EY Tax and Regulatory Alert

April 2018

Prepared for ACMA

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Indirect Tax

This Section of Tax alert summarizes the Indirect tax updates for the month of April 2018

Judicial Precedents

1. M/S Ashok Automotive Sales & Services Private Limited Vs Commissioner of Central Excise, Pune-III

[TS-430-CESTAT-2017-ST]

Background and facts of the case

- In the M/s Ashok Automotive Sales & Services Private Limited (" M/s Ashok Automotive") was engaged in carrying out the work of servicing of the Tata Vehicles by virtue of an internal agreement entered into with M/s Pandit Automotive Pvt. Ltd. ("M/s Pandit Automotive"), who is an Authorized Dealer and Service Centre of M/s Tata Motors.

- The servicing was undertaken by the appellant in the premises of M/s Pandit Automotive.

- In case of service work undertaken on vehicles during the warranty period, the appellant was charging M/s Pandit Automotive who in turn charged to M/s Tata Motors and also discharged the service tax liability being the authorized service station of Tata Motors.

- The spare parts used in the vehicle outside the warranty period was recovered separately by Pandit Automotive from the vehicle owners only.

- The revenue issued show cause notice on appellant alleging that the activity of servicing/ repairing of vehicles undertaken by the appellant for customers fall under the category of Authorized Service Station and thus, it is liable to pay service tax.

Appellant's Contention

- Ashok Automotive defended that M/s Tata Motors has appointed M/s Pandit Automotive as its authorised service centre and M/s Pandit has further sub-contract the servicing work to us by way of entering into a separate agreement.

- Since, there is no prior written consent of M/s Tata Motors to M/s Ashok Automotive for servicing / repair of vehicles on behalf of M/s Pandit Automotive, the appellant cannot be considered as authorised service station of M/s Tata Motors.

Revenue's Contention

- The Revenue contended that the Appellant was using nomenclature "Authorized Workshop of M/s Tata Motors" on the job card and other stationeries and were also using software provided by M/s Tata Motors for generating bills.

- The Revenue argued that the law does not provide that authorisation given to Authorized Service Station should be written.

- M/s Tata Motors in their previous letter has stated that is aware of arrangements made by M/s Pandit Automotive with M/s Ashok Automotive to provide after sales service to their customers.

Held by CESTAT

- The Appellant cannot become an authorized service station of M/s Tata Motors merely for the reason that it was using job cards bearing brand name of M/s Tata Motors and using software of M/s Tata Motors for generating bills.
- No objection by M/s Tata Motors on the servicing work carried out by appellant cannot lead to the conclusion that appellant is an authorised service centre of M/s Tata Motors.
- Further, appellant was neither agent of M/s Tata motors nor has performed any act on behalf of M/s Tata motors and thus, agency by estoppel could not be invoked.
- Basis above observations and findings, CESTAT has set aside the impugned order and remanded back the case to the adjudicating authority for fresh adjudication.

2. Ashok Leyland Limited Vs ASSISTANT STATE TAX OFFICER SQUAD NO.1, STATE GST DEPARTMENT, PALAKKAD

[2018-VIL-148-KER]

Background and facts of the case

- A consignment of motor vehicle chassis that was being stock transferred at the instance of the petitioner (Ashok Leyland Limited) was detained by the respondent (Assistant state tax officer).

- In the writ petition, the petitioner is aggrieved by the insistence of the respondent that the petitioner must pay the security deposit demanded in the detention notice as a condition for release of the goods and the vehicle.

Petitioner's Contention

- They have submitted all the necessary declarations under the CGST Rules were made in the KVATIS system and there is also copy of invoice which accompanied with transportation of the goods.

Respondent's Contention

- The transportation of the goods was not accompanied by a valid copy of the stock transfer invoice/delivery challan that ought to have accompanied the goods as per the provisions of Rule 55 of the Central Goods and Services Tax (CGST) Rules.

Judgement

- There is no dispute with regard to genuineness of the invoice, a copy of which accompanied the transportation of the goods.

- Respondent was directed to release the goods and the vehicle to the petitioner on his producing a copy of this judgment before the said respondent.

3. M/S Mahindra & Mahindra Ltd

Vs

CCE&ST, Hyderabad-I

[2018-VIL-281-CESTAT-HYD-CE]

Background and facts of the case

- In the present case M/s Mahindra & Mahindra Limited, the appellants herein, are manufacturers of motor vehicles and parts thereof. Amongst other models, they manufacture "Mahindra Bolero Camper" and its variants. Till June 2008 or thereabouts, appellants were classifying the vehicles as "Motor Vehicle" principally designed for transport of persons under chapter subheading 8703 of the Central Excise tariff.

- By a letter dated 23.06.2008, appellants informed the jurisdictional Central Excise authorities that they intend to classify the said "Bolero Camper" as motor vehicle for transportation of goods under CETH classification 8704.21.90, w.e.f. 01.07.2008. Department took the view that the impugned motor vehicle is not primarily meant for carrying loads but for transporting persons and hence would merit classification under CETH 8703 only. Accordingly, show cause notices were issued to the appellants proposing classification of the vehicles under 8703.33.99 of CETH, demand of differential duty liabilities with interest thereon as also imposition of penalty.

Appellant's Contention

- Appellant submitted that for vehicle the vehicle has a crew cab in the front and open load body portion at the rear and is thus a hybrid vehicle for carrying both persons and goods.

- He further pointed out the fact that for a vehicle to fall under Heading 87.03, it should be principally designed for the transport of persons. However, for it to fall under heading 87.04, it need not be principally designed for transport of goods. Thus, if a vehicle is principally designed for the transport of goods, it will definitely fall under heading 87.04.

- Even if the vehicle is not principally designed for transport of goods, but if it is for transport of goods and persons, neither of which is its principal design, it would fall under heading 87.04. Therefore a hybrid vehicle which is for carrying both persons and goods would fall under heading 87.04. This also gets established from the above that once the vehicle is not principally designed for the transport of persons, it would fall under 87.04 and would be out of Heading 8703.

Respondent's Contention

- Revenue contended that the description/purpose of "Mahindra Camper" variants as per their company's website and in advertisements is marketing the vehicle for the purpose "whether you have loads to deliver or places to visit for persons/with the family" and that the said descriptions highlight the plush interiors of the vehicle, which is not but one would expect in a vehicle for transportation of goods.

Held by CESTAT

- It was held by CESTAT that for a motor vehicle to find a fit in Heading 8703, will necessarily have only a single enclosed interior space, have rear windows along two side panels, have sliding, swing out or lift up doors, with windows, on the side panels or in the rear and more importantly, will not have any permanent panel or barrier between the area for the driver and front passengers and the rear area to enable it being used for transport of both persons and goods.
- Moreover, as per HSN, to find place in 8703, there should be presence of comfort features and interior finish throughout the vehicle interior. Discernibly, the impugned vehicle namely "Mahindra Camper" and its variants by no such imagination can be said to be satisfying these requirements.
- The impugned vehicle will not merit classification under 8703.

4. M/S Giorgio Armani India (P) Ltd

Vs

CC, New Delhi

[2018-VIL-248-CESTAT-DEL-CU]

Background and facts of the case

- Giorgio Armani India Private Limited ('the Company') imported fashion apparel from various group companies. The foreign suppliers as well as company were related persons in terms of Rule 2(2) of the Customs Valuation Rules, 2007, the said imports were examined by the Customs Special Valuation Branch ('SVB'). The SVB authorities issued an Order loading the declared import value with (1) franchise fees, (2) institutional advertising and promotional campaign as well as (3) advertising expenditure required to be undertaken by the Company in India as per the terms of the agreement with the overseas related party suppliers. The revenue contended that such expenditure incurred is a condition of sale of goods by the foreign entity to the Company and that the Company is allowed to import goods from their principal only on payment of franchise fee and share of advertising fee.

Held by CESTAT

<u>For (1) – Franchise fees</u>

- The payment of franchisee fee is being paid in the nature of royalty so as to enable the company to legally sell the goods imported from the foreign principals. Thus, the franchise fee is being paid by the.
  Company is a condition for the sale of goods by the foreign supplier. Accordingly, **such franchisee fee will be includible in the assessable value.**

<u>For (2) – Institutional advertising and promotional</u>

- The share of institutional advertising and promotional campaign is sharing of the cost of the worldwide advertisement of the foreign supplier. It is not in disputed by the Company that they are required to remit such amount and unless such amounts are paid, they will not be entitled to import goods from the foreign principal. Accordingly, it was held that such payments are being made as a condition of sale of the imported goods and **such value is to be loaded on the assessable value.**

<u>For (3) – Advertising expenditure incurred in India</u>

- As per the agreement with the foreign buyers, the Company is required to incur an expenditure towards advertising in India. Such advertisement is carried-out in India for promotion of 'Giorgio Armani' Brands. Such expenditure is incurred after import of the goods. Even though the Company is required to incur such expenditure as per the agreement with the foreign principal, it cannot be said that such expenditure has been incurred to satisfy the obligation of the foreign principal. Accordingly, **the loading of value to the extent of such amount has been set aside.**

5. M/S Mercedes Benz India Private Limited

Vs

CCE, Pune-III

[2018-VIL-271-CESTAT-MUM-CE]

Background and facts of the case

- In the present case appeal has been filed by M/s. Mercedes-Benz India Private Ltd. against denial of

CENVAT Credit on input services of insurance used in respect of family members of their employees.

Decision Held

- It is pointed out by Commissioner that group insurance is mandatory only for the employees. There is no such mandatory provisions for their families. Thus, it is apparent that the said decisions have been given on the basis of erroneous assumption.

- In case of Reliance Industries (supra) relied upon by the Ld. Counsel, it is seen that the group insurance cover of family members have not been admitted by the appellant as the entire credit was reversed by them on their own. In the case of Biesse Manufacturing Co. Ltd. (supra), there is no specific discussion on the admissibility of credit in respect of family members and the said decision relies solely on other decisions in respect of the group health insurance without any findings in respect of admissibility of credit on the said insurance in respect of family members.

- In the case of Millipore India Private Limited vs Commissioner of Central Excise, Bangalore-II insurance was taken for the employees or personal accident of the employees and not of the family members of employees. Therefore the said decision is not relevant to the facts of this case. Therefore the credit is denied.

- Penalty is set aside on the basis that there could be bonafide doubt in the mind of the appellant as it can be issue of interpretation and appeal was pertly allowed.

6. M/S Commercial Engineers & Body Builders Co. Pvt. Ltd

Vs

CC, Jabalpur

[2018-VIL-205-CESTAT-DEL-CE]

Background and facts of the case

- The brief facts of the case are that, both the Units of the assessee-Appellants (Unit-I and Unit-II) were engaged in fabricating body over the chassis of the motor vehicles supplied by various manufacturers of chassis, such as, M/s Tata Motors Ltd. Both the units were also availing benefit of Notification No. 06/2006-CE dated 01.03.2006. Serial no. 41 of the Notification provides for effective rate of duty payable on the value of the body part on the chassis where no CENVAT Credit is availed in respect of such duty paid chassis received for body building. In case Cenvat Credit of duty paid on such chassis is availed, the duty is required to be discharged on the complete value of the vehicle including chassis as well as body built thereon.

Appellant's Contention

- Appellant submits that from the point of view of Unit-I as well as Unit-II, the exercise of demand is revenue neutral as the chassis cleared by Unit-I and Unit-II have since been returned by Unit-I to Unit-II on payment of duty on the value of body built by Unit-II. From the perspective of Unit-II, appellant submits that since no CENVAT Credit was availed by Unit-II on the duty paid on the chassis was not required to include the same for payment of duty. Likewise, he argued that no demand can be made in respect of Unit-I as well as Unit-II;

- Appellant also submits that any differential duty demanded from Unit-I and Unit-II and paid will also be available as CENVAT Credit in respect of other unit. Ultimately, there is no loss of revenue inasmuch as the motor vehicles after body is built on them stand cleared on payment of duty on the full value back to M/s Tata Motors Ltd.; and

- Appellant further submits that both from Unit-I as well as Unit-II, the differential duty has already been paid as a consequence of the audit objection after transferring the CENVAT Credit available on the duty paid chassis. However, the Revenue has demanded the payment of interest on such duty already paid alleging delay in payment of such duty.

Revenue's Contention

- Revenue justified the impugned order. He submits that at the time of clearance of the body built chassis, the Unit-I as well as Unit-II was required to pay the duty in full. However, in the present case, even though Unit-I as well as Unit-II has paid the differential duty, still they are liable to pay the demand raised.

Held by Commissioner

- Appellant has raided the plea that this is a case of revenue neutral situation and Commissioner is inclined to accept the idea.

- If the differential duty is paid by the body building unit, the same will be available as CENVAT Credit to the unit which has sent the chassis. Since both the units belong to M/s Commercial Engineers Body Building Company Private Ltd., this is a classic case of revenue neutrality. In the case of M/s Jay Yushin Ltd. vs. CCE, New Delhi [2000 (119) ELT (Tri. LB)] the larger Bench held that the case of clearance of goods from one unit to another of the same company is one of Revenue Neutrality.

- Differential duty raised in the course of audit objection has already been paid by both the units but Revenue has raised the issue that such duty has been paid after delay and hence interest is required to be paid. As discussed above Commissioner is of the view that there is no liability on the part of either unit to pay the differential duty. Consequently, the liability to payment of interest also does not arise.

- In view of the above discussions, both the impugned orders are set aside and appeals allowed.

Key Indirect Tax Developments

This section summarizes the regulatory updates for the month of April 2018.

1. Notification released by CBIDT & Customs viz Notification no. 29/2018-Customs (NT) dated 2 April 2018 ('the regulations') applicable w.e.f. 2 April 2018

- The regulations provide for the manner in which pre-notice consultation shall be made with the assesses before any Show Cause Notice is issued upon the assesses by the Customs officials.

- Per the regulations, the assesse who is liable to pay customs duty or interest would be given 15 days to respond to the communication of pre-notice consultation and submit his response to the tax officer.

- After the consultation, the tax officer, if satisfied with the response of the assessee, can communicate to him that he does not intend to proceed with the formal notice.

- The consultation process, the regulations said, has to be completed within 60 days of the date of issuance of communication for pre-notice consultation.

- The intent of the authorities to come up with such regulations was with the aim at reducing tax litigation and encouraging amicable settlement of tax issues.

2. Ruling of Authority for Advance Ruling (West Bengal) in the case of M/s Switching Avo Electro Power Ltd. ('Applicant') wherein it was held that the supply of UPS and battery at combined single price is to be considered as 'mixed supply' for the purpose of levy of GST.

- <u>Facts of the Case</u>

  - M/s Switching Avo Electro Power Ltd. is a supplier of power solutions, including UPS, servo stabiliser, batteries etc.
  - Further, the Applicant was supplying UPS alongwith rechargeable battery under a single contract for a composite price

- <u>Issues on which advance ruling was sought</u>

  - Whether supply of UPS along with battery can be treated as 'Composite Supply' within the meaning of Section 2(30) of the Central Goods and Services Tax Act, 2017 ('Central Tax Act')/ the West Bengal Goods and Services Tax Act, 2017 ('WB Tax Act').

- <u>Observations of the AAR</u>

  - Note 3 to Section XVI of the Customs Tariff Act, 1975 ('Note 3') defines a composite machine as the one consisting of two or more machines fitted together to form a whole for the purpose of performing two or more complementary or alternative functions. It was observed that Note 3 is applicable for determining the classification of goods under the Central Tax notifications, subject to the definitions of composite supply and its taxability under Section 8(a) of the Central Tax Act.

  - Machines designed for the purpose of performing two or more complimentary or alternative functions can be classified with the help of Note 3 *only if they are naturally bundled and supplied in conjunction with one another in the ordinary course of business.*

- It was observed that while determining whether two items are naturally bundled or not, it should be noted that ancillary supplies are *inseparable* from the principal supply and form an *integral part* of the composite supply.

- The Authority further noted that in a retail set-up, a standalone UPS and a battery can be supplied by the Applicant himself (this was a fact admitted by the applicant) ; a person can also purchase a standalone UPS and a battery from different vendors. Hence, the AAR has observed that in light of the above fact, the UPS and battery are products having separate commercial values as goods and should be taxed under the respective headings when supplied separately.

Ruling

- It was held that that if the contract is divisible and the recipient of supply can split it into supply contracts if he chooses, the same can no longer be said to be naturally bundled and cannot be treated as a composite supply. Hence, as per the AAR, since the goods supplied in terms of such contracts are no longer naturally bundled, they cannot be treated as a composite supply

- As per the AAR, though the UPS and battery are two different and independent items, they are billed together and a single price is quoted for the same, the supply would be a mixed supply.

3. Advance Ruling issued by the Authority for Advance Ruling (West Bengal) in the case of M/s Joint Plant Committee ('Applicant'), wherein it has been held that applicant is not liable to be registered under GST law if he is engaged in making exempt supplies, except under reverse charge mechanism.

- The Applicant is a non-profit organisation set up by the Central Government under Clause 17 of the Iron & Steel (Control) Order.

- The applicant main source of income is interest consideration received by way of interest on services like extending deposits, loans or advances and such income is specifically exempted from GST by virtue of Notification 12/2017- Central tax (Rate).

- Besides above source of income, the applicant is engaged in supply of journals & periodicals and also providing accommodation in guest houses at a rent below INR 1000; such supplies are also exempt from GST *vide* aforesaid notification.

- While the aggregate turnover from these sources exceeds threshold of Rs. 20 lakh but all of such income is exempt from GST and therefore, applicant is not be liable to get registered under GST law in terms of Section 23.

- AAR held that applicant is not required to obtain registration u/s 23(1) of CGST Act / WB GST Act if he is engaged exclusively in supply of exempt goods and services.

- However, AAR also clarifies that applicant would be liable to registration u/s 24, irrespective of quantum of aggregate turnover and exclusively making exempt supplies, if he is otherwise liable to pay tax under 'reverse charge mechanism' u/s 9(3) or 5(3) of GST Act / IGST Act.

4. Advance Ruling issued by the Authority for Advance Ruling (Kerala) wherein it has been held that recovery of food expenses from employees for the canteen facility provided by the employer comes under the definition of outward supplies and is therefore taxable under GST

- The Company is a Private Limited Company engaged in the manufacture and sale of footwear. They are providing canteen services exclusively for their employees for which they are incurring certain expenses which is subsequently getting recovered from the employees without any profit margin;

- It was submitted that the canteen facility being provided was in accordance with Section 46 of the Factories Act, 1948 which makes it mandatory or any factory employing more than 250 workers to provide canteen facility to its employees. Further, it was contended by the applicant that the facility being provided to the employees is not being carried out as a business activity;

- Basis the above, it was contended that the activity of providing canteen services does not fall within the scope of 'supply' as the same is not in the course or furtherance of its business as the Company is only facilitating the supply of food to its employees which is a statutory requirement and is recovering only the actual expenditure without any mark-up. Further, reliance was also placed on an exemption entry in the erstwhile service tax Mega exemption Notification exempting services provided in relation to serving of food or beverages by a canteen maintained in a factory under the Factories Act, 1948;

- The Advance Ruling Authority, relying on the definition of business under the CGST Act, held that the supply of food by the Company to its employees would fall under the definition of business as it is a transaction incidental or ancillary to the main business. Further, even though no profit is claimed by the Company on the supply of food to its employees, the same would be covered under the definition of supply;

- Also, since the applicant recovers the cost of food from its employees, there is a consideration involved as defined under Section 2(31) of the CGST Act, 2017. Further, it was also observed that there is no similar exemption entry under GST as was prevalent under the erstwhile service tax laws.

- Basis the , basis the above, it was ruled that recovery of food expenses from the employees for the canteen services would come under the definition of outward supply and therefore taxable under GST.

5. CGST Circular No. 40/14/2018 -GST dated 06 April 2018 issued by CBEC providing clarifications on issues related to furnishing of Bond/Letter of Undertaking for exports

- <u>Form for LUT</u>: An exporter is required to fill and submit FORM GST RFD-11 on the common portal.

- <u>Documents for LUT</u>: There is no need to submit any document physically to the jurisdictional office for the acceptance of LUT.

- <u>Acceptance of LUT/Bond:</u> The LUT would be deemed to be accepted as soon as an acknowledgement for the same, *bearing the Application Reference Number (ARN)*, is being generated online. However, if it is discovered that an exporter whose LUT has been so accepted, was ineligible to furnish a LUT in place of bond as per Notification No. 37/2017-Central Tax, then the exporter's LUT will be liable for rejection.

6. Circular by CBEC on IT Grievance Redressal Mechanism

- IT-Grievance Redressal Mechanism is setup to address the difficulties faced by a section of taxpayers owing to technical glitches on the GST portal and the relief that needs to be given to them. Problems which are proposed to be addressed through this mechanism would essentially be those which relate to Common Portal (GST Portal) and affect a large section of taxpayers.

- Any issue which needs to be addressed through this mechanism shall be identified by GSTN and the method of resolution approved by the GST Implementation Committee ('GIC') which shall act as the IT Grievance Redressal Committee.

- Taxpayer has to make an application to the field/ nodal officers, where there was an evident glitch on the Common Portal in relation to an identified issue, due to which the due process as specified in law could not be completed within the prescribed statutory timelines, on the Common Portal. Application would first be reviewed by GSTN and GSTN after due examination of application and verification of electronic records shall forward the same to the IT Grievance Redressal Committee with suggested solutions for resolution of the problem.

- IT-Grievance Redressal Committee after meeting of GST Council Secretariat and Law Committee for suggested solution may give directions as necessary to GSTN and field formations of the tax administrations for implementation of the decision.

- Where an IT related glitch has been identified, the consequential fine and penalty would also be required to be waived.

- All **such taxpayers, who tried but were not able to complete Form TRAN-1** procedure (*original or revised*) of filing them on or before 27 December 2017 due to IT-glitch, shall be provided the facility to complete Form TRAN-1 filing. Although the taxpayer shall not be allowed to amend the amount of credit in Form TRAN-1 during this process. The taxpayers shall complete the process of filing of Form TRAN 1 stuck due to IT glitches, as discussed above, by 30 April 2018 and the process of completing filing of Form GSTR-3B which could not be filed for such Form TRAN-1 shall be completed by 31 May 2018.

7. Circular no. 38/12/2018 dated 26 March 2018 issued by CBEC providing clarifications on job-work related issues under GST regime

- Scope/ambit of Job-work: The scope of job work is determined on the basis of facts and circumstances of each case. It is clarified that the job worker, can use his own goods for providing the services of job work, in addition to goods received from the principal.

- Requirement of Registration of Job-worker: It is clarified that a job-worker is required to obtain registration only in cases where his aggregate turnover, on all India basis in a financial year exceeds the threshold limit (i.e., INR 20 lakhs or INR 10 lakhs in case of special category states except Jammu & Kashmir) regardless of whether the principal and the job- worker are located in the same state or in different states.

- Supply of goods directly from the job-worker's place of business/ premises: This facility is available only if the principal declares the job worker's place of business as his additional place of business or the job worker is registered.

  It is clarified that supply of goods by the principal from the job-workers place of business/ premises will be treated as supply made by the principal and not by the job-worker as specified in Section 143(1)(a) of the CGST Act, 2017.

- Documents and intimation required on movement of goods;

  - **Where goods are sent by the principal to the job worker only**: The principal shall prepare delivery challan in triplicate. Two copies may be sent to the job worker along with the goods.

  - **Where goods are sent from one job-worker to another job-worker**: The goods may move under the cover of delivery challan issued either by the job-worker or the principal. Alternatively, the job-worker may endorse the delivery challan issued by the principal, to another job-worker. The endorsed delivery challan should contain the description and quantity of goods sent to another job-worker.

  - **Where the goods are returned to the principal by the job-worker**: The job-worker shall send one copy of delivery challan received from the principal while returning the goods back to the principal.

  - **Where the goods are directly sent by the supplier to the job-worker**: The goods in this case, will move under the copy of invoice issued by the supplier to the place of Job worker issued in the name of the buyer (i.e., the principal). The invoice shall contain the name and address of the job-worker as the consignee. In case on imports, the goods shall move directly from the customs stations to the job worker's premises with a copy of the Bill of Entry. In both the cases, the principal shall issue the delivery challan and send the same to the job-worker as mentioned in para (i) above.

  - **Where the goods are returned by the job-worker in piecemeal**: Where the job worker sends the goods to another job worker or the principal in piecemeal, the original delivery challan cannot be endorsed in such cases. The job worker is required to issue fresh delivery challan for each piecemeal.

  - **Submission of Intimation**: The principal is required to submit the details of delivery challans in respect of goods sent to job worker or received from the job worker during a quarter in **Form GST ITC-04** by 25th of the month succeeding the quarter or within such period as may be extended by the Commissioner.

  Please note that e-way bill shall be compulsorily generated by the principal or the job worker, irrespective of the consignment value in case the movement of goods is inter-state.

- Liability to issue invoice, determination of place of supply and payment of GST:

  - **Value of moulds & dies, jigs and fixtures or tools:** It has been clarified that the values of moulds & dies, jigs and fixtures or tools supplied by the principal and used by the job worker may not be included in the value of job –work services provided its value have been factored in the price for the supply of such services by the job worker.

- **Supply of goods by the principal from the job worker's place of business/ premises (*including direct export*)**: The time, value and place of supply would be determined by the principal irrespective of job worker's location. In case of exports, the LUT or bond, shall be executed by the principal. An illustration in this regard has also been cited in the circular.

  Please note that the above facility is available to the principal only if he declares the job worker's place of business / premises as his additional place of business or if the job worker is registered.

- **Supply of waste and scrap generated during the job work: Scrap or waste generated may be supplied directly by the job worker or the principal in case the job worker is not registered. The time, value and place of supply shall be similar to para (ii) above**

- <u>Violation of conditions of Job work as mentioned in Section 143:</u>

  - If the inputs or the capital goods are neither returned nor supplied from the job worker's place of business/ premises within the specified time period, the principal shall issue invoice for the same and declare such supplies in his return for the particular month in which the time period of one/ three years has expired. The date of supply shall be the date on which inputs or capital goods were initially sent to the job worker, and interest for the intervening period shall also be payable on the tax.

  - If such goods are returned by the job worker after the stipulated time period, the same would be treated as supply by the job worker to the principal and the job worker would be liable to pay GST if he is registered. If the job worker is not registered, GST would be payable by the principal on the reverse charge basis. However, such provision is kept on hold for the time being.

- <u>Availability of ITC to the principal and the job worker:</u> The principal would be entitled to avail the credit on the inputs and capital goods sent to the job worker irrespective of the fact that goods are sent by the principal or the goods are sent directly sent by the supplier to the job worker.

The job worker shall be eligible to avail ITC on inputs, services, etc. used by him in supplying the job work services if he is registered.

8. Intra State E-way Bill Rollout Status as on 20 April 2018

State	Notification/Order
Andhra Pradesh	CCTs Ref. in CCW/GST/74/2015; w.e.f. 15 April 2018
Gujarat	No.GSL/GST/RULE-138(14)/B.12; w.e.f. 15 April 2018 E-Way Bill required for 19 notified goods of consignment value exceeding fifty thousand rupees
Himachal Pradesh	Notification No. 12-4/78-EXN-Tax-Part/12438; w.e.f. 20 April 2018 [E-Way Bill required for eight notified goods of consignment value exceeding fifty thousand rupees]
Jharkhand	Notification No. S.O. 35; w.e.f. 20 April 2018
Karnataka	1 April 2018
Kerala	E-Way bill is mandatory for Intra-State movement of goods from 15 April 2018
Maharashtra	Notification No. 15B; w.e.f. 1 May 2018
Telangana	E-Way bill is mandatory for Intra-State movement of goods from 15 April 2018
Tripura	Notification No.F.1-11(91)-TAX/GST/2018 (Part-I); w.e.f. 20 April 2018
Uttar Pradesh	Notification No. 38 w.e.f. 15 April 2018
Uttarakhand	Notification No. 239/CSTUK/GST-Vidhi/2018-19; w.e.f. 20 April 2018
Haryana	E-Way bill is mandatory for Intra-State movement of goods from 20 April 2018 [Notification awaited]
Bihar	E-Way bill is mandatory for Intra-State movement of goods from 20 April 2018 [Notification awaited]

Direct Tax

This Section of Tax alert summarizes the Direct tax updates for the month of April 2018

Judicial Precedents

1. Supreme Court (SC) rules commission payments by Doordarshan to advertising agencies liable for tax withholding

Background and facts of the case

- Under the ITL, any payment of income in the nature of commission or brokerage attracts tax withholding obligation for the payer. The term "commission or brokerage" is defined, inter alia, to include any payment received or receivable, directly or indirectly, by a person acting on behalf of another person for the services rendered (not being professional services).

- The Taxpayer, a fully-owned Government of India undertaking, is engaged in the telecast of news, sports, entertainment, cinemas and other programs through a TV channel called "Doordarshan". The Taxpayer has also been regularly telecasting the advertisements of several consumer companies. With a view to have a better regulation of the practice of advertising and to secure best advertising services for the advertisers, the Taxpayer entered into the agreement with several advertising agencies (Agency/ies).

- In terms of the agreement, the advertising agency was required to make an application to the Taxpayer to secure the "accredited status" for their Agency so as to be able to telecast advertisements on the channels of the Taxpayer. The Agency was required to provide minimum annual business to the Taxpayer, failing which the accreditation could be withdrawn.

- The agreement, inter alia, provided that the Taxpayer would pay 15% by way of commission to the Agency. The Agency was forbidden from parting with commission either directly or indirectly with any person for whom it may be acting or has acted as an advertising agency.

- The Agencies were to collect the advertisement charges from various advertisers and retain 15% of the amount as its commission and balance was required to be remitted to the Taxpayer. The Taxpayer accounted full amount as received from the customer for whom the advertisement was undertaken [As provided in the underlying High Court (HC) decision].

- Further, the Agencies agreed to pay to the Taxpayer the amount of taxes required to be withheld by the Taxpayer on the commission retained by them through demand draft or cheque.

- The Taxpayer did not withhold any taxes on the payments made to the Agencies under the premise that the same was not liable to tax withholding under the ITL.

- The Tax Authority treated the payments to be in the nature of commission attracting withholding obligation under the ITL. This view was also upheld by the first appellate authority. On further appeal, the second appellate authority (Tribunal) ruled in favor of the Taxpayer. However, the HC, on further appeal by the Tax Authority, ruled against the Taxpayer and upheld the payments to be in the nature of commission subject to withholding under the ITL.

- Aggrieved, the Taxpayer filed an appeal before the SC.

- The relationship between the Taxpayer and the Agencies was in the nature of principal-to-principal and, hence, the payment made was not in the nature of commission income of the Agency.

- The Agencies, in terms of the agreement, purchased air time from the Taxpayer at the discount of 15% and then sold airtime to their customers in the market.

Supreme Court ruling

- The SC referred to the terms of agreement entered into between the Taxpayer and the Agencies, and basis the below reasoning upheld that the payments made to the Agencies were in the nature of commission to secure more business and, hence, was liable to tax withholding under the ITL.

  - The agreement itself used the expression "commission" in all relevant clauses and there was no ambiguity thereabout in any of the clauses. There was no cause of complaint for the Taxpayer in this behalf.

  - Both the parties intended that the amount be paid to the Agencies by way of commission and it was for this reason, the parties used the expression “commission” in the agreement.

- The transaction in question did not show that the relationship between the Taxpayer and the Agencies was one of principal-to-principal. Rather, it was a principal and agent relationship.

- The tenure and nature of the transaction clearly stipulates that the amount was paid by way of commission and not under any other head.

- The payment of 15% was made out of advertising fees collected by the Agencies from the customers for securing more advertisements and to earn more business from the Agencies. Also, the agreement contained a clause for tax withholding on the commission income payable by the Taxpayer to the Agencies.

- Moreover, the definition of expression “commission” under the ITL is an inclusive definition giving a wide meaning to the expression “commission" so as to cover the present transaction within in its scope.

- Reliance placed by the Taxpayer on the decision of Allahabad HC in the case of Jagran Prakashan Ltd. v Deputy CIT (TDS) [(2012)345 ITR 288] was factually distinguishable. In that case, the Agency was never appointed as an agent of publisher (but, was a service provider to the advertisers), unlike in the present case. The Jagran’s case was governed by rules and regulations of the society governing accreditation of Ad agencies wherein publishers were specifically prohibited to appoint Ad agencies as their representative.

Source: recent ruling in the case of Prasar Bharati Doordarshan Kendra [[TS-156-SC-2018] (Taxpayer) wherein the issue before the Supreme Court.

2. Madras High Court (HC) upholds attachment of immovable property transferred after service of recovery notice by Tax Recovery Officer (TRO)

Background and facts of the case

- The ITL provides various powers to the TRO for recovering any dues payable under the Indian Tax Laws (ITL) in respect of which the taxpayer has committed a default (defaulter). These powers include, for instance, attachment and sale of movable and immovable property, attachment of bank accounts, arresting and detaining the defaulter.

- There are separate procedures for attachment and sale of movable and immovable properties. The ITL provides the following sequence of procedure for attachment and sale of immovable property:

    - The TRO shall prepare and sign a certificate (recovery certificate) specifying the arrears under the ITL due from the defaulter.

    - The TRO shall issue a notice (recovery notice) to the defaulter, requiring payment of the arrears as specified in the recovery certificate within 15 days from the date of service of the recovery notice to the defaulter.

    - In case of default, the TRO may realize the arrears by attachment and sale of the defaulter’s immovable property. The process of attachment involves prohibiting the defaulter from transferring or creating a charge on the property, which is eventually followed by sale of the immovable property through public auction to the highest bidder.

    - If any person (other than the defaulter) objects to the attachment of the immovable property by the TRO, the TRO is required to investigate into the objection. The person is required to establish that, as on the date of service of the recovery notice to the defaulter, the person had some interest in, or had possession of, the immovable property being attached.

- The objection shall be rejected if the TRO is satisfied that, on the date of service of the recovery notice, the immovable property was in the possession of, and was owned by, the defaulter and not by the person making the objection.

- In case the objection is rejected, the person aggrieved by the attachment may file a suit in a Civil Court to establish his right to the immovable property. Till such decision by the Civil Court, the attachment of immovable property by the TRO shall be conclusive.

- Once the recovery notice is served, the defaulter is not competent to transact in the immovable property, except after obtaining the TRO’s permission. The attachment of the immovable property also relates back to the date of service of the recovery notice.

- There is a separate scheme of provisions in the ITL that regulates the validity of transfers made by the defaulter before the date of service of the recovery notice. According to these provisions, if any assessment or other proceedings under the ITL are pending against the taxpayer, or such proceedings under the ITL are complete but the recovery notice has not been served, the ITL statutorily provides that sale or transfer of an immovable property by the taxpayer in favor of any other person is void to the extent of the arrears involved, except under the following circumstances:
  - The sale or transfer s made with the previous permission of the Tax Authority; or
  - The sale is made for adequate consideration and the purchaser had no knowledge of the arrears payable by the seller under the ITL or pendency of proceedings against the seller under the ITL (saving clause).
- The taxpayer, an individual, defaulted in payment of dues under the ITL (Defaulter). The TRO quantified the arrears due in a recovery certificate and served a recovery notice on the Defaulter on 5 January 2013.
- After service of the recovery notice, the Defaulter sold his immovable property to the 'Petitioner, also an individual. The sale was for adequate consideration and the Petitioner had no knowledge of the taxpayer being a defaulter under the ITL.
- After the Petitioner purchased the immovable property from the Defaulter, the TRO passed an order for attachment of the immovable property on 21 December 2015. After the Petitioner objected to the attachment, the TRO conducted an inquiry and passed an order not only declining to vacate the attachment, but also declaring the purchase of the immovable property from the Defaulter as null and void.
- Aggrieved, the Petitioner filed the present writ petition to the HC challenging the aforesaid order passed by the TRO.
- The Petitioner argued that he was eligible for the saving clause under the ITL because the Petitioner had acquired possession of (and interest in) the immovable property before the date of attachment (21 December 2015). There was no dispute that the purchase was for adequate consideration and was made without the Petitioner having knowledge of the taxpayer being a defaulter under the ITL.
- The Petitioner relied on a Gujarat High Court [TRO v. Industrial Finance Corporation of India [(01) 346 ITR 11 (Gujarat HC)]] ruling, which had granted benefit of the saving clause to bona fide transactions in immovable properties made during the pendency of proceedings under the ITL against the defaulter. The Petitioner argued that the Bombay High Court ruling [Inayat Hussain v. UOI [(1980) 122 ITR 227 (Bombay HC)] relied upon by the TRO was not applicable because, as per the principle of fiscal jurisprudence, if there are conflicting rulings of two non-jurisdictional High Courts, the ruling which was beneficial to the taxpayer should be preferred (principle of beneficial interpretation).
- The Petitioner argued that only a Civil Court, and not the TRO, has the jurisdiction to declare the purchase of the immovable property as null and void [Supreme Court decision in the case of TRO v. Gangadhar Vishwanath Ranade [(1998) 6 SCC 658]]. The TRO only has the jurisdiction under the ITL to investigate into the objection raised by the Petitioner against the attachment, for the purpose of determining whether the Petitioner had some interest in, or had possession of, the immovable property on the date of service of the recovery notice to the Defaulter.
- The TRO relied on a Bombay High Court [Inayat Hussain v. UOI [(1980) 122 ITR 227 (Bombay HC)]] ruling, which had held that the ITL has a separate and distinct scheme of provisions for transactions (in immovable properties) entered into before service of the recovery notice and transactions entered into after that date, and the saving clause applied only to transactions before service of the recovery notice.
- The saving clause is not applicable to transactions after service of the recovery notice because the defaulter has no authority to transact in the immovable property after such date, except with the TRO's permission. Since, in the Petitioner's case, the purchase happened after service of the recovery notice, the saving clause did not apply, even if the purchase was bona fide.
- **High Court's ruling**
- On the validity of the attachment by the TRO: The HC upheld the validity of the attachment by the TRO for the following reasons:

- The HC noted that, undisputedly, in the present case, the Petitioner had purchased the immovable property from the Defaulter after service of the recovery notice. But, the attachment was after the date of purchase.

- The HC affirmed that the ITL has a separate and distinct scheme of provisions governing transactions in immovable properties before and after service of the recovery notice. The HC affirmed the TRO's contentions that the saving clause applied only to transactions in immovable properties before service of the recovery notice. In the present case, because the Petitioner had purchased the immovable property after service of the recovery notice, the saving clause did not apply.

- After service of the recovery notice, the ITL provides that the defaulter shall not be competent to sell the immovable property, except with the TRO's permission. If the attachment happens at a later date after service of the recovery notice, the ITL provides that the attachment takes effect retrospectively from the date of service of the recovery notice.

- The HC referred to the Indian Contract Act, 1872, which provided the following three conditions regarding a person's competency to contract:

  (1) The person has attained the age of majority.

  (2) The person is of sound mind.
  (3) The person is not disqualified from contracting under any law that applies to the person.

- The HC held that the third condition stood attracted in the case of the Defaulter because, once the recovery notice had been served, the ITL made the Defaulter incompetent from selling the immovable property to the Petitioner. If the Defaulter had no competency to transfer the immovable property, the Petitioner could not have acquired valid or legal title from the Defaulter.

- Regarding the validity of the Petitioner's objection to the attachment, the HC held that the ITL required the Petitioner to establish that, on the date of service of the recovery notice, the Petitioner had some interest in, or had possession of, the immovable property. In the present case, this condition was not satisfied because the Petitioner had purchased the immovable property only after the date of service of the recovery notice.

- The HC held that the rule of evidence is significantly different in a case of attachment of movable property, where the person objecting to the attachment of movable property is required to establish interest in, or possession of, the movable property as of the date of attachment by the TRO. In the case of immovable property, the person objecting to the attachment has to establish interest in, or possession of, the immovable property as of the date of service of the recovery notice.

- The HC rejected the applicability of the principle of beneficial interpretation because, as per the HC, only one interpretation, as provided by it, was possible on a plain reading of the ITL. ‣ The HC further observed that, as per the ITL, the Petitioner can require TRO to lift the attachment by filing a suit in the Civil Court to establish his interest in the immovable property as of the date of service of the recovery notice. Till such suit is decided by the Civil Court, the attachment by the TRO stands conclusive.

- On the TRO's powers to declare the purchase transaction as null and void: The HC quashed the TRO's order to the extent of declaring the purchase as null and void. Based on judicial precedents, the HC affirmed that the TRO had no jurisdiction to declare the transaction of purchase of the immovable property as null and void. The ITL itself declares that a transfer is void under specified circumstances, and does not grant powers to the TRO to pronounce upon the validity of the purchase.

Source: Madras High Court (HC) ruling, dated 7 March 2018, in the case of D.S. Senthilvel (Petitioner) v. Tax Recovery Officer on the validity of the attachment of an immovable property in the course of recovery proceedings under the Indian Tax Laws (ITL)

Key Direct Tax Developments

1. India signs its first tax treaty with Hong Kong

Background and facts

- Hong Kong has emerged as an investment holding hub for Multinational enterprises (MNEs) looking for investment, especially in Asia region. Further, the trade relations between India and Hong Kong have strengthened in the recent times. So far, there was no Double Taxation Avoidance Agreement (DTAA) between India and Hong Kong; accordingly, the tax implications in relation to transactions between India and Hong Kong were evaluated as per the Indian Tax Laws (ITL).

- Section 90 of the ITL authorizes the GoI to enter into a DTAA with a foreign country or specified territory. Hong Kong was notified as a specified territory in April 2010 [GoI Notification No S.O.909(E) (Source – www.pib.nic.in)]. This paved the way for India to negotiate and sign a DTAA with Hong Kong. On 10 November 2017, the Union Cabinet of India issued a press release indicating the approval for entering into a DTAA with Hong Kong [Source – www.pib.nic.in]. On 19 March 2018, India signed its first DTAA with Hong Kong.

Key features of the DTAA

- **Taxes covered.**

The DTAA covers income tax in India, including surcharge thereon. It also covers identical or substantially similar taxes that may be imposed in future. It does not include any penalty or interest or fine imposed under the domestic laws relating to the covered taxes.

- **Residential status**

In Hong Kong, the residential status for individuals is determined basis the physical stay in Hong Kong and includes an individual who ordinarily resides in Hong Kong [By way of protocol, it is clarified that an individual 'ordinarily resides' in Hong Kong if the individual has a substantial presence, permanent home or habitual abode in Hong Kong, and he has personal and economic relations with Hong Kong.], whereas for the companies/other persons, the criteria is its place of incorporation/ constitution and place from where it is normally managed or controlled, if incorporated/constituted outside Hong Kong [By way of protocol, it is clarified that a company incorporated/ any other person constituted outside Hong Kong is "normally managed or controlled" in Hong Kong if its executive officers and senior management employees make day-to-day key decisions in Hong Kong for the strategic, financial and operational policies of the company or the person, and the staff of the company or the person conduct in Hong Kong, the day-to-day activities necessary for making those decisions].

In India, every person who is liable to pay tax by the reason of his/her domicile residence, place of management or any other similar criterion, is considered as resident for the applicability of the DTAA.

The term 'person' is defined in the DTAA to include partnership, trust and any other body of persons which is treated as a taxable unit.

Tie-breaker tests in case of dual residency:

On the lines of the OECD Model Convention (MC), residential status of an individual shall be determined based on his/her permanent home or centre of vital interests or habitual abode or lastly, through MAP.

Treaty residency of other taxpayers (non individuals) shall be determined by MAP having regard to its Place of Effective Management (POEM), place of incorporation or constitution, and any other relevant factors. This provision is along the lines of MLI.

In absence of MAP, dual residents are not entitled to any relief or exemption from tax under the tax treaty, except as may be agreed by the CA.

- **Scope of Permanent Establishment (PE) and profit attribution:**

In addition to fixed place PE, the DTAA covers other forms of PE like Construction PE, Service PE and Agency PE. These provisions are comparable to the 2011 UN MC.

The DTAA provides six months threshold to trigger a Construction PE and it includes a building site, assembly or installation project or supervisory activities.

A Service PE is created when services, including consultancy services, are furnished for the same or a connected project for an aggregate period of more than 183 days within any 12-month period.

Agency PE definition covers authority to conclude contract (except preparatory and auxiliary activities), maintaining stock of goods/merchandize for regular delivery, securing orders wholly or almost wholly for the principal or its associated enterprises. The provision does not incorporate the MLI recommended provisions on Agency PE.

The DTAA also states that where the activities of an agent are devoted wholly and almost wholly on behalf of the enterprise, the agent will not be considered as an independent agent. Unlike the UN

MC as well as certain Indian treaties, the additional condition of satisfying arm's length requirement for qualifying as an independent agent, is absent in the DTAA.

Certain activities are listed as exempt from creating a PE like storage/ display, maintenance of stock for storage/ display/ processing, purchasing goods/ merchandize or collecting information, preparatory or auxiliary activities.

- **Attribution of business profits**

Article 7 of the DTAA provides for source taxation of business profits to the extent attributable to PE in source country. The provision is modelled along the lines of Article 7 of the 2011 UN MC, however, the force of attraction rule is absent in the DTAA.

Further, unlike the UN MC, the restriction on allowability of expenses payable to Head Office by way of royalties, fees, commission, etc. is absent in the DTAA.

The provision allows for application of a formulary apportionment method or any other prescribed method, as may be customary in the source country and to the extent it is in accordance with the principles of Article 7.

The DTAA also contains the exclusion for purchasing activity. This provision is not present in the 2011 UN MC or the 2017 OECD MC.

- **Shipping and Air transport:**

Profits of an enterprise from operation of ships or aircraft in international traffic is taxed only in the **resident country**. Unlike the 2011 UN MC as well as various Indian treaties, resident country taxation is not specifically linked to the POEM of the enterprise.

Profits from operation of ships in international traffic may also be taxed in the source state with 50% reduction in taxes imposed.

Along the lines of this Article, Capital Gains from alienation of ships or aircraft or movable property pertaining to their operation is also be taxable only in the resident state of the alienator.

Further, remuneration derived in respect of an employment exercised aboard such ship or aircraft is only taxable in the resident state of an operating enterprise.

- **Associated Enterprises (AE) – Corresponding adjustment on account of transfer pricing provision**

The DTAA provides that a corresponding adjustment may be made in the profits of AE in the other contracting state:

  - where an adjustment has been made by a country to profits of a resident, based on arm's length condition and taxes are levied on such profits adjusted and

  - such profits are also taxed in the hands of AE in the other contracting state

This provision is to relieve double taxation in the other contracting state and is in line with India's commitment made as part of Article 14 on dispute resolution mechanism of OECD's BEPS.

- **Taxation of Dividends, Interest, Royalty, FTS:**

Passive streams of income like dividend, interest, royalty and FTS are primarily taxable in the resident country. Such income are also taxed in source country at a tax rate of 5% on dividend and 10% on interest, royalties and FTS on gross basis. Where such incomes are effectively connected to a PE in source country, taxation will be governed by the provisions of Article 7 on net basis.

Under a unique provision, such beneficial tax rates cannot be availed if the main purpose or one of the main purpose of any person concerned with creation/assignment of shares /other rights or debt or royalty rights or performance of services is to take advantage of these Articles by means of that creation/assignment. This is similar to Principal Purpose Test laid down in MLI.

Definition of royalty and FTS is similar to those in the UN/ OECD MC. Further, there is no condition of "make available" in FTS making its scope broader compared to India' treaties with Singapore, Netherlands, etc.

- Capital Gains taxation:

Capital gains arising from sale of immovable property and from sale from of shares of a company which derives more than 50% of its asset value directly or indirectly from immovable property will be taxed in the country where the immovable property is situated.

Capital gains from sale of other shares will be taxable in the country which the company is a resident.

Gains from sale of any other property may be taxed in each country in accordance with the provisions of its domestic laws.

Similar to other passive income streams, benefits under this Article are also subject to the ‘main purpose or one of the main purpose’ test.

- **Independent Personal Services:**

  Income derived by an individual from the performance of professional services or other similar independent activities shall be taxable only in the resident state unless such individual has a fixed place in the source state or his/her aggregate stay in the source state exceeds 183 days in any 12-month period commencing or ending in the year concerned.

- **Dependent Personal Services**

  Income in respect of employment may be taxed in source country where employment is exercised unless:

  - His/her aggregate presence in the source state does not exceed 183 days in any 12-month period commencing or ending in the tax year under consideration and

  - The remuneration is paid by an employer who is not resident of source country and

  - The remuneration is not borne by the PE or fixed base which employer has in other country.

- **Other income**

  Primary rights to tax ‘other income’ is accorded to the resident country. Such income may also be taxed in in the source country where such income is arising.

- **Method to eliminate double taxation:**

  In order to eliminate the double taxation on a person, both countries India and Hong Kong allows foreign tax credit for the taxes paid in either of the countries. The relief is provided by way of credit method subject to maximum deduction limit.

- **Non-discrimination**

  Like the OECD/ UN MCs, the DTAA provides nondiscrimination provisions on the basis of nationality of taxpayer, treatment of PE in source country, deductions claimed as well as on the basis ownership of taxpayer

- **MAP**

  The DTAA provides for MAP on the lines of MLI provision. Amongst other things, it states that a taxpayer may present its case to a CA in its resident country within three years from the first notification of the action resulting in taxation. The CA would then endeavour to resolve the case by mutual agreement which will be implemented notwithstanding any time limits in the domestic laws.

- **Exchange of information (EOI):**

  The scope of the EOI provision in the DTAA aligns with international standards on transparency and the provisions in the OECD/ UN MC. This EOI provision works to exchange the information that is foreseeably relevant for carrying out the provisions of the DTAA or to the administration or enforcement of the domestic law concerning taxes of every kind and description [It is clarified, by way of protocol, that in addition to the taxes covered by the DTAA, the EOI Article shall also apply to (i) the wealth tax (ii) the excise and customs duties (iii) the goods and services tax (GST) and (iv) the sales and value added taxes.].

  The information can be used for purposes other than tax, with the prior approval of the authority providing such information and if such information may be used for such other purposes under the laws of both states.

  EOI would also be possible in respect of persons who are not residents of the Contracting State, as long as the information requested is in possession of the concerned State.

  Specifically, information held by banks or financial institutions can be exchanged under the EOI Article.

  By way of protocol to the treaty, it is clarified that the requested state shall also disclose any past information insofar the information is foreseeably relevant for a fiscal year or taxable event following that date on which the DTAA has effect.

- **Anti-avoidance provisions**

  The provisions of the DTAA will not prevent a country from the application of its domestic law and measures concerning tax avoidance or evasion.

Also, treaty benefits shall not be granted if the main purpose or one of the main purposes of any persons is non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in the DTAA for the indirect benefit of residents of third jurisdictions). This provision is comparable to the PPT rule as well as language of the Preamble as per BEPS Action 6 incorporate in the MLI.

Cases of legal entities not having bona fide business activities shall also be covered by the provisions of this Article.

Source: On 19 March 2018, India and Hong Kong signed a comprehensive tax treaty for the avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income (the treaty or DTAA). As per a press release of the Government of India (Source – www.pib.nic.in)

2. CBDT invites feedback and suggestions from stakeholders and general public on new Direct Tax Law

Background

- During Rajaswa Gyan Sangam (annual conference of tax administrators) held on 1 and 2 September 2017, the Hon'ble Prime Minister of India observed that the current ITL was drafted more than 50 years ago and needs to be redrafted.
- Accordingly, the GOI constituted a Task Force in order to review the current ITL and to draft a new DTL in consonance with the economic needs of the country and changing times. The Task Force consisted of highranking Government officials and eminent professionals.
- The terms of reference for the Task Force was to draft an appropriate direct tax legislation and submit its report to the GOI within six months, keeping in view the following aspects:
  - The direct tax system prevalent in various countries;
  - International best practices.
  - The economic needs of the country
  - Any other matter connected thereto. Feedback and suggestions invited

Feedback and suggestions invited

- With this background, the CBDT has invited feedback and suggestions from stakeholders and the general public in relation to the new DTL, in the form of a questionnaire comprising 25 questions under five broad categories viz., filing of return of income, grant of tax credits, processing/scrutiny of return, litigation and recovery of disputed tax demand, and penalty and prosecution. The CBDT has also invited suggestions on any other issues.
- On filing of returns, the questions seek feedback on the ease of compliance and the level of details sought in the returns.
- On grant of tax credits, the questions seek feedback on the ease of compliance and if tax credits are correctly granted.
- On processing/scrutiny of return, the questions seek feedback on the speed of processing of returns and rectification applications, issue of refunds, adequate opportunity before any additions are made, efficacy of the Dispute Resolution Panel and whether the proposed electronic process of assessment would be helpful in improving transparency, accountability and effectiveness of the tax administration.
- On litigation and recovery of disputed tax demand, the questions seek feedback on the need for a strong alternative dispute resolution mechanism, efficacy of different fora of dispute resolution like Mutual Agreement Procedure, Authority for Advance Rulings, Income Tax Settlement Commission, Tribunals, etc.
- On penalties and prosecution, the questionnaire seeks views on levy of penalties for various defaults under the ITL and the stage at which such penalty should be levied. It also seeks feedback on whether prosecution for withholding tax default is being launched in an appropriate manner and whether the present system of compounding of alleged offence has worked well.
- The feedback and suggestions on the said issues are required to be submitted latest by 2 April 2018.

Source: the recent Press Release dated 21 March 2018 (Press Release) issued by the Central Board of Direct Taxes (CBDT)[1],seeking feedback and *suggestions from stakeholders and the general public on a new direct tax law (DTL).*

3. CBDT notifies Income Tax Return (ITR) forms for tax year 2017-18

Background

- The CBDT, vide the Notification, has amended Rule 12 of the Income Tax Rules, 1962 (Rules), as also notified the ITR forms for all categories of taxpayers for tax year 2017- 18 (Assessment Year 2018-19). However, instructions for filing the ITR forms are awaited.

- This Tax Alert summarizes the key changes in the ITR forms as compared to the immediately preceding tax year 2016-17.

Key changes in the ITR forms

- **1.0 Key changes which commonly apply to most of the ITR forms:**

  - 1.01 While verifying the tax return, the taxpayer is required to mention in whose capacity it is furnishing such tax return and also declare that it is competent to furnish the said tax return in that capacity (ITR 1, 2, 3, 4).

  - 1.02 In reporting details of tax withheld on income, the taxpayer is to provide break-up of credit claimed in the hands of the taxpayer, details of taxes withheld and claimed in the name of spouse governed by Portuguese Civil Code or any other person in respect of whom the declaration has been filed (ITR 2, 3, 4, 5, 6, 7).

  - 1.03 Non-resident taxpayers need to submit details of any one foreign bank account for the purpose of remitting tax refund due, if any (ITR 2, 3, 4, 5, 6, 7).

  - 1.04 The requirement of reporting of cash deposit into each bank account of the taxpayer during the demonetization period (9 Nov 2016 to 30 Dec 2016) has been omitted, as the same is not relevant for the current tax year (ITR 1, 2, 3, 4, 5, 6, 7).

  - 1.05 In addition to details of capital gains not chargeable to tax as per the Double Taxation Avoidance Agreement (DTAA/tax treaty), the Schedule now also requires to report the capital gains chargeable at special rates as per the tax treaty. Consequently, the Schedule requires information of rate of tax as per the tax treaty, rate of tax as per the Indian Tax Laws (ITL) provisions etc. (ITR 2, 3, 5, 6).

- **2.0 Key changes which commonly apply to ITR forms of taxpayers earning income from business or profession:**

  - 2.01 Consequent to the amendment in the ITL last year, curtailing the maximum rate of depreciation to 40% from the earlier rates of 50%/60%/80%, the depreciation schedule has been modified to merge the closing balance of written-down value under such old block of assets to the block of asset on which depreciation is charged at the rate of 40% (ITR 3, 5, 6).

  - 2.02 The depreciation Schedule now provides for separate disclosure of the quantum of depreciation disallowable on the asset used for a purpose other than business or profession during the tax year (ITR 3, 5, 6).

  - 2.03 Separate disclosure of the quantum of proportionate aggregate of depreciation in the event of business reorganization such as merger, demerger, succession etc., is required (ITR 3, 5, 6).

  - 2.04 Like in the case of erstwhile indirect taxes, the taxpayers are required to furnish the details of Goods and Services Tax (GST) collected on sale or supply of goods and services, component of GST paid on their purchases, GST claimed as an expense and GST outstanding as payable, with break-up of Central GST, State GST, Integrated GST and Union Territory GST (ITR 3, 5, 6).

- **3.0 Key changes which apply to ITR-1 (Sahaj) Form**

  - **3.01 Applicability restricted to resident and ordinarily resident** [Resident and ordinarily resident means an individual who has been a resident in India in two out of ten tax years preceding the current tax year and has been in India for a period of 730 days or more during the seven tax years preceding the current tax year] individuals: ITR-1, applicable to individual taxpayers having aggregate total income up to INR5m from salary or one house property or other sources [Refer Annexure 1 for details], is now restricted only to resident and ordinarily resident individuals. Thus, individuals being resident, but not ordinary resident, and non-residents, including expatriates, will not have the benefit of furnishing the simplified one-page ITR form.

- 3.02 Reporting of different components of salary and house property income: Instead of reporting a final single amount of taxable salary and house property income, the new form requires a break-up of such incomes. For salary income, break-up components include basic salary, taxable allowances, value of perquisites, profits in-lieu of salary and eligible deductions under the ITL, along the lines of Form 16. Likewise, for house property income, details of gross rent received/receivable, taxes paid to local authorities and interest payable on borrowed capital need to be specifically disclosed.

4.0 Key changes in ITR-2 applicable to individuals and Hindu Undivided Families (HUFs) not having income from business or profession:

- 4.01 Revised ITR-2 is not applicable to taxpayers earning income from business and profession and, thus, consequential amendment to the ITR form has been made by deletion of information relating to business heads such as business income, business loss schedule.

- 4.02 The ITL provides an option to resident taxpayers which were non-resident in earlier years and having income from specified investment derived from foreign exchange assets, to continue with the benefit of concessional rate of taxation until such assets have been transferred or converted into money. The taxpayer is required to opt for the said option at the time of furnishing the tax return. Now, ITR-2 provides for such option in the tax return itself [Similar option is now provided in ITR-3 also].

- 4.03 In addition to information of house property which is let out and deemed to be let out (vacant) property, the taxpayer will now also have to give information of self-occupied property, which includes address of the property, details of co-owners, if any.

5.0 Key changes in ITR-3 applicable to individuals and HUFs having income from business or profession

- 5.01 Earlier, ITR-3 was applicable to individuals and HUFs having income from a proprietary business or profession. Now, it applies to individuals and HUFs having income from any business or profession

6.0 Key changes in ITR-4 (Sugam) applicable to taxpayers covered by presumptive tax provisions

- 6.01 Taxpayers covered by presumptive taxation are required to submit GST registration number and the amount of turnover/gross receipt as per returns furnished under the GST laws.

- 6.02 Requirement to furnish compressed balance sheet: The scope of reporting details of assets held in business has been expanded substantially. As against specific details of four items, [3] Similar option is now provided in ITR-3 also being inventory, cash in hand, debtors and creditors, the revised ITR-4 requires additional details of capital balance, secured loans, unsecured loans, advances, other liabilities, fixed assets, bank balances, loans and advances, and other assets.

7.0 Key changes in ITR-6 applicable to corporate taxpayers

- 7.01 Indian Accounting Standards (Ind- AS): ITR-6 has been suitably amended for companies covered by Ind-AS to include balance sheet and statement of profit and loss as per Ind-AS, together with amendment to the Schedule of Minimum Alternate Tax.

- 7.02 Details of ultimate beneficiaries: Unlisted companies are obliged to furnish particulars of natural persons who are the ultimate beneficial owners holding, directly or indirectly, not less than 10% of voting power at any time during the tax year. These particulars include name, address, percentage holding and PAN [Permanent Account Number] of such natural persons.

- 7.03 Break-up of details as per GST returns: Corporate taxpayers whose turnover is up to INR10m are required to provide the break-up of total expenditure with GST registered and non-registered entities. In relation to expenditure with GST registered entities, it further requires the break-up of expenditure relating to exempt supply covered under the composition scheme, and other registered entities for the period on or after 1 July 2017, being the GST applicability date.

- 7.04 Transaction in foreign currency: Corporate taxpayers whose turnover is up to INR10m are required to submit details in INR of aggregate receipt and payment of foreign currency made during the tax year on revenue/capital account. Most of this information may be available from financial statements prepared in accordance with Indian Generally Accepted Accounting Principles (IGAAP).

- **8.0 Key changes in ITR-7 applicable to charitable trusts and other institutions, political parties, business trusts [E.g., Alternative Investment Funds, Real Estate Investment Trusts]**

  - 8.01 In case of a charitable trust obtaining fresh registration on account of changes in objects or activities during the year, information about fresh registration is to be given.

  - 8.02 ITR-7 now provides for mandatory filing of particulars of author, founders, trustees or managers of the trust or institution, as against the optional requirement in past. The information to be provided includes name, address, PAN and Aadhaar number of such persons.

- **9.0 Changes to give effect to amendments in the ITL:**

  - 9.01 Additionally, all the ITR forms also incorporate certain consequential modifications to give effect to the amendments made by the Finance Act, 2017, which are effective from tax year 2017-18. Illustratively, this includes:

    - In respect of capital gains on unquoted shares, the Schedule of computing capital gains on sale of share and securities requires information of sale consideration and fair value as per the prescribed rules (ITR 2, 3, 5, 6, 7).

    - A separate Schedule has introduced for reporting of receipt of specified property by way of gift or for inadequate consideration (ITR 2, 3, 5, 6, 7).

Applicability of ITR forms to various category of taxpayers

Form	*Category of taxpayers*	*Sources of income covered*
ITR - 1 (Sahaj)	Individuals (resident and ordinarily resident)	**Who can file ITR-1** Has income from salaries or family pension, or Income from one house property, or Income from other sources **Who cannot file ITR-1** Who has an asset or signing authority in any account outside India or earns income from any source outside India, or Who has claimed tax treaty relief and/or unilateral double tax relief, or Has agricultural income above INR5,000, or Has total income above INR5m, or Has dividend income exceeding INR1m attracting super rich dividend tax levy, or Has unexplained credits or investment taxable at 60% under the provisions of the ITL, or Has capital gains or business income, or Income from more than one house property or has brought forward loss or loss to be carried forward under the house property head, or Income from lotteries or horse races or loss under the other sources head

ITR-2	Individuals and HUFs	Has income from salaries, or Income from house property, or Capital gains, or Income from other sources
ITR-3	Individuals and HUFs	Has income from business or profession
ITR-4 Sugam	Individuals, HUFs, firms (other than limited liability partnerships (LLPs))	Profits and gains from business and professions to which presumptive tax provisions apply
ITR-5	For firms/LLPs/Association of Persons (AOPs)	Income from house property Capital gains Profits and gains from business and profession Income from other sources
ITR-6	Companies other than those filing ITR-7	Income from house property Capital gains Profits and gains from business and profession Income from other sources
ITR-7	Persons requiring to furnish return of income in circumstances specifically provided for under the ITL viz., charitable trusts and other institutions, political parties, business trusts etc.	Income from house property Capital gains Profits and gains from business and profession Income from other sources

Source: key amendments made to the Income Tax Return (ITR) forms for tax year 2017-18, vide Notification No. 16/2018 dated 3 April 2018 (Notification) issued by the Central Board of Direct Taxes.

Key Regulatory amendments

This section summarizes the regulatory updates for the month of April 2018.

Press release issued by Government of India

1. Minimum Capital Requirements for foreign investment in 'Other Financial Services' which are not regulated by any Financial Sector Regulator

- In terms of the extant FDI policy, a company engaged in other regulated financial service activities are under the automatic route subject to meeting the minimum capitalisation as per the concerned regulator/ Government Agency. However, a company engaged in other financial service activities, which are not regulated by any financial service regulator, requires approval from the Department of Economic Affairs subject to minimum capitalisation. However, the FDI Policy did not specify the minimum capitalization requirement for such unregulated companies engaged in financial services activities.

- In order to avoid any confusion and bring clarity, the Government of India have provided clarity on minimum capitalisation requirement for a company engaged in fund based and non-fund based, unregistered/ exempted financial service activity.

- The Government has introduced minimum capitalization of USD 20 million for fund based activities and USD 2 million for non-fund based activities. Fund based and non-fund based activities have been defined as per the erstwhile FDI policy for Non-Banking Financial Company (NBFC) which are re-produced as below:

  - **Fund based activities**- Merchant Banking, Under Writing, Portfolio Management

Services, Stock Broking, Asset Management, Venture Capital, Custodian Services, Factoring, Leasing & Finance, Housing Finance, Credit Card Business, Micro Credit, Rural Credit

- **Non-fund based activities**- Investment advisory services, Financial Consultancy, Forex Broking, Money Changing Business, Credit Rating Agencies

- This requirement will impact inter alia entities which are not registered or are exempted from registering with the concerned financial sector regulator such as SEBI/ RBI.

Source: Press Release dated 16 April 2018

Notifications/ circulars issued by Reserve Bank of India (RBI)

2. RBI enhanced the limit for foreign portfolio investor's (FPI) investment in corporate bonds

- RBI has decided to enhance the limits for FPI investment in corporate bonds.

- FPI limit in corporate bonds would now be up to INR 2.66 lakh crore in the first half of fiscal year 2018 from existing INR 2.44 lakh crore.

- The said limit would be INR 2.89 lakh crore in the second half of 2018-19.

Source: A.P. (DIR Series) Circular No. 22 dated 06 April 2018

3. Introduction of daily reporting of Liberalised Remittance Scheme (LRS) transactions for resident individuals

- RBI has, in order to improve monitoring and also to ensure compliance with the LRS limits, decided to put in place a daily reporting system by AD banks of transactions undertaken by individuals under LRS, which will be accessible to all the other AD banks as well.

- The same is effective from the date of issuance of the said circular.

Source: A.P. (DIR Series) Circular No. 23 dated 12 April 2018

4. RBI issued the revised regulation in respect of acquisition and transfer of immovable property in India

- RBI has issued a revised regulation i.e. Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2018 [commonly referred as 'FEMA 21 (R)'] with effect from March 26, 2018 in supersession of the Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2000.

- The key amendments in FEMA 21 (R) are as under:

  - The FEMA 21(R) has now done away with the concept of a 'person of Indian origin (PIO) and all references therein to PIO have been substituted with references to Overseas Citizen of India (OCI)

  - OCIs can now sell immovable property (other than agricultural land / farmhouse / plantation etc.) to NRIs and OCIs, in addition to resident Indians.

  - FEMA 21 (R) grants permission for joint acquisition of one immovable property (other than agricultural land/ farm house/ plantation property) by the spouse of an NRI or an OCI subject to certain conditions.

- FEMA 21 (R) grants general permission to a person being a citizen of Afghanistan, Bangladesh or Pakistan belonging to minority communities in those countries, namely, Hindus, Sikhs, Buddhists, Jains, Parsis and Christians who is residing in India and has been granted a Long Term Visa (LTV) by the Central Government to purchase only one residential immovable property in India as dwelling unit for self-occupation and only one immovable property for carrying out self-employment subject to the conditions mentioned therein.

- The ceiling (equal to cost of acquisition of property) on repatriation of proceeds from the sale of immovable property (other than agricultural land/ farm house / plantation property) by an NRI or OCI has been removed i.e. henceforth gains made by NRI/ OCI from such sale can be repatriated, subject to tax and other levies.

- RBI has inserted the citizen (individual and/ or legal entities) of Democratic People's Republic of Korea in the list of prohibition to acquire immovable property in India. However, such prohibition would not apply to an OCI in any case.

Source: Notification No. FEMA.21(R)/2018-RB dated 26 March 2018

5. Issuance of cross border merger regulations

- RBI has issued Foreign Exchange Management (Cross Border Merger) Regulations, 2018 ('Cross border merger regulations') which would apply to all cross border mergers pending before the competent authorities as on the date of commencement of these regulations and the said regulations pertains to cross border merger, amalgamation between Indian and foreign companies.

- The salient features of the said regulations are as under:

  - RBI has granted deemed approval, as required under Rule 25A of Companies (Compromise, Arrangement and Amalgamation) Rule, 2016, provided the cross border merger is in compliance with conditions mentioned the Cross border merger regulations.

  - <u>Inbound mergers- resultant company is an Indian company:</u>

  - The resultant Indian company can issue or transfer any capital instruments to a non-resident subject to complying with foreign direct investment (FDI) regulations viz. pricing guidelines, entry routes, sectoral caps, etc.

  - If the foreign company, merging / amalgamating with Indian company, is a JV/WOS of an Indian company, then said Indian company must comply with disinvestment provisions mentioned under overseas direct investment (ODI) regulations. Further, if the aforesaid JV/WOS has a step down subsidiary abroad, then Indian company, has to comply with ODI regulations for undertaking fresh overseas investments.

  - Pursuant to sanction of the scheme of cross border merger, an office outside India of foreign company will be deemed to be a branch office outside India. Accordingly, the resultant company may undertake any transaction only if it is permitted to a branch office under the Foreign Exchange Management (Foreign Currency Accounts by Person Resident in India) Regulations, 2015.

  - Any guarantees or outstanding borrowings of a foreign company will be permitted to become borrowing of the resultant Indian company provided within two years, the ECB or Trade Credit or other applicable borrowing norms are complied with viz. Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 or Foreign Exchange Management (Borrowing or Lending in Rupees) Regulations, 2000 or Foreign Exchange Management (Guarantee) Regulations, 2000. The regulations have put a condition that no repayment of the liability will be permitted within the aforesaid two years period. The regulations have also clarified that end use restrictions will not be applicable.

  - The resultant Indian company can acquire and hold any assets outside India which are permitted to be acquired under extant FEMA regulations. In case where the resultant Indian company is not permitted to acquire or hold any asset / security outside India, then such assets / securities should be sold within a period of 2 years from the date of sanction of the scheme by NCLT. The sale proceeds can be utilized for payment of any liability which is not permitted to be held by the resultant Indian company.

  - The resultant Indian company has also been permitted to open and maintain a foreign currency bank account outside India for purpose of putting through transactions incidental to the cross border merger for a maximum period of 2 years.

  - <u>Outbound mergers- resultant company is a foreign company:</u>

  - The Indian entity are permitted to acquire or hold foreign securities which is in compliance with ODI regulations. Resident Individuals are permitted to acquire foreign securities provided the fair value is within LRS limits and which is in compliance with ODI regulations.

  - Pursuant to sanction of the scheme of cross-border merger, an office in India of an Indian company will be deemed to be branch office in India of a foreign company. Accordingly, the resultant company may undertake any transaction only, if it is permitted to a branch office under Foreign Exchange Management

(Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016.

  - Any guarantees or outstanding borrowings of an Indian company will be permitted to become borrowing of the resultant foreign company provided within two years the same is repaid as per the Scheme sanctioned by the NCLT. The regulations have put a condition that a foreign company shall not acquire any liability towards a lender in India in Rupees which is not in accordance with extant FEMA regulations and a NOC to this effect is obtained from the lender in India of the Indian company.

  - The resultant foreign company can acquire and hold any assets in India which are permitted to be acquired under the extant FEMA regulations. In case where the resultant foreign company is not permitted to acquire or hold any asset / security outside India, then such assets / securities should be sold within a period of 2 years from the date of sanction of the scheme by NCLT. The sale proceeds can be utilized for payment of any liability which is not permitted to be held by the resultant foreign company.

  - The resultant foreign company has also been permitted to open and maintain a SNRR account in India for purpose of putting through transactions incidental to the cross border merger for a maximum period of 2 years.

- **Valuations:** The valuation of the Indian company and the foreign company shall be done in accordance with Rule 25A of the Companies (Compromises, Arrangement or Amalgamation) Rules, 2016.

- Other provisions:

  - Companies involved in the cross border merger shall ensure that the regulatory actions, if any, prior to merger, with respect to non-compliance, contravention, violation etc. of the Act or the rules or regulations shall be completed.

  - The resultant company and/or the companies involved in the cross border merger shall be required to furnish reports as may be prescribed by the Reserve Bank, in consultation with the Government of India, from time to time.

  - In view of the deemed approval by RBI in terms of this notification, a certificate from Managing Director/ Whole Time Director and Company Secretary, ensuring compliance to these Regulations has to be furnished along with the application made to NCLT.

Source: Notification No. FEMA. 389 /2018-RB dated 20 March 2018

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