consumables, parts and packing material) used for export are imported and are not procured from DTA.
36. The new policy permits export from EOU/ EHTP/STP/BTP to a BTP, which was restricted in the erstwhile policy.
37. The exemption from industrial licensing for manufacture of items reserved for micro and small enterprises (earlier only for small scale industries.)
38. Conditions for claiming exemption from the requirement to furnish bank guarantee at the time of import or going for job work in DTA:
    (a) unit has turnover of INR 50 Million or above; and
    (b) Existence for at least three years; and
    (c) Achieved positive NFE/ export obligations wherever applicable;
    (d) and has not been issued a SCN or a confirmed demand, during the preceding three years, on grounds other than procedural violations, under the penal provision of the indirect tax laws or import/ export/ payment regulations on account of fraud / collusion / willful mis- statement / suppression of facts or contravention
39. In case of Authorised Economic Operators (AEO), an exemption has been granted from the requirement to furnish bank guarantee at the time of import or going for job work in DTA, subject to the condition (iv) mentioned above.

40. The list of procurement of goods including captive power plants from DTA expanded to include solar power and wind power plants subject to the condition that no tax / duty benefits stipulated under EOU Scheme shall be available for setting up, as well as operations and maintenance of such plant.

41. the formula for calculation of positive NFE has been aligned to include supplies made by person(s) or employee(s) authorised by a unit of IT related EOU/STP/BHTP to work from a place outside the unit in the FOB value of exports.

Chapter 7: Deemed Export

42. Allow the Duty Drawback claimant to opt between All Industry Rate/ Brand Rate versus earlier allowance basis BCD.

43. Application for drawback and TED can no longer be filed from Branch office. Further, the Registered Office, Head Office or Manufacturing Unit can continue to file the same.

Chapter 8: Quality complaints and trade disputes

44. The scope of complaints/disputes to include the supply of services and technology, in addition to goods.

45. A dispute settlement mechanism would not apply to disputes between two or more Indian entities or two or more foreign entities, cementing the 'cross-border' nature of disputes intended to be covered.

Chapter 9: Promoting cross border trade in digital economy

46. A new chapter providing a structure for promoting cross-border trade in digital economy and exports of goods and services, which under the policy is defined as exports made via e-commerce platforms using internet and payment received through international debit and credit cards or specific authorised payment platforms as notified by the RBI. It covers export of goods through internet.

47. The FTP also provides for promotion of e-commerce export via postal route by establishing 'Dak Ghar Niryat Kendras' all over India, in order to facilitate export and enable artisans, MSMEs, etc., in landlocked regions to have an easy access for export route.

48. Export through Courier Service/Post for an enhanced value limit of INR 1 Million as against the earlier limit of INR 0.5 Million per consignment.

49. Establishment of E-Commerce Exports Hubs (ECEH) to act as a centre for favorable business infrastructure and facilities for cross-border e-Commerce activities.

50. Either private initiative or Public-Private Partnership mode in partnership with the State governments / Central government. Application for creation of an ECEHs area shall be made to the DGFT. The authority for approval for an ECEH vests with the DGFT. The DGFT shall constitute a committee for evaluation of ECEH applications.

51. The DGFT may specify export products or markets which shall not be eligible for ECEH operations.

52. Role of ECEHs may include the following activities:

    (a) To achieve agglomeration benefits for e-commerce exporters;

    (b) To bring capital goods, on exclusive use basis and provide facility of storage (including cold storage facilities), packaging, labelling, certification, testing and other common facilities such as customs clearances, returns processing, etc., for the purposes of export;

    (c) To provide for dedicated logistics infrastructure for connecting to and leveraging the services of the nearest Logistics hub(s);

    (d) To build infrastructure for handling of all goods including SCOMET and restricted goods subject to the fulfillment of rules and conditions as may be applicable.

Chapter 10: SCOMET

53. Export of SCOMET items is either prohibited or permitted under an authorisation to be obtained by the exporter.

54. Imported goods covered under the SCOMET list under ITC (HS) are not permitted for export, even from the Customs bonded warehouse, without an export authorisation, unless specifically exempted.

55. Provision pertaining to voluntary self-disclosure of export of SCOMET items in case, any exporter fails to comply with the export control provisions. A voluntary self-disclosure request along with the supporting documents shall be sent to the DGFT upon discovery of the violation. Inter-ministerial working group may consider each case on merits and may make recommendations on further action to be taken by the DGFT. Exporter will be liable for stricter action for any violation of SCOMET policy where it comes to the notice of the DGFT other than under the voluntary self-disclosure option.

A. GIFT City Boosters

1. <u>**No surcharge on certain income of specified funds**</u>: In order to further incentivise funds located in Gift City, the amended Finance Bill, 2023 provides that no surcharge or cess would be applicable on calculation of advance tax payable by specified Category III Alterative Investment Funds ("**AIF**"), located in International Financial Services Centre ("**IFSC**"), on income received in relation to certain specified securities.

2. <u>**Tax neutral relocation exemption extended to ADIA's investment vehicle**</u>: One of the important incentives introduced by the government to promote relocation of offshore funds to Gift City, is the tax neutrality of such relocation. This exemption is available to specified offshore funds, which meet the prescribed conditions. The amended Finance Bill, 2023, has extended this benefit to investment vehicles in which Abu Dhabi Investment Authority ("**ADIA**") is directly or indirectly the sole shareholder/beneficiary, provided such funds are wholly owned and controlled by ADIA or Government of Abu Dhabi.

   This specific amendment is likely to spur investment from ADIA into Gift City.

3. <u>**Deduction available to Offshore Banking Units increased from 50% to 100%**</u>: Under the extant provisions, a tax holiday is available to certain Offshore Banking Units of a scheduled bank or bank incorporated outside India in special economic zones ("**SEZs**"). Pursuant to such tax holiday, Offshore Banking Units could claim deduction for 100% of the profits for the first five years from the year of registration and 50% of profits for the subsequent five years.

   Pursuant to the amendments proposed to Finance Bill, 2023, such deduction of 50% for the next five years has been increased to 100% where it pertains to assessment year ("**AYs**") 2023-24 or subsequent AYs. Hence, in effect, going forward a 100% deduction would be available for 10 consecutive AYs to Offshore Banking Units setup in SEZs.

4. <u>**Additional benefits to aircraft leasing industry in IFSC**</u>:

   Under the extant provisions, most of the exemptions available to foreign investors and aircraft lessors are in place for exemption for royalty and interest income. However, the amended Finance Bill, 2023 has now extended the scope of such exemptions, to include capital gains and dividend received by a company in IFSC, which leases an aircraft through a step-down special purpose vehicle. The amended Finance Bill, 2023 provides:

   (a) Capital gains arising to non-resident or unit of an IFSC from transfer of equity shares of domestic company, being an IFSC unit engaged in aircraft leasing business, shall be exempt from taxation in India, subject to certain conditions. This exemption is available for a period of 10 years from the year in which the domestic company commences its operations.

   (b) Dividend income arising to IFSC units from a company, being an IFSC unit engaged in aircraft leasing business, shall be exempt from taxation in India

   This had been a key demand of the industry and will encourage investment into aircraft leasing in IFSC.

5. **Lower rate of tax on dividend income from IFSC**: In order to provide boost to investments from non-residents into the IFSC, the amended Finance Bill, 2023 proposes to tax dividend received by non-residents from IFSC units at the rate of 10% (as against 20%), plus applicable surcharge and cess. While this amendment brings the tax rates on dividend income in-line with most of India's Tax Treaties, the non-resident investors may continue to rely on such Tax Treaties to save tax on account of surcharge and cess, if any.

6. **Relaxation for ECB bonds and Masala bonds listed in IFSC**: Section 194LC of the IT Act provides for a concessional rate of taxation at 5% (plus applicable surcharge and cess) on interest paid by an Indian company to non-resident, subject to certain conditions, on money borrowed in foreign currency from source outside India under a loan agreement signed before July 1, 2023 or by way of issuance of long-term bond or rupee denominated bond issued before July 1, 2023. Similarly, a concessional rate of 4% (plus applicable surcharge and cess) is provided on interest paid by Indian companies to non-resident on or by the way of issuance of long-term bond or rupee denominated bond issued before July 1, 2023 and which are listed only on a stock exchange in IFSC.

   While many representations had been made to extend the time limits with respect to the aforementioned beneficial rates, Finance Bill, 2023 did not provide for the same. Accordingly, such interest income would now be taxed at 20% (plus applicable surcharge and cess) under the IT Act, subject to any beneficial rates available under the relevant Tax Treaty (i.e. with respect to interest on bonds or loans issued after July 1, 2023).

   However, the amended Finance Bill, 2023 provides relief in respect of interest income received on long term bond or rupee denominated bond issued after July 1, 2023 and stipulates that such interest income would be subject to tax at the rate of 9% (plus applicable surcharge and cess), provided such bonds are only listed on stock exchange located in IFSC.

7. **Tonnage tax scheme made available to units setup in IFSC**: Under the current provisions an entity undertaking eligible ship leasing business through a unit in IFSC is allowed to claim a deduction under Section 80LA of IT Act on 100% of its income for 10 consecutive years out of its initial 15 years.

   However, in order to further incentivise such ship leasing activities the amended Finance Bill, 2023 has extend the option to such units to be governed by the provisions of tonnage tax scheme, after the tax holiday under Section 80LA of the IT Act cease to be available, by making an application to the specified authority, within the stipulated timelines. Tonnage tax scheme is an optional taxation regime available to specified ship operators wherein their taxable income is determined basis the net tonnage of the entire fleet of vessels under operation or use.

   While the tonnage tax scheme has not found many takers till date owing to its inherent complexities, it will be interesting to see whether the IFSC units would opt for such an option after availing the tax holiday under Section 80LA of the IT Act.

B. Amendments pertaining to Business Trusts

8. **Marginal relief for unit holders of Business Trusts**: Typically, distributions by Business Trusts (includes Real Estate Investment Trsuts ("**REIT**") and Infrastructure Investment Trust ("**InvIT**")) to its unit holders are generally structured in the form of dividend payment, interest, rental income and debt repayment (i.e. return of principal amount of debt extended to the special purpose vehicles). Such distribution in form of debt, owing to the pass-through status conferred upon business trusts under the IT Act, did not suffer taxation either in the hands of Business Trust or in the hands of unit holder.

   Accordingly, the Memorandum to Finance Bill, 2023, noted that a double benefit was not the intention of the legislature when it introduced the pass-through structure. Thereafter, the Finance Bill, 2023 introduced Section 56(2)(xii) of the IT Act, which *inter alia*, sought to tax distribution received as repayments of debt under the head of 'income from other sources' in the hands of unit holders i.e., the entire amount of distributions in nature of repayment of debt were sought to be brought within the tax ambit.

   This proposal saw significant push back from various stake holders. Accordingly, now in order to provide some relief in this regard, the amended Finance Bill, 2023, provides a formula for calculating the tax implications when distributions are made as 'repayment of debt', wherein essentially the cost of acquisition of unit would be excluded.

   This can be better understood with an example. Assume the per-unit issue price at the time of listing of the Business Trust was INR 100. In 2024, the unit holder received INR 10 as 'repayment of debt'. There will be no tax implications because the amount is less than the issue price. Now

assume that by 2034, this cumulative distribution has become INR 210. Hence, only in that year, the INR10 will become taxable in the hands of the investor.

Further, relief has been provided to sovereign wealth funds and specified pension funds (which have been granted exemption under Section 10(23FE) of the IT Act) with respect to distributions which were otherwise taxable under Section 56(2)(xii) of the IT Act. Amendments are also proposed now to provide that any sum received by the unit holder, other than the following income (a) dividends, (b) interests, (c) rental income of REITs, (d) the income which are not taxed under Section 56(2)(xii) and (e) the income, which are not taxable in the hands of Business Trust, will go on to reduce the cost of acquisition of units in the hands of unit holders.

9. **TDS not required to be deducted on interest payable to business trust**: Under the extant provisions, a special purpose vehicle is not required to deduct tax at source on interest payment (other than interest payment on securities) made to business trust.

   However, no such carve out was provided with respect to the interest paid by special purpose vehicle on securities. The amended Finance Bill, 2023 seeks to address this anomaly and exempts special purpose vehicle from deducting tax on interest payment made to business trusts in respect of any securities.

C. Increased Taxation on Passive Income

10. **Income from debt-mutual funds are to be taxed as short-term capital gains**: The Finance Bill, 2023 proposed to amend the IT Act to tax the gains arising from transfer or redemption or maturity of Market-Linked Debentures ("**MLDs**") as short-term capital gains, i.e. at the applicable rates. Investors had expressed their unhappiness on this proposal and stated this would make the MLDs entirely unattractive.

    However, the Government has now further amended the Finance Bill, 2023, to extend the same treatment to debt-mutual funds as well. The recent amendment proposes that capital gains arising from transfer or redemption or maturity of mutual funds, where not more than 35% of the proceeds are invested in equity shares of domestic companies, shall be taxed as short-term capital gains.

    The proposed move seems to bring taxation of such mutual funds on par with bank deposits that are taxed at slab rates. While the proposed amendment shall impact transfer of the units of specified mutual funds acquired on or after April 1, 2023, the grand fathering benefit is not available for market linked debentures.

11. **Change in tax rates in hands of non-resident under Section 115A**: The amended Finance Bill, 2023 has proposed to increase the rate of tax applicable to a non-resident, on royalty or Fee for Technical Services ("**FTS**") to 20% (plus applicable surcharge and cess), as against 10% under the extant provisions.

    Such non-resident taxpayer would still be available to claim the beneficial rates/provisions under the applicable Tax Treaty benefits. However, this amendment would have significant impact on royalty payments made to countries like the USA and the UK, where the beneficial rate provided under the respective Tax Treaties is capped at 15% (i.e. 5% more than what they would paid under the extant provision of the IT Act).

D. Additional Exemptions and rebates

12. **Exemption to National Credit Guarantee Trustee Company Limited and Credit Guarantee Fund**: The amended Finance Bill, 2023 has introduced a new provision to exempt income arising to (i) National Credit Guarantee Trustee Company Limited from operating of credit guarantee funds; (ii) credit guarantee funds managed by National Credit Guarantee Trustee Company Limited; and (iii) Credit Guarantee Fund for Micro and Small Enterprises.

13. **Exemption from capital gains for PSU exiting joint ventures**: The amended Finance Bill, 2023 has introduced a new provision to exempt gains arising to a public sector company on transfer of shares/interest in a joint venture, in exchange for shares of a foreign company incorporated by a foreign government. Corresponding changes have also been made to the IT Act to provide for the cost of acquisition of such shares of the foreign company.

14. **Marginal relief to taxpayers having income exceeding INR 7 lakh**: Section 87A of the IT Act, as amended by Finance Bill, 2023, provides that where income of a resident individual does not exceed INR 7 lakh in a financial year, then such individual may claim a tax rebate of 100% of the income tax payable on such income, provided he/she opts for the new tax regime

    In the amendments proposed to Finance Bill, 2023, benefit of marginal relief has been provided to taxpayers where there

is a marginal increase in income beyond INR 7 lakh. The amendments address an anomaly wherein if taxable income exceeds INR 7 lakh even by a small amount, say INR 2,000, then the taxpayer would see an immediate ~INR 26,200 tax liability. The amendment provides marginal relief so that the additional tax would not be more than the amount by which income exceeds INR 7 lakh.

15. **Amendment to Section 10(26AAA) of the IT Act**: The amended Finance Bill, 2023, has proposed to amend Section 10(26AAA) of the IT Act, which provides exemption to Sikkimese Individual with respect to certain specified incomes. Pursuant to the said amendment, the Finance Bill, 2023, seeks to provide a wider definition of the term 'Sikkimese', with effect from April 1, 1990.

E. Other Changes

16. **Change in Securities Transaction Tax**: The amended Finance Bill, 2023, proposes to increase the securities transaction tax ("**STT**") on the sale of options to 0.062% from 0.05%. Similarly, amended Finance Bill, 2023, proposes to increase the STT on sale of future contracts to 0.0125% from 0.01%.

    While this could shore up revenues for the government to a certain extent, the main reason for this amendment could be to discourage excessive trading in futures and options segment where a large number of retail traders end up losing money.

17. **Changes in TDS provisions in relation to online gaming**: Finance Bill, 2023, introduced a new Section 194BA in IT Act for tax deduction at source ("**TDS**") on net winnings from online games w.e.f. July 1, 2023, and therefore, excluded TDS on such online games from the ambit of Section 194B of IT Act w.e.f. July 1, 2023. Vide the amendments proposed to Finance Bill, 2023, the date of effect of aforesaid amendments has been modified to April 1, 2023.

    Further, Section 194BA of the IT Act has been excluded from the scope of Section 206AB of the IT Act, which provides for withholding of taxes at a higher rate in case of non-filers of income tax return.

18. **Other amendments: Few other amendments are as follows**:

    (a) Section 206C(1G) of the IT Act has been amended to make TCS on amounts remitted under Liberalised Remittance Scheme ("**LRS**") of RBI not limited to payments 'out of India'. Thus, it appears that TCS provisions would need to be complied with even at the time of making remittances to Gift City under the LRS scheme.

    (b) Section 206CC and Section 206CCA of the IT Act, respectively provide for TCS at a higher rate in case of non-furnishing of Permanent Account Number ("**PAN**") and on non-filers of return of income. The rate of collection is higher rate of (i) twice the rate given under the IT Act and (ii) 5%. The said TCS rates under both the Sections have now been amended to subject them to a maximum rate of 20%.

A. Amendments in Customs Act, 1962

1. **Requirement to pay IGST and GST Compensation Cess**: The amendment proposed to the Finance Bill, 2023, has amended Section 65 of the Customs Act to include a new condition for undertaking the manufacturing process or other operations upon the imported goods in the warehouse by the owner of any private warehouse.

   The new condition has been inserted in the form of a new Section 65A, which provides that dutiable goods would be warehoused, subject to payment of Integrated Goods and Services Tax (“**IGST**”) and GST Compensation Cess at the time of clearance of goods for depositing in the warehouse. Accordingly, the following would have to be done:

   (a) the warehouse owner would be required to file a bill of entry for home consumption for payment of IGST and GST Compensation Cess, get it assessed and deposit the same before depositing the goods in his warehouse.

   (b) Similarly, even for removal of goods from one warehouse to the other, the bill of entry for home consumption would have to be filed for payment of IGST and GST Compensation Cess, before the removal of goods.

   (c) The compliance pertaining to warehousing bond would be for the unpaid customs duty only.

   However, the above provision would not be applicable to goods that have been removed for deposit prior to the date of notification of this Section. Further, the Central Government has the power to exempt the nature or class or categories of goods, importers, exporter or industry from application of this provision.

   The aforesaid change would impact the ongoing and new manufacturing facilities located in customs warehouse that were provided with benefit of complete customs duty deferment. With the said change, the warehouse owner would have to now borne the IGST and Compensation Cess at the time of import, leading to capital blockage, even when the goods are not cleared for home consumption. Unless, certain categories are exempted, the warehouses would have to reconsider and redesign their business model.

B. Amendments in the CGST Act, 2017

2. **Compliance related changes**:

   (a) **No requirement of compulsory registration for class of taxpayers engaged only in supply of exempted products**: Section 23 of the CGST Act provides for the persons who are not mandatorily required to obtain a registration under the GST regime.

   The Finance Bill, 2023, proposes to amend the language of Section 23 of the CGST Act to provide an overriding effect over requirement of compulsory registration under Section 24 of the CGST Act or on meeting threshold under Section 22 of the CGST Act to particular category of taxpayer to be notified. The Finance Bill, 2023, also proposes to bring the aforesaid change with a retrospective effect i.e. from July 1, 2017.

   The proposed change would be beneficial for the notified taxpayers engaged only in supply of exempted goods or/and services. Thus, such person would no more be required to obtain GST registration even when he receives supplies exigible to GST under reverse charge or

undertakes any inter-State taxable supply or through an e-commerce operator.

(b) **Extension of timeline**: The Finance Bill, 2023, proposes to amend Section 30 of the CGST Act, which provides 30 days' time limit to a taxpayer to make an application for revocation of cancellation of a registration to the concerned officer to a time limit to be prescribed.

In case of assessment of non-filer of return by the proper officer, the taxpayer had an option to file valid return within 30 days for withdrawal of assessment undertaken by proper officer. The Finance Bill, 2023, proposed the time limit to 60 days. The time limit is further extendable by further 60 days on payment of additional late fee of INR 100 for each day of delay beyond 60 days of the service of the said assessment order. However, this would not impact the interest on the delay in payment of GST or late fee applicable for filing delayed return.

The proposed changes would promote ease of doing business and provide additional time to taxpayer to undertake compliances.

(c) **Constitution of GST Appellate Tribunal ("GSTAT")**: The Finance Bill, 2023 proposes to substitute the GSTAT-dealing Sections 109, 110 and 114 entirely in order to cure various defects that were challenged before the Madras High Court and the Delhi High Court along with certain other risky provisions. Various appeals are yet to be filed as GSTAT was not constituted leading taxpayer in dilemma or forcing them to file writ before High Court. The Finance Bill, 2023, proposes to remove the concept of Regional Bench and Area Bench. Thus, only Principal Bench and State Bench is proposed. It is now proposed that State Benches would have two judicial members as opposed to one. Additionally, the Finance Bill, 2023, proposes that the cases dealing with the issue of place of supply will only be heard by the Principal Bench. Also, a single member bench may now hear matters upto the limit of INR 5 million, which would not involve question of law, with prior approval of the President.

The qualification criteria for the appointment of president and members of the GSTAT has been revised to exclude High Court judge with five years' experience for being a President, exclude member of Indian Legal Service as a judicial member. Whereas for technical member, the list has been expanded. The Finance Bill, 2023, also proposes changes like institution of a search-cum-selection committee for appointment of Technical Member for a State Bench and for other appointments. Further, the Finance Bill, 2023, also proposes for an increased age for retirement of the President of the appellate tribunal -- from 65 years to 67 years -- and has reduced the tenure from five years to four years for the service provided by the President.

The above-mentioned proposed changes provide for institution of search-cum-selection committee, which will have both judicial and technical members and will enable appropriate appointment of technical members to the bench with better understanding and knowledge to deal with disputes. Since, the constitution of tribunal is pending before the larger bench of the Supreme Court, the GSTAT may get impacted. Although, it is proposed that no judgment would affect the GSTAT's constitution.

C. Amendments in the IGST Act, 2017

3. Section 13(9) of the IGST Act provides that the place of supply in case of transportation of goods, other than mail or courier, where either supplier or recipient is outside India shall be the place of destination of such goods. The same is proposed to be omitted by the Finance Bill, 2023. Thus, the Finance Bill, 2023, proposes that the place of supply of such services would location of recipient which may impact the GST analysis, irrespective of destination of goods.

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GLOSSARY

ABBREVIATION	MEANING
AAR	Hon'ble Authority for Advance Rulings
AAAR	Hon'ble Appellate Authority for Advance Rulings
AO	Learned Assessing Officer
AY	Assessment Year
Customs Act	Customs Act, 1962
CBDT	Central Board of Direct Taxes
CENVAT	Central Value Added Tax
CESTAT	Hon'ble Customs, Excise and Service Tax Appellate Tribunal
CGST	Central Goods and Service Tax
CGST Act	Central Goods and Service Tax Act, 2017
CGST Rules	Central Goods and Service Tax Rules, 2017
CIT	Learned Commissioner of Income Tax
CIT(A)	Learned Commissioner of Income Tax (Appeal)
CVD	Countervailing Duty
DGFT	Directorate General of Foreign Trade
DRP	Dispute Resolution Panel
DTAA	Double Taxation Avoidance Agreement
ECB	External Commercial Borrowing
EPCG	Export Promotion Capital Goods
FA	Finance Act
FMV	Fair Market Value
FTP	Foreign Trade Policy
FY	Financial Year
GST	Goods and Services Tax
HC	Hon'ble High Court
HUF	Hindu Undivided Family
IBC	Insolvency and Bankruptcy Code, 2016
IFSC	Indian Financial Services Centre
IGST	Integrated Goods and Services Tax
IGST Act	Integrated Goods and Services Tax Act, 2017

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GLOSSARY

ABBREVIATION	MEANING
INR	Indian Rupees
IRA	Indian Revenue Authorities
IT Act	Income-tax Act, 1961
ITAT	Hon'ble Income Tax Appellate Tribunal
ITC	Input Tax Credit
ITO	Income Tax Officer
IT Rules	Income-tax Rules, 1962
Ltd.	Limited
NCLT	National Company Law Tribunal
NCLAT	National Company Law Appellate Tribunal
OECD	Organisation for Economic Co-operation and Development
PAN	Permanent Account Number
PCIT	Learned Principal Commissioner of Income Tax
PE	Permanent Establishment
Pvt.	Private
RBI	Reserve Bank of India
SAD	Special Additional Duty
SC	Hon'ble Supreme Court
SCN	Show-cause Notice
SEBI	Security Exchange Board of India
SEZ	Special Economic Zone
SGST	State Goods and Services Tax
SGST Act	State Goods and Services Tax Act, 2017
SLP	Special Leave Petition
TDS	Tax Deducted at Source
USA	United States of America
UTGST	Union Territory Goods and Services Tax
UTGST Act	Union Territory Goods and Services Tax Act, 2017
VAT	Value Added Tax
VAT Tribunal	Hon'ble VAT Tribunal

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