NEWS CRUNCH

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DIRECT TAX

1. Capital Gains arising from indirect transfer of shares of a foreign company by another foreign company on account of internal group restructuring held to be taxable in India

Assessee is a non-resident company incorporated under tax laws of UK and is a tax resident of the. Assessee held 100% shares of another foreign group holding company, namely Cairn India Holdings Ltd. ("CIHL"), incorporated in the Jersey. CIHL in turn held shares in various operating subsidiaries holding Indian assets.

Assessee also held 100% share capital an Indian company, namely Cairn India Limited ("CIL"). During Financial Year 2006-07, as a part of group re-organization and re-structuring, it was decided that holding of all Indian operating assets be consolidated under CIL, which was also going for Initial Public Offering ("IPO") and listing of its shares on Indian recognized stock exchanges.

Accordingly, during October-December 2006, 100% of shares held by Assessee in CIHL were transferred to its Indian subsidiary CIL in different tranches. It is important to note that in this transfer, 75.69% of shares of CIHL were transferred by Asssessee to CIL by way of a share-swap (i.e. shares of CIL issued by Assessee for transfer of shares in CIHL by Assessee to CIL) and only 24.31% of shares of CIHL were transferred by Assessee to CIL for cash consideration.

In January 2014, survey was conducted by Income tax department at office premises of CIL and based on copies of share transfer agreements and other documents received by Income tax authorities in course of survey, the Assessing Officer initiated assessment proceedings u/s 147 of the Act in case of Assessee alleging its income from transfer of shares of CIHL to CIL to have escaped income tax.

Subsequently, the Assessing Officer passed assessment order determining total income of Assessee at Rs. 24,503 crores taxable as short-term capital gain arising from transfer of 100% shares in CIHL to CIL in different tranches for alleged total sale consideration of Rs. 26,681 crores, chargeable to tax in the hands of appellant taxable at the rate of 40%. While computing this amount of capital gains, Assessing Officer considered both cash as well as non-cash (i.e. shares of CIL) considerations received by Assessee for transfer of shares of CIHL. Assessment order was confirmed by DRP *in toto* and subsequently, Assessee filed appeal before Income Tax Appellate Tribunal, Delhi ("Tribunal").

<u>Assessee's Arguments before Tribunal:</u>

- Gains, if any, arising to the non-resident Assessee on account of transfer of shares of another foreign company can not be deemed to accrue or arise in India under section 9 (1) (i) of the act and is thus, not chargeable to tax in India. It was claimed by Assessee that retrospective amendment to section 9 (1)(i) of the Income Tax Act subjecting "Indirect transfers" to income tax in India by Finance Act, 2012 is bad in law and ultra vires.

- On date of transfer of shares in question, the retrospective amendment to section 9 made by the Finance Act 2012 was not in existence and therefore, since Assessee is eligible for benefit of India-UK DTAA, domestic tax law is required to be read ignoring the retrospective amendment made by The Finance Act, 2012.

- Transfer of shares of CIHL by Assessee to CIL is an internal reorganization of group, as there is no change in controlling interest as a result of these internal reorganization from one group entity to another group entity and therefore there is no real income accruing to the Assessee, which could be taxed.

- Substantial portion of the transfer is for non-cash consideration, i.e. issuance of shares of CIL to Assessee for transfer of shares of CIHL and therefore the same can not be said to be real income in hands of Assessee

- Without prejudice the above, methodology of computation of capital gains by Assessing Officer was also questioned by Assessee and it was claimed that while computation of capital gain in the hands of the assessee is made, the cost of acquisition should be stepped up to the fair value of the shares of CIHL on the date of acquisition by Assessee.

Tribunal's Decision:

- Tribunal is not the right forum to decide constitutional validity of provisions of Income tax Act, thus Assessee's argument challenging validity of retrospective amendment to Section 9(1)(i) of the Act subjecting "Indirect transfers" as bad in law and 'ultra vires', rejected by Tribunal

- Tribunal also rejected "no real income" and "internal re-organisation" argument of Appellant holding that substantial value in shares of CIL (as acquired by Assessee as consideration for transfer of shares of CIHL) was unlocked by process of IPO and a portion of IPO proceeds was also paid by CIL to Assessee by way of cash consideration and thus it can not be said that there was no real increase in wealth of Assessee

- CIHL is holding company of subsidiary operating companies holding Indian assets and Assessee was holding company of CIHL. Therefore, it is apparent that Assessee is holding rights in control and management of the shares of the 9 Indian subsidiary companies engaged in business of Indian oil and gas sector.

- The complete financial arrangement of group has been completed through series of transfer of shares from UK Jurisdictions to Jersey Jurisdiction to India. On divesting 30 % stake in the oil and gas assets located in India certain amount was paid to the assessee in UK. Therefore, it cannot be concluded that these series of transactions entered in to by the group is merely a business reorganization process in consolidation of its oil and gas business India.

- Tribunal said that there is no difference between the full value of the consideration determined by the both the parties received accruing to the assessee as a result of the transfer of the capital asset. As there is no difference between the full value of consideration taken by revenue as well as the assessee, there is no reason to go in to the controversy whether the transaction is of exchange or sale.

- Assessee claim that as there is no timing difference between the acquisition and disposal of shares, the full value of consideration and the cost of acquisition is same, rejected by the Tribunal, holding that provisions of section 48, 49 and 55(2) do not allow such treatment.

- Assessee's reliance on Supreme Court decision in case of Vodafone International Holdings BV versus Union of India and another (341 ITR 1) (SC) also rejected by Tribunal in light of retrospective amendment in law.

- In respect of assessee's contention that if the assessee is eligible for the benefit of DTAA then the domestic tax law is required to be read ignoring the retrospective amendment made by The Finance Act, 2012. the tribunal rejected the argument of assessee for the reason that:

  - ✓ Provision in the DTAA cannot make the domestic law static with respect to taxability of a particular income when unequivocally both states have left it to the domestic laws of the countries.

  - ✓ Suppose if there is an exemption provided with retrospective effect under the domestic law can Non-resident assessee be also denied the benefit as it was also not the law at the time of notification of DTAA, the answer is in negative .

  - ✓ DTAA are mechanism of avoiding multiplicity of taxation globally of an assessee. Therefore, if in the country of residence taxes are chargeable then the assessee must not suffer the tax burden in the country of source of income.

NANGIA'S TAKE:

This decision again reinforces position of Income tax authorities for taxing gains from transfer of Indian assets (directly or indirectly) in India and Indian Tribunals/ Courts confirming such position. However, reopening past assessments taxing such gains based on retrospective amendment in law definitely brings confidence deficit in investors and foreign companies planning to invest in India and Indian government must take steps to avoid such cases.

Source: TS-89-ITAT-2017(DEL)]

2. Payment to Non-resident for employee secondment characterised as FTS, ITAT rejects salary-reimbursement plea

Background

1. Flughafen Zurich AG, incorporated and tax resident of Switzerland ("assessee"), was engaged in providing operations and management services to airport;
2. The assessee had made an Expatriate Remuneration Reimbursement agreement ((referred to as "agreement") with Bangalore International Airport Limited ("BIAL") for secondment of skill personnel. It filed return of income, declaring 'NIL' income, based on the principle that the seconded personnel were appointed to work exclusively for BIAL on full time and work under their direct control and supervision, thus the payment by the BIAL is for reimbursement of salary not Fees for Technical Services ("FTS");

3. The assessee contended that as per the agreement, the assessee shall not be held responsible for any act or omission of the seconded personnel during the assignment. The seconded personnel would be entitled to remuneration outside India in foreign currency in addition to sum directly paid by BIAL and the same amount has been reimbursed to the assessee by BIAL. The assessee further contended that since the seconded personnel satisfy the test of employee-employer relation and hence amounts received it from the BIAL is nothing but only a reimbursement of salary, therefore, not chargeable to tax in the hands of the assessee;

4. The assessee also contended that the definition of FTS as mentioned in the relevant Double Tax Avoidance Agreement ("DTAA") is different from definition of FTS under the Income tax Act, 1961 ("IT Act");

5. The Tax officer taxed the amount received by the assessee from BAIL as fees for technical services. The action of the tax officer was challenged by the assessee before the Dispute resolution panel. The Dispute resolution panel upheld the action of the tax officer, which was challenged by the assessee before the Hon'ble Tribunal.

Proceedings before the Tribunal

❖ The tax department contended that, the assessee was under an obligation to pay the personnel remuneration in foreign currency outside India even after secondment and the status and relationship between the assessee and seconded personnel has not ceased to exist.

❖ The tax department further submitted that the remuneration was to be first paid by assessee and then reimbursed by BAIL and all the seconded personnel are holding high managerial position in the management as CEO and CCO, which clearly establish the fact that they were not ordinary employees but having the expertise in the field of management therefore the payment for such services is in the ambit of Fees for Technical Services ('FTS').

6. Tribunal's findings: :

a) Tribunal was of the view that the secondees were under the employment of the assessee and therefore, not under an employment/recruitment by BIAL. Even if there is a restriction of the right to continue in the employment with the assessee the same would not prove that the relationship between the BIAL and the seconded personnel is employer and employee. The terms and conditions of the employment of the assignees with the assessee cannot determine the relationship between the personnel and the BIAL. Further even if the assignment tenure is relatively longer that would not amount to cessation of the existing employment of the personnel. [Principle laid down in the case of Deputy Commissioner of Income Tax vs. Centrica offshore Pvt. Ltd. (2016) 364 ITR 336 (Delhi High Court) relied upon]

b) The personnel were not ordinary employees but having the expertise, thus, the assignment is to avail the service of highly qualified and expertise personnel. The definition of FTS as per the first limb as provided under Section 9(1)(vii) of the IT Act as well as Article 12(4) of DTAA means payment to any kind in consideration for rendering of any managerial, technical or consultancy services and to that extent, the definition of Fees for Technical Services under IT Act as well as DTAA is identical. In this case, when the payment is considered for managerial service, then, it becomes irrelevant to go into second aspect of provision of service by technical or other personnel as used in Article 12(4) of the DTAA.

NANGIA'S TAKE

In the absence of any contrary ruling from any other High Court, other than the ruling of Hon'ble Delhi High Court in the case of Centrica Offshore, or Supreme Court, all such cases of payment towards secondment of employees are treated as FTS by tax authorities. We all will have to wait and watch how these matter are dealt with by the High Courts, if challenged by the tax payers.

3. India's Comprehensive Social Security Agreements with Germany and Portugal comes into force

The following are coming into force on May 2017:

a) Social Security Agreement between India and Germany (comprehensive) – with effect from 1 May 2017

The limited Social Security Agreement between India and Germany came into force on 1 October 2009. Now, a comprehensive Social Security Agreement with Germany, also covering totalization of benefits and export of benefits is coming into force. With the comprehensive Social Security Agreement coming into force, the limited Social Security Agreement with Germany will cease to have effect.

Employers who have assigned employees between India and Germany should take steps to claim applicable benefits under these Agreements. Employees assigned between India and Germany can continue claiming exemption from the host country social security scheme by availing a Certificate of Coverage from their home country. With the Comprehensive Agreement coming into force, the Indian / Germany authorities will consider the period of service in both countries to determine employees' eligibility for benefits. Also, the employees will have an option to claim benefit directly in their home country bank account

b) Social Security Agreement between India and Portugal – with effect from 8 May 2017

Employers who have assigned employees between India and Portugal should take steps to claim applicable benefits under these Agreements.

In particular, in respect of Portuguese employees on assignment to India, once the Agreement comes into force, the employers should begin the process of applying for Certificate of Coverage in Portugal and stop contributing to Indian social security. Also, on completion of Indian assignment, the employees should claim withdrawal / benefit from the Provident Fund Scheme and Pension Scheme.

Similarly, in respect of Indian employees on assignment to Portugal, the employers should obtain Certificate of Coverage in India and / or claim applicable benefits from Portugal social security once the Agreement comes into force.

4. Supreme Court rules payments made for use of common facility not fees for technical services

In the case of A.P. Moller Maersk the issue before the Supreme Court was whether income received from Indian agents for the use of global telecommunication facility can be classified as fees for technical services ('FTS') under the India-Denmark Tax Treaty ('Tax Treaty').

Background

A.P. Mollers Maersk AS, existing under the laws of Denmark and a resident of Denmark ("assessee"), was engaged in shipping operations in the international traffic at the global level. The assessee had agents working for it in India. The scope of work of the agents was to book cargo and also acting as clearing agents for the assessee. The assessee had set up and was maintaining a centralized global telecommunication facility across the globe (referred to as "Communication System") for helping its agents. The cost of the communication system was paid by agents on pro-rata basis, and hence it was claimed to be merely a cost sharing arrangement and in nature of reimbursement of expenses. The assessee contended that the amounts received from the agents for use of communication system were in the nature of reimbursements without any profit element.

Proceedings before Lower Authorities/Court

The Tax officer taxed the amount received by the assessee from its agents as FTS. The action of the tax officer was challenged by the assessee before the first appellate authority. The first appellant authority upheld the action of the tax officer, which was reversed by the second appellate authority. The tax department filed an appeal before the High Court of Bombay ("High Court") against the order passed by second appellate authority. The High Court confirmed the order of second appellate authority holding the nature of amount received by the assessee as reimbursement on the basis of the fact that it was not the case of the tax officer that the amount received by the assessee includes any markup. The tax department challenged the order of High Court before the Supreme Court.

Proceedings before Supreme Court

Relying on the case of Kotak Securities[1], supreme court observed that once it is accepted that the communication system facility provided by the assessee is an integral part of the business and that such facility enables the agents to discharge their role more effectively, by no stretch of imagination it can be treated as technical services. Also, the cost of this system has been borne by all the agents around the world on pro-rata basis and all the reimbursements were accepted as such, at arm's length.

NANGIA'S TAKE

For the first time before the Supreme Court, the tax department contested that, the amount received by the assessee from its agents could constitute royalty. This contention/argument of the tax department, being raised for the first time, was dismissed by Supreme Court at the threshold. The Supreme Court has reiterated well established principle that consideration for use of standard facility cannot be taxed as FTS. Also the Supreme Court has observed that once it is not disputed at the assessment level or before the first appellate authority that the amount was not reimbursement (i.e. it included profit element), the same can now not be contested.

Source: [TS-70-SC-2017]

[1]CIT vs. Kotak Securities Limited (2016) 383ITR1 (SC)

INTERNATIONAL TAX

5. Mauritian Regulator sets deadline for applications for Tax Residency Certificates ('TRC's) by newly-licensed Category 1 Global Business Companies ('GBC1')

Financial Services Commission ('FSC') had observed that newly licensed GBC1s do not submit their first application for a TRC as soon as they have been licensed but months after their licence date, which results in a situation where the GBC1s do not have a valid TRC starting from their licence date. FSC has stated that "Where first time applications for TRCs are received after three months of the licence date, the FSC Mauritius will recommend to the MRA to issue TRCs valid for a period of one year starting from the date the application has been received at the FSC Mauritius".

6. Singapore Budget 2017 proposes BEPS-compliant IP regime and R&D safe harbor

Singapore Budget 2017 presented today introduces new IP Regime called the 'IP Development Incentive' (IDI), which incorporates the BEPS-compliant modified nexus approach. It also proposes enhancement and extension of corporate income tax rebate as well as extension of the qualifying period for claiming exemption from withholding tax on payments made to non-resident non-individuals for structured products till March 31, 2017.

With a view to ease compliance, safe harbour rule has been introduced for payments under cost sharing agreements ('CSA') for R&D projects, wherein taxpayers may opt for claiming deduction towards 75% of the payments made under a CSA incurred for qualifying R&D projects. Encouraging the digital economy, Singapore budget recommends extension of withholding tax exemption on payments for international telecommunications submarine cable capacity to December 2023. On personal income tax front, it proposes tax rebate of 20% (capped at 500 dollars per taxpayer) to resident individual taxpayers.

7. European Union publishes Apple's appeal against European Commission (EC) ruling in the Apple-Ireland state aid case

EC had held that tax rulings issued by Irish Revenue in favor of Apple subsidiaries in Ireland conferred a 'selective advantage', and had ordered Irish Government to recover 13 billion Euros from Apple in taxes plus interest. Apple's 14 pleas of law, inter alia, allege that the EC erred in its interpretation of Irish law and made fundamental errors relating to the activities of Apple subsidiaries in and outside of Ireland. Apple has also claimed that arm's length price does not operate as the test for State aid in tax assessments, and there was no 'selective' treatment afforded by the Irish Revenue. Relying on its 14 grounds, Apple has sought annulment of the EC decision from the Court, or alternatively, annulment in part and ordering EC to pay the applicants' costs.

TRANSFER PRICING

8. The ITAT affirmed the need of attributing profits to Permanent Establishment if its actual functions performed falls beyond the scope of functions outlined in inter-company agreement

Facts of the case

SIS Live ["the taxpayer"], is a non-resident partnership firm based in the UK. The taxpayer came into existence through two partners, namely, Satellite Information Services Ltd. (70%) and SIS OB Ltd. (30%), for the purpose of carrying out a contract for Common Wealth Games, 2010, New Delhi. During the assessment year under review, the taxpayer neither reported any international transaction nor filed Form 3CEB in this regard. During course of assessment proceedings, the taxpayer admitted to have few international transactions owing to which the Assessing authority ["AO"] referred the taxpayer's case to the Transfer Pricing Officer ["TPO"]. The TPO recomputed the Arm length price ["ALP"] of the taxpayer's international transactions [pertaining to of technical service, reimbursement of expenses and hiring of equipment] at Nil and made addition on interest chargeable from inter-company loan. Consequently, the AO passed its draft order including TP adjustment amounting to INR 136 crore.

The taxpayer challenged the action of the TPO before Dispute Resolution Panel who allowed certain reliefs from additions proposed in the draft order of AO & computed total income of the taxpayer at INR 33 Crores. The aggrieved taxpayer filed appeal before the Income Tax Appellant Tribunal ["the ITAT"/ "the Tribunal"]. The appeal was first decided by the ITAT in its order dated 2.12.2015 wherein the Tribunal declined to adjudicate TP issue as no addition had been made by AO in final assessment order. On appeal by Revenue before the High Court ["HC"], the HC noted that prior to the date of passing order by the ITAT, the AO had already passed a rectification order under section 154 of the Income-tax Act, 1961 ["the Act"] incorporating TP adjustment in the final assessment order. Consequent to the same, the HC remanded the appeal back to the Tribunal. Thus, the TP grounds reached ITAT stage in second round of litigation.

Taxpayer's Contentions before the Tribunal

Owing to the fact that the taxpayer followed cash basis of accounting, the taxpayer neither paid nor received any sum of money in relation to its international transactions with its associated enterprises ["AEs"]. Accordingly, the taxpayer was of the view its transactions with its AEs did not impacted the taxpayer's profit and loss account in any manner and hence, such transactions do not fall within the definition of "international transactions" as provided under section 92B of the Act. Thus, the taxpayer is not subject to Indian TP regulations. In the light of the same, reference made to the TPO was bad in law and void ab-initio.

The Tribunal's Verdict

The Tribunal referred provisions of Section 92B of the Act [along with retrospective amendment made therein vide Finance Act 2012] and held that:

S. No.	International Transactions	Falls within following category of 'international transaction'	Remarks by the Tribunal
1	**Provision of technical services**	**Provision of services**	**In absence of necessary skills with AEs, the taxpayer provided such services**
2	Reimbursement of expenses		it is not required that such transaction should affect the profitability of the taxpayer
3	Availing of equipment on hire	Purchase, sale or lease of tangible or intangible property	Irrespective of the transaction's impact on taxpayer's profitability
4	Advancement of interest free loan	Lending or borrowing money	Irrespective whether the taxpayer has charged any interest or not

The Tribunal held clearly that following either cash or mercantile basis of accounting cannot be a deciding factor whether the taxpayer's related party transactions falls within the definition of 'international transactions'. In the light of the same, the Tribunal dismissed the taxpayer's grounds of appeal.

NANGIA'S TAKE

It is for the first time, the Tribunal has made its observations with regard to the applicability of Indian TP provisions in the light of method of accounting adopted by a taxpayer while reporting transactions with its AEs. The ITAT has clearly stated that the applicability of provisions of Chapter X of the Act is irrespective of the following:

- ✓ ***Method of accounting followed by the taxpayer; and***
- ✓ ***Impact of transactions with AEs on the profitability of the taxpayer***

Source: SIS Live Vs. ACIT [TS-149-ITAT-2017(DEL)-TP]

9. Once the Tribunal adjudicates a matter on merits of the case then any rectification application to re-evaluate the facts of the case by the Tribunal is not sustainable

Facts of the case

Abott Medical Optics Private Limited ["the taxpayer"] is engaged in the distribution of goods imported from its associated enterprise ["AE"]. During assessment year under consideration, the taxpayer adopted resale price method ["RPM"] to benchmark the transaction. In course of the taxpayer's assessment proceedings, the Transfer Pricing Officer rejected the RPM and proposed Transactional Net Margin Method ["TNMM"] as the most appropriate method ["MAM"]. This was further upheld by the lower level appellate authority and by Income Tax Appellant Tribunal ["the ITAT"/"the Tribunal"] subsequently.

Aggrieved with the order to the Tribunal, the taxpayer filed a rectification application by way of a miscellaneous petition before the Tribunal stating that the Tribunal, in its original order, has not considered the precedent in relation to the selection of MAM decided in the taxpayer's own case for preceding assessment year.

The Tribunal's Verdict on the Taxpayer's Miscellaneous Petition

The ITAT observed difference in the merits of the case for the assessment year under review vis-à-vis the previous assessment year. The Tribunal noted that the facts pertaining to the existence of huge selling/ sales promotion and distribution expenses in case of the taxpayer in comparison to comparable companies were duly taken into consideration by the ITAT in its original order. The Tribunal further observed such a scenario did not exist in case of the taxpayer during previous assessment year and hence the rule of consistency could not be applied. Owing the same, the ITAT upheld the actions of TPO in rejecting the RPM as MAM in case of the taxpayer in assessment year under consideration.

In addition to the above, the Tribunal further observed the following:

- The issue has been decided by the Tribunal on merit and does not fall in the ambit of mistake apparent from record.
- The issue has been decided on merits after considering facts and law, therefore jurisdiction of tribunal u/s 254(2) of the Income Tax Act, 1961 ["the Act"] does not permit revaluation of evidence already considered In original order.

In the light of above, the Tribunal dismissed the taxpayer's miscellaneous petition for rectification in its original order passed in the instant case of the taxpayer.

NANGIA'S TAKE

The provisions of Section 154 of the Act clearly provide an opportunity to the taxpayer to make an application to rectify mistakes (apparent from the records) in the orders of the tax authorities (including the ITAT). In the instant case, the ITAT has clarified that the tax authorities are not authorized to entertain the taxpayer's rectification application in relation to a matter/ issue when such matter/issue has been decided based on the merits by analyzing the facts and evidences of the case.

Source: Abott Medical Optics Private Limited [TS-75-ITAT-2017(Bang)-TP]

10. The Tribunal clarifies the "power confinements" of the Dispute Resolution Panel which renders that the Panel has no authority to direct either Assessing officer or Transfer Pricing Officer to make any further enquiry or decide the matter

Facts of the case

This case of the taxpayer (i.e. India Trimmings Private Limited) is with reference to whether the Ld. Dispute Resolution Panel ("DRP"/ "the Panel") was correct in directing the Transfer Pricing Officer ("TPO") to decide the matter in dispute.

In the instant case, during the course of taxpayer's proceedings before the Ld. DRP, the Panel directed the TPO to include one of the comparable companies earlier rejected and decide the percentage of the risk adjustment to be made in case of the taxpayers' disputed international transactions with its associated enterprises ("AEs") transactions.

Aggrieved with actions of the Ld. DRP, an appeal was filed by the Revenue authority before Income Tax Appellate Tribunal ("the Tribunal") wherein the Department's Representative ("DR") submitted that the Ld. DRP has gone beyond its jurisdiction to direct the TPO in order to decide the matter in case of the taxpayer. On the contrary, the taxpayer argued that the Ld. DRP has a liberty to decide the issue itself or can direct the TPO to reconsider the matter in dispute based on its directions. It was further argued by the taxpayer that merely because the Ld. DRP directed the TPO to decide the percentage of risk adjustment, it cannot be said that Ld. DRP exceeded its directions.

The Tribunal's Ruling

The Tribunal referred to the provisions of Section 144C of Income-tax Act, 1961 ("the Act") and observed the following:

- The provisions of subsection 7 of section 144C of the Act requires the Ld. DRP to make an enquiry or calls any enquiry to be made by any income tax authority and report the same to it before issuing any directions;

Subsection 8 of section 144C of the Act provides that the Ld. DRP may confirm, reduce or enhance the proposed order of the Assessing Officer ("AO"), but it shall not aside any proposed variation or issue any direction for further enquiry and passing of assessment order; and

- Ld. DRP may call for remand report from AO or TPO to make further enquiry itself **but has no authority either to direct the AO or TPO to make further enquiry and decide the matter**.

Basis the above, the Tribunal held that the Ld. DRP had no power to direct the TPO to decide the percentage of risk adjustment to be calculated. The Tribunal, thus, set aside the directions passed by the Ld. DRP and directed the Panel to decide the issue afresh after considering the relevant material on records.

NANGIA'S TAKE

The instant ruling clarifies the limits of DRP in deciding the matter in disputes before it whereby the Panel is authorized to conduct further enquiries on its own and thus, cannot delegate this responsibility to AO/ TPO in order to decide the pending matters. However, it is open for the Panel to call for remand reports from AO/ TPO in order to decide the disputed matters.

Source: India Trimmings Private Limited [TS-62-ITAT-2017(CHNY)-TP]

11. The Tribunal elucidates that it is burden of the lower tax authorities to establish the fact that taxpayer's Advertisement, Marketing and Promotional Expenditure is contributing towards promotion of the brand owned by associated enterprise

Background

M/s Nippon Paint India Private Limited ["the taxpayer"] is engaged in the manufacturing and trading of paints, primers and other related chemicals. During assessment year under consideration, the taxpayer entered into certain international transactions with its associated enterprise ("AE") viz. Nippon Japan. Further the taxpayer selected Resale Price Method ("RPM") as the most appropriate method ("MAM") to benchmark the aforesaid transactions.

During the course of assessment proceedings, the Transfer Pricing Officer ("TPO") observed the taxpayer's Advertisement, Marketing and Promotional ("AMP") expenditure significant and viewed them as promotion of brand 'Nippon' in India which was legally owned by its AE, i.e. Nippon Japan. Further, the TPO also rejected the adoption of RPM as the MAM observing that the taxpayer purchased the raw materials from its AE which were partly used in the manufacturing activity and not directly sold in the open market. The TPO worked out that the AMP is a separate international transaction.

By applying the Bright Line Test approach, he arrived at the arm's length price ("ALP") of the aforesaid AMP transaction and consequently, made an upward adjustment to the income of the taxpayer. The taxpayer filed its objections before the Dispute Resolution Panel who confirmed the actions of the TPO. In addition, the TPO applied Transactional Net Margin Method and further made an upward adjustment in income of the taxpayer.

Aggrieved by the same, the taxpayer filed a petition before the Income Tax Appellant Tribunal ("the ITAT").

The ITAT Ruling

A. On AMP Expenses

- Observed that the Assessing Officer/ TPO made no substantial evidence on record to show that the expenditure incurred by the taxpayer was incurred towards brand building of the AE;

- Reliance was placed on several judicial pronouncements and co-ordinate bench rulings viz. ***Maruti Suzuki Limited [TS-595-HC-2015(DEL)-TP]***, ***Sony Ericsson [TS-96-HC-2015(DEL)-TP]***, ***Good year India [TS-226-ITAT-2016(DEL)-TP*** and ***Whirlpool of India [TS-622-HC-2015(DEL)-TP]*** and it was held that the AMP transaction does not fall under the purview of international transaction as per Section 92B(1) of the Income Tax Act, 1961 ("the Act").

- The tax authorities failed in establishing that there was an agreement or arrangement formal or informal between the taxpayer and its AE to promote the brand "Nippon" in India and to spend towards AMP expenses.

Based on above, the ITAT held that the AMP is not a separate international transaction and deleted the TP additions made in this regard.

NANGIA'S TAKE

The instant case focuses on the much talked about AMP issue. The verdict of the ITAT clearly explains the fact that it is the burden of the AO/ TPO to examine, make enquiries and bring an evidence to demonstrate that the AMP expend of the taxpayer is actually contributing in building its AE's brand in India. Another principle that has been reiterated by the ITAT in the instant case is that it is essential to have an agreement in place amongst the taxpayer and its AE which should appropriately make the taxpayer accountable for incurring AMP expenditure.

Source: M/s Nippon Paint India Private Limited vs. The Asst. Commissioner of Income Tax ITA No. 779/Mds/2016

12. Service rendition through oral communication possible.

Facts of the case

- Max India Limited ("the Taxpayer") is engaged in various activities such as packaging, metallise, max foil, pharma, treasury and healthcare divisions.

- During AY 2002-03, the Taxpayer incurred expenditure of about INR 1.25 crores towards legal and professional charges paid to its associated enterprise i.e. Max UK Ltd. Same has been reported as an international transaction in audit report u/s 92E of Income Tax Act, 1961.

- For the purpose of above referred international transaction pertaining to payment of legal and professional charges to its AE; the Taxpayer entered into an inter-company agreement, relevant provisions of which are mentioned below:-

  - *Max UK will explore business opportunities initially in the field of health care, financial services, life insurance and allied areas;*

  - *Max UK will identify potential collaborations/ partners desirous of entering into ventures in aforesaid business areas;*

  - *Conduct due-diligence of the potential collaborators/ partners as regards its financial, management, technical capabilities, etc.;*

  - ✓ *Max UK will share information and bridge cultural gap between potential collaborators and the Taxpayer;*

  - ✓ *Max UK will assist the Taxpayer for establishing contract with such potential collaborators/ partners; and*

  - ✓ *Max UK will provide other support services.*

During the course of the assessment proceedings for AY 2002-03, the Transfer Pricing Officer ["TPO"] rejected the claim of the Taxpayer for legal and professional charges on the grounds that the Taxpayer failed to establish the benefit received from incurring such legal and professional expenses.

Taxpayer filed appeal an appeal before CIT(A) and ITAT but failed to find any relief. As a consequence, the Taxpayer filed writ petition before High Court ("HC") of Punjab and Haryana at Chandigarh.

HC's Adjudication

- HC observed that the nature of services rendered by Max UK was supported by an agreement and an invoice;

- HC further observed that the nature of services provided by Max UK were such that it was difficult to provide evidence of the services having actually been rendered.

- HC also observed that the Taxpayer was in-fact able to achieve an export turnover of INR 29 crores and that the same demonstrated prima-facie that the services were rendered by Max UK.

❖ HC, concluding in favor of the Taxpayer, held that services such as of the nature mentioned in the agreement between the Taxpayer and its AE would not necessarily be recorded in writing. Advice, introductions, information may well be communicated orally between group companies.

NANGIA'S TAKE

Intra-group services transactions have already been one of the most litigated subject matter in transfer pricing in India. The Revenue authorities in India typically consider that the very basis of determining the ALP of such transaction is by evaluating the business need for such services, benefits accrued therefrom and the actual receipt of services. This High Court's observation that oral communication for rendition of service is acceptable within group companies, is a welcome decision.

[Source: Max India Limited; ITA No. 186 of 2013 (O&M)]

INDIRECT TAX

13. Turnkey contracts undertaken for Delhi Metro cannot be vivisected to levy service tax

M/s. Siemens Limited ('Assessee'), an engineering and manufacturing company, filed a refund claim of Service Tax wrongly charged on the invoices raised on M/s. Delhi Metro Rail Corporation Limited ("DMRC"). Assessee's contention was that the tax was not payable, as the contract with DMRC was a turnkey contract which cannot be vivisected.

Revenue however rejected the said refund claim. Assessee approached Custom Excise and Service Tax Appellate Tribunal ("CESTAT").

After hearing the parties, CESTAT, *inter-alia*, held the following:

❖ CESTAT has placed reliance on the case of ***Afcons Infrastructure Limited ("AIL") vs. Commissioner of Central Excise***[1] wherein on similar facts it was held that the definition of 'Commercial and Industrial Construction Services' defined under section 65(25b) of the Finance Act 1994 ('Act') excludes activities relating to roads, ports, railways, dams etc. There is no distinction between monorail & metro and the term 'railways' used therein has to be given a wider scope to include all types of railway lines.

❖ In the aforementioned case, CESTAT referred to Notification No. 12/2012-ST, which provides exemption from Service tax on the services provided by the way of construction, erection,

[1] A/1583-1590/13/CSTB/C-I dated 4 July 2013

commissioning and installation of original works pertaining to Railways, including monorail and metro. The said exemption clearly indicates the Legislative intent of not taxing construction work pertaining to railways.

- CESTAT also relied on the ruling of Hon'ble Delhi High Court in DMRC case which held that Delhi Metro Rail is Government Railway as defined in the Indian Railway Act, and in that case the question of levy of service tax under 'Commercial and Industrial Construction Service' would not arise as such construction in respect of Railways stands excluded from the scope of levy.

- On the issue of vivisection of the contract, CESTAT relied on the ruling of Hon'ble Apex Court in the case of ***Commissioner of Central Excise & Customs, Kerala vs. Larsen & Toubro Limited***[2], wherein it was specifically settled that in works contract, there cannot be vivisection and calculation of tax under various categories of services.

In light of the above, it was held that the Assessee was eligible for refund of service tax wrongly charged on the contracts with DMRC.

NANGIA'S TAKE

The judgement of the CESTAT brings clarity that turnkey contract undertaken for metro rail projects cannot be vivisected to levy service tax under 'Commercial and Industrial Construction Service', as definition of railways is wide to include metro rail as well.

[Source: M/s. Siemens Limited vs. Commissioner of Service Tax, Mumbai in Appeal No. ST/33/11-Mum]

[2] 2015(39) STR 913 (S.C)

14. 1st July 2017: An optimistic date for GST implementation

- Moving a step closer towards implementation of the Goods and Services tax (GST), GST Council in its 11th meeting approved the draft CGST and IGST Laws.

- UGST & SGST Laws to be approved in the next meeting and after that the all laws will be placed before the parliament in forthcoming session and state assemblies.

Highlights:

- "The GST Council has cleared the final draft of CGST, IGST law and the approval of draft of state-GST (SGST) which is to be cleared by state assemblies is on the anvil," Finance Minister Arun Jaitley said.

- "CGST, IGST and Union Territory-GST (UTGST) law to be taken to Parliament in the second half of Budget session starting March 9," Mr Jaitley said. "UTGST and SGST draft bills will be taken up for discussion and approval at the council's next meeting on March 16," he added.

- Hopefully the laws will be in Parliament in this session. Once the GST council completes this round of legislative activity, then the work will start on fitment of goods and services into the various rate structures.

- Revenue Secretary Hasmukh Adhia said there were demands that restaurants should be included in the composition scheme, particularly those with less turnover.

- The Council has decided to levy a 5 per cent GST (2.5 per cent by Centre and 2.5 per cent by state) on small hotels, restaurants and dhabas with an annual turnover of up to Rs 50 lakh.

- The Council will have its 12th meeting on March 16 in which SGST and UTGST bills will be cleared.

NANGIA'S TAKE

Pace at which the government is moving ahead July 1, 2017 seems to be a realistic date for GST implementation. Government is taking big strides forward, which requires the industry to gear up. We believe that GST being a business process change would require a lot of changes in businesses processes and information technology network also. These changes will take its own course of time and efforts to implement this revolutionary change.