EY Tax and Regulatory Alert

February 2019

Prepared for ACMA

Contents

Building a better working world

Indirect Tax

This Section of Tax alert summarizes the Indirect tax updates for the month of February 2019

Judicial Precedents

1. M/s Tata Motors Ltd.

Vs

The Deputy Commissioner of Commercial Taxes

[2019-VIL-03-SC]

Background and facts of the case

- The appellant/ assessee is engaged in manufacture of motor vehicles which are sold through appointed dealers to buyers
- There is a warranty given to buyers for free replacement of defective parts from any dealer, and not confined to dealer from whom purchase was made
- The dealer is required to keep a stock of spare parts. Sales tax is paid on the stock of spare parts purchased by the dealers from the appellant
- The defective parts are sent back to the appellant and credit notes are issued for the purpose by the appellant to the dealers
- The issue that arose is in the case of such warranty provided by manufacturer (appellant) to purchaser for the supply of free spare parts under warranty; whether sales tax would be payable based on the credit notes issued by the manufacturer to the dealer upon such return of defective spare parts

Discussions and findings

- The assessment order and the appeal went against the appellant/ dealer while the Tribunal held in favour of the appellant/ dealer. However, the High Court relied upon the judgement passed by the Hon'ble Supreme Court in the case of Mohd. Ekram Khan & Sons v. Commissioner of Trade Tax, UP, Lucknow ((2004) 6 SCC 183) and the High Court set aside the order passed by the Tribunal, restoring the order passed by the assessing authority.
- The Ld. Counsel for the appellant referred the following judgements:
  - Premier Automobiles Ltd. & Anr. Etc. v. Union of India (1972 (2) SCR 526) wherein the principle of warranty covering cars sold has been well enunciated. In the said case, it was discussed that all defects on account of faulty manufacture in workmanship have to be set right and the defective parts have to be replaced, free of cost, by the manufacturer or his dealer, within a specified period of time or a given distance travelled by the car
  - Commissioner of Sales Tax v. M/s. Prem Nath Motors (P) Ltd. (ILR (1978) II Delhi 273) wherein observations have been made to the effect that a dealer sells cars along with a warranty, under which it is agreed that it would replace the parts free of cost. There is no separate consideration paid for the part so transferred and, thus, the only reasonable inference is that the consideration for the part or parts that might be replaced, under the warranty, was not separately specified because it was included in the price fixed and paid for the car at the time of its sale
  - Prem Motors v. Commissioner of Sales Tax, Madhya Pradesh ((1986) 61 STC 244) wherein it was opined that the warranty given is a warranty from the manufacturer and therefore, if during the warranty period, any part is found to be defective and is to be replaced, the responsibility of replacement is on the manufacturer. This is neither a sale of parts by the dealer to the customer nor to the manufacturer. What is effectively done is a passing on, of the parts, from the anufacturer to the customer, but in order to avoid delays and prevent any inconvenience to the customer, he replaces the part first and gets them from the manufacturer later. The cost for the same is reimbursed by the manufacturer
  - Geo Motors v. State of Kerala ((2001) 122 STC 285) wherein it was adopted to conclude that the transaction could not be categorised as a 'sale' even

though the dealer had purchased spare parts by giving 'C' Forms. Such a transaction was purely for replacement and not for sale

- The Ld. Counsel for the appellant referred the case of Mohd. Ekram Khan & Sons v. Commissioner of Trade Tax, UP, Lucknow wherein the relation was of a principal to agent and not of principal to principal. However, it was discussed that in the present case, the dealership agreement between the manufacturer (Tata Motors) and the dealer is on a principal to principal basis

- The Ld. Counsel for the respondent referred to the judgement of Bharat Heavy Electricals Ltd. v. Commissioner of Customs & Central Excise, Indore ((2003) 9 SCC 185) to contend that while considering the issue of excise duty in respect of components towards the "complaint reserve", it was held that the same would be excisable. It was observed that while the initial price charged for the machinery may include the element of the "complaint reserve", at the time of purchase, it is not known whether there will be any requirement to replace any part and, in many cases, the parts are not required to be replaced. In such an eventuality, the price equivalent of the "complaint reserve" is not returned to the customer

Decision by the Tribunal

- The moot point for consideration is whether credit notes can be treated as a mode of payment or not

- The issue has been referred to larger bench based on the crucial point for consideration that whether, in the case of such a warranty for the supply of free spare parts; once the replacement is made, and the defective part is returned to the manufacturer, sales tax would be payable on such a transaction relating to the spare part, based on a credit note, which may be issued for the said purpose

2. PSN Automobiles Private Limited

Vs

The Union of India

[2019-VIL-19-KER]

Background and facts of the case :

- The petitioner M/s PSN Automobiles Private Limited is a private limited company having its main focus on Dealership Operations for Commercial Vehicles & Construction Equipment

- The Company had filed a Writ Petition before the Hon'ble Kerala High Court regarding a clarification on the correct valuation for ascertainment of GST on Tax collected at source (TCS) in light of the Circular issued by CBIC vide Circular No. 76/50/2018-GST

- The petitioner had submitted that 1% TCS collected by auto dealer (assessee) from purchaser cannot be treated as an integral part of value of goods and services supplied by assessee, as dealer only acts as an agent for the State while collecting such amount which eventually goes to vehicle purchaser's credit.

Observations of High Court

- The HC took note of the petitioner's submission that the amount of 1% which the dealer collects from the purchaser, purchasing the car valued at more than ten lakhs, under Section 206C(1F) of the Income Tax Act, 1961, cannot be treated as an integral part of value of goods and services supplied by the petitioner as being the dealer of the motor vehicle he only acts as an agent for the State to collect the Income Tax amount which is ultimately credited to the purchaser of the motor vehicle.

- Reference has also been made to section 15(2)(a) of the Central Goods and Services Tax Act, 2017 which mandates value of supply to include any taxes, duties, cesses, fees and charges levied under any other law in force.

- Further, reference has been made to decision passed by Hon'ble Supreme Court in Dilip Kumar & Co. wherein it was held that any ambiguity in taxing provision should be resolved in State's favour.

Order

- The High Court has granted stay on the recovery of GST on TCS u/s 206C (1F) of Income Tax Act and held that further adjudication would be required to conclude the said matter. It has also restrained the Revenue to act on Circular No. 76/50/2018-GST pending the Writ outcome.

3. M/s Pasco Motors LLP

Haryana AAR

[2019-VIL-40-AAR]

Background and facts of the case

- M/s Pasco Motor LLP is into the business of "retail trading" of trucks and has made following submissions

- It purchases goods from M/s Tata Motors Ltd from different locations and the goods remain in transit for roughly five to ten days

- A lot of times, the material arrives at the end of the purchaser in the next month whereas the sale invoices are raised in the end of previous month by the seller when the goods were dispatched. The payment is made in advance by the applicant after which the invoice is raised

- Since the returns are to be filed on monthly basis, a practical problem is being faced by the applicant that the purchases are being booked by the purchaser in the next month only

- Further, towards the end of the month, the company announces lucrative incentives for the end customer to boost the sale. The applicant, in the month end; to meet the monthly sale targets (high volume) raises the invoice/5 to the end customer/s, deposit the due tax on the raised invoices but before receiving the physical delivery of goods from its supplier since the goods are in transit (as discussed above) and makes the delivery of goods only after receiving the same in the next month

- The applicant has filed the application to ascertain the below two things :

  - When will he be entitled to claim its Input Tax which stands charged and deemed to be paid by the seller in the previous month (time of receipt of goods so as to understand the time when credit shall be available)

  - If he is liable to pay the tax in the same month in which the invoice is raised and tax is collected by him even though he is not in physical possession of goods to be delivered under invoice & delivery/supply of goods is to take place at a later stage to end customer (time of supply of goods vis-a-vis raising the tax invoice to actual supply of goods)

Discussions and findings of the authority

- The explanation to clause (b) of sub-section (2) of Section 16 of the Acts ibid, is not applicable in the instant case, as in the instant case the buyer and recipient of goods is same, i.e. the applicant himself. Therefore, input tax credit on goods is only available when the applicant has received the goods

- With regard to tax invoices issued by the applicant without having goods in possession, it is observed that as per Section 12 of the CGST/HGST Act, 2017, the liability to pay tax on goods arises at the time of supply. The provisions of Section 12 clearly stipulates that in case the invoice has been issued by the supplier, the date of issue of invoice is the date of supply, hence, in such cases where the goods are delivered by the applicant later on but invoice is raised earlier, the date of issue of invoice will the time of supply for the purpose of determining the tax period for filing of return and payment of tax for such supplies

Ruling

- In case of invoices being raised by supplier in previous month and goods being received in the succeeding month, input tax credit on goods so received shall be available to the applicant, only when applicant has received the goods

- The liability to pay tax shall arise on the basis of time of supply, which in case of supply of goods is earlier of the following dates –

  - the date of issue of invoice by the supplier or the last date on which he is required, under sub-section (1) of section 31, to issue the invoice with respect to the supply; or

  - the date on which the supplier receives the payment with respect to the supply

4. M/s Diesel Garage
M/s Autozone Impex Pvt Ltd

Vs

CC, New Delhi

[2019-VIL-103-CESTAT-DEL-CU]

Background and facts of the case

- The appellants are the importers of automobile parts, such as, clutch plates, spring brake chamber, accelerator pedal etc. which are imported through ICD, Tughlakabad, New Delhi

- The department searched the premises of the applicant and seized certain goods namely automobile parts of SORL, PHC and SABRO brands primarily on the ground that RSP/MRP was not affixed on the imported auto parts and the appellant was not able to produce any import documents for verification to prove their legitimate import at the time of the visit of the officers and, therefore, the goods were put as per the provisions of detention under Section 110 of the Customs Act, 1962

- The appellant have been making request for provisional release of the seized goods which was not exceeded to by the Department and, therefore, the appellant had approached Hon'ble Delhi High Court for allowing the provisional release of the seized goods as per Section 110A of the Customs Act, 1962

- The Hon'ble High Court vide its order No. WP (C)/11024/2017 dated 16 February 2018, asked the Department to pass an order under Section 110A of the Customs Act regarding provisional release of the seized goods within 10 days from the receipt of Hon'ble High Court's order

- In deference to Hon'ble High Court's orders, the Department vide its order dated 23 February 2018 has allowed provisional release of the seized goods under Section 110A of the Customs Act, 1962 to the appellants on the following conditions :-

  - Submission of Bond, for the provisional release of the goods, of amount Rs. 92,90,825/- (Rupees Ninety Two Lacs Ninety Thousand and Eight Twenty Five only) i.e. a bond value equivalent to the redetermined/estimated value of the seized goods

  - Submission of Bank Guarantee of Rs. 8,67,087/- as the redetermined/ estimated differential duty leviable on the seized goods being provisionally released and Bank Guarantee should contain a clause by binding the issuing bank to keep it renewed and valid till final adjudication of the case

  - Submission of the Bank Guarantee of Rs. 3,00,000/- to cover the redemption fine and penalty and Bank Guarantee should contain a clause by binding the issuing bank to keep it renewed and valid till final adjudication of the case

- The appellant felt that the conditions of provisional release are too harsh and had approached the Commissioner (Appeals) for some relief in this regard. However, the Commissioner (Appeals) vide his impugned order dated 24/07/2018 had endorsed the above conditions of provisional release. The appellants have therefore filed this appeal against the above-mentioned order of Commissioner (Appeals) dated 24/07/2018

Observations of the Court

- The import documents namely bills of entry prove it clearly that the declared value has been enhanced at the time of import and assessment of the goods

- The description of the import consignment given on the bill of entry has been declared as of retail sale price indicated category and same has been cleared after the physical verification of the description declared by the importer

- It has been found that a show cause notice has been issued in the meantime which is dated 1st March 2018 whereunder it has been alleged that the declared price at the time of the import is much lower than the prices provided in the price list in respect of auto mobile parts of "SORL" brand goods. Since the declared value of the import consignment has already been enhanced by the Department and as it is a settled legal principle that once enhanced, the same value cannot be re-visited again without any concrete evidences

- As alleged in the show cause notice dated 01/03/2018 that price list mention the higher prices than declared by the importer, the court has mentioned that the price list of any product cannot be taken as the basis for determining the transaction value

Order

- The price list cannot only form basis for rejecting the transaction value under Section 4 of Customs Act, 1962 and, therefore, there is no valid ground of alleging any mis-declaration in the declared value of the import consignment

- The court has refrained from expressing its views on this question on merit at this stage as the matter has not reached the stage of taking final decision on the merits of the case, however, the conditions of provisional release imposed by the proper officer for release of goods seized/detained in the given facts and circumstances, appear to be harsh and inappropriate and, therefore, the court has ordered the provisional release of the detained/seized goods on following conditions:

  - Provisional release of the goods should be allowed to the appellant on submission of a bond for an amount of Rs. 92,90,825/- backed by bank guarantee of Rs. 2 lakhs as per provisions of Section 110 (2) of Customs Act, 1962

  - That the seized goods should be released to the appellant on meeting the requirements as mentioned above forthwith

- The appeal is accordingly allowed

5. M/s Delphi Automotive Systems Pvt Ltd

Vs

Commissioner of Central Tax, Pune I

[2019-VIL-87-CESTAT-MUM-CE]

Background and facts of the case

- The appellant is a manufacturer of parts of auto air conditioner and is registered under the central excise department for such manufacturing to supply auto air conditioner to M/s. General Motors

- The appellant procured mould and dies from M/s. Sanjay Technoplast, carrying out its operation from the same premises where the appellant's unit is situated

- The appellant received moulds and dyes as capital goods from M/s. Sanjay Moulds for Rs.1,80,46,000/- and availed cenvat credit of Rs.18,58,737/- in respect of excise duty paid on such capital goods. Subsequently it delivered those capital goods vide challan dated 17.10.2011 as per Rule 4(5)(b) of Cenvat Credit Rules 2004. Further, in order to recover cost from General Motors, the appellant raised tax invoice on 19.12.2011 on General Motors with assessable value of Rs.1,94,00,000/- along with VAT component @12.5% of Rs.24,25,000/-

- Further, case of the appellant is that ownership of the moulds and dyes was transferred to General Motors as a set of tools on the commercial invoice but its possession remained with M/s. Sanjay and therefore it was never removed from the premises of the appellant, but vide audit report dated 22.08.2014 the respondent department had observed that appellant availed cenvat credit of Rs.18,58,737/- on purchase of moulds and dyes and sold those goods to General Motors on 19.12.2011 for which appellant was not to be considered as in possession of those goods since the same transaction amounts to sale of goods

- Therefore, the appellant was liable to discharge excise duty of Rs.19,98,200/- as the assessable value at which the dies and moulds was sold was Rs.1,94,00,000/-

- It was put to show-cause, reply was furnished denying the allegation, the matter was adjudicated by Asst. Commissioner, Central Excise North Division and vide Adjudication order no. 8/Adj/NSD/CX/16-17 dated 30.03.2017 equivalent cenvat credit availed to the tune of Rs.18,58,737/- along with interest with effect from 19.12.2011 and penalty of equivalent duty amount has been imposed on the appellant

Observations of the Court

- The removal of dies and moulds to another factory though available in the same premises, would have the effect of reversal of entire cenvat credit availed had the appellant not shown him as job worker, but while the mould and dies were with the job worker, appellant sold it to M/s. General Motors with payment of VAT
- Going by the definition of sale under the CEA, 1944, sale means any transfer of the possession of goods by one person to another in the ordinary course of trade or business for cash or deferred payment or other valuable consideration
- Such a transfer with physical delivery of possession was not made but appellant had earned profit on sale of such mould and dyes in the guise of recovering the cost from General Motors. This being the factual position, going by the provision of sale of goods act, such sale after receipt of amount can only be completed with symbolic delivery of possession and in the case in hand, there is no such reference to such delivery of possession. Therefore, in the impugned order such transaction was held to be deemed removal
- However, having regard to the fact that when sale was done through invoice, the articles were not in possession of the appellant
- Further, after the appellant had received the consideration amount, it has lost its title over the goods despite the fact that no evidence is apparent on the delivery of possession
- Therefore, it can only be concluded that with effect from raising of invoice, consequent upon receipt of payment of sale price, appellant had lost its ownership right over the capital goods and manufacturing by the job worker, can only be treated as manufacturing being made by General Motors itself and not by the appellant

Order

- The appellant is, therefore, duty bound to reverse the credit with effect from invoice date which it had not done under the erroneous interpretation of law
- The appellant is liable to pay differential duty along with applicable interest with effect from the invoice date. Penalty under section 11AC(c) is set aside
- The appeal is allowed in part

6. Varroc Engineering Pvt Ltd

Vs

CC (Import), Nhava Sheva

[2019-VIL-59-CESTAT-MUM-CU]

Background and facts of the case

- The appellant had filed a Bill of entry on 03.11.2010 for clearance of Liquid Crystal Display – LCD under CTH 90138010 and claimed benefit of notification 24/2005 (Sr. No. SR. 29)
- On examination it was found by the department that the goods were complete devices used for motorcycle and therefore the benefit of notification no. 24/2005 (Sr. No. 29) and the classification under CTH 9013 was not applicable for the said item
- The Appellant waived that the show cause notice and after hearing, the Adjudicating Authority vide Order-in-Original dated 09.02.2011 ordered that goods "Liquid Crystal Display" is a specific part of motorbike and therefore the claimed CTH 90138010 was rejected and it were classified under CTH 8714990 as parts of accessories of vehicle
- On Appeal, the learned Commissioner (Appeals) vide impugned order dated 21.03.2012, rejected the appeal filed by the appellant. In the impugned order, the learned Commissioner has also observed that the Appellant has not produced any drawing/design of dashboard and of its parts before the Adjudicating Authority in support of their contention that the said part is nothing more than a Liquid Crystal Device cut to required shape

- Since the Appellant claims that the LCDs fall under Chapter Heading 9013 80 10 and the argument of the Revenue is that these are rightly classified under Heading 8714 99 90

Observations of the Court

- The LCDs imported by the Appellants are without electrical connections, presented in piece or cut to special shapes and consist of a liquid crystal layer sandwiched between two sheets of plastic

- Merely because LCDs were used as parts in dashboards of motorcycle, the same could not be classified under Heading 8714. It cannot be disputed that LCDs are specifically provided in tariff item 9013. Only conditions is that such LCDs should not "constitute articles" provided more specifically in other headings

- The LCD imported by the Appellant did not constitute such "article" which is more specifically provided in other headings

- The only reason for including the goods under Chapter Heading 8714 is that LCDs were to be used in the motorcycles

- The tariff entry 8714 does not pertain to LCD but parts and accessories of vehicles of heading 8711 to 8713. It nowhere include LCD or the dash board of Motorcycle specifically

Order

- The appeal filed by the Appellant is allowed

7. Tyresoles India Pvt Ltd

Vs

1) The Union Of India
2) The Ministry of Finance
3) The commissioner of Customs, Central Excise and Service Tax, Goa, Panaji
4) The Additional Commissioner of Customs, Excise and Service Tax, Goa, Panaji

[2019-VIL-28-BOM-ST]

Background and facts of the case

- The Petitioner carries on the activities of re-treading of motor vehicle tyres

- The Petitioner is registered for the purpose of payment of service tax under the category "management, maintenance or repair services"

- The Petitioner also pays the sales tax/VAT on the portion of gross receipts representing the value of goods and materials sold by way of consumption in carrying out the activity of re-treading of motor vehicle tyres in terms of Goa Value Added Tax Act (GVAT)

- For the period between October 2006 and October 2010, the Petitioner was served with show cause-cum-demand notices, requiring the Petitioner to show cause as to why the value of demanded sale in terms GVAT should not be added to the gross amount of value of taxable service and service tax levied thereon. In addition, the Petitioner was required to show cause as to why penalty and interest be not levied for failure to pay service tax on the basis suggested in the show cause notices

- The Petitioner filed detailed responses, mainly urging that deemed sale value could not be exigible to service tax as sales tax and service tax were mutually exclusive taxes and the Central Government did not have the power to tax that portion of the value attributable to sale of goods, whether deemed or actual

- The cause shown by the Petitioner did not find favour with the Commissioner, who proceeded to pass an order in original dated 23 November 2015, confirming the demands in the show cause notices

Observations of the Court

- The exemption under Notification dated 20 June 2003 makes no provision requiring the sale value to be quantified and shown separately in the invoice

- The exemption notification nowhere requires the service provider to indicate on the bill/invoice the value of materials consumed/sold while providing taxable service. The only requirement is that there must exist documentary proof indicating the value of goods and materials which are subject matter of sale/deemed sale

- The impugned order is wrong in denying the Petitioner the benefit of the exemption under Notification dated 20 June 2003 by reading into the exemption notification some conditions which do not find place in the same

- The Petitioner had produced documentary proof indicating the details and value of the goods and materials which formed the subject matter of sale/deemed sale

- Further, the Petitioner had produced on record documentary proof that sale/deemed sale component corresponding to 70% of the gross value

Order

- There is no justification on the part of the Commissioner in denying the Petitioner the benefit of exemption notification

- The impugned order is set aside and assessee petition is allowed

Key Indirect Tax updates

This section summarizes the regulatory updates for the month of February 2018

Notification No 2/2019- Central Tax dated 29 January 2019

The above notification notifies 1st February 2019 as the date on which provisions of Central Goods and Services Tax (Amendment Act) 2018 shall come into force, except the following sections of Amendment Act:

- Clause (b) of section 8, which amends Section 16(1)(c) of CGST Act relating to Input Tax Credit

- Section 17, which amends Section 39 of CGST Act relating to GST returns

- Section 18, which provides for insertion of Section 43A in CGST Act

- Clause (a) of section 20, which amends Section 49(2) relating to payment of tax, interest and other amounts

- Section 28(b)(i) and Section 28(c)(i), which amends Section 140 of Transitional Provisions

Notification No 3/2019- Central Tax dated 29 January 2019

The notification amends the Central Goods and Services Tax Rules 2017. Few of the major changes brought in by the notification are as follows:

- Rule 11 has been amended to provide that separate registration shall be required for multiple Places of Business instead of business verticals, subject to conditions as mentioned in the rule;

- Rule 21A has been inserted providing provisions for Suspension of Registration

- Rule 41A has been inserted to provide for Transfer of input tax credit on obtaining separate registration for multiple places of business within a State or Union Territory. Provides that a registered person can transfer unutilised credit to its other places of business on filing GST ITC-02A

- Sub Rule 1A has been inserted in Rule 53 , sub rule 1 to prescribe the particulars of a Credit Note/ Debit Note

Notification No 1/2019- Central Tax (Rate) dated 29 January 2019

Rescinds Notification No 8/2017- Central Tax (Rate) dated 28th June 2017, which provided exemption to intra-state supplies by an unregistered person to registered person, subject to a limit of INR 5000 per day. Reverse charge mechanism on procurement from Unregistered Dealers which was deferred till 30.09.2019 to be completely withdrawn with effect from 1st February 2019

Notification No 1/2019- Integrated Tax dated 29 January 2019

1st February 2019 has been notified as the date on which provisions of the Integrated Goods and Services Tax (Amendment) Act, 2018 shall come into force.

Notification No 1/2019- Compensation Cess dated 29 January 2019

1st February 2019 has been notified as the date on which provisions of Goods and Services Tax (Compensation to States) Amendment Act, 2018 shall come into force.

Notification No 2/2019- Customs dated 29 January 2019

This notification amends Notification No. 57/2017-Customs dated 30th June, 2017 to prescribe effective BCD rate on various products including parts of power bank of Lithium ion and Battery pack of cellular mobile phones

Notification No 3/2019- Customs dated 29 January 2019

This notification amends Notification No. 50/2017-Customs dated 30th June, 2017 to prescribe effective BCD rate on various products including Electric Vehicle (EV) and their specified part and raw material for manufacture of Lithium ion cells

Direct Tax

This section of tax alert summarizes the Direct tax updates for the month of February 2019.

Key Direct Tax Developments

1. **Calcutta High Court (HC) upholds initiation of prosecution under Black Money Act for non-disclosure of foreign bank account pertaining to years prior to enactment of Black Money Act**

Background

- The Section (S.) 153A of the Income Tax Act (ITA) provides that in case of search proceedings, the Tax Authority can re-assess the income of six years immediately preceding the year in which the search proceedings were conducted.

- The Tax return forms published for tax year 2011-12 for individuals for the first time introduced Schedule FA requiring the reporting of details of foreign assets, and it is made applicable every year thereafter. One of the assets required to be disclosed is the details of foreign bank account. This column of tax return requires details about, amongst others, name and address of the foreign bank, name mentioned in the account, account number, peak balance during the year etc.

- The Black Money Act was enacted in 2015 and is operative from 1 July 2015. It applies to every person who is resident in India.

- Ss.49 and 50 of the Black Money Act provide for prosecution, if a person being resident in India as per the ITA, who holds any asset (including financial interest in any entity) located outside India, wilfully fails to file a return of income or wilfully fails to disclose such foreign asset in his return of income.

- Chapter VI of the Black Money Act (comprising ss. 59 to 72) provided for one-time voluntary disclosure scheme for taxpayers to come clean and avoid the rigor of the Black Money Act. The Scheme was operative for a limited period from 1 July 2015 to 30 September 2015. The eligible declarant had to declare his undisclosed foreign assets/income and pay tax at a special rate. Once the declaration stands accepted by Tax Authority, the declarant is immune from any other penalty or prosecution under the ITA/Black Money Act.

- However, the said disclosure Scheme disqualified certain taxpayers from availing the benefit of the scheme. One such disqualification was a case where search action was taken on taxpayer and his assessments were pending as on the date of declaration.

- A search proceeding was conducted on the Taxpayer on 17 March 2015 and during the search proceedings, it transpired that the Taxpayer held four foreign bank accounts with HSBC Singapore which he had not disclosed to Indian Tax Authority. The Taxpayer explained that the bank accounts belonged to his deceased mother and were received by him as inheritance.

- Pursuant to notice u/s 153A of the ITA the Taxpayer furnished the return of income for the tax years 2008- 09 to 2014-15. However, he did not disclose foreign bank accounts in his tax returns.

- During the pendency of assessment in search proceedings, the Taxpayer approached the Settlement Commission. The ITA provides for an option to a taxpayer to approach the forum of Settlement Commission during the pendency of assessment proceedings for settlement of taxes to be paid on undisclosed income by making a full and true disclosure of his income. However, the application of the Taxpayer was rejected as being invalid perhaps, for want of true and correct disclosure of foreign bank accounts. Further, rectification application for re-consideration of the rejection order was also rejected by the Settlement Commission.

- The Tax Authority completed the assessments for the years impacted by search proceedings, after taking into account the amount (exact nature of addition made, if any, is not coming out in the HC ruling) lying in the undisclosed foreign bank accounts. The Tax Authority initiated the penalty proceedings under the ITA and prosecution proceedings under the Black Money Act for non-disclosure of foreign bank accounts in the tax returns and for wilful attempt to evade tax.

- The HC ruling does not throw light on the following facts:

  - Date of mother's demise upon which the Taxpayer inherited the foreign bank accounts
  - Whether the amount lying in the foreign bank accounts of the mother was from known sources of the mother and/or was disclosed to the Indian Tax Authority.
  - What exactly was alleged to be the default of the Taxpayer – was it non-reporting of foreign bank accounts in Schedule FA of the tax return or was it relating to income earned out of the bank balance.
  - Whether prosecution was initiated for non-reporting of foreign bank account details in the tax return or was it for evasion of tax on unaccounted foreign sourced income.
  - Whether any addition to total income was made in the assessment of the Taxpayer in respect of the foreign bank accounts.
  - Was there any specific explanation why the Taxpayer did not disclose foreign bank accounts inherited by him in the tax returns filed in response to search proceedings despite the fact that Tax Authority was always having these details.

- The Taxpayer filed a writ petition before the Calcutta HC for quashing the sanction by the Tax Authority for initiation of prosecution proceedings under the Black Money Act.

Taxpayer's contentions

- The Black Money Act is enacted in 2015 which is applicable from 1 April 2016. The said Act is prospective in nature and cannot be made applicable to the years prior to its enactment. The Taxpayer is not guilty of violation of any provision of the Black Money Act and hence, he cannot be proceeded against for prosecution under the Black Money Act.

- The Taxpayer was statutorily precluded from making disclosure under the one-time voluntary disclosure scheme under the Black Money Act on account of disqualification and there was no failure on the part of the Taxpayer to trigger penal action for failure to disclose foreign bank accounts.

- There was no *mens rea* on the part of the Taxpayer to attract the prosecution proceedings under the Black Money Act and mens rea is required to be established in any criminal proceedings.

- The Taxpayer cannot suffer double jeopardy for the same violation, as the Tax Authority has invoked penal provisions under the ITA as also invoked the prosecution proceedings under the Black Money Act.

Tax Authority's contentions

- The Taxpayer is not suffering double jeopardy. The ITA and the Black Money Act both operate in different fields. Under the ITA, the Taxpayer is penalized financially, while under the Black Money Act the taxpayer is punished with prosecution.

- The Tax Authority relied on the Supreme Court (SC) decision in the case of Gujarat Travancore Agency, Cochin v. CIT for the proposition that *mens rea* is not required in the penalty proceedings and the SC decision in the case of State of Maharashtra v. Sayyed Hassan for the proposition that there is no bar to a trial or conviction of an offender under two different enactments; bar is only to the punishment of the offender twice for the same offence.

- The Taxpayer had two opportunities to make the disclosure of the undisclosed bank accounts, first before the Settlement Commission and second while filing the return of income under the search proceedings. The Taxpayer failed to make disclosure on both the occasions.

- Since the Taxpayer failed to disclose bank accounts on both the occasions and since the failures were subsequent to the Black Money Act coming into effect, provisions of the Black Money Act stand triggered. There is, therefore, no infirmity in the Tax Authority invoking the prosecution provision under the Black Money Act.

<u>HC ruling</u>

The HC dismissed the writ petition of the Taxpayer and upheld initiation of prosecution proceedings under the Black Money Act against the Taxpayer for the following reasons:

- The HC noted that the Taxpayer had several opportunities to make disclosure about the foreign bank accounts. Even if the Taxpayer could not avail the benefit of one- time voluntary disclosure scheme under the Black Money Act, the Taxpayer had an opportunity to disclose the bank accounts while filing the return of income under ITA in response to the search proceedings and also before the Settlement Commission. The Taxpayer failed to make true and proper disclosure on both these occasions.

- Further, any failure to make a disclosure in search returns is an offence punishable under the Black Money Act. Both the above opportunities were subsequent to the Black Money Act coming into effect. Therefore, the failure of the Taxpayer to furnish information about an asset located outside India in his return of income attracts prosecution proceedings under the Black Money Act.

- The HC noted that the Taxpayer himself admitted the possession of foreign bank accounts. Having regard to such an admitted position, he ought to have disclosed information concerning the same in his tax returns. Mere fact that the Taxpayer has inherited the bank accounts on demise of his mother cannot prevent him from disclosure. According to the HC, there are sufficient material on record for proceedings against the Taxpayer under Black Money Act.

- The HC distinguished the SC ruling in the case of Rao Shiv Bahadur Singh & Anr relied upon by the Taxpayer. In that case, the SC held that law applicable to the offence is the law when offence is committed. The law which is enacted post the commission of offence cannot provide for punishment retrospectively. As it seems, the Taxpayer sought to claim that the offence of non-reporting of foreign bank accounts in tax returns for relevant years if at all, relates to years prior to the enactment of the Black Money Act while filing original tax returns and, hence, initiation of prosecution proceedings under the Black Money Act may result in giving retrospective effect to the Black Money Act which is not permissible under the law. However, according to the HC, in the present case the Taxpayer's failure to make disclosure of foreign bank accounts under ITA as aforesaid was during the period when the Black Money Act was in operation; it cannot be said to be a case of giving retrospective effect to the Black Money Act.

- The HC relied on the SC decision in the case of Sayyed Hassan in which the SC had held that there is no bar to a trial or conviction of an offence under two different enactments and the bar is only to the punishment of the offender twice for the same offence.

- The HC, however, did not deal with the issue as to whether mens rea is required to be established by the Tax Authority. This, according to the HC, can be dealt within the criminal proceedings during the trials and not at the stage of mere grant of sanction for prosecution.

Source: TS-64-HC-2019(CAL)

2. Bombay High Court rules transfer of shares does not constitute transfer of 'undertaking'

Background and facts:

- Indian Tax Laws (ITL) provides for a general mode of computation of capital gains arising on transfer of a capital asset by deducting cost of acquisition and cost of improvement of the capital asset from the full value of the consideration received or accruing on transfer of the capital asset (general computation mechanism). The term 'capital asset' is defined very widely to mean property of any kind held by a taxpayer except for specified items like stock-in-trade, personal effects etc.

- S. 50B of ITL provides for a special mechanism for computation of capital gains arising on slump sale of one or more undertakings wherein the net worth of the undertaking computed in a specified manner is deemed to be the cost of acquisition and cost of improvement of the undertaking.

- 'Slump sale' is defined u/s. 2(42C) of ITL to mean transfer of one or more undertakings for a lump sum consideration without assigning values to the individual assets and liabilities in such sale. Further, for the purpose of slump sale, the term 'undertaking' includes any part of an undertaking, or a unit or division of an undertaking or a business activity taken as a whole, but does not include individual assets or liabilities or any combination thereof not constituting a business activity.

- Taxpayer, an Indian company, was engaged in the business of production of television programs, air time sales, movie production and distribution of films. Taxpayer held 49% shares in another Indian company (ICo). During the year under consideration, Taxpayer along with other shareholders of ICo who held balance 51%, sold their shares in ICo to a third party. Taxpayer computed the capital gains arising from such sale as per general computation mechanism provided under ITL.

- The Tax Authority contended that sale of 100% shares in ICo3 resulted in slump sale of an undertaking and hence, capital gains arising from such sale was to be computed as per section 50B of ITL.

- Being aggrieved, Taxpayer appealed to the First Appellate Authority(FAA), who upheld the decision of the Tax Authority. Taxpayer appealed further to the Tribunal.

- The Tribunal ruled in Taxpayer's favour and held that the sale of shares does not amount to transfer of an 'undertaking' and hence, the computation mechanism of section 50B applicable to slump sale does not apply to simpliciter transfer of shares of ICo by Taxpayer.

- Being aggrieved by the Tribunal ruling, the Tax Authority appealed to the Bombay HC.

<u>Ruling of the Bombay HC:</u>

The HC upheld the decision of Tribunal ruling in favour of Taxpayer. The reasoning of the Tribunal which was accepted by HC is as follows:

- The subject matter of transfer by the Taxpayer was shares in ICo and not the undertaking of ICo. Transfer of shares simply cannot be equated with the sale of an undertaking under ITL.

- A company is a juristic person and is distinct from its shareholders. Shareholders of a company merely get a right to participate in the profits of the company but they do not own the property of the company. Reliance in this regard was placed on the Supreme Court decisions in cases of Bacha F. Guzdar v CIT and Vodafone International Holdings B.V. v Union of India & Anr. Thus, sale of shares of a company does not tantamount to sale of assets of such company.

Source: TS-44-HC-2019

3. Supreme Court reverses its earlier ruling and allows 100% deduction for new units undertaking "substantial expansion" for fresh five years

Background

- The ITL contain provisions for grant of profit-linked tax holiday for industrial undertakings in some specified areas. Each provision is targeted at a specific class of undertakings which are set up within a prescribed qualifying period in specified areas and subject to fulfilment of prescribed conditions. The object of granting such incentive is the economic and industrial development of backward areas. The general trend of such incentives is that the incentive period starts from a year ("initial assessment year") in which the undertaking begins to manufacture or produce any article or thing.

- Prior to insertion of S.80-IC, vide the Finance Act, 2003, the tax holiday for industrial undertakings set up in specified backward areas was governed by S.80-IA up to tax year 1998-99 and S.80-IB from tax year 1999-2000 onwards. Similarly, S.10C, inserted with effect from tax year 1998-99 offered tax holiday for undertakings set up in the North-eastern region up to tax year 2002-03.

- The Finance Act, 2003, inserted S.80-IC with a view to give effect to a package of fiscal and non-fiscal concessions announced by the Central Government for certain Northern and North-Eastern states of India.

- For units based in specified areas of Northern states of HP and Uttaranchal, S. 80IC allows a two-tier income-linked tax holiday at a prescribed percentage for 10 years viz., a full tax holiday (100%) of profits for the first five years followed by a partial (25%/30%) tax holiday for the next five years. In contrast, the tax holiday period for units located in North-Eastern States is full 100% of profits for 10 years.

- Tax holiday is available either to: (a) a new unit which begins to manufacture or produce qualifying articles or things or (b) an existing unit which implements "substantial expansion".

- "Substantial expansion" is defined to mean an increase of investment in plant and machinery by at least 50% of the book value of plant and machinery (before claiming depreciation in any year), as on the first day of the tax year in which substantial expansion is undertaken. Objectively defined "substantial expansion" (i.e. incremental investment > 50% of existing book value) is a new feature of S.80-IC as compared to its predecessor provisions.

- The qualifying period within which unit should begin to manufacture/produce or complete "substantial expansion" in certain specified areas of HP and Uttaranchal was between 7 January 2003 and 31 March 2012.

- The unit should also satisfy certain other conditions, inter alia, that it should not be formed by splitting up or reconstruction of a business already in existence or it should not be formed by transfer to a new business of machinery or plant previously used for any purpose (commonly referred to as "formative conditions").

- Tax holiday period of 10 years begins from the "initial assessment year" which is, inter alia, defined to mean the tax year in which the unit begins to manufacture or produce articles or things or completes substantial expansion.

- S.80-IC also contains a specific overall period limitation which states that the total period of deduction under the predecessor provisions and S.80-IC cannot exceed 10 years.

Facts of the case:

- The Taxpayer had established new units in specified areas of Himachal Pradesh (HP) and Uttaranchal within the qualifying period. For such new unit, Taxpayer treated the year of manufacture or production of articles of things as the initial assessment year.

- The Taxpayer claimed 100% deduction for the first five years from the year of set up of new industrial units which was allowed by the Tax Authority.

- Subsequently, in the sixth year, the Taxpayer undertook substantial expansion of the existing unit by way of investment in plant and machinery exceeding 50% of book value as on first day of the fifth year. The Taxpayer claimed the year of completion of substantial expansion as “initial assessment year" qua the whole of unit and claimed 100% deduction for the entirety of the profits of the unit (including substantially expanded portion) from sixth year by contending that it became entitled to a fresh five-year tax holiday period for claiming 100% deduction by virtue of completion of substantial expansion.

- The Tax Authority disallowed the claim by holding that the Taxpayer had already claimed deduction of 100% of profits for the first five years from the date of set up of new unit and, hence, restricted the deduction to 25% of eligible profits for the said year. Accordingly, the Tax Authority held that the Taxpayer was entitled to only 25%/30% deduction from the sixth year to the tenth year and cannot avail a fresh five-year tax holiday for 100% deduction on account of substantial expansion.

- Further, the Tax Authority contended that, for the purpose of claiming benefits under S. 80-IC, taxpayers can have only one "initial assessment year”.

- The First Appellate Authority and the Tribunal ruled against the Taxpayer and upheld the Tax Authority's action of restricting the deduction to 25% from the sixth year onwards. Being aggrieved, the Taxpayer appealed to Himachal Pradesh High Court (HP HC).

- The HP HC clubbed the Taxpayer's case with that of many other taxpayers, who had completed “substantial expansion” during different time periods and based on plain and literal interpretation of S. 80-IC, the HP HC ruled in favor of the Taxpayer and permitted a fresh tax holiday claim of 100% from the year of substantial expansion subject to total period of exemption not exceeding 10 years from the date of commencement of manufacture. The HC held that (a) there is no bar on having more than one “initial assessment year", (b) Since S.80-IC benefit is geared towards additional investment, the Taxpayer can claim 100% deduction for a fresh five-year period within the overall period of 10 years by making a “substantial expansion" during the qualifying period, (c) Substantial expansion cannot be confined to one expansion. As long as the requirement of S. 80-IC is met, there can be multiple substantial expansions within the qualifying period.

- Aggrieved, the Tax authority appealed before the Supreme Court (SC) wherein the Division Bench ruled against the Taxpayer in the case of Classic Binding Industries and restricted the claim of deduction to 25% of profits from year of substantial expansion.

- The Division Bench distinguished the SC ruling in the case of Mahabir Industries relied upon by the Taxpayer. In Mahabir Industries case, the taxpayer claimed 100% of profits as deduction under S.80IB for the initial five years and thereafter carried out a substantial expansion during the qualifying period under S. 80-IC. The SC, in that case, allowed deduction of 100% of profits under S.80IC for the balance five years period by reckoning “initial assessment year” from the completion of substantial expansion. The Division Bench distinguished Mahabir Industries ruling on the ground that it involved deductions under two separate sections whereas in the case before the Division Bench, the Taxpayer claimed deduction under S. 80-IC itself by considering the substantial expansion as a separate event to trigger ‘initial assessment year' which was not correct.

- The Division Bench has also clubbed a bunch of other appeals. However, while disposing of appeals, many of the taxpayers were neither served with notices of hearing nor heard. On application being filed by these taxpayers, their appeals were restored for fresh hearing. The Division Bench ruling was recalled for fresh hearing. Tax authorities had also filed Special Leave Petition before SC in certain taxpayers matters. All these appeals and Special Leave Petitions were clubbed together for the hearing by the Larger Bench.

Issue before HC

Whether the Taxpayer, who had set up a new unit during qualifying period and thereafter completed substantial expansion before sunset date, was entitled to 100% deduction for a fresh five-year period?

Larger Bench Ruling

The Larger Bench ruled in favor of the Taxpayer by allowing the enhanced claim of deduction of 100% of profits from the year of completion of substantial expansion, subject to total period of exemption under S.80IC not exceeding 10 years. It further stated that the Division Bench ruling is erroneous for the reason that it was delivered by referring erroneously to the definition of "initial assessment year" as provided in a different provision viz. S. 80-IB(14) and without having regard to the definition of "initial assessment year" under S. 80-IC itself which is materially different in its scope.

The Larger Bench decision is based on the following principles:

- The definition of "initial assessment year" mentioned in S. 80-IB could not have been the basis of determination of initial assessment year under S. 80-IC since S. 80-IC itself encompasses the definition of "initial assessment year".

- S. 80-IB (14) starts with the words "'for the purpose of this section". Thus, 'initial assessment year' defined therein is relatable only to the deductions that are provided under the provisions of S. 80-IB, namely, in respect of profits and gains from certain industrial undertakings other than infrastructure development undertakings.

- S. 80-IC is materially different from S. 80-IB, since S.80-IC is a special provision in respect of only those undertakings established in particular States viz., Sikkim, Himachal Pradesh, Uttaranchal or any of the North-Eastern States.

- The interpretation of "initial assessment year" contained in S. 80-IC(8) is materially different. As per S.80-IC, "initial assessment year", means the year in which the undertaking or the enterprise (i) begins to manufacture or produce article or things; or (ii) commences operation; or (iii) completes substantial expansion. Thus, undertaking or enterprise can have more than one "initial assessment year" for S.80IC depending upon the relevant event.

- Further, S. 80-IC provides 100% of profits and gains for first five initial assessment years commencing with the initial assessment year and thereafter 25%/30% of the profits and gains. The deduction @ 25% for the next five years in on the assumption that the new unit remains static without involving substantial expansion thereof. However, the moment substantial expansion takes place, another "initial assessment year" is triggered. This new event entitles that unit to start claiming deduction @ 100% of the profits and gains from year of substantial expansion.

- The purpose for which S. 80-IC was enacted was to encourage the undertakings or enterprises to establish and set up units in the aforesaid States in hilly areas to make them industrially advanced States as well. Having regard to the objective of the provision, 100% of profits and gains is allowed even when there is substantial expansion of the existing unit. As substantial expansion referred to in the provision would result in increase in production as also generation of more employment, the year in which substantial expansion is carried out is treated as "initial assessment year".

- The Larger Bench referred to SC ruling of five-judges bench (Constitution Bench) in the case of Commissioner of Customs v. Dilip Kumar and Co. in support of the proposition that Statute must be interpreted according to intention of the legislature. Constitution Bench did also hold that where statutory provision is open to more than one meaning, court is to choose the interpretation which represents the intention of the legislature.

- The Larger Bench endorsed the SC ruling in the case of Mahabir Industries and held that there can be two initial assessment years under S.80IC also; one for setting up of new unit and another for substantial expansion.

Source: TS-75-SC-2019

Regulatory amendments

This section summarizes the regulatory updates for the month of February 2019.

Notifications/ circulars issued by RBI

1. **Investment by Foreign Portfolio Investors (FPI) in Debt**

- As per the extant norms, no FPI shall have an exposure of more than 20% of its corporate bond portfolio to a single corporate (including exposure to entities related to the corporate).

- In order to encourage a wider spectrum of investors to access the Indian corporate debt market, RBI has decided to withdraw the above requirement of 20% limit and hence FPI can now have beyond 20% exposure in a single corporate bond.

Source: A.P. (DIR Series) Circular No.19 dated 15 February 2019 read with A.P. (DIR Series) Circular No.31 dated 15 June 2018

2. **Liberalization of External Commercial Borrowing (ECB) framework for resolution applicants under the Corporate Insolvency Resolution Process (CIRP)**

- In terms of the extant ECB framework, ECB proceeds cannot be utilised for repayment of domestic Rupee loans, except when the ECB is availed from a Foreign Equity Holder as defined in the ECB framework.

- RBI has decided to relax this end-use requirement for resolution applicants under the CIRP and allowed them to raise ECBs from the recognised lenders, except from the branches/ overseas subsidiaries of Indian banks, for repayment of Rupee term loans of the target company under the approval route.

- Accordingly, the resolution applicants, who are otherwise eligible borrowers, can now forward such proposals to raise ECBs, through their AD bank, to RBI, for approval.

Source: A.P. (DIR Series) Circular No.17 dated 16 January 2019 read with FEMA Notification.3(R)/2018 dated 17 December 2018

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