KPMG
cutting through complexity

January 2015

India Tax Konnect

Contents

Editorial

In its sixth bi-monthly monetary policy review, in line with industry expectations, the Reserve Bank of India (RBI) reduced the repo rate to 7.75 per cent, reverse repo to 6.75 per cent and the bank rate to 8.75 per cent due to the steady decline in the country's inflation. The rate cuts are likely to result in lowering of lending rates by banks which in turn are expected to provide a much needed boost to the economy. The RBI maintained the cash reserve ratio at 4 per cent.

On the international tax front, the Pune Tribunal in the case of Sandvik AB held that the management service fees received from its Indian subsidiaries are not taxable as Fees for Technical Services (FTS) under the India-Sweden tax treaty by applying the Most Favoured Nation (MFN) clause. The Tribunal observed that on the basis of the MFN clause in the India-Sweden tax treaty, the taxpayer can claim the benefit of more favourable definition of Fees for Included Services under the India-Portuguese tax treaty which restricts the scope of taxability on FTS.

The Delhi High Court in the case of Delhi Race Club (1940) Ltd. dealt with the issue of taxability of income from transfer of broadcasting rights of a live race. The High Court held that the broadcast/live telecast is not 'work' under the Copyright Act and it does not have a 'copyright'. Accordingly, the payment for transfer of broadcasting rights of live races does not amount to royalty under the Income-tax Act, 1961 (the Act).

The Delhi High Court in the case of Brown And Sharpe Inc. held that the income attributable to the Liaison Office (LO) was taxable in India under the India-USA tax treaty. The High Court observed that the activities of the LO in India of the U.S. company, included actual marketing of the products of the taxpayer in India. Accordingly, the activities of the LO were not confined only to being a channel of communication between the head office in the US and prospective buyers in India, as allowed to the LO by the RBI.

On the transfer pricing front, the Bombay High Court in the case of Shell India Markets Pvt. Ltd. held that to apply Chapter X of the Act (Transfer Pricing provisions), income chargeable to tax should arise from an international transaction under the Act. Further, the High Court observed that there is no charge in the Act on account of capital amounts received and/or arising on account of issue of shares by an Indian entity to a non-resident entity. Chapter X of the Act does not contain any charging provision but is a machinery provision to arrive at the arm's length price of a transaction between associated enterprises.

We at KPMG in India would like to keep you informed of the developments on the tax and regulatory front and its implications on the way you do business in India. We would be delighted to receive your suggestions on ways to make this Konnect more relevant.

International tax

Decisions

Management service fees are not taxable as FTS under the India-Sweden tax treaty by applying the MFN clause

The taxpayer is a Sweden based company. It does not have a Permanent Establishment (PE) in India. During the year under consideration the taxpayer has received fees from its Indian subsidiary companies for providing commercial, management and production services.

The taxpayer claimed that payment received from subsidiary companies are not taxable in India in view of the beneficial provisions of the India-Sweden tax treaty read with the Protocol. Further, by virtue of MFN clause, the taxpayer was entitled to use the definition of Fees for Included Services (FIS) under the India-Portuguese tax treaty which restricts the scope of taxability on FTS. Accordingly, the fees received towards rendering management services are not taxable as FTS under Article 12 of the India-Sweden tax treaty.

The Assessing Officer (AO) held that the payments received by the taxpayer from its subsidiaries are in the nature of FTS under Section 9(1)(vii) of the Act as well as under Article 12 of India-Sweden tax treaty.

The Pune Bench of the Income-tax Appellate Tribunal (the Tribunal) applied the MFN clause under the India-Sweden tax treaty and observed as follows:

- The definition of the FTS given in Article 12(3)(b) of the India-Sweden tax treaty does not include make available clause. However, under the India-Portuguese tax treaty there is a 'make available' clause in Article 12 which defines FIS.
- In the present case, the condition of 'make available' clause is not fulfilled by the India-Sweden tax treaty. However, as per the Protocol to the India-Sweden tax treaty which contains the MFN clause, the taxpayer can use the definition of FIS under the India-Portuguese tax treaty which restricts the scope of taxability of FTS.
- On the basis of the Protocol to the India-Sweden tax treaty, the taxpayer can claim the benefit of the conditions imposed for bringing to tax the FTS in the India-Portuguese tax treaty.
- The Protocol attached to the tax treaty takes care of a situation where either of the contracting states enter into a bilateral agreement in the nature of tax treaty with another sovereign state and where the same subject matter has been given more favourable treatment by way of a definition or mode of tax, then the parties can claim the benefit on the recognised principle of the MFN clause.
- Accordingly, by applying the MFN clause under the India-Sweden tax treaty, the payment received by the taxpayer from its Indian subsidiaries cannot be brought to tax.

Sandvik AB v. DDIT (ITA No. 1720/PN/2011) (Pune)

Payment for transfer of broadcasting rights of live races does not amount to royalty

The taxpayer was engaged in the business of conducting horse races and derived income from betting, commissions, entry fee ,etc. The taxpayer had made payment to other centres whose races were displayed in the taxpayer's club. The payment was made without deduction of tax.

The AO held that payment made towards live telecast is in the nature of royalty under Section 194J of the Act. However, since tax has not been deducted by the taxpayer, the payment was disallowed under Section 40(a)(ia) of the Act. The Commissioner of Income-tax (Appeals) [CIT (A)] upheld the findings of the AO. However, the Tribunal relying on the decision of Neo Sports Broadcast (P) Ltd, allowed the appeal of the taxpayer.

The Delhi High Court held as follows:

- Explanation (ba) to Section 194J of the Act stipulates that 'royalty' shall have the same meaning as provided in Explanation 2 to Section 9(1)(vi) of the Act. Perusal of Explanation 2(v) to Section 9(1)(vi) of the Act indicates that the word 'copyright' is followed by the words 'literary', 'artistic' or 'scientific work'.
- If the intention of the legislature was to include other works like; dramatic, musical, etc. in the Explanation 2(v) to Section 9(1)(vi) of the Act the legislature would have said so or would not have qualified the word 'copyright' with the words 'literary' and 'artistic' as the word 'copyright' encompasses in itself all the categories of work. Having not done so, it is a case of 'Expressio Unis' (The mention of one thing is the exclusion of the other).
- The provision would be more meaningful if the word 'in' is read by implication in between the words 'copyright' and 'literary'.
- The Copyright Act does not contemplate broadcast as a work in which 'copyright' subsists as it contemplates 'copyright' to subsist in literary, dramatic, musical and artistic work, cinematograph films and sound recording.
- 'Copyright' means exclusive right to reproduce, issue copies, translate, adapt, etc. of a work which is already existing.
- In view of above, broadcast or the live coverage does not have a 'copyright'. Accordingly, payment for transfer of broadcasting rights of live horse races does not amount to royalty.

CIT v. Delhi Race Club (1940) Ltd (ITA 6/2014) (Delhi High Court)

Payment for hiring dredgers does not amount to royalty under the India-Netherlands tax treaty

The taxpayer is a company incorporated in the Netherlands. The management and control of the taxpayer is situated in the Netherlands. During the financial year 2002-03, the taxpayer had let out dredging equipment to its Indian subsidiary company. The taxpayer claimed that the income earned from letting out of industrial equipment would not be taxable in India under the India-Netherlands tax treaty. The AO held that consideration for use or right to use any industrial, commercial or scientific equipment falls within the definition of royalty under Section 9 of Act and therefore, the same was liable to tax in India.

The Madras High Court held as follows:

- Payments for the use of equipments were covered under Article 12(1) of the old India-Netherlands tax treaty. However, Article 12(1) of the tax treaty was modified with effect from 1 April 1991 and by virtue of this modification, the payment for the use of equipment has been excluded.
- Article 12(6) of the old tax treaty defines the term equipment as payment of any kind received as a consideration for the use of or the right to use industrial, commercial or scientific equipment. However, as per the modified tax treaty under Article 12(6) of the tax treaty the definition for payments for the use of equipments has been excluded.
- Article 12(4)(b) of the tax treaty is modified with effect from 1 April 1991 and it included the payments for the use of, for the right to use industrial, commercial and scientific equipment within the category of 'royalties'. However, Article 12(4) was restored to original position with effect from 1 April 1998 which did not include equipment royalty clause.
- The above position would clearly indicate that the 'payments for the use of equipment' originally found in Article 12(1) as defined in Article 12(6) of the India-Netherlands tax treaty was incorporated in the definition of the term 'royalties' in Article 12(4) of the tax treaty with effect from 1 April 1991, and subsequently deleted with effect from 1 April 1998, and thereby completely taken out from Article 12(1) and Article 12(2) of the tax treaty. This means that the payment for the use of equipment or any consideration for the use of, for the right to use industrial, commercial or scientific equipment was deleted and it was not taxable in the contracting state, in which they arise viz., in the given case.
- The decision in the case of Poompuhar Shipping v. ITO [2014] 360 ITR 257 (Mad) was distinguishable on facts of the present case since in the present case the amendment was made in Article 12(4) of the tax treaty with effect from 1 April 1998 by deleting the term 'payments for the use of the equipment' from the definition of 'royalties'. Further, in the decision of Poompuhar Shipping, it was a case of hiring the ship on time-charter basis, whereas in the present case, dredging equipment was leased out on bareboat basis, namely, without a master and crew.
- The tax department contended that the taxpayer could be treated as having installation PE in India. However, plea of the tax department cannot be accepted as the dredging equipment was leased out on bareboat. Therefore, it will not be treated as having a PE. Further, the entire control over the equipment was not with the foreign company, but with the Indian company. Accordingly, the amount received by the taxpayer for hiring out dredgers to an Indian company for use at Indian ports was not taxable in India.

CIT v. Van Oord ACZ Equipment BV (T.C.(A).No.1202 of 2007) (Madras High Court)

Liaison Office is engaged in the actual marketing of the products of the foreign company, and therefore the income attributable to the Liaison Office is taxable in India

The taxpayer is a company incorporated in the U.S. In November 2002, the Registrar of Companies issued a certificate of registration as a foreign company, to the taxpayer. During the relevant year, the taxpayer had received an approval from the RBI for establishing a LO in India. During the assessment proceedings, the taxpayer disclosed that besides the fixed remuneration, it had a sales incentive plan under which the employees were entitled to receive upto 25 per cent of their annual remuneration as an incentive.

The AO held that the taxpayer was carrying on business activities in India. On this basis, the AO computed the taxable profit from business activities carried on in India.

Before the High Court, the taxpayer contended that the activities of the LO in India fall within the exception under Article 5(3)(e) of the India-USA tax treaty. The LO was engaged merely in acting as a communication link between the head office in the U.S. and prospective buyers in India, and the activities that were carried out in India were not in the nature of marketing activities.

The Delhi High Court held that the disclosures which were made by the taxpayer before the AO clearly indicate that the activities of the LO were not confined only to being a channel of communication between the head office in the U.S. and prospective buyers in India. The activities of the LO included: (i) explaining the products to buyers in India; (ii) furnishing intimation in accordance with the requirements of the buyers; and, (iii) a discussion of commercial issues pertaining to the contract through the technical representative, after which an order was placed by the buyer directly.

The LO was involved in activities which traversed the actual marketing of the products of the taxpayer in India because it was on the basis of the orders generated that an incentive was envisaged for the employees. Activities of the LO established that it was promoting the sales of the taxpayer in India and the AO was justified in holding that the income attributable to the liaison office was taxable in India.

Brown and Sharpe Inc. v. CIT [Income Tax Appeal No. - 219 of 2014]

Corporate tax

Decisions

Consultancy charges incurred on bid-cum-delisting of shares of a subsidiary is revenue expenditure allowable under Section 37 of the Act

The taxpayer with a view to acquire controlling interest in its subsidiary company incurred certain expenditure on account of bid-cum-delisting of shares of a subsidiary company. The taxpayer pursuant to this intention, made an open offer to public share-holders to acquire their shares and delist the subsidiary company from the stock exchange. For this purpose the taxpayer employed the services of J M Morgan Stanley Pvt. Ltd (Merchant Banker) and ILFS Investments Securities Limited (Syndicate Member) and incurred consultancy expenses. The taxpayer claimed this consultancy expenditure as allowable expenditure under Section 37(1) of the Act. However, the AO rejected the taxpayer's contention as he was of the view that although the purchase of shares of the subsidiary company through public offer did not result in expansion of capital base, it resulted in acquisition of new asset and therefore needed to be treated as a capital expenditure.

The Delhi Tribunal observed that the taxpayer was a promoter of the subsidiary company and the acquisition of shares was to strengthen its controlling interest in that company in furtherance of its business only. The Tribunal referred to various High Court decisions wherein it was held that the interest expenditure incurred on borrowed funds utilised for acquiring controlling interest in companies would be allowable as business deduction since the acquisition of controlling interest in a company is in furtherance of the business purposes of the taxpayer. The Tribunal noted that although the above mentioned decisions were rendered in the context of allowability of claim of interest under Section 36(1)(iii) would equally be applicable to the claim of deduction under Section 37(1) of the Act as the conditions precedent for deduction under both the provisions is same, namely, an expenditure must have been incurred for the purposes of business. Thus the Tribunal held that the expenditure incurred for acquiring controlling interest was allowable as a business expenditure under Section 37(1) of the Act.

Eicher Motors Ltd v. DCIT [TS-760-ITAT-2014(DEL)]

Allows premium on share buy-back from recalcitrant shareholders as revenue expenditure

The taxpayer in its return of income had claimed deduction of INR 81.6 million on account of premium paid on buy back of shares from the Mac Charles group and the Gupta group. During the assessment proceedings, the AO noted that due to oppression and mismanagement by Mac Charles Group, the Company Law Board (CLB) permitted the taxpayer to buy back 1,07,50,000 shares for an amount of INR 192.1 crores. Further, Gupta Group had filed a petition before the CLB for oppression and mismanagement. However, the taxpayer and Gupta Group agreed to settle the matter and agreed for sale consideration of INR 25 per share as against the face value of INR 10 per share. Therefore, a premium of INR 54.3 million was paid to the Gupta Group and an amount of INR

27.3 million was paid to the Mac Charles Group. The taxpayer claimed the same as revenue expenditure. However, the AO disallowed the said claim of the taxpayer.

The Pune Tribunal relying on the earlier year's Tribunal Order in the taxpayer's own case observed that the reduction of the share capital was merely a consequence of the agreement which has to be given effect to, that too by an order of the court where the interest of the company as well as of the public has to be necessarily kept in mind. Thus, writing off of share capital by way of reduction as per the terms of consent decree merely was a consequential action and did not itself represent any effect on the capital structure or the acquisition of any right yielding income or advantage on capital account. Therefore, the impugned expenditure, which was incurred in order to facilitate the smooth running of the business by getting rid of the recalcitrant group of shareholders, was an expenditure incurred out of business expediency and, therefore, wholly and exclusively incurred in the course of carrying on of the business. Hence, the view canvassed by the tax department that the taxpayer has obtained any right or advantage which would affect its capital structure was not acceptable. The Tribunal also referred to the decision of the Mumbai Tribunal in the case of USV Ltd. v. JCIT (ITA No.376/M/2001) wherein expenditure incurred in order to protect the business of the taxpayer was allowed as revenue.

DCIT v. Bramha Corp. Hotels & Resorts Ltd. [TS-740-ITAT-2014(PUN)]

Sim card distribution is equal to sale of 'right to service', provisions of Section 194H is inapplicable

The taxpayer is engaged in the business of providing telecommunication services across the country. They provide telecommunication services, sell service products such as; Starter Kits and Recharge Coupon Vouchers (RCV). RCVs are prepaid vouchers used for selling talk time to pre-paid subscribers. Starter Kits are the new connections containing 'Removable User Identity Module' for providing a telecommunication connection. For the distribution and marketing of SIM cards/RCVs, the taxpayer appointed various distributors/channel partners. Such distributors were provided with SIM cards/ RCVs at the MRP less discount. Thus, discount being profit margin given to the distributors to be realised on resale of such SIM cards/ RCVs to the ultimate customers.

Department conducted surveys under Section 133A of the Act in the premises of the taxpayer. During the course of the survey, the Department alleged that the discount given to the distributors by the taxpayer was not actually a discount but was in the nature of commission paid to the distributors for the services they rendered in marketing and soliciting

customers and consequently, held the taxpayer as assessee-in-default under Section 201 of the Act for not deducting tax at source from the said alleged commission under Section 194H of the Act. On appeal, the CIT(A) as well as the Tribunal ruled in favour of the tax department.

The Karnataka the High Court after referring to the Supreme Court rulings in Bharat Sanchar Nigam Limited and another v. UOI and others [2006] 282 ITR 273 (SC) and Idea Mobile Communication Limited v. Commissioner of Central Excise and Customs (2011) 43 VST 1(SC) (on issue of whether sales tax or service tax was to be paid to the Govt on supply of SIM cards) arrived at the conclusion that SIM cards were never sold as goods independent of the services provided by the telecom service provider and the dominant purpose of the transaction was to provide services and not to sell the materials.

On perusal of the agreements, High Court noted that there was an express mention that the relationship between the taxpayer and its distributors was that of principal to principal. It was further noted that the distributor/channel partner had to pay consideration for the product supplied and it was treated as sale consideration. It was also observed that there was a clause, which specifically stated that after such sale of products, distributor/channel partner could not return the goods to the taxpayer and it was the channel partner who had to insure the products and the godowns at their cost.

In light of the above observations, the High Court concluded that, what is given by the taxpayer to its Distributor/ Channel Partner is a trade discount and not commission. The SIM Card is only a device to have access to a mobile phone network, therefore, it hardly has any value on its own. What is sold by the service provider to the distributor is the right to service.

At the time of sale of a prepaid card by the taxpayer to the distributor, income has not accrued or arisen to the distributor, there is no primary liability to tax on the Distributor. In the absence of primary liability on the distributor at such point in time, there is no liability on the taxpayer to deduct tax at source.

Bharti Airtel Ltd & Ors. v. DCIT [TS-722-HC-2014(KAR)]

Section 79 is inapplicable as both the predecessor and successor companies were subsidiaries of the same holding company, is not acceptable

During the Assessment Year 2009-10, the taxpayer's, shareholding changed hands from Yum Restaurant Asia Pte Ltd. to Yum Asia Franchisees Pte Ltd. Therefore, the AO disallowed carry forward and set off brought forward losses of past years against the taxpayer's income for the current year in terms of Section 79 of the Act, owing to a change in the share holding of the taxpayer company. The CIT(A) confirmed the action of the AO.

The Delhi Tribunal observed that in order to invoke the provisions of Section 79 of the Act it is sine qua non that the change in shareholding pattern should be more than 51 per cent of the voting power of shares beneficially held. It has two important components. One is the percentage of change at 51 per cent and the second is the change of such percentage of voting power of shares beneficially held. In the instant case, it is noticed that the change in shareholding is 100 per cent. It means that the first condition for magnetising Section 79 of the Act is satisfied. The entire dispute is on the second condition of such change in voting power of shares beneficially held. The Tribunal held that although holding and subsidiary companies are bound by their relationship, but do not lose their individual existence in the commercial world. Both are separately liable for the respective transactions undertaken by them. The corporate veil cannot be pierced to treat both as one and the same so as to escape the natural consequences of Section 79 of the Act. If the contention of the taxpayer is taken to a logical conclusion, it would obliterate the separate legal entity of the subsidiary and require the assessment of its income in the hands of the holding company alone, which is patently incorrect. Thus, taxpayer's stand that Section 79 is inapplicable as both the predecessor and successor companies were subsidiaries of the same holding company is not acceptable.

Yum Restaurants (India) Pvt. Ltd. v. ITO [TS-755-ITAT-2014(DEL)]

Difference between the NPV and the future liability of the deferred sales tax is a capital receipt and early settlement of the same cannot be termed as remission / cession of trading liability under Section 41(1) of the Act

The taxpayer under the Industrial Backward Area Scheme of the Government of Maharashtra, was entitled to defer the sales tax liability for a period of seven years under the Deferral Scheme of 1983 and for a period of six years under the Deferral Scheme of 1988. The total sales tax liability which was deferred was INR 7,52,01,378. Subsequently the notification was issued by the Government of Maharashtra regarding premature repayment of deferral Sales Tax at Net Present Value (NPV). The taxpayer availed the option given in said notification and made premature payment of INR 3,37,13,393 against the total liability of INR 7,52,01,378. The taxpayer credited the balance amount of INR 4,14,87,985 to its capital reserve account. The AO taxed the said amount under Section 41(1). The CIT(A) sustained the additions made by the AO. When the matter reached before the Tribunal, a special bench was constituted to adjudicate the issue. Special bench of the Tribunal concluded that the deferred Sales Tax liability of INR 4,14,87,985 being the difference as noted above and credited under the capital reserve account could not be termed as remission/cessation of liability. Consequently, no benefit had arisen to the taxpayer in terms of Section 41(1)(a) of the Act. Aggrieved by the same, the Revenue preferred an appeal before the Bombay High Court.

The Bombay High Court observed that under the deferral sales tax scheme, the taxpayer was allowed to pay the sales tax collected from customers not immediately but after 7 to 12 years. However, as per subsequent notification, an option was given to the taxpayer to pay the NPV of the amount which was to be paid after 7 to 12 years prematurely. The High Court held that the obligation to pay to the government the sales tax amount already recovered and collected from the customers

was in no way wiped out or diluted but the same remained. Under the scheme of deferral of sales tax only an option was given to the taxpayer to approach SICOM and request it to consider the application of the taxpayer of premature payment and discharge of the liability by finding out its NPV.

The High Court noted that the Special Bench had pointed out two requirements that trigger application of Section 41(1) of the Act. First was allowance or deduction is made in respect of the loss, expenditure or a trading liability incurred by the taxpayer, second was that the taxpayer has subsequently obtained any amount in respect of such loss and expenditure or obtained a benefit in respect of such trading liability by way of a remission or cessation thereof. The High Court concluded that there is no evidence to show that there has been any remission or cessation of the liability by the state government, since the taxpayer had to pay whole of the NPV of the amount which he was supposed to pay after 12 years. The High Court thus upheld Special Bench ratio that difference between the NPV, INR 3,37,13,393 against the future liability of INR7,52,01,378 credited by the taxpayer under the capital reserve account in its books of account, was a capital receipt and that the same could not be termed as remission or cession of trading liability and hence the taxpayer did not receive any benefits under Section 41(1) of the Act.

CIT v. Sulzer India Limited and Others [TS-734-HC-2014(BOM)]

Transfer pricing

Decisions

Bombay High Court upholds decision on the issue of share valuation on equity infusion in favour of Shell India

The taxpayer is an affiliate of and belonging to Shell group of companies headquartered in Holland. In 2009, the taxpayer issued 0.85 million equity shares to its non-resident associated enterprise (AE) at a face value of INR 10. The same, was not disclosed in the Form 3CEB as the taxpayer was of the view, that in absence of income arising, it is not an international transaction. However, the Transfer Pricing Officer (TPO) held that in view of Chapter X of the Act, once a transaction between the parties is an international transaction, adjustment to transfer pricing can be done even on capital account. The TPO held that the shares were allotted to the AE at a price which was lower than the Arm's Length Price (ALP) of issue of shares resulting into short receipt of consideration. Accordingly, the TPO on the basis of the ALP, computed enhancement of the issue price which was considered as a deemed loan to the AE and also charged interest on the amount received.

The Bombay High relied on its earlier ruling in the case Vodafone. The High Court inter alia held that to apply Chapter X of the Act, income should arise from an international transaction chargeable to tax under the Act. Further, the High Court observed that there is no charge in the Act on account of capital amounts received and/or arising on account of issue of shares by an Indian entity to a non-resident entity. Chapter X of the Act does not contain any charging provision but is a machinery provision to arrive at the ALP of a transaction between AEs.

Shell India Markets Pvt. Ltd. v. ACIT LTU and others (Writ Petition No. 1205 of 2013 – Bombay High Court)

Delhi Tribunal holds that Other Method as per rule 10AB shall have retrospective effect and provides realistic and purposive interpretation to the term 'price' under CUP method and Other Method

The taxpayer is engaged in the business of freight transportation, time defined air and ocean transport and freight forwarding. The taxpayer enters into two types of international transactions – a) arranging import of cargo and b) arranging export of cargo by air and sea transportation for delivery to consignees through AEs. While the taxpayer controls the domestic pricing, the pricing for end customers in connection with consignment picked up abroad is determined by the AE, and the profits earned after deduction of transport costs are shared in a 50:50 ratio.

The taxpayer selected Comparable Uncontrolled Price (CUP) method as the most appropriate method as the profits were shared equally between the associated parties, which was in line with the industry norms and thus the transaction with the AEs and with unrelated parties, being on equal terms, were comparable. The TPO rejected this approach and adopted Transactional Net Margin Method (TNMM) as the most appropriate method as it was of the contention that the taxpayer had failed to demonstrate the actual price charged for comparable services was the same as in case of independent parties.

Tribunal ruling

The Tribunal analysed the definition of ALP determination under Rule 10B which sets out that the CUP method can be used only when the amount charged for similar uncontrolled transaction was the same as an international transaction between the AEs and observed that the term 'price' for CUP method as per Rule 10B(1)(a) includes not only monetary amount but also 'mechanism in terms of formulae to arrive at the consideration'.

Further, the Tribunal relied on the Supreme Court's judgment in the case of CIT v. Vatika Township Private Limited (2014 TIOL 78 SC), where it was held that 'If a legislation confers a benefit on some persons but without inflicting a corresponding detriment on some other person or on the public generally, and where to confer such benefit appears to have been the legislators object, then the presumption would be that such a legislation, giving it a purposive construction, would warrant it to be given a retrospective effect.'

Accordingly, the Tribunal held that the Other Method under Rule 10AB which confers the benefit of an additional method of ascertaining ALP and, inter alia, relaxes the rigour of CUP method, can only be retrospective in effect i.e. w.r.e.f. 1 April 2002.

The Tribunal also held that the Other Method is not a residual method but it is at par with all other methods and is thus a direct method to determine ALP, and has an inherent edge over indirect methods such as TNMM and Profit Split Method

Toll Global Forwarding India Pvt Ltd v. DCIT (ITA No. 5025)

Indirect tax

Service Tax - Decisions

CENVAT credit on outdoor catering service allowed even for the period post 1 April 2011

In the instant case, the issue was whether CENVAT credit, with respect to cost borne by the company for provision of outdoor catering services to its employees, would be eligible.

The Mumbai Tribunal on the basis of the following observations held that CENVAT credit on such outdoor catering would be eligible:

- 'Outdoor catering' per se is eligible input service but it is not eligible for credit only when it is used for personal use or consumption of any employee.
- Employees have used these services during normal business hours only and cost of such services is borne by the company and not recovered from employees.
- Cost of such input services forms part of the cost of final product

Hindustan Coca Cola Beverages Pvt Ltd v. CCE [2014-TIOL-2460-CESTAT-MUM]

Circulars/Notifications/Press Releases

Non-applicability of restriction of availment of credit after 6 months in case of re-availment

The Central Board of Excise and Customs (CBEC) has clarified that the restriction for availment of CENVAT credit within six months from the date of a relevant document (i.e. invoice, challan, any other specified document, etc.) pertains to availment of credit for the first time. Such restriction will not apply while taking re-credit of amount reversed in the following cases:

- Where the payment of value of input service and service tax payable is not made within three months of date of the relevant document
- Where the value of any input or capital goods before being put to use on which CENVAT credit has been taken, is written off or provisions are made in books of accounts
- Where the inputs sent to a job worker are not received back within 180 days.

Circular No. 990/14/2014-CX-8, dated 10 November 2014

Service tax department can conduct service tax audit along with an officer authorised by a designated authority or a nominated chartered/cost accountants

CBEC, vide a Notification, amended Service tax Rules to provide for power to conduct scrutiny of records by an officer (authorised by designated authority) or a nominated chartered/cost accountants. The CBEC also clarified (vide a Circular) that such scrutiny would include audit by the departmental officers.

The Circular also provided that with effect from 6 August 2014, the central government has power to formulate rules involving imposition of a duty for furnishing information, keeping records and the manner in which such records shall be verified (which includes within its ambit, audit by the departmental officers).

Notification no. 23/2014-Service tax dated 5 December 2014 and Circular No. 181/7/2014-ST dated 10 December 2014

Central Excise - Decisions

No need to submit further applications before the CESTAT for extension of the stay

The Ahmedabad Tribunal held that any stay order passed by the CESTAT, if in force beyond 7 August 2014, would continue till the disposal of the appeals and there is no need for filing any further applications for extension orders granting stay either fully or partially.

Venketeshwara Filaments Private Limited & Others v. CCE, [2014-TIOL-2388-CESTAT-AHM]

Customs Duty

Notifications/Circulars/Press Releases

Revised All Industry Rates of Duty Drawback notified

The central government notified the revised All Industry Rates (AIR) of Duty Drawback (effective from 22 November 2014). Key changes are as follows:

- Drawback caps continued on most tariff items with AIRs above 2 per cent.
- It has been made explicit that where the claim for duty drawback is filed with reference to the rate in the AIR Schedule, an application for fixation of Brand Rate will not be admissible.
- Several entries have been rationalised by merging them at respective four digit level.
- The hitherto residuary rate of 1 per cent (composite) and 0.3 per cent (Customs) has been changed to 1 per cent (composite) and 0.15 per cent (Customs).
- Existing residuary rates of 1.3 per cent and 1.7 per cent have been increased to 1.4 per cent and 1.9 per cent, respectively, with some exceptions.
- Separate entries have been created distinguishing certain export products
- In continuation of a transitory arrangement, for the items incorporated in the drawback schedule from the erstwhile DEPB Scheme there has been a reduction in the AIR.

Notification No 109/2014-Cus (NT) and Notification No 110/2014-Customs (N.T.), both dated 17 November 2014 read with Circular No. 13/2014-Cus dated 18 November 2014

Foreign Trade Policy

Instructions

No fresh approval is required from UAC, in case the services were earlier approved

Earlier despite of issue of default list of authorised services by the Department of Commerce, the SEZ Developers and Units were forced to apply afresh to the Unit Approval Committee (UAC) even for those authorised services which are already approved earlier by the UAC for the said Developers/Units. Now, the Ministry of Commerce and Industry has instructed the Development Commissioners that they should not insist on fresh application for authorised services that have already been approved by the UAC.

Instruction No. 83/2014 dated 21 November 2014

VAT - Decisions

Profit retained by contractor towards sub-contracted works is non-taxable under the Kerala VAT law

In the present case, a writ petition was filed before the Kerala High Court regarding the issue of taxability of profit element of main contractor, where the entire work was sub-contracted for execution.

The taxpayer, a works contractor, was awarded a contract by BPCL and in turn, the entire work was sub-contracted. The taxpayer applied to the Commercial Tax Officer for issuance of a liability certificate in Form 20B under the Kerala VAT Rules to show that the tax liability, if any, has been discharged. The amount mentioned in the certificate represented the profit component earned by the taxpayer under the said contract. The taxpayer contended that it was not liable to discharge any tax liability on the said amount as it merely represented profit under the works contract. However, the Commercial Tax Officer declined the request, resulted as discharge of tax liability under protest. After payment of tax liability under protest, the taxpayer was issued Form 20B, and subsequently obtained the final payment from BPCL. Aggrieved thereby, the taxpayer filed the Writ petition before the Kerala High Court.

The High Court referred to the Apex Court ruling in the State of Andhra Pradesh and Others v. Larsen & Tourbo Ltd. and Others [(2008) 17 VST 1(SC)], wherein it was observed "work executed by a sub-contractor, results in a single transaction and not multiple transactions….if the argument of the Department is to be accepted it would result in plurality of deemed sales which would be contrary to article 366(29A)(b) of the Constitution." The High Court observed that in the present case, taxpayer had sub-contracted the entire work and had also obtained Form 20H certificate (a certificate to be issued by sub-contractor to the main contractor under the Kerala VAT Act) from the sub-contractor. The sub-contractor discharged the tax liability in respect of entire work that was sub-contracted, and the amounts retained by taxpayer, represented only the profit element that accrued to it in the capacity as main contractor. HC held that the taxpayer was not liable to pay any tax under the Kerala VAT Act, as there was no sale of material in the execution of the said works contract. In the absence of any taxable event under the Kerala VAT laws, the authorities could not have demanded tax on the amounts retained as profit.

Surya Constructions v. State of Kerala and others [TS-552-HC-2014(KER)-VAT]

Notifications/Circulars/Press Releases

Maharashtra

The exemption for non-filing of CST returns in case of no interstate sales during any return period (provided the MVAT Return for the said period shows NIL turnover of interstate sales) has been withdrawn. Accordingly, the dealers who are affecting interstate sales, stock transfers, sales outside the state, sale in course of export or sales in the course of import, are now required to file CST returns. It is to be noted that the dealers who are not filing CST returns in the above cases shall be treated as defaulters. This Circular will be applicable for the Returns pertaining for the period starting from 1 October 2014 onwards.

Trade Circular No. 20T of 2014 dated 25 November 2014

Rajasthan

The cutoff date for waiver of interest for outstanding demand on account of non-furnishing of declaration form or nonpayment of purchase tax on marble has been extended from 31 October 2014 to 31 January 2015.

Notification S.O.47. No. F.12(59)FD/Tax/2014-25 dated 14 July 2014

Tamil Nadu

The Circular clarifies that the exporters of exempted goods which have been manufactured out of taxable inputs are eligible to avail the benefit of refund of ITC on related purchases of taxable goods.

Circular No.59/2014 Acts Cell III/34185/2014 dated 27 November 2014

Realisation of revenue is showing a downward trend due to lack of understanding of procedures and provisions on the part of some of the officers as well as disregard for principles to be followed, despite various Circulars issued in connection thereto. Also, many works contractors indulge in suppression of whole projects such as suppression of inter-state purchases, suppression of value addition/sales turnover, etc. Therefore, the Tamil Nadu VAT department has issued a comprehensive Circular stating legal history, current legal status and provisions applicable in regard to Works Contract in the State of Tamil Nadu.

Circular No.54/2014 D3/ 34875 / 2014 Ref. No. D3/34875/2014 dated 24 October 2014

Gujarat

With effect from 18 November 2014, the following scheme for tax payment by civil works contractors, for the period 1 April 2006 has been notified:

- Only civil works contractors are eligible to get benefit under this scheme;
- Tax at 0.6 per cent is required to be paid from 1 April 2006 on works contract turnover. Purchase tax is also required to be paid on purchases made from unregistered dealers;
- Dealers who wish to apply for this scheme can do so during the assessment, reassessment and during revision proceedings;
- Dealers who have applied for the scheme shall be eligible to get remission from interest and penalty provided the tax is paid within 180 days from the effective date of the notification.

Notification No. Gujarat/VAT/14-15/185/137 dated 18 November 2014

Procedures for electronic generation of Forms 402, 403 and 405 for every movement of taxable and exempt goods to and from the state (including movements within the state) have been prescribed. The online generation of forms and online declaration shall come into effect from 22 December 2014 for the goods of the dealers whose annual total turnover exceeds Rs. 50 Crore. For remaining taxable goods, the order shall come into effect from the date as may be declared in future.

Notification No. Guj/VAT/Check post/form 402-403-405/2014-15/160/138 dated 3 December 2014), an order (GVL/VAT/Sec. 68 and 69/(1) dated 3 December 2014 and order No.GVL/VAT/ Sec.68 and 69/(3) dated the 20 December, 2014)

KPMG in India

Ahmedabad
Commerce House V
9th Floor, 902 & 903,
Near Vodafone House,
Corporate Road, Prahlad Nagar
Ahmedabad - 380 051.
Tel: +91 79 4040 2200
Fax: +91 79 4040 2244

Bengaluru
Maruthi Info-Tech Centre
11-12/1, Inner Ring Road
Koramangala, Bengaluru 560 071
Tel: +91 80 3980 6000
Fax: +91 80 3980 6999

Chandigarh
SCO 22-23 (Ist Floor)
Sector 8C, Madhya Marg
Chandigarh 160 009
Tel: +91 172 393 5777/781
Fax: +91 172 393 5780

Chennai
No.10, Mahatma Gandhi Road
Nungambakkam
Chennai 600 034
Tel: +91 44 3914 5000
Fax: +91 44 3914 5999

Delhi
Building No.10, 8th Floor
DLF Cyber City, Phase II
Gurgaon, Haryana 122 002
Tel: +91 124 307 4000
Fax: +91 124 254 9101

Hyderabad
8-2-618/2
Reliance Humsafar,
4th Floor, Road No.11,
Banjara Hills
Hyderabad 500 034
Tel: +91 40 3046 5000
Fax: +91 40 3046 5299

Kochi
Syama Business Center
3rd Floor, NH By Pass Road,
Vytilla, Kochi 682 019
Tel: +91 0484 3027000
Fax: +91 0484 3027001

Kolkata
Unit No. 603 – 604, 6th Floor,
Tower – 1, Godrej Waterside, Sector - V,
Salt Lake, Kolkata - 700 091
Tel: +91 33 4403 4000
Fax: +91 33 4403 4199

Mumbai
Lodha Excelus, Apollo Mills
N. M. Joshi Marg
Mahalaxmi, Mumbai 400 011
Tel: +91 22 3989 6000
Fax: +91 22 3983 6000

Pune
703, Godrej Castlemaine
Bund Garden
Pune 411 001
Tel: +91 20 3058 5764/65
Fax: +91 20 3058 5775

Contact us:

Girish Vanvari
Co-Head of Tax
T: +91 (22) 3090 1910
E: gvanvari@kpmg.com

Hiten Kotak
Co-Head of Tax
T: +91 (22) 3090 2702
E: hiten@kpmg.com

Punit Shah
Co-Head of Tax
T: +91 (22) 3090 2681
E: punitshah@kpmg.com

www.kpmg.com/in

Latest insights and updates are now available on the KPMG India app.
Scan the QR code below to download the app on your smart device.

Google Play | **App Store**

Printed in India (NEW0115_023)