EY Tax and Regulatory Alert

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Contents

Building a better working world

Indirect Tax

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

Judicial Precedents

1. Tata Motors Ltd Vs Commissioner of Central Excise and ST (LTU), Mumbai

[2019-VIL-23-CESTAT-MUM-ST]

Background and facts of the case

- **Authorized Service Station Services**
  - The appellants have been registered for providing taxable services under the category "Authorized Service Station Services".
  - The authorized dealers of the Appellants provided "Authorized Service Station" service to the customers of appellants and the cost of such service is paid by the appellants to the dealers.
  - Appellants for meeting this expense make a provision for the warranty on the basis of their sales. When so ever such service is provided by the authorized dealer, a debit entry is passed on in the provision for the warranty made.
  - The reimbursement received by the dealer/ authorized service station from the assessee for carrying out service of any motor car, light motor vehicle or two wheeled motor vehicle manufactured by the appellant is includible in the value of taxable service provided by the appellant.
  - The normal practice is that appellants provide certain free services at the service station.
  - The reimbursement towards the consideration for the services rendered by the dealer on account of appellants is made by the Appellants to the dealer.
  - These service charges reimbursed by the Appellant to the dealer for providing free services during the warranty period are includible in the value of taxable services provided by the Appellants.
- Dealers provide the maintenance service to the customers and such cost is paid by the appellant to the dealers and a debit entry is passed on in the provisions for warranty made.

Revenue's Contention

- Appellants are themselves having Tata Car Service Centre, Worli Mumbai for providing similar services. They have taken registration in respect of the said shop from 1.04.2007 and have been paying service tax in respect of the service provided from there. The said car repair shop at Worli is not an Authorized Service Station, and is their own repair shop, hence they were not liable to pay service tax in respect of services provided from the said shop.
- However in view of the department since they have registered themselves with effect from 01.04.2007 and have been paying service tax in the category of "Authorized Service Station Service" with effect from 01.04.2007 their contention for not paying the service tax for the period prior to that date is not tenable. Thus service tax is demanded in respect of the value of the service provided from the Tata Car Repair Shop.

Decision by the Tribunal

- The revenue has Confirmed the demand made in respect of the amounts reimbursed by appellant to their authorized dealers for services provided by them under the category of Authorized Service Station Services
- For levy of service tax it is essential to identify the person who has provided the taxable service and the person who has received the service
- The appellants have provided the warranty services to their customers through the dealers network and for providing free warranty services as per their contractual obligation they have made the payments to the dealer's which is evident from the debit entries made by them in their book of accounts
- These debit entries by themselves will not mean that taxable services have been provided by them. However, the fact that these debit entries made were inclusive of service tax is a fact that needs to be verified
- The customers of Appellants have received the taxable service from the dealers of the customer, and appellants have to ensure that these services are provided free, hence appellants are under contractual obligation to discharge the legal liabilities arising out of such provisioning of service through their dealers or agents

- These services cannot be said to be provided because of the arrangement made without payment of tax liabilities.

- The matter needs to be relooked for determination of tax liability and all the documents that appellants would like to produce in their support. The order of Commissioner proceeds on no availability of certain documents for his consideration.

- The demand of Service Tax in respect of services provided from Tata Car Care Centre, and also in respect of the services provided under the category of Business Auxiliary Services is upheld. In respect of the Service Tax demands made for the reimbursements made to Authorized Dealers and that in respect of Banking & Financial Services, the matter is remanded for redetermination of the issues and quantum of demand

- **Business Auxiliary Services :**

- The appellant paid commission in foreign currency to foreign agents in respect of goods exported outside India. Whenever appellants export vehicles directly to customers outside, they paid commission to the overseas parties who assisted them in procuring orders and in other activities associated with the deliver, realization of payment, after sale services etc - Appellants have challenged the demand stating that these services have been provided by the foreign buyers outside India, they cannot be taxable in India

HELD :

- Section 66A clearly and unambiguously provides that, the services provided by the person (person A) having any fixed establishment from which the service is provided or to be provided or has his permanent address or usual place of residence, in a country other than India to any person (person B) who has his place of business, fixed establishment, permanent address or usual place of residence, in India, shall be treated to be provided by the person B to himself and shall be taxable in India.

- <u>Classification of certain incomes claimed by appellant as "interest on loan"</u>

- The assessee is not in the business of giving 'loan' on interest and consequently, the consideration received for the various services provided does not qualify as 'interest on loan'.

- The aforesaid services provided by the assessee would appropriately fall under the category of 'Banking and Other Financial Services' - It is question of common understanding that the Banking and Financial services are not service simplicitor as loan, deposit or advances but are Financial Products, designed with combination of various isolated services so that adequate finance is made available to consumer/buyer at competitive prices.

- How these products are organized is not relevant, but whether these products get classified under the category of taxable services specified under Banking and Financial Services needs to be examined Commissioner have concluded on the basis of extraneous or irrelevant considerations and concluded that the transactions are not of extending the loan.

HELD:

- The matter has been remanded back for consideration of the issues afresh

2. Commissioner of Customs (Import), Mumbai

Vs

M/s Chasys Automotive Components Pvt Ltd

[2019-VIL-16-CESTAT-MUM-CU]

Background and facts of the case :

- Appeal has been filed by Revenue against the Order-in-Appeal dated 25.6.2012 passed by the Commissioner of Customs (Appeals), Mumbai Customs Zone-I, by which the Commissioner (Appeals) rejected the Appeal filed by the department and upheld the Order-In-Original dated 25.2.2011 passed by the Deputy Commissioner of Customs, Gatt Valuation Cell, Mumbai.
- The goods were supplied by the parent company to the respondent by adding a margin of profit of 11%. The issue to be determined in this Appeal is whether the relationship between the parent company i.e. the supplier from abroad and their subsidiary company i.e. the respondent herein, has influenced the import price or not and whether the department is justified in rejecting the transaction value.

- From the record it is clear that the goods are supplied as per standard price fixed. As per the said contract, all payments described in the contract shall be paid by means of banking transfer and/or Letter of Credit (L/C) and all payments of this contract price shall be made by GM India after Production Part Approval Process

- As per the terms of contract, if it is necessary to change the contract toolings or buy additional toolings, only then it is possible to change the contract price by mutual agreement.

- The goods supplied by the parent company to the respondent are the capital goods used in the manufacture of final product i.e. chasis designed by them.

- These goods can't be used by any other manufacturer. The goods supplied by the parent company to the respondent are purchased goods (i.e. not manufactured by supplier) and the copies of supplier's purchase invoices were also produced by the respondent before the adjudicating authority.

Revenue's Submission

- The main thrust of argument of Revenue is that it is not possible to compensate the technical know-how, contracts for machinery & equipments and supply of tooling, sea freight from Korea to Indian Port, supplier's profit, handling and storage charges as the goods have been purchased by the supplier from different manufacturer and that in terms of Rule 10(2)(c)(iii) the sea freight alone constitutes 20% of the assessable value and therefore the impugned order is liable to be set aside.

- He also argued that the margin of profit is more than 11% and therefore a further loading of 5% has to be allowed by the authorities below.

Court findings and Decision taken

- As per the invoices produced by the respondent before the Adjudicating Authority, the goods were supplied by the parent company to the respondent by adding a margin of profit of 11% and the said goods were thereafter sold by the respondent to General Motors by adding 2% to the price to cover their expenses. This was only a one time import.

- According to the scheme of valuation under the Customs Act, 1962, and in particular as per Section 14, the transaction value is required to be accepted for assessment purposes except in circumstances, outlined in Rule 3 of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007. Where the buyer and seller are related, assessable value of the imported goods is determined only in accordance with the provisions of Rule 3(3) of Customs Valuation Rules, 2007 which mandatorily require that where the buyer and seller are related and where the circumstances of the sale indicated that the relationship has not influenced the price of the imported goods, the transaction value has to be accepted.

- Unless the price actually paid for the transaction falls within the exceptions, Customs authorities are bound to assess the duty on the transactional value.

- The Revenue failed to produce any evidence before any of the authorities below in support of its contention. Revenue also did not produce any document about contemporaneous import at a higher price.

- Whereas the respondent had submitted documents such as the Contract Agreement between the respondent and the foreign supplier which provides a basic idea about the terms of sale and payment, copies of invoices etc.

- The Revenue has not brought out any evidence in its appeal to cast any doubt on the genuineness of the documents produced by the respondent before the Adjudicating Authority or first Appellate Authority nor provided any contrary information to about sale/purchase of identical/similar goods at higher prices or any evidence of payment over and above the invoice value.

- In view of the above, although the supplier and the respondent were 'related persons' for the purpose of Customs Valuation Rules but the relationship between them had not influenced the price.

- The allegation of the revenue that the margin of profit is more than 11% is without any basis and therefore rejection of transaction value by the revenue cannot be approved.

- Allegations of mis-declaration of value also cannot be sustained.

3. (1)Kerala State Screening Committee on Anti-Profiteering
(2)Director General Anti-Profiteering, CBIC, New Delhi (DGAP)
Vs
M/s Maruti Suzuki India Limited (MSIL)

[2019-VIL-01-NAA]

Background and facts of the case

- The brief facts of the case are that the Kerala State Screening Committee on Anti-Profiteering, vide the minutes of it's meeting held on 08.05.2018 had referred the present case to the Standing Committee on Anti-profiteering, alleging profiteering by the Respondent i.e M/s Maruti Suzuki India Limited on supply of four models of Motor Car, namely, 'Wagon R VXI AMT', 'Swift VXI', 'Alto 800 LXI' & Wagon R VXI' (HSN code- 8703), by not passing on the benefit of reduction in the rate of tax at the time of implementation of GST w.e.f. 01.07.2017.

- The DGAP has stated in his Report dated 28.09.2018 that the two invoices issued for each of the four products by the Respondent were scrutinized and it was observed that in the pre-GST era, the products namely, 'Wagon R VXI AMT', 'Swift VXI', 'Alto 800 LXI' & Wagon R VXI' (HSN code 8703) attracted total 15.63% duty incidence which included Central Excise Duty 12.50%, CST @ 1%, National Calamity Contingent Duty (NCCD) @ 1%, Auto Cess @ 0.125% and Infra Cess @1%. On implementation of GST, w.e.f. 01.07.2017, the GST rate on the above models was fixed at 29% which included Central GST @ 14%, State GST @ 14% and Compensation Cess @ 1%.

- The DGAP also stated that as per the Section 171(1) of the CGST Act, 2017 the anti-profiteering provisions are attracted only when there is a reduction in the rate of tax or increase in the input tax credit and therefore in the present case as there has been no reduction in the rate of tax, the allegation of profiteering by the Respondent was not established.

- The DGAP further observed that the selling price of the Respondent to his dealer had increased primarily because of the incidence of rate of tax had gone up from 15.63% to 29% as the afore mentioned transactions were in inter-state sale (Sale from Haryana State to Kerala State) where 1% CST was charged in pre-GST period whereas in post-GST 29% tax was charged. Therefore, the cum-tax price had increased.

Court findings and Ruling

- First of all it is observed that the rate of tax was 15.63% in the pre-GST era which was increased to 29% in the post-GST era. Secondly from the invoices referred above, it is evident that before discount base prices of all the products had remained the same. Hence the provisions of Section 171 of the CGST Act 2017 are not attracted.

- Based on the above facts it is clear that the Respondent has not contravened the provisions of Section 171 of the CGST Act, 2017 and hence there is no merit in the application filed by the above Applicant and the same is accordingly dismissed.

4. M/s. PSN Automobiles Private Limited Vs The Union of India; The Central Board of Indirect Taxes and Customs

[WP(C) 680/2019]

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 the Hon'ble 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

- 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

Key Indirect Tax updates

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

32nd GST Council Meeting

Below are the key updates :

- Rate reductions:
  - The GST rate on products of Chapter Heading 8483 like pulleys, transmission shafts, etc. have been reduced from 28% to 18%
  - Third party insurance premium of goods carrying vehicles from 18% to 12%;
  - The GST rate on Fly ash blocks have been reduced from 12% to 5%
  - The GST rate on re-treaded or used pneumatic tyres of rubber has been reduced from 28% to 18%
  - The GST rate on monitors and TVs of up to screen size of 32 inches has been reduced from 28% to 18%
  - For EPC contracts executed for setting up of solar power plants, it shall be deemed that 70% of the gross value of the contract is the value of goods attracting 5% rate and the remaining portion (30%) of the aggregate value of such EPC contract shall be deemed as the value of supply of taxable service attracting standard GST rate. However, the exact entry in the Notification for the said change would need to be analysed, to better understand as to whether the deemed valuation is obligatory and its scope.
  - Exemption on services provided by Central or State Government or Union Territory Government to their undertakings or PSUs by way of guaranteeing loans taken by them from financial institutions has been extended to guaranteeing of such loans taken from banks.
- Rate clarifications:
  - Movement of Rigs, Tools & Spares and all goods on wheels on own account where such movement is not intended for further supply of such goods but for the provision of service does not involve a supply (e.g., movement of testing equipment etc.) and is not be liable to GST.
- Miscellaneous:
  - Security services (supply of security personnel) provided to a registered person, except Government Departments which have taken registration for TDS and entities registered under composition scheme, shall be included under the RCM category
  - The new return filing system shall be introduced on a trial basis from 1 April 2019 and on mandatory basis from 1 July 2019
  - ITC in relation to invoices issued by the supplier during FY 2017-18 may be availed till the due date for furnishing of FORM GSTR-3B for the month of March, 2019, subject to specified conditions.
  - The due date for furnishing the annual returns in FORM GSTR-9, FORM GSTR-9A and reconciliation statement in FORM GSTR-9C for the Financial Year 2017 – 2018 shall be further extended till 30 June 2019
  - Certain clarifications in relation to the scope of disclosures in Form GSTR-9 and GSTR-9C would be issued; inter-alia including disclosures would need to be made for the transactions made during the year and not only those disclosed in the returns filed, HSN code for inward supplies would only need to be disclosed for those whose value independently accounts for 10% or more of the total value of inward supplies, etc.
  - The due date for submitting FORM GST ITC-04 for the period July 2017 to December 2018 shall be extended till 31 March 2019
  - Extension of Form GST RFD -01A for refunds to be filed for excess payment of tax, tax paid as intra-state but subsequently held to be inter-state or any other refund
  - Changes made by CGST (Amendment) Act, 2018, IGST (Amendment) Act, 2018, UTGST (Amendment) Act, 2018 and GST (Compensation to States) Amendment Act, 2018 and the corresponding changes in SGST Acts would be notified with effect from 1 February 2019
- Legislative changes proposed:
  - Creation of a Centralized Appellate Authority for Advance Ruling for cases where there are conflicting Rulings by two or more State Appellate Authorities of Advance Ruling
  - Interest to be charged only on the net tax liability of the taxpayer ie, after taking into account the admissible ITC

Circular No. 01/2019-Customs dated 2 January 2019 issued by CBIC

CBIC vide this circular has given clarifications regarding failure of refund of IGST on exports. Following are the summarised reasons and their respective clarifications regarding the issue of delay in IGST refund claims:

- Non filing or late filing of Online Local and Gateway EGM

  This is with the regard to the instances of non-filing or late filing of local EGM and reaching of cargo at gateway port without filing of local EGM. And hence it has been instructed, by CBIC, that the custodians / carriers / shipping lines operating at ICDs/ Gateway ports should file EGM online.

  As per Section 41 of The Customs Act, the customs officer is authorised to take action against the non-filers of EGM. In this regard it has been clarified that penal provisions may not be invoked for EGMs filed till 31st January, 2019.
  However, continued non-compliance beyond 1st February, 2019 may be dealt strictly by taking recourse to penal provisions in accordance with the law.

- Mismatch in Local EGM and Gateway EGM:

  In relation to the hindrances in gathering information with regard to LCL cargo from Shipping lines and Custodians. In this regard, Circular No. 55/2000-Customs dated 30.06.2000 has provided that the custodian of the gateway port or CFS near gateway port is required to maintain a tally sheet container-wise, giving details of the export consignments, the previous Container No., Shipping Bill No., AR-4 No. and the details of new container in which goods have been re-stuffed.

  Further, the concerned shipping line would issue the Bill of Lading, a copy of which would be handed over to the custodian, and the other transference copy would be returned to the originating ICD/CFS.

- Non-filing of stuffing report by the Preventive officers at Gateway Ports for the LCL cargo being consolidated at the Gateway Ports/CFSs in the system

  In cases of mismatch in information in local and gateway EGMs, the preventive officer shall supervise de-stuffing and re-stuffing, so as to verify the details like number of package(s), quantity etc. and satisfy himself that there is no short shipment, replacement or diversion of cargo etc. Further the gateway port officer shall also verify the correctness of package(s) and container details for cargo coming from inland ICDs cargo immediately in ICES, using the Gateway EGM CTR Amendment option.

Circular No. 76/50/2018- GST dated 31 December 2018 issued by CBIC

Following are the clarifications given by CBIC vide this circular :

- Inclusion of TCS under Income Tax Act for GST valuation

  - It has been clarified that section 15(2) of CGST Act, 2017 specifies that the value of supply shall include "any taxes, duties cesses, fees and charges levied under any law for the time being in force other than this Act, the SGST Act, the UTGST Act and the GST (Compensation to States) Act, if charged separately by the supplier."

  - Hence, the taxable value for the purposes of GST shall include the TCS collected under the provisions of the Income Tax Act, 1961, since the value to be paid to the supplier by the buyer is inclusive of the said TCS.

  - Key takeaways with respect to TCS clarification:

    - The clarification appears to have adopted a narrow interpretation to the meaning of the phrase "any taxes, duties cesses, fees and charges levied under any law for the time being in force other than this Act, the SGST Act, the UTGST Act and the GST (Compensation to States) Act, if charged separately by the supplier."

    - The clarification declines to consider a possible position that TCS is merely a mechanism for collection of taxes and not a tax in itself.

- GST rate on debit/ credit notes issued with respect to original supplies under pre-GST regime

  - This is with regard to issuance of a supplementary invoice or debit/ credit note in case of revision of prices of any goods or services or both on or after the appointed day (i.e., 01.07.2017) – the said supplementary invoice or debit/ credit note is deemed to have been issued in respect of an outward supply made under the CGST Act [as per the provisions of section 142(2) of the CGST Act].

  - In this regard it is accordingly clarified that the GST rate for such supplementary invoice or debit/ credit note shall be as per the provisions of the GST Acts (both CGST and SGST or IGST) would be applicable.

  - The said clarification may cause practical issues with respect to credit note

adjustments on account of difference in pre and post GST rates.

- Penalty for delayed filing of Form 3B return

  - Section 73(11) of the CGST Act provides that penalty is payable in case self-assessed tax or any amount collected as tax has not been paid within a period of 30 days from the due date of payment of such tax.

  - However, the said penalty shall generally not be applicable in cases where filing of return in FORM GSTR-3B is delayed because tax along with applicable interest has already been paid, however, after the due date for payment of such tax.

  - It is further clarified that a general penalty under section 125 of the CGST may be levied since the tax has been paid late in contravention of the provisions of the CGST Act.

- Other aspects clarified by the circular

  - Sales by Government of seized assets (Government to register where such sale is made to unregistered persons);

  - Scope of what constitutes "Governmental Authority" for TDS purpose; and

  - Determination of owner of goods under the CGST Act.

Notification No. 74/ 2018 -GST dated December 31, 2018 issued by CBIC

CBIC has prescribed the revised formats for Annual Return in Form GSTR 9 / 9A and Reconciliation Statement in Form GSTR 9C. Some of the key changes made has been summarized hereunder for ease of reference:

- Amendment of headings in the Form GSTR-9 to specify that the return would be in respect of supplies etc. 'made during the year' and not 'as declared in returns filed during the year';

- All returns in Form GSTR-1 and Form GSTR-3B have to be filed before filing of Form GSTR-9 and Form GSTR-9C;

- Additional liability for the FY 2017-18 not declared in Form GSTR-1 and Form GSTR-3B may be declared in Form GSTR-9;

- Input tax credit unclaimed during FY 2017-18 cannot be claimed through Form GSTR-9;

- Value of "non-GST supply" shall also include the value of "no supply" and may be reported in Table 5D, 5E and 5F of Form GSTR-9;

- HSN code may be declared only for those inward supplies which in value independently account for 10 % or more of the total value of inward supplies in Form GSTR-9;

- Additional payments, if any, required to be paid in Form GSTR-9 can be done through Form GST DRC-03 only in cash. Thus, the Input Tax Credit balance cannot be utilised for payment of additional liability;

- Verification by taxpayer who is uploading reconciliation statement has been included in Form GSTR-9C.

Order No. 2/2018 - Central Tax dated December 31, 2018 issued by CBIC

Vide the above Order, the CBIC has made the following amendments in Section 16(4) and Section 37(3) of CGST Act, 2017:

- Rectification of error / omission in respect of Form GSTR-1 for the FY 2017-18 shall be allowed till the due date of furnishing of Form GSTR-1 for the month of March 2019 i.e. April 11, 2019;

- Input Tax Credit in respect of invoices or debit notes in relation to such invoices raised during FY 2017-18 can be claimed till the due date of furnishing Form GSTR 3B for the month of March 2019 i.e. April 20, 2018. However, it is mandatory that the supplier should have furnished the details of such invoices in the Firm GSTR-1 filed by such supplier till the due date of filing Form GSTR-1 for the month of March 2019 i.e. April 11, 2019.

Press Release dated October 18, 2018 implied that assesses can avail the Input Tax Credit on self-assessment basis and the facility to view the details of outward supplies furnished by the supplier in FORM GSTR-2A is in the nature of taxpayer facilitation. Basis the above amendment, it appears that the taxpayer is required to reconcile the Input Tax Credit to be claimed in Form GSTR-3B with auto-populated GSTR-2A and only in cases where the details have been furnished by the supplier within the above timeline, the credit thereof may be available to the recipient. This aspect requires detailed evaluation and possibly a specific tax position being adopted.

Order No. 3/2018 - Central Tax dated December 31, 2018 issued by CBIC

CBIC has extended the due date for filing of the Annual Return in Form GSTR-9 / GSTR -9A (as the case may be) and Reconciliation Statement in Form GSTR 9C till 30 June 2019.

Direct Tax

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

Key Direct Tax Developments

1. Delhi High Court upholds PE for multiple companies of a multinational group due to sales and marketing activities in India

Background

- The taxpayer, a company resident of USA (US Co.1) and part of the GE Group, was engaged in the business of manufacture and sale of highly sophisticated equipment to customers all over the world, including India.

- US Co.1 sells its products offshore on a principal to principal basis to customers all over the world, including to customers located in India, whereby the title to the goods sold to Indian customers passes from it outside India.

- One of the entities of the group, also a resident of USA (US Co.2), has set up a liaison office (LO) in India to carry out liaison activities i.e. to act as a communication channel and not carry on any business activity.

- These assessees contended that employees are deputed to various GE companies and they work as their employees and they remain on the payroll of US CO. 2 till their transfer to other entities.

- Further, the GE Group had an Indian entity, GE India (or I Co), which is party to the Global Service Agreement (GSA) with US CO. 2, for providing limited market support services to GE and its affiliates (including US Co. 1.). In exchange, it was remunerated on a cost-plus basis. It was assessed to income tax and also subjected to arms' length price (ALP) determination by a Transfer Pricing Officer (hereafter "TPO") who held that the transaction with its associated enterprise (AE) was at arm's length.
  The GSA forbids I CO. from:
  a) entering into any contract on behalf of GE Group companies (US CO. 2 and affiliates);
  b) from acting as an agent for any GE Group company (US CO. 2 and affiliates).

- Various expatriate employees of GE Companies outside India (collectively referred to as “GE Overseas companies”) worked in India along with employees of I Co. to support various businesses of GE overseas companies (the support team).

- A survey was conducted at the premises of LO to scrutinize and inspect documents and records and statement of the expatriates deputed to the Indian companies were recorded.

- Based on the information collected during the survey, as well as subsequent information collected by the tax authority, following facts were noted:

  - Various expatriates of GE overseas companies were working in India from premises of LO
  - Expatriates worked in leadership roles in India along with support team of the employees of I Co to look after business and sales of the GE Group as a whole in India.
  - Expatriates and support team carried out core sale activities in India and were not merely acting as communication channel.
  - Specific rooms/chambers in the LO were allotted to the expatriates at the premises of the LO.

- Basis the above facts, the Tax authority held that the GE overseas companies had a fixed place PE at the premises of LO and an agency PE in India due to the activities of the expatriates and I Co (through its employees) under the DTAA.

- In the absence of any year-wise-entity-wise profits, the tax authority deemed 10% of the value of supplies made to the clients in India as the profits arising from such supplies and attributed 35% of such profit to the Taxpayer's PE in India.

Taxpayer’s arguments

- The Taxpayer submitted that the all strategy decisions reside with the Company outside India – work in India is only limited to providing market inputs and interface as the LO is only collecting information about potential customers in India and passing on this information to its non-resident businesses; and creating awareness of the business products, which is a small part of the overall business of research and development, design, fabrication and manufacture, all of which happened outside India. The activities carried in India are merely preparatory or auxilliary (PoA) in nature.

- Further, the Taxpayer submitted that mere participation in negotiations or even negotiation of some terms of the contract by employees of non-resident tax payer does not result in a PE unless all

terms of the contract are negotiated and finalized by such employees.

Tribunal's conclusion

On Fixed place PE

- Specific rooms were allotted to the expatriates in the LO premises which were constantly used by the expatriates to carry on the activities on behalf of the GE overseas companies.
- The support team of I Co. were also present at the LO Premises and worked under the control and supervision of the expatriates, who in turn worked for GE overseas entities.
- The expatriates were highly qualified and were working at senior positions in the GE group. They were managing the business, securing orders and doing everything possible that could be done regarding the Indian operations of GE overseas companies in India.
- Documentary evidence indicated that core sales activities of finding the customers and finalizing the deals with them including the pre-sale and post sales activities were done by the expatriates and support team in India from premises of the LO. Such activities being core activities does not qualify as PoA in nature. Hence the LO premises constituted a fixed place PE in India.

On Dependent Agent PE (DAPE)

- Expatriates along with support team were working not for a single entity but for the GE overseas group companies who were related to each other and, hence they qualify as dependent agents.
- Constitution of DAPE does not require negotiating all elements and details of a contract. Further, lack of active involvement by an enterprise in transactions may be indicative of grant of authority to agent.
- As expatriates carried on core sales activities in India, which do not qualify as PoA activities, it resulted in DAPE for all GE overseas companies in Inida.

Attribution of profits

- The ITAT observed that the AO was correct in its approach in estimating total income at 10% of sales made in India. It, however, reduced the extent of profit attribution to PE to 26% of profits, instead of 35% estimated by the AO.

Question of Law Framed before the High Court

The High Court addressed the following matters:

(1) Existence of Fixed place PE

(2) Existence of DAPE; and,

(3) Attribution of profits to PE

Delhi High Court Ruling

a) Fixed Place PE

- ***Disposal test:*** The LO premises were at the constant disposal of US CO. 2 and was used by GE staff for their work as specific rooms/chambers were allotted to the expatriates.
- Relying on the OECD commentary and various Supreme Court judgements, HC held that the term 'place of business' is understood as any premises, facilities or installations used for carrying on the business of the enterprise.
- Moreover, having space at disposal did not require a legal right to use that place – mere continuous usage was sufficient if it indicated being at disposal.
- ***Business Activity test:*** The process adopted by GE for business development was divided into four steps namely: Stage 1-Pre-qualification; Stage 2-Bid/no bid and Proposal development; Stage 3-Bid approval and negotiations; and Stage 4-Final contract development and approval. HC opined that the process of sales and marketing of GE's product through its various group companies, was not simple. Entering into contract with stakeholders (mainly service providers in these segments) involved a complex matrix of technical specifications, commercial terms, financial terms and other policies of GE. Thereby, to address these, GE had stationed several employees and officials at high and middle ranks in India.
- The employees explored commercial opportunities, undertook business development, approached customers to communicate the available options and undertook intensive negotiations in relation to the technical and commercial parameters like consideration payable, warranty etc. These are "core activities" undertaken in India.
- The discharge if vital responsibilities and prominent involvement in the contract finalization process, revealed that GE group carries on business through the LO in India.
- **Preparatory or Auxiliary exemption**: The "core activity" of developing the customer (identifying a client), approaching that customer, communicating the

available options, discussing technical and financial terms of the agreement, even price negotiations, needed a collaborative process in which the potential client along with I. Co.'s employees and its experts, had to intensely negotiate the intricacies of the technical and commercial parameters of the articles.

- This also involved discussing the contractual terms and the associated consideration payable, the warranty and other commercial terms.

- Although, at later stages of contract negotiations, the India office could not take a final decision, but had to await the final word from headquarters. But that did not mean that the India office was just for mere data collection and information dissemination.

- Significant and essential part of the sales activity was undertaken in India. Such activities in India are not PoA in nature.

b) Agency PE

- HC accepted ITAT's conclusion that as long as the activities of the agent in concluding contracts is not auxiliary, and at the same time, does not require concluding every single element of the contract. Therefore, GE India's activities clearly constitute activities that would establish agency PE in India.

- Also, the I Co. comprising expatriates and support team were not working for a particular enterprise, but, for multiple enterprises dealing in major businesses of GE group. Accordingly I Co. qualifies as a dependent agent of the GE overseas companies.

- The nature of activities carried by I Co., clearly indicated its authority to conclude contracts on behalf of GE Overseas, which signified that I Co. constituted agency PE for all the GE Overseas entities in India.

c) Attribution of profits to PE

- The Court noted that the analysis carried out by the Revenue i.e. not merely by the ITAT but also by the AO in the assessment order, was after considering the relevant decisions.

- Thus, the Court affirms the 26% attribution made by the Tribunal in this regard.

Source: TS-765-HC-2018(DEL)

2. Delhi Tribunal rules professional fees paid to foreign affiliates non-taxable; 'Independent Personal Services' Article applicable to LLP

Background and facts

- The taxpayer is a partnership firm providing international accountancy and advisory services to various clients in India and abroad.

- Notice was issued to the taxpayer u/s 143(2) and in the scrutiny proceedings, AO identified payment of professional fee to non-resident firms on which TDS was not deducted.

- The services from non-resident firms were obtained to render services to foreign clients of the taxpayer outside India.

- Taxpayer contended that professional fees was paid for services rendered outside India and same is covered under Article 15 "Independent Personal Services" (IPS) of respective DTAA. Since there is no fixed base in India, thus no withholding tax obligation arises u/s 195 and hence, no disallowance us 40(a)(i) is required under the Income Tax Act "The Act".

- The AO contended that article 15 of the respective DTAAs is applicable to an individual and in the instant case, the parties are Limited Liability Partnerships (LLP) and thus, not covered by Article 15. According to AO, the services are technical in nature and thus are covered u/s 9(i)(vii) of the Act (deemed to accrue/arise in India). The AO disallowed the expenses u/s 40(a)(i).

- The CIT(A) analyzed the provisions of Article 15 (IPS) and concluded that income derived by an individual/ partnership firm by rendering professional services is taxable in the country of residence. Also, on examination of provisions of Article 13 (Fee for technical services), CIT(A) concluded that no technical knowledge was being made available and thus, in view of "make available clause in DTAAs, payments were not in nature of Fee for Technical services (FTS).

- Accordingly, CIT(A) deleted the disallowance made by the AO and held that taxpayer was not liable to deduct TDS u/s 195.

- The Revenue filed an appeal against the order of CIT(A).

CIT(A)'s submissions

- If DTAA of UK is considered for illustration, income of a UK firm for rendering professional services in UK will be taxable in UK. However, such income may also be taxable in India if the individual or any partner of

the professional firm is present in India up to 90 days in a previous year or the person / firm has a fixed base regularly available to him / it in India for performing his / its activities.

- However, in this case, none of the members / employees of foreign entities came to India.
- There is no fixed base or office or permanent establishment (PE) of the said non-resident LLP in India. Therefore, in the absence of a PE / fixed base of the recipient (i.e., non-resident LLP) in India and on account of the fact that no one from the said firm had even a single day stay in India, professional fees for rendering services in the foreign country will be taxable only in foreign country and not in India.
- In the case of DTAAs with USA, UK and France, it is unambiguously written in the said Article on "Independent Personal Services" itself that it is applicable on Income derived by a person who is an individual or firm of individuals; or by an individual, whether in his own capacity or as a member of a partnership; or by an individual or partnership of individuals.
- In the case of Netherlands, the word 'resident' is used in Article 14 on 'Independent Personal Services', and it has been explained by Clause 1 of Article 4 of the said DTAA as: "For the purposes of this Convention, the term 'resident of one of the States' means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature." Further, 'person' has been defined by Clause 1(e) as: "the term 'person' includes an individual, a company, any other body of persons and any other entity which is treated as a taxable unit, under the taxation laws in force in the respective States."
- Thus, even in this case, Article 14 on 'Independent Personal Services' is definitely applicable on the income derived by a partnership firm or an LLP
- Moreover, in each of these DTAAs the term "professional services" includes the independent activities of 'lawyers' and 'accountants' amongst other such professional. The appellant is undisputedly engaged in rendering accounting and advisory services of international standards to various clients in India and abroad.
- Therefore, it cannot be doubted that the impugned professional fees paid are squarely covered by the provisions of Article on "Independent Personal Services" of the said DTAAs.
- As per Article 13 of the DTAAs, rendering of technical/consultancy service includes making available of technical knowledge, experience or skill in Indiaor development or transfer of a technical plan or technical design.
- However, in the said case, "make available" condition is not satisfied.

Tribunal's Ruling

- In the DTAA with Netherland, the word resident has been used for the benefit of independent personal services, which is wider than individual and the firm, who has rendered services is entitled to benefit of said provision. Thus, there is no error in order of CIT(A) in this regard.
- In absence of not making available, the technical knowledge to the assessee, in view of the Article 13 of the respective DTAAs, the payment for services cannot be held as fee for technical services under the provisions of the respective DTAAs. Hence CIT(A) has not erred in its order in this regard
- CIT(A) has further observed that Article 13 of DTAAs provisions defining Fee for Technical Services being more favourable to the assessee as compared to the provisions of section 9(1)(vii) of the Act which has defined Fee for Technical Services, and thus the assessee was having option of choosing more favourable provisions of the DTAAs.
- Based on the above, the order of CIT(A) has been upheld by the Tribunal.

Source: TS-10-ITAT-2019(DEL)

Regulatory

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

Key Regulatory Amendments

1. **Press Notes issued by Department of Industrial Policy and Promotion (DIPP)**

Review of foreign direct investment (FDI) policy in e-commerce sector

- DIPP in order to provide clarity on FDI in the e-commerce sector had issued Press Note No. 3 (2016 series) formulating guidelines in relation to e-commerce sector.
- Now, DIPP has issued Press Note 2 of 2018 (PN2) reviewing the guidelines on FDI policy in e-commerce sector.
- The key changes brought *vide* PN2 are provided as under:

Restriction on e-commerce marketplace entity:

- E-commerce marketplace entity or its group companies, having equity participation, or control on inventory of an e-commerce marketplace, will not be permitted to sell its products on the platforms run by such e-commerce marketplace entity.
- Seller shall not be mandated by the e-commerce marketplace entity to sell its products exclusively on its platform.
- FDI in inventory based model of e-commerce amounting to multi-brand retail trading is prohibited.
- **Control over inventory**: Along with the ownership criteria, the PN2 has also provided that E-commerce marketplace entity will not exercise control over the inventory i.e. goods purported to be sold and such an ownership or control over the inventory will render the business into inventory based model, in which FDI is not permitted. DIPP has also clarified that if more than 25% of the purchases of a vendor, are from the marketplace entity or its group companies, then e-commerce entity will be deemed to be having control over the inventory of such vendor.
- **Services by e-commerce marketplace entity**: Services to be provided by e-commerce marketplace entity or other entities in which e-commerce marketplace entity has direct or indirect equity participation or common control, to vendors, should be at arm's length and in a fair and non-discriminatory manner. Even Cash back provided by group entities of such e-commerce marketplace entity to buyers shall be fair and non-discriminatory. In this regard, it may be noted that for provision of services to any vendor on such terms which are not made available to other vendors in similar circumstances will be deemed to unfair and discriminatory.
- **Specific reporting requirement**: E-commerce marketplace entity will be required to furnish a certificate along with a report of statutory auditor to the Reserve Bank of India (RBI) by 30th September every year confirming compliance of the FDI guidelines.
- The aforementioned proposed changes would be effective from 01 February 2019.
- Further, DIPP has responded to comments reported in the media on the e-commerce policy and has provided clarification on certain matters
- The key clarifications are provided as below:
- The Press note was issued to ensure better implementation of the policy in letter and spirit and to ensure that rules are not circumvented directly or indirectly;
- It is reiterated that FDI in inventory based model of e-commerce amount to multi-brand retail trading, which is prohibited;
- It is clarified that policy does not impose any restriction on the nature of products which can be sold on marketplace; and
- The e-commerce guidelines issued *vide* PN2 are applicable to entities operating in marketplace and do not extend to other trading companies such as companies operating through e-commerce in respect of food products retailing of Indian manufactured and/ or produced items.

Source: Press Note No. 2 (2018 Series) dated 26 December 2018; Response to comments reported in the media on Press Note 2 (2018)" issued by DIPP dated 03 January 2019

2. **Defence items list vide Press Note No. 1 (2019 Series)**

- DIPP *vide* Press Note No. 1 (2019 Series) (PN1) has segregated the list of defence items requiring compulsory license into two categories in consultation with Department of Defence Production (DoDP) and Ministry of Home Affairs (MHA). The key changes are provided as under:

a. List of defence items requiring compulsory license is divided into two categories, as follows:

b. List of defence items requiring Industrial License under Industries (Development and Regulations) Act, 1951 (IRDA).

c. List of defence items requiring license for manufacturing and/ or proof testing of arms and ammunitions.

Source: Press Note No. 1 (2019 Series) dated 01 January 2019

Notifications/ circulars issued by RBI

1. Liberalisation of External Commercial Borrowing (ECB) framework

RBI has liberalized the ECB policy framework with respect to availing of ECB. The key changes are provided as under:

a. Division of tracks into two categories basis the currency in which the ECB is raised, instead of 3 tracks earlier. Two categories are as under:

- Foreign Currency Denominated ECB (merging of Tracks I and Track II as provided in the erstwhile regime);
- Rupee Denominated ECB (merging of Track III and Rupee Denominated Bonds as provided in the erstwhile regime)

b. Eligible borrowers:.

- All the entities which are eligible to receive FDI are eligible borrowers to avail ECB. Therefore, given that LLPs, service/trading sector entities, etc. are eligible to raise FDI, it should now be eligible to avail ECB as well.
- Port trusts, units in SEZ, SIDBI, EXIM bank, registered entities engaged in micro finance activities viz. registered societies/trusts/cooperatives and NGO's are also permitted.

c. End uses:

- End use restrictions are revised as under:
  - i. business of chit fund or Nidhi Company;
  - ii. investment in capital market including margin trading and derivatives;
  - iii. agricultural or plantation activities;
  - iv. real estate activity* or construction of farm houses; and
  - v. trading in Transferrable Development Rights (TDR).
- ECB raised is allowed to be used for working capital, general corporate purposes and repayment of rupee loans provided raised from foreign equity holder.
- Also, purchase of land for self-use is permitted.

d. Eligible Lender: Lender should be a resident of Financial Action Task Force (FATF) or International organisation of Securities commissions (IOSC) compliant country.

e. Minimum Average Maturity (MAM) period: It will be 3 years for all ECB's irrespective of the amount except for:

- ECB up to 50 million in the manufacturing sector – 1 year
- ECB from foreign equity holder and utilised for specific purposes – 5 years

f. Amendment in relation to Trade credit (import of goods)

- Trade credit for import of capital or non- capital goods- limit changed from US$ 20 million to US$ 50 million;
- Trade credit can now be availed in Indian rupees;
- Trade credit can be availed for import of capital goods for max period of three years (as against 5 years earlier);
- Trade credit permissible within SEZ.

g. Further, it has been clarified that hybrid instruments such as optionally convertible debentures (presently covered under ECB framework) will be governed by a separate hybrid instrument guidelines to be notified by the Government.

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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