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India Tax Konnect

Contents

Editorial

The Finance Minister, while responding to discussions on the Finance Bill in the Rajya Sabha on 7 May 2015, announced the constitution of a Committee headed by Justice A.P. Shah to look into the issue of Minimum Alternate Tax on Foreign Institutional Investors as well as other issues which are referred to it. The Committee held its first meeting on 25 May 2015 and has invited suggestions and representations from all stakeholders, including industry associations on the above issue under examination.

On 14 May 2015, the Finance Act, 2015 received the President's assent. Certain amendments introduced in the Finance Act, 2015 were to be made effective post this assent. One of the key amendment is increase in the rate of service tax from 12 per cent to 14 per cent (subsuming the cess of 3 per cent).

The Government of India passed the Black Money (Undisclosed Foreign Income and Assets) and imposition of Tax Act, 2015 on 26 May 2015 to set out an unequivocal regime that makes it easier for taxpayers to disclose previously undisclosed income which is being held overseas, e.g., in foreign financial accounts and other foreign assets. It seeks to check the black money menace with stringent provisions for those stashing illegal wealth abroad.

The Central Board of Direct Taxes (CBDT) formulated the Central Action Plan for FY 2015-16 setting the timelines for key taxpayer services with a view to bring focus on collection of direct taxes in a non-adversarial and fair manner and facilitating voluntary compliance.

Since its introduction in 2001, the Indian transfer pricing (TP) regulations have been a significant area of controversy between the tax department and taxpayers. While computing arm's length price (ALP), availability of range as a standard deduction and use of single year v. multiple year data, has been two most litigious TP issues. The CBDT, on 21 May 2015, issued the draft scheme of the proposed rules on implementation of range concept and multiple year data for computation of the ALP of international transactions or specified domestic transactions undertaken on or after 1 April 2014. Comments and suggestions from stakeholders and general public were invited until 31 May 2015.

We at KPMG in India would like to keep you informed about 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

Income from booking seats/space under code sharing agreement with third party airlines cannot be held as space/slot charter and therefore benefit under India-USA tax treaty is not available

The taxpayer, a U.S. based company, was engaged in the business of carriage of cargo and passengers on its own aircraft and/or on third party aircrafts. The taxpayer obtained an approval from the Director General of Civil Aviation (DGCA) to undertake scheduled air services in India. The taxpayer was also granted approval by the Reserve Bank of India (RBI) to establish branches in India for undertaking activities related to booking of air passengers and air freight. The taxpayer has 'Interline Cargo Special Prorate Agreements' with other airlines for carriage of cargo and 'code sharing agreements' with other airlines for carriage of passengers. These agreements provide for space sharing for cargo and seat sharing for passengers at agreed rates. There is no chartering of aircrafts.

During the year under consideration, the taxpayer filed a return of income declaring 'nil' income from business operations. The taxpayer did not offer the revenue received on account of the usage of third party carriers for carriage of cargo and passengers. The taxpayer claimed that such revenues cannot be taxed in India pursuant to exemption under Article 8 of the India-USA tax treaty. The Assessing Officer (AO) held that the arrangement of the taxpayer with third party carriers is not akin to that of pooling/chartering under Article 8 of the tax treaty. The AO held that the revenue generated from the usage of third party carriers for carriage of taxpayer's cargo and passengers would not fall under Article 8(1) or Article 8(2) or Article 8(4) of the tax treaty. Hence, benefit of Article 8 cannot be given to the taxpayer in this regard.

The Mumbai Tribunal held that income derived from booking of seat/space under code sharing agreement cannot be held as space/slot charter in the absence of inextricable link between voyage from India to interim destination by third parties under code sharing agreement and from interim destination to final destination by taxpayer's owned/chartered/leased aircraft. Therefore, receipts to the extent of code sharing agreement cannot be said to be profits derived from operation of aircraft/ship in international traffic under Article 8(1) read with Article 8(2) of the India-USA tax treaty.

Further, pool arrangement under Article 8 of the tax treaty requires coming together of several persons to contribute and combine the resources and sharing them amongst the members of the pool. However, in the present case, the third party is contributing its aircraft and the taxpayer is only using the resources of the third party by booking seats in the aircraft. Therefore, the arrangement does not meet the principle of pool arrangement under Article 8(4) of the tax treaty, and accordingly profits cannot be claimed as exempt under the said Article.

Delta Air Lines, Inc. v. ADIT (ITA No. 1256/Mum/2014) (Mum) – Taxsutra.com

The taxability under Section 172 of the Income-tax Act is qua a ship and not qua the enterprise owning or using it under a charter agreement. A foreign shipping company owning a ship is eligible for treaty benefit on freight earned in India

The taxpayer, an agent of a U.K. based Trans Shipping ltd, was engaged in the business of rendering services relating to port and income tax clearances to the foreign vessels touching the port in Gujarat. For Assesment Year (AY) 2001-02, the taxpayer requested the Tax Recovery Officer (TRO) for the issuance of income tax clearance certificate with respect to M.V stove Campbell (a foreign vessel) carrying cement in bulk.

The TRO granted a certificate and treated the freight income earned as exempt under Article 9(1) of the India-U.K. tax treaty. Article 9(1) of the tax treaty provides that income of an enterprise of a contracting state (i.e. Trans shipping ltd. U.K.) from the operation of ships in international traffic would be taxable only in that state (i.e. U.K.). However, almost after the expiry of three years, the TRO noticed that as per the charter party agreement between the owner and the charterer ,the 'charterer' had to the pay tax on freight income, and as the 'charterer' was based in the Bahamas with which India does not have tax treaty, tax treaty relief would not be available. Subsequently, a show cause notice was issued to the taxpayer to explain as to why the tax treaty benefit should not be withdrawn and why the freight income earned should not be made taxable.

After analysing the facts of the case, the Tribunal observed that it was erroneous on the part of the authorities to determine the eligibility of treaty benefits on the basis of domicile of the person having contractual liability to pay tax. It does not matter as to whether under the charter party agreement the owner was liable to pay the tax or whether the charterer was liable to pay the tax. What really, therefore, matters is as to who was chargeable to tax in respect of such an income.

After analysing provisions of Section 172(1) of the Income-tax Act, 1961 (the Act), the Tribunal held that the taxability under Section 172 of the Act is qua a ship and not qua the enterprise owning or using it under a charter agreement. The AO himself assessed the U.K. based company that is the owner of the ship and not the charterer of the ship. If the TRO himself accepts that the income was earned by the owner of the ship (based in U.K.) and not the charterer of the ship (based in Bahamas), the India-U.K. tax treaty was rightly invoked. The Tribunal held that

since the income belonged to the owner in the U.K. the benefit of Article 9 would be applicable to the taxpayer.

Separately, the Tribunal also observed that the assessment order under Section 172(4) was framed in 2005, whereas the ship had already left the Indian port in 2001. The assessment was thus framed almost three years after the end of the relevant previous year. Undoubtedly, at the relevant point in time, there was no time prescribed under the statue for framing the assessment under Section 172(4) and the provisions of Section 172(4A), which set this time limit as nine months from the end of the financial year in which return under Section 172(3) is filed, came into effect from 1 April 2007, but that does not mean that in the absence of this time limit under Section 172(4A), the assessment under Section 172(4) could have been done at any point in time. The Tribunal relied on the Bombay High Court ruling in the case of DIT v. Mahindra & Mahindra Limited [2014] 365 ITR 560 (Bom) and observed that even when the statute did not prescribe a time limit for completing assessment under Section 172(4), such assessments could be framed only within a reasonable time.

With effect from 1 April 2007, the statute itself has considered the period of nine months from the end of the financial year in which return under Section 172(3) is filed, as reasonable time limit within which assessment order under Section 172(4) is to be framed. When this time limit is statutorily treated as a reasonable time limit for the returns filed after 1 April 2007, this time limit can also be treated as a reasonable time limit for the return filed prior to 1 April 2007 as well. Therefore, impugned assessment order under Section 172(4) was indeed barred by limitation.

H. K. Dave Limited v. TRO (I.T.A. No. 1049/Ahd/2006) (Ahd) – Taxsutra.com

Corporate tax

Decisions

Notional interest income on domestic advances cannot be taxed in absence of specific provision under the Act

The taxpayer, a private limited company, filed the return of income declaring a loss. During the assessment proceedings, the AO made an addition on account of notional interest earned on advances given to Smart Tourist Private Limited. Consequently, the taxpayer filed the revision petition under Section 264 of the Act before the Commissioner but the same was rejected. Against such order, the taxpayer filed a writ petition before the Delhi High Court.

The High Court referred to the decision of the Guwahati High Court in the case of B and A Plantations & Industries Ltd. wherein it was observed that there was nothing to show that the taxpayer had received interest or that the company to whom the loan was given had paid interest to the taxpayer. The only finding recorded by the tax department was that the taxpayer 'ought to' have charged interest. Referring to an earlier decision of the Guwahati High Court, in Highways Construction Co. Private Limited, the Court observed that their attention had not been invited to any provision of the Act empowering the income-tax authorities to include in the income, interest which was not due or not collected.

The High Court held that in the absence of any specific provision under which the so called notional income on advances could be brought to tax, the addition on account of a notional income on advances is deleted.

Shivnandan Buildcon Pvt. Ltd. v. CIT [W.P.(C) 6265/2013 and 6326/2013] (Delhi High Court) – Taxsutra.com

Carried forward depreciation becomes the depreciation of the current year and has to be set-off against the profits of the current year prior to the carried forward investment allowance

The taxpayer is a public limited company. The business income for that year was arrived at INR28,715,912. The taxpayer had unabsorbed investment allowance and unabsorbed depreciation of the earlier years. In its income-tax return, however, it chose to carry forward unabsorbed depreciation and claimed set-off of the said unabsorbed investment allowance to the extent of INR28,715,912, thereby showing the returned income as 'nil'. According to the AO, it was not the investment allowance, but unabsorbed depreciation of the earlier years which had to be set off first. Therefore, instead of allowing the taxpayer to carry forward, the AO adjusted the unabsorbed depreciation of the earlier years, and accepted 'nil' income return.

The Supreme Court observed that as per Section 32(2) of the Act, the depreciation allowance or part thereof to which effect has not been given in a particular assessment year owing to there being no profits or gains chargeable for previous years or owing to profits and gains chargeable being less than the allowance, such unabsorbed depreciation allowance is to be added to the amount of the allowance for depreciation for the following previous year and it is 'deemed to be part

of that allowance for that previous year or the succeeding previous years, as the case may be'. Thus, by legal fiction, the unabsorbed depreciation of the past years, becomes the depreciation of the relevant year and can be set off against income chargeable under any head. According to the CBDT Circular No. 202 dated 5 July 1976, the combined effect of the provisions of Sections 32, 32A, 33, 33A and 72 is that in a case where there are allowances in the nature of depreciation allowance, investment allowance, etc. such allowances and losses would be deductible in the order mentioned there. It emerges from Section 32A(3) that unabsorbed investment allowance takes precedence over current investment allowance. In the present case, the taxpayer claimed the depreciation allowance insofar as it pertained to the current year. At the same time, it did not want to claim the set off of the unabsorbed depreciation allowance of the previous years. Once the unabsorbed carried forward depreciation has become a part of the depreciation of the current year, it is not open to the taxpayer to bifurcate the two again and exercising its choice to claim the depreciation of the current year under Section 32(1) of the Act and take a position that since unabsorbed depreciation of the previous years is not claimed, it cannot be thrusted upon the taxpayer.

Seshasayee Paper & Boards Limited v. DCIT (SC) [Civil Appeal nos. 1812-1813 of 2005, Civil Appeal no. 4498 of 2015 - (Arising out of SLP (C) no. 15251 OF 2008)]

Circulars/Notifications/Press Releases

CBDT Circular prescribes the action to be performed by the taxpayer and the AO for verification and correction of demand available or uploaded by AOs on the CPC demand portal

The CBDT vide Instruction No.4, dated 7 April 2014 had prescribed Standard Operating Procedure (SOP) for verification and correction of demand available or uploaded by AOs on the CPC demand portal. Further, a facility has been made available to taxpayers on the e-filing website (www.incometaxindiaefiling.gov.in) to provide online responses to such demands.

The CBDT through Circular No. 8/2015 issued on 14 May 2015 prescribed the actions required to be performed by the taxpayer and the AO.

Action to be performed by taxpayers

- The taxpayer needs to login on the e-filing website with the respective details. The taxpayer has to select the respective options available on the portal i.e. demand is

correct, demand is partially correct, disagree with demand. The taxpayer may also be required to provide additional information as the case may be.

- Once it is confirmed that the demand is correct, the taxpayer cannot disagree with the demand. If any refund is due, the outstanding demand along with interest will be adjusted against refund due. In any other case, the taxpayer has to immediately pay the demand.
- If the demand is partially correct, the taxpayer needs to provide reasons for incorrect demand i.e. demand is already paid, demand has already been reduced by rectification/ revision, appeal has been filed, etc. Further based on the reasons selected, the taxpayer needs to provide prescribed additional information.
- If the taxpayer disagrees with the demand, he must furnish the details of disagreement along with reasons.

Action on the part of the tax department

The AO or CPC Bangalore after verification of the details should reduce/remove/confirm the demand in appropriate cases as per the procedure prescribed in the aforesaid circular and in accordance with earlier instructions issued by CBDT. However, following cases are to be verified on priority basis:

- The taxpayer has furnished information in response to notice under Section 245 of the Act (Set off of refunds against tax remaining payable), or
- The taxpayer has requested for reduction/removal of demand, or
- Information regarding demand reduction/removal is available in department records, or
- Details are already available in the system, such as additional Tax Deduction at Source (TDS) credits reported by deductor in case of earlier TDS mismatch.

This Circular also dealt with the tax department's actions during different scenarios during verification and confirmation of demand.

CBDT Circular No. 8/2015, dated 14 May 2015

Annual Report - 2014-15

The Finance Ministry released its Annual Report for Financial Year (FY) 2014-15. The report, inter alia, provides the development of the Indian Government made during the FY 2014-15 on matters concerning direct tax laws particularly international taxation, TP, etc. The highlights of the Annual Report relating to the developments on tax laws are as follows:

Steps for negotiation of agreements with foreign countries

The Government of India can obtain information from more than 130 countries/jurisdiction under tax treaties/TIEAs/ Multilateral Convention/SAARC Multilateral Agreement. Effective investigation of tax evasion and avoidance, including unearthing of unaccounted money stashed abroad, is possible only if there is access to information from foreign countries. However, foreign governments, particularly tax havens, are most unlikely to provide information on the basis of just letters or on a plea regarding their moral obligations to prevent tax evasion. Such information about money and assets hidden abroad and about undisclosed transactions entered into overseas, can be obtained only through 'legal instruments' or treaties entered between India and those countries. For this purpose the Government of India is in negotiation of various tax treaties, entering into new tax exchange information agreements, multilateral agreements and limited agreements.

Automatic Exchange of Information

India has taken a lead role in international fora, including at G20 and Working Party 10 of the Organisation for Economic Co-operation and Development (OECD), towards building an international consensus amongst major economies. The problem of offshore tax evasion and flow of illicit money can be addressed only by the free flow of financial account information, exchanged amongst countries on an automatic basis.

Advance Pricing Agreement

The Advance Pricing Agreement (APA) provisions seek to provide certainty to taxpayers and the tax administration on TP issues, thereby reducing litigation. APA provisions were introduced in India vide the Finance Act, 2012. Thereafter, the APA Scheme was notified in the Income-tax Rules, 1962 (the Rules) on 30 August 2012. In May 2013, a taxpayer series on 'Guidance on APA Scheme and FAQs' was released. Roll-back of APAs was announced by the Finance Minister in his Budget Speech on 10 July 2014. The necessary legislative changes in this regard were carried out through the Finance (No. 2) Act, 2014.

Global Forum on Transparency and Exchange of Information

The Global Forum carries out an in-depth monitoring and peer review of the standards of transparency and exchange of information for tax purposes through a Peer Review Group (PRG) which is chaired by France and India is one of the vice-chairs of the PRG. Through the process of Peer Review, the PRG examines the extent to which the jurisdictions have implemented the international standards on transparency and exchange of information for tax purposes and suggests ways and means by which the deficient jurisdictions can improve and come at par with the recognised international standards.

G20/OECD Project on Base Erosion and Project Shifting

In July 2013 the OECD, working with G20 countries, launched an Action Plan on BEPS, identifying 15 specific actions needed in order to equip governments with domestic and international instruments to address this challenge. After detailed negotiations in G20, it was agreed that all the eight non-OECD G20 countries including India would participate in the 'Project on BEPS' on an equal footing. India, Brazil, China and South Africa now represent the eight non-OECD G20 countries in the 'Bureau Plus' on the BEPS Project.

Source: www.taxsutra.com

Transfer pricing

Decisions

Delhi High Court rules that higher or abnormal profits/ losses cannot be a factor for exclusion of a comparable

The taxpayer used Transactional Net Margin Method (TNMM) and identified four comparables which were engaged broadly in the same economic activities as the taxpayer. The Transfer Pricing Officer (TPO) concluded that multiple year data could not be used and also introduced two new comparables with abnormal business profits. Further, all the lower authorities included three entities which had very high profit margins as compared to the taxpayer and rejected three other comparables selected by the taxpayer.

High Court ruling

- The High court reiterated the application of Section 92C of the Act, Rule 10B(1), 10B(2), 10B(3) and 10B(4) of the Rules and provided a tabular statement containing reasoning given by previous 21 Benches of the Tribunal to conclude on similar grounds of exclusion of 'supernormal' profit making companies, which was relied on by the taxpayer. It also discussed the Maersk Global Centres v. ACIT 43 Taxmann 100 (2014) (Mumbai Special Bench) ruling, wherein a Special Bench was formed to specifically address this question.
- Mere circumstance of a company which otherwise conforms to all stipulations in Rule 10B, presenting a peculiar feature such as a huge profit or a huge turnover, ipso facto does not lead to its exclusion and would require an enquiry under Rule 10B(3).
- The use of multiple year is permitted only in the event that they have an influence on the determination of price. The Court rejected the taxpayer's contention for relying on the previous years' data. Wide fluctuations in the profit margin of the comparables year-on-year, does not justify the need to take into account the previous years' profit margins. Multiple year data can only be included in the manner provided in Rule 10B(4).
- India is not a member of the OECD and hence these Guidelines have only a persuasive status and do not have any legal sanction. The Court acknowledged that the OECD Guidelines and Rules in the specific case, are in consonance, since both do not in any manner, prescribe automatic exclusion of entities with extreme financial results.
- Remitted the matter with regard to three comparables to Dispute Resolution Panel (DRP). For all the three companies, the Court directed that the DRP shall carry an analysis under Rule 10B(3) and with regard to one comparable, enquiry regarding the functional similarity also to be carried out. Further to the analysis, if there are material differences arising out of their exceptionally high profits, which cannot be eliminated, the said company cannot be included as a comparable.

ChrysCapital Investment Advisors (India) Pvt Ltd v. DCIT (ITA No 417 of 2014)

Mumbai Tribunal held that the taxpayer is not entitled for deduction under Section 10B of the Act in respect of the suo-moto addition made by the taxpayer as per Form No. 3CEB but not brought into India within the stipulated time frame

The taxpayer was engaged in the business of software development and export of software and was a registered 100 per cent Export Oriented Unit (EOU). While filing the Form No. 3CEB the taxpayer had made a suo-moto adjustment to its income but had not recorded the aforementioned adjustment amount as income in its books of accounts and did not bring the aforementioned adjustment amount in India. The TPO accepted suo-moto adjustment made by the taxpayer and did not dispute the ALP of international transactions. The AO however did not allow a tax holiday benefit under Section 10B of the Act on the amount of suo-moto adjustment and computed the taxpayer's income accordingly. Commissioner of Income-tax (Appeals) [CIT(A)] confirmed the action of the AO.

Tribunal ruling

- The first proviso to Section 92C(4) of the Act provides that, in case of enhancement of income consequent to determination of the ALP by the tax authorities, tax holiday benefit is not to be allowed in respect of the enhanced income. If Section 92C of the Act is read in isolation to other provisions of the Act, there would be no difficulty in interpreting the word 'enhance' as done by the Tribunal in the case of I Gate Global Solutions Ltd. v. ACIT (ITA No. 248 and 249(Bang) of 2007). However, in the present case the provisions of Section 92C of the Act have to be read in consonance with the provisions of Section 10B of the Act.
- Section 10B of the Act is a special provision in respect of newly established 100 per cent EOUs wherein the legislative intention is to give incentive to 100 per cent EOUs but at the same time expecting such EOUs to bring the sale proceeds in convertible foreign exchange in India within a period of six months from the end of the previous year. Thus, the tax holiday is extended only when the money is brought into India in convertible foreign exchange. If in the taxpayer's case, benefit of Section 10B of the Act is allowed, without the taxpayer having brought the money to India, then every taxpayer will first under price its sale with Associated Enterprises (AEs) and thereafter suo-moto enhance the sale price by making TP adjustment and claim the deduction under Section 10B of the Act.
- Keeping the legislative intent in mind, the taxpayer cannot be permitted to stretch a benevolent provision to avail benefit which the legislature never intended to provide. Thus, the taxpayer is not entitled for deduction under Section 10B of the Act in respect of the suo-moto addition

declared by the taxpayer in the Form No. 3CEB but not brought into India within the stipulated time frame of six months.

Agilisys IT Services India Pvt. Ltd. (Formerly known as Netdecisions Pvt. Ltd.) v. ITO (ITA 2113/M/11, ITA 2226/M/11 and C.O. 89/Mum/2011)

Bombay High Court held that the considerations applied for issuance of a corporate guarantee are distinct and separate from that of a bank guarantee and such comparison is not appropriate

During FY 2006-07, the AE of the taxpayer had taken a loan of USD20,000,000 from ICICI Bank for which the taxpayer provided a corporate guarantee and charged a guarantee commission at 0.5 per cent. The TPO observed that the taxpayer became more leveraged with an increase in its overall risk exposure due to the corporate guarantee provided which would ultimately effect the cost of borrowing. Further, the AE was newly established and had a low credit rating. Thus the TPO concluded that without the taxpayer's guarantee, ICICI Bank would not have given the loan to the AE. The TPO further held that banks and companies were charging at least 3 per cent for providing guarantees and therefore, the ALP for the guarantee given by the taxpayer to ICICI for the benefit of the AE was 3 per cent of the amount of guarantee and made TP adjustment. The CIT(A) held that the return of 3 per cent arrived at by the TPO was justified. The taxpayer approached the Tribunal which deleted the TP adjustment.

High Court Ruling

- The TP adjustment was based on instances restricted to commercial banks providing guarantees and did not contemplate the issue of a corporate guarantee. Commercial banks issue bank guarantees which are easily encashable in the event of default and hence in case a bank guarantee is obtained from a commercial bank, a higher commission can be justified; but in the present case, it is the taxpayer that is issuing a corporate guarantee.
- The High Court held that the considerations applied for issuance of a corporate guarantee are distinct and separate from that of bank guarantee and cannot be compared as done by the TPO. The comparison is not between like transactions but between guarantees issued by the commercial banks as against a corporate guarantee issued by a holding company for the benefit of its AE. Accordingly, the High Court ruled that there was no substantial question of law and dismissed the appeal.

CIT v. Everest Kento Cylinders Ltd. (ITA No. 1165 of 2013) (Bombay High Court)

Circulars/Notifications/Press Releases

OECD - BEPS Action Plan 8 – Draft Guidance on Revisions to Chapter VIII of the Transfer Pricing Guidelines on Cost Contribution Arrangements

The OECD released a Draft Guidance on Revisions to Chapter VIII of the Transfer Pricing Guidelines (TPG) on Cost Contribution Arrangements (CCAs) (Discussion Draft / Draft) with an objective to align the transfer pricing of intangibles under CCAs with the general guidance on the TP aspects of intangibles as contained in the revised Chapter VI.

The Discussion Draft defines a CCA as a contractual arrangement among business enterprises to share the contributions and risks involved in the joint development, production or the obtaining of intangibles, tangible assets or services with the understanding that such intangibles, tangible assets or services are expected to create direct benefits for the businesses of each of the participants. The Draft lists out two types of commonly encountered CCAs namely: (i) Development CCAs - for the joint development, enhancement, maintenance, protection or exploitation of intangibles or tangible assets; and (ii) Services CCAs - for obtaining services.

The Discussion Draft lays down that the value of participants' contributions must be consistent with what independent enterprises would have agreed to contribute under comparable circumstances given their proportionate share of the total anticipated benefits which they reasonably expect to derive from the arrangement. The Draft discusses certain aspects to be considered for an arm's length analysis which includes:

1. **Determining participants** - assigning an interest in intangible, tangible assets or services that are the subject of the CCA to each participant and there being a reasonable expectation of benefit from that interest.

2. **Expected benefits from the CCA** - The shares of expected benefits might be estimated using relevant allocation keys such as sales (turnover); units used, produced, or sold, etc.

3. **The value of each participant's contribution** - The Draft talks about measuring the value instead of cost of each participant's contributions to the arrangement for the purpose of determining whether a CCA satisfies the arm's length principle. Under the arm's length principle, the value of each participant's contribution should be consistent with the value that independent enterprises would have assigned to that contribution.

4. **CCA entry, withdrawal or termination** - The Discussion Draft also highlights about buy-in and buy-out payments when reassessment of proportionate shares of participants' contributions and expected benefits is done on the basis of the ALP.

Recommendations for structuring and documenting CCAs - The Discussion Draft lays down a list of information that would be useful for determining the initial terms of a CCA but emphasises that the information described in this list is not exhaustive. This list includes information like a list of participants, list of any other AEs that will be involved with the CCA activity, the scope of activities/specific projects covered by the CCA, the duration of the arrangement, the manner in which a participants' proportionate shares of expected benefits are measured, the manner in which any future benefits are expected to be exploited, the form and value of each participant's initial contributions, anticipated allocation of

responsibilities and tasks, procedures for and consequences of a participant entering or withdrawing from the CCA and the termination of the CCA, etc.

Public Discussion Draft on BEPS Action 8: Revisions to Chapter VIII of the Transfer Pricing Guidelines on CCAs

CBDT rolls out draft scheme for range concept and multiple year data prescribed under TP regulations for public comments

The Finance minister announced in his Budget speech in July 2014 that the 'range' concept for determination of ALP would be introduced in the Indian TP regime and use of multiple year data would be permitted for undertaking comparability analysis to align the TP regulations to international standards. The CBDT issued the draft scheme of the proposed rules on 21 May 2015, for computation of the ALP of international transactions or specified domestic transactions undertaken on or after 1 April 2014. Comments and suggestions from stakeholders and general public were invited until 31 May 2015.

Key Highlights

'Range' Concept

- The 'Range' concept shall be used only in case the most appropriate method used for determination of ALP is TNMM, Resale Price Method (RPM), or Cost Plus Method (CPM)
- A minimum of 9 comparable companies would be required to be selected based on the similarity of their functions, assets and risks (FAR) with that of the tested party;
- For these 9 comparables (or more), a weighted average of a minimum of 2 out of 3 years of data would be considered to construct the data set.
- The data points lying within the fortieth to sixtieth per centile of the data set of series would constitute the range.
- If the transfer price of the tested party falls outside the range, the median of the range would be taken as ALP for making an adjustment to transfer price. If the transfer price is within the range no adjustment shall be made.

Use of Multiple year data

- Multiple year data should be mandatorily used in case of determination of ALP is by TNMM, RPM or CPM
- The multiple year data should comprise three years including the current year (i.e. year in which transaction has been undertaken);
- The use of data of two out of relevant three years shall be permitted in any of the following cases:
  - Current year data of the comparables may not be available in the databases at the time of filing of returns of income by taxpayers;
  - A comparable may fail to clear a quantitative filter in anyone out of the three years; and
  - A comparable may have commenced operations only in the last two years or may have closed down operations during the current year.
- If during the TP audit, current year data is available, the same can be used by both the taxpayer and the department.

Continued use of Arithmetic Mean

In cases, where 'range' concept does not apply, the arithmetic mean concept would continue to apply in the same manner as it applied earlier along with benefit of tolerance range. Further, in cases where multiple year data is to be used, the same would apply in both cases whether ALP is computed based on range or arithmetic mean.

F. No. 134/11/2015-TPL, Government of India, Ministry of Finance, Department of Revenue, CBDT

Indirect tax

Service Tax - Decisions

Back to back subcontract of works contract would not be considered as provision of works contract services by the main contractor

In the instant case, the issue inter-alia was whether back to back sub-contracting of execution of work by the main contractor to sub-contractors would be subject to service tax in the hands of the main contractor.

The Larger Bench of the Tribunal relied on the Supreme Court decision in A.P. v. Larsen & Tourbo Ltd. [2008-TIOL-158-VAT-SC] in the context of applicability of VAT in a back to back subcontracting scenario, wherein it was held that the main contractor would not be liable to pay VAT when there is no transfer of property in goods by the main contractor to the contractee.

Relying on the said decision, the Tribunal held that where the principal contractor assigns the works to a sub-contractor and the transfer of property in goods involved in the execution of such works passes on accretion to or incorporation into the works on the property belonging to the employer/contractee, the principal contractor cannot be considered to have provided works contract services.

M/s Lanco Infratech Ltd. and Others vs. Commissioner of Customs, Central Excise and Service Tax, Hyderabad [2015-TIOL-768-CESTAT-BANG-LB]

Notifications/Circulars/Press Releases

Service tax exemption extended to specified schemes under general insurance and life insurance business

Mega exemption notification under service tax has been extended to services provided under specified general insurance and life insurance business which are now exempted from service tax (such as Pradhan Mantri Suraksha Bima Yojna, Pradhan Mantri Jeevan Jyoti Bima Yojana, etc.). Further, services by way of collection of contribution under specific pension scheme is (i.e. Atal Pension Yojana) exempted from service tax.

Notification No. 12/2015-ST dated 30 April 2015

Central Excise – Decisions

Applicability of exemption in case a part of the processing is done by the job worker

The Notification No. 4/06-CE prescribes a concessional rate of duty for paper and paper board, where the entire manufacturing activity starting from the stage of manufacture of pulp shall be carried out in the factory. In the present case, the taxpayer manufactured the pulp in their own factory and some quantity of such pulp is also procured from outside. However, conversion of pulp into paper, has been outsourced to a job worker, who convert the pulp into paper and returned the paper rolls without payment of duty under job work challans under Notification No. 214/86-CE. Subsequently, the taxpayer cleared the finished paper sheets on payment of duty by availing the exemption under Notification 4/06-C.E.

The Central Excise authorities have denied the exemption on the grounds that, for availing of exemption, the conversion of pulp into paper must be done in the same factory from which the paper is cleared, and that since, in this case the conversion of pulp into paper rolls has been outsourced and has done in the factory of the job worker, the exemption would not be available.

In this background the CESTAT has held that, in this case the taxpayer is liable to pay duty on the paper and not the job worker who converted pulp into paper rolls on a job work basis. Accordingly, the exemption under these notifications cannot be denied.

ABC Paper v. CCE [2015-TIOL-784-CESTAT-DEL]

Activity of labelling will amount to 'manufacture' irrespective of whether it enhances the marketability of the product or not

In the present case, the taxpayer manufactures coco butter and coco powder in their Jammu factory and sent the said goods to their other unit located at Taloja. In their Taloja unit, labels were affixed on the packages of the said goods and cleared for export on payment of duty and claimed rebate of duty paid on the exported goods. The Central Excise authorities took a view that, the labels were already affixed on the boxes at the Jammu factory, and therefore additional labels affixed at the Taloja Unit does not amount to 'manufacture', as affixing of an additional label does not enhance the marketability (as the goods are already marketable). Accordingly, proceedings were initiated to deny the Cenvat Credit and consequently denying the rebate claim.

The CESTAT based on Chapter note of Central Excise Tariff Act held that, in view of the use of the word "OR" in the provisions, it is clear that the activity of labelling or re-labelling of containers is an independent activity, similarly the activity of repacking from bulk packs to retail packs is another activity and also the activity of adoption of any other treatment so as to render the product marketable to the consumer is another activity. These activities are independent and separate. Accordingly, it is held that, the activity of labelling/re-labelling would amount to 'manufacture' being an independent activity and it is not necessary that the activity of labelling must enhance the marketability of the product.

Jindal Drugs Limited v. CCE [2015-TIOL-857-CESTAT-MUM]

The Rule 8 (3A) of the Central Excise Rules is declared as violative of Article 14

As per Rule 8 (3A) of the Central Excise Rules, 2002, if the taxpayer defaults in payment of duty beyond thirty days from the due date, the taxpayer shall pay duty for each consignment at the time of removal, without utilising the Cenvat Credit till the date the outstanding amount including interest thereon is paid.

In this regard, the Madras High Court has held that, the right to pay duty by utilising the Cenvat Credit had accrued and cannot be defeated, unless it is a case of illegal or irregular credit. To that extent, this sub-rule (3A) is arbitrary and

therefore violative of Article 14 of Constitution of India. It is also held that, the right that was accrued to the taxpayer by way of Cenvat Credit, cannot be taken away under a rule, which only provides for the manner and method of payment of duty and for levying of interest, if there is a default.

Malladi Drugs and Pharmaceuticals Limited v. UOI and Others [2015-TIOL-1262-HC-MAD-CX]

Notifications/Circulars/Press Releases

Notifications issued to implement certain Budget announcements

The Central Government issued Notifications to give effect to certain announcements made in Budget 2015-16.

The Rule 3 (7) (b) of the Cenvat Credit Rules, 2004 has been amended so as to allow utilisation of credit of education cess and SHE cess for payment of basic excise duty in the following situations:

- The inputs or capital goods are received in the factory on or after 01 March 2015;
- The balance 50 per cent of Education Cess and SHE Cess on capital goods may be utilised, in case the said capital goods are received in the factory in the financial year 2014-15;
- The input services are received by the manufacturer on or after 01 Mar 2015.

Notifications No. 13/2015-Central Excise (N.T.) dated 30 April 2015

Refund and rebate could be claimed on clearances to SEZ units

Vide Notification No. 6/2015-C.E (NT) and 8/2015-C.E (NT), the term 'export' has been elaborated in Rule 5 of CENVAT Credit Rules, 2004 and rule 18 of Central Excise Rules, 2002 to mean 'taking out of India to a place outside India'. In this regard the CBEC has clarified that, since SEZ is deemed to be outside the customs territory of India, any licit clearances of goods to an SEZ from the DTA will continue to be export and therefore be entitled to the benefit of rebate under rule 18 of CER, 2002 and of refund of accumulated Cenvat Credit under rule 5 of Cenvat Credit Rules, 2004, as the case may be, irrespective of the meaning assigned to the term 'export' in the aforesaid Rules.

Circular No. 1001/8/2015-CX dated 28 April 2015

Customs – Decisions

Arbitrary loading of 1 per cent as loading, unloading and handling charge, is unsustainable

As per Rule 9 of the Customs Valuation (Determination of Price of Imported Goods) Rules, 1988, the value for determining the Customs duty shall include loading, unloading and handling charges associated with the delivery of the imported goods at the place of importation. As per the said rule, these charges are fixed at 1 per cent of free on board (FOB) value of the goods.

In the instant case, the actual cost of loading and handling charges incurred by the taxpayer is less than the amount prescribed under the said provision, i.e., less than 1 per cent of FOB value of goods. The Customs authorities have accordingly loaded the assessable value with the differential loading and handling charges, determined at the rate of 1per cent on the FOB value of goods.

The Supreme Court has held that, no doubt the rule making authority has the power to make Rules but such power has to be exercised by making the rules which are consistent with the scheme of the Act and not repugnant to the main provisions of the statute itself. Such a provision to add 1per cent FOB value in determining handling charges, etc. could be justified only in those cases where actual cost is not ascertainable and not in all cases. It is also held that, the said provision is unsustainable and bad in law as it exists during the relevant period and it has to be read down to mean that this clause would apply only when actual loading, handling charges, etc., are not ascertainable.

Wipro Limited v. Asstt. Collector of Customs [2015-TIOL-79-SC-CUS]

Circulars/Notifications/Press Releases

Setting up of 'Customs Clearance Facilitation Committee'

If the provisions of other Allied Acts are attracted in respect of the imported/exported goods, permission to clear the goods is given by the Customs only after getting the suitable clearance/response/NOC from the Government Department/agency concerned, such as Drug Controller of India, Pollution Control Board, etc. Since the aforementioned regulatory agencies are critical contributors to the Customs clearance process, a delay in receipt of a clearance from one regulatory agency holds up the Customs clearance of goods. To overcome this delay, the Board has decided to set up a Customs Clearance Facilitation Committee (CCFC) at every major Customs seaport and airport. The CCFC would be headed by the Chief Commissioner/Commissioner of Customs and its membership would include the senior-most functionary of the departments/agencies such as Drug Controller of India, Pollution Control Board, etc.

Circular No. 13/2015-Cus, dated 13 April 2015

VAT - Decisions

Input Tax Credit allowed where sale price is lower than purchase price due to turnover discount

In the present case, the taxpayer, a dealer of cement, sold goods at a rate lower than the price shown in the VAT invoice keeping in view the discount/incentive receivable. However, input tax credit (ITC) was claimed on the basis of VAT invoice received. The AO disallowed the ITC as according to him, ITC could not have been allowed on the basis of VAT invoice which was claimed higher. The Deputy Commissioner (Appeals) allowed appeals holding that the taxpayer was entitled to the excess ITC and the Tax Board also upheld the orders of the Commissioner (Appeals). Aggrieved by the same, the Revenue filed revision petitions before the High Court.

The High Court observed that the taxpayer received discount/ incentives from wholesaler/manufacturer on account of turnover by way of credit notes, etc. which was separately shown by the taxpayer and which was not in conflict under the provisions of Rajasthan Value Added Tax Act, 2013 (VAT Act). HC stated that the VAT act does not prohibit selling goods lower than purchase value as per VAT invoice but ITC is to be allowed on the basis of VAT invoice. The High Court has also referred the case of Commercial Tax Officer Circle-B, Bharatpur v. M/s Narendra Kumar Govind Prasad wherein same issue was analysed. Accordingly, High Court held that there is no illegality or infirmity in the Tax Board's order and thereby, dismissed Revenue's revision petitions.

Commercial Taxes Officer v. Sharda Agencies [TS-172-HC-2015(RAJ)-VAT]

Revised Return would be considered as Original Return once it is accepted

In the present case, the taxpayer is engaged in the business of providing passive infrastructure telecom services to its operators and is registered under the Karnataka Value Added Tax Act, 2003 ('KVAT Act').

Due to software issues at the Head Office, the taxpayer was unable to ascertain a turnover for the month of January 2009 and to comply with the filing of the return required by the due date, the taxpayer had filed a 'nil' return, which was within the prescribed time. Subsequently when the correct facts and figures were available, the taxpayer voluntarily discharged the entire tax liability along with interest and filed revised return, without any receipt of intimation or notice from the authorities. After a period of three years, a notice was issued to the taxpayer to submit a reply as to why a penalty for understatement of tax liability should not be imposed. The taxpayer submitted a reply to the said notice. Subsequently, the Assistant Commissioner passed an order imposing penalty at 10 per cent of the alleged understated tax liability. Challenging the same, the taxpayer filed an appeal before the Joint Commissioner (Appeals) which was dismissed and also filed a second appeal before the Karnataka Appellate Tribunal, which was also dismissed. Aggrieved by the same, the taxpayer filed a revision petition before the High Court.

The High Court observed that the definition of returns under the KVAT Act also includes a 'revised return'. The High Court also observed that 'once a revised return has been filed and accepted by the department, the original return gets obliterated and the only return which remains for consideration would be the revised return, as there cannot be two live returns pending for consideration of the department'. Accordingly, the High Court held that there was no understatement of tax liability and in such a case, the penalty provisions would not be attracted.

Indus Towers Ltd. v. State of Karnataka and Others [TS-173-HC-2015(KAR)-VAT]

Notifications/Circulars/Press Releases

Andhra Pradesh

With effect from 1 May 2015, manual CST waybills shall not be accepted at check posts. The incoming or outgoing goods whether taxable or exempt are required to be covered by eWaybills.

Circular CCT's Ref No. Enft/E3/455/2015, dated 5 May 2015

A circular has been issued clarifying that, in order to prevent misuse of VAT registrations, the Commercial Tax Officers ('CTO's') shall compulsorily visit the business premises of the dealers dealing in sensitive commodities viz Iron and Steel, Pulses and Dhalls, sugar, etc. before issuing registration to ensure that the dealers are genuine and do not resort to bogus transactions. The CTO's shall also conduct advisory visits in atleast 10 per cent cases after registrations are issued. Further, the circular has also laid down the list of documents to be submitted at the time of obtaining registration.

Circular No. CCTs Ref. No. Enft /E3/476/2015, dated 5 May 2015

Gujarat

With effect from 28 April 2015, every dealer is required to electronically generate forms 402, 403 and 405 for every movement of taxable goods to and from the state (including movements within the state).

Order No. GVL/VAT/ Sec.68 and 69/(5), dated 18 April 2015

Maharashtra

With effect from 7 May 2015, the sales tax department has developed a system in which the applicant will not be required to attend the sales tax office to obtain registration. The procedure for application for registration has been laid down in the Trade Circular No. 4T of 2015, 9 March 2015.

Circular No. 5T of 2015, dated 6 May 2015

Punjab

With effect from 15 April 2015, the Commissioner shall be required to formulate the criteria for making the assessment or the provisional assessment, of a person or a class of persons, with the approval of the government from time to time. Further, it has been provided that, no case for assessment of tax or otherwise for making assessment or provisional assessment, shall be taken up by the designated officer without the prior approval of the Commissioner. The cases to be taken up for assessment or provisional assessment, as the case may be, during a financial year, shall be displayed on the website of the department.

Notification No. GSR 26/P.A.8/2005/S.70Amd(55)2015, dated 15 April 2015

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