Tax Glimpses 2015

We bring you a concise analysis of important judgements and noteworthy regulatory developments in corporate and financial services tax, global mobility, M & A tax, transfer pricing and indirect taxes during 2015.

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Foreword

I am delighted to present our annual publication, Tax Glimpses 2015.

Numbers tell a good story about India these days – with a 7.3% growth rate in Q3 of 2015, much ahead of the projected global average growth rate of 3.1%, India is presently amongst the fastest growing economies worldwide. This is echoed in the optimism, although as yet a bit cautious, that pervades the Indian industry and investors alike.

The incumbent government has on its part, kept the wheels of the economy turning, bringing forward several important policy initiatives and economic reforms that hold the promise of cranking up the GDP growth rate a few more notches. These include the Land Acquisition Bill, continuing attempts to roll out the bold Goods and Services Tax initiative to transform India into a single market with low friction and reduced logistics and transaction costs, significant foreign direct investment policy reforms to kick-start investment flows into India and revamping of the labour laws.

While the Digital India programme attracted global attention, the Make in India campaign is aimed at attracting sufficient foreign investment in the country's manufacturing sector to power an investment-led economic growth plan. The reversal of the downward trend in the global World Bank-IFC joint survey, "Doing Business 2016" has made the government more ambitious and hopeful of further improvement in India's ranking in the next survey.

On the corporate tax front, the Government is moving toward implementing the statement made by the Finance Minister during the Budget in February, 2015, by proposing phasing out deductions and exemptions. This is still at the proposal stage, with comments/ suggestions invited from the public.

This year, the Government of India signed an Inter-Governmental Agreement with the United States to implement the FATCA in India, according to which financial institutions in India are required to report tax information about US account holders to the Indian Government, which will, in turn relay that information to the US IRS. India will also receive information on their citizens' bank balances in the United States, which would help unearth unaccounted money. This agreement follows in quick succession to the Anti-Black Money Act which empowers the taxation of undisclosed foreign incomes and assets of residents, and recovery of tax, hitherto onerous and difficult, in a simple manner and without being time-barred, with a non-discretionary penalty of 300%, interest and prosecution. A new manual was published on Exchange of Information for educating tax officials, and many more Tax Information Exchange Agreements and clauses are being signed and negotiated. This reflects the government's focus on tightening tax collections and applying Big Data technology to detect possible tax leakages.

In the world of Transfer Pricing, the signing of a few more Advance Pricing Arrangements heralds the beginning of a new era. At the same time, a High Court ruling recently settled a simmering controversy regarding adjustments for marketing intangibles of taxpayers engaged in import, marketing and distribution of branded products of their AEs. In addition, the highly debated issue of the manner of determining the arm's length interest rate for outbound loans denominated in foreign currency was discussed, and the High Court reconfirmed certain established principles and provided direction on tax authorities' powers to restructure transactions and interpret global guidance.

The Government has also taken several decisions, such as increasing monetary limits for filing appeals to Tribunal, High Court and Supreme Court by the tax authorities and accepting the High Court decision of holding the receipt of premium on share issue to be on capital account not giving rise to income, and therefore, outside the purview of transfer pricing adjustments to signal both their intention to make the tax administration more reasonable and less 'adversarial' and to reduce the quantum of revenue-initiated tax litigation clogging the Indian tax tribunals and courts.

The FDI policy was liberalised for 15 major sectors. The changes introduced include an increase in sectoral caps for foreign investment, bringing more activities under the automatic route and easing of conditions for foreign investment.

As a handbook that captures the important developments in the past year, *Tax Glimpses 2015* brings to you a succinct analysis of important judgements and noteworthy regulatory developments in corporate tax, mergers and acquisitions, transfer pricing and indirect tax during calendar year 2015. This publication also includes a listing (with web-links, if available) of various PwC Thought Leadership initiatives such as news alerts and flashes, newsletters and articles published during 2015.

Trust you will find this useful. I look forward to hearing from you, and wish you the very best for 2016.

Gautam Mehra

Leader, Tax and Regulatory Services

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Non-compete fee

Non-compete fees re-characterised as consideration for transfer of shares – Vodafone test applied for tax planning *v.* tax evasion

CIT v. Shiv Raj Gupta [2014] 52 taxmann.com 425 (Delhi)

The taxpayer and his family members sold their shares of a company to another group company. The taxpayer also contemporaneously entered into a non-compete agreement for a consideration with the group company, with a restrictive covenant that he shall not conduct any manufacturing or marketing activities relating to IMFL for 10 years.

According to the HC, the consideration for transfer of shares was artificially and deceitfully bifurcated under a sham agreement, between a non-compete fee and consideration for transfer of shares. The entire amount received by the taxpayer was held to be for transfer of shares, and therefore taxable as capital gains. The HC discussed the distinction between tax mitigation and tax evasion, and between acceptable tax avoidance and abusive tax avoidance; and applied the principle laid down by the SC in the Vodafone decision.

Facts

The taxpayer was the CMD of C Ltd a public listed company engaged in the business of manufacturing and sale of IMFL and beer. A group company, a giant in liquor business in comparison to C Ltd, offered and purchased through its subsidiaries the shares of C Ltd held by the taxpayer and his family members under a MoU. The taxpayer entered into a deed of covenant in his individual capacity with the group company. Another MoU was executed between the group company and the taxpayer as an individual, with a restrictive covenant that he shall not, directly or indirectly, conduct any manufacturing or marking activities relating to IMFL for 10 years. As per the MoU the taxpayer received a non-compete fee, which he claimed to be non-taxable, being treated as a capital receipt. The TO invoked section 28(ii) of the Act and held that the amount ostensibly paid as non-compete fee, was nothing but a colourable device, and the tax treatment should not be accepted. The Appeal upheld the TO's addition, but relied on section 28(iv) of the Act for the same. The Tribunal, relying on the SC decision in the case of Guffic Chem Private Limited *v.* CIT [2011] 332 ITR 602 (SC) decided the issue in favour of the taxpayer.

Held

In view of the discussion and findings on the true and real nature of the transaction being camouflaged as a 'non-compete fee', the HC had no hesitation and reservation in concluding that the taxpayer had indulged in abusive tax avoidance. The true nature of the transaction was the sale of shares of C Ltd in favour of the group company. The consideration received was not a non-compete fee, and would not be exempt. Transfer of majority shareholding would include consideration receivable towards the controlling interest. The price paid by the group company and received by the taxpayer was for purchase of shares, including the controlling interest. The price paid would therefore include the right to control and manage C Ltd. Any division or bifurcation would result in the court or the Revenue splitting the amounts between capital gains and section 28(ii)(a) of the Act.

It was equally important to distinguish and differentiate between acceptable tax avoidance and abusive tax avoidance. The SC, in CIT *v.* Raman (A.) & Co. [1968] 67 ITR 11 (SC), had observed that avoidance of tax liability by so arranging commercial affairs that the charge of tax was distributed, was not prohibited. The taxpayer could resort to a device to divert the income before it accrued or arose to him. Effectiveness of the device depended not upon considerations of morality, but on the operation of the Act. In clear and categorical terms, this ratio resonated with, and was approved by the SC in the case of Vodafone International Holdings B.V. B.V. *v.* UoI [2012] 341 ITR 1 (SC). Thus, the test of 'devoid of business purpose' or 'lack of economic substance' was not accepted and applied in India, as it was too broad and dissatisfactory. The dividing line between acceptable and abusive tax avoidance could not be deduced or inferred from lowering or elimination of the tax liability. The later was the consequence and the tax effect. The dividing line as per the ratio in the Vodafone's case (*supra*) was ethically principled and moralistic, as tax

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avoidance was disapproved when the taxpayer adopted a colourable device, dubiousness and otherwise indulged in a sham arrangement or transaction. For example, in Vodafone's case (*supra*), the taxpayer had several options, and therefore, the right to choose a particular tax event. As long as the choice was within the framework of law, the TO could not disturb the tax effect or liability, which was the consequence of the event. The taxpayer's choice was not abrogated or invalidated. Thus, when a specific anti-tax avoidance section/ rule was invoked, the court and Tribunal must look at, and interpret the relevant provision to decipher whether the chosen tax event was covered within that provision, and accordingly the tax consequences would apply.

In the context of the test applied in the Vodafone case (*supra*), the court opined that when there was one transaction, or a series or combination of transactions intended to operate as such, the courts were entitled to look at the real scheme or as a whole, even when a particular stage was only an expectation without any contractual force. This did not mean that the transaction, or any step in the transaction, was treated as sham or given a legal effect different from the legal effect intended by the parties. Nor did it imply going behind the transaction or the series of transactions for some supposed underlying substance. It meant looking at the document(s) or the act(s) in the context to which it properly belonged. The HC had concluded that the current case was a clear case wherein the sale consideration for transfer of shares had been artificially and deceitfully bifurcated under a sham agreement/ document, which was unreal and not a true record of the intention. The entire 'non-compete fee' payment had been made to the taxpayer; his family members had not shared any part of the payment. This meant that the taxpayer had chosen the taxable event, i.e., to receive the entire sale consideration in his name; hence he should bear and face the tax consequences. Thus, the entire amount was held to be taxable in the taxpayer's hands, and would be treated as part of the sale consideration received on transfer of shares in C Ltd held by him.

Editor's note

Applying the test laid down in the Vodafone case (supra), the HC has gone into substance of the matter to determine true and real nature of the receipt. This is a good example of "judicial General Anti Avoidance Rule".

Make available condition

Tribunal invokes MFN clause to bring the 'make available' condition into the India-Sweden tax treaty

Sandvik AB v. Dy. DIT [2014] 52 taxmann.com 211 (Pune-Tribunal)

Management service fee received by the taxpayer from its group companies in India was not taxable in India as a 'FTS' as the 'make available' condition was not satisfied. While holding so, the Tribunal referred to the protocol attached to the India-Sweden tax treaty and invoked the MFN clause from another treaty that India had signed, to import the 'make available' condition into the India-Sweden tax treaty.

Further, the Tribunal relied on the Delhi HC ruling in the case of Maruti Udyog Limited v. ADIT [2009] 34 SOT 480 (Delhi-Tribunal) and the AAR ruling in the case of Poonawala Aviation Private Limited, In re [2012] 343 ITR 202 (AAR-New Delhi) and held that the protocol appended to the tax treaties was an integral part of a tax treaty, and could be relied upon to understand the scope of taxation.

Facts

During the year, the taxpayer, a resident of Sweden, received a management fee from its group companies for rendering commercial, management and marketing related support services. The taxpayer filed its ROI stating that such receipts were not taxable in India. The taxpayer claimed that FTS under Article 12 of the India-Sweden tax treaty read with the protocol thereto enable the invocation of the MFN clause. With reference to the MFN clause, a restricted definition of FTS under the India-Portugal tax treaty could be imported into the India-Sweden tax treaty. During the course of assessment, the TO/ DRP held that such receipts were taxable in India as FTS.

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Held

The Tribunal held that reference to the India-Portugal tax treaty, which allowed a restricted definition of FTS, was valid in the light of the protocol attached to the India-Sweden tax treaty.

- A protocol was an integral part of the tax treaty and had the same binding force. The Tribunal placed reliance on the Delhi Tribunal decision in Maruti Udyog Limited (*supra*) and on the AAR's order in the case of Poonavala Aviations (*supra*).
- In tax treaties, the MFN clause finds a place when countries were reluctant to forego their right to tax some elements of the income. An MFN clause can direct more favourable treatment available in other treaties only in regard to the same category of matter, or the "same clause of the matter" (*sic*).

Further, the Tribunal stated that the expression 'making available' was imported for deciding in which contracting state the amount received for rendering the services relating to the technical know-how, was to be taxed. The expression, 'make available', was used in the context of supplying or transferring technical knowledge in performance of the services. The technology would be considered as 'made available' when the person receiving the services was able to apply the technology by himself/ herself. The Tribunal relied on the decisions of its co-ordinate bench in Sandvik Australia Pty Limited *v.* Dy DIT [2013] 141 ITD 598 (Pune-Tribunal) and of the Karnataka HC in CIT *v.* De Beers India Minerals Private Limited [2012] 346 ITR 467 (Kar).

Editor's note

The ruling re-emphasises that a protocol appended to a tax treaty is an integral part of that tax treaty, and has the same binding force as any other clause.

For the interpretation of the term, 'make available', it has re-emphasised the fact that technical knowledge/ skill would be considered to have been made available only when the person receiving the services is able to apply the technology by themselves.

Marketing and other support services not taxable as FIS where 'make available' test not satisfied; where dependent agent PE remunerated at arm's length, no further amount attributable to PE

[2015] 59 taxmann.com 159 (Bangalore-Tribunal)

- *The 'make available' test for taxability of FIS was not satisfied unless there was a transfer of technology involved in rendering of technical services by the service provider to the service recipient.*
- *Where a PE had been remunerated on arm's length basis, no further income could be attributed to it and brought to tax in India.*

Facts

The taxpayer was a company incorporated, and fiscally domiciled, in the USA. The taxpayer was engaged, inter alia, in providing business development, market services and other support services to its two AEs in India. The taxpayer, in its ROI, claimed that the fees earned from providing these services in the FY under consideration, was not liable to tax in India under Article 12(4)(b) of the India-USA tax treaty, since the services did not 'make available' any technical knowledge, experience, skill, etc. to the AEs. During assessment, the TO held that a person without technical knowledge could not have provided such services. Having held so, the TO concluded that the taxpayer was providing technical services to its AEs, and it was also 'making available' technical knowledge to its AEs, i.e., the service recipients. Accordingly, the TO held that the fees earned pursuant to rendering of services by the taxpayer were taxable as FIS under the India-USA tax treaty. The taxpayer filed objections with the DRP. The DRP confirmed the TO's stand. Further, the DRP also stated that one of the AEs of the taxpayer was acting as its agent for purchase and sale of the taxpayer's products. Accordingly, it was alleged that the taxpayer had a dependent agent PE in India through the presence of the Indian AE, and the profits attributable to the operations in India were to be brought to tax in India. In this backdrop, the TO proceeded to tax the sum in the taxpayer's hands as FIS. Further, an additional

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sum was brought to tax as business profits on account of the dependent agent PE's estimated profits, in accordance with the DRP's directions.

Held

Taxability of fees as FIS

A condition precedent for invoking the 'make available' test in Article 12(4)(b) of the India-USA tax treaty was that the services should have enabled the person acquiring the services to apply the technology contained therein. The Karnataka HC's decision in CIT *v*. De Beers India Minerals Private Limited [2012] 346 ITR 467 (Kar) approving this school of thought, was relied upon. Unless there was a transfer of technology involved in the technical services extended by the taxpayer, the 'make available' test was not satisfied. With respect to taxability of a consideration under the India-USA tax treaty, the decisive factor was not the rendering of training services per se, but whether the training services were of such a nature that they resulted in a transfer of technology. The consideration could not be brought to tax under Article 12(4)(b) of the India-USA tax treaty as the services did not enable the recipient to utilise the knowledge or know-how on his own in future without the aid of the service provider.

Constitution of dependent agent PE

Even if a PE existed, and the taxpayer carried on business through it, under Article 7(1) of the India-USA tax treaty, the taxpayer's profits could be taxed in the source jurisdiction – that too, only so much as was attributable to that PE. This also included attribution of profit to sales of goods or business activities carried on in the other state, which was of the same or similar kind as those effected through the PE. On facts, even if the PE existed, it was constituted on account of trading transactions only. Therefore, no part of the earnings from the rendering of services to the AE could be related to the nature of the PE's activities and thus be brought to tax in India. Since the Indian AE, which was treated as the taxpayer's dependent agent PE, had been paid an arm's length remuneration, nothing further could be attributed to the PE and brought to tax, in view of the settled legal position in SET Satellite (Singapore) Pte Limited *v*. DDIT [2008] 307 ITR 205 (Bombay). Even if there was a dependent agent PE based on facts, it would have no taxable profits in the hands of the taxpayer, in absence of a finding that the PE had been paid less than arm's length remuneration. Accordingly, existence of the PE, being academic, need not be examined.

Editor's note

This is a welcome ruling wherein the aspect of 'make available' in connecting to the marketing services has been analysed. The Tribunal has endorsed the well-settled principle of the 'make available' condition.

Further, the ruling has reiterated that in cases where the impugned PE is being remunerated at arm's length, the issue of constitution of PE is academic, as nothing additional can be attributed to the PE and brought to tax in India.

Off-shore supply

Off-shore supply of equipment and design and drawings not taxable in India

[2015] 58 taxmann.com 232 (Kolkata-Tribunal)

German entity's income earned from off-shore supply of equipment and from sale of designs and drawings held not subject to tax in India. The Tribunal concluded on the basis that since the title to the equipment was transferred outside India, and no service was provided in India on account of supply of equipment, no income could be taxed in India as per the provisions of both, the Act as well as the India-Germany tax treaty. The Tribunal also held that designs and drawings were supplied by outright sale. Further, designs and drawings were used for internal business purposes of the Indian customers, and not for their commercial exploitation. Hence, the taxpayer's income from supply of designs and drawings did not constitute royalty and was thus not taxable in India.

Facts

The taxpayer was a German resident engaged in the business of providing innovative and environmentally sound solutions for a variety of customers in metal and mining processing industries. During AY 2010-11, the taxpayer earned revenue from Indian customers through

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sale of equipment, supply of designs and drawings, and provision of supervisory services. It had a supervisory PE for certain projects in India in terms of the tax treaty. In the income tax return filed, the taxpayer attributed 17.93% of the gross revenue earned from supervisory activities to the Indian supervisory PE. The income earned from sale of equipment and from supply of designs and drawings was not offered to tax in its return. The TO, in his draft assessment order, proposed to tax part of the income earned from sale of equipment to Indian customers. Further, the income earned from supply of designs and drawings was considered taxable as royalty. In relation to income from supervisory services, the attribution percentage was enhanced to 27.5% of the gross revenue, from 17.93% offered by the taxpayer. Additionally, interest under sections 234A and 234B were also proposed to be levied.

The taxpayer filed objections before the DRP against the draft assessment order. The DRP confirmed the TO's additions on all issues, and the final assessment order was passed accordingly. Aggrieved by the final assessment order, the taxpayer filed an appeal before the Tribunal.

Held

Sale of equipment

The Tribunal concluded that the sale of equipment took place outside India, and hence no portion of the receipts from the sale could be taxed in India. This conclusion was reached based on the following facts:

- All activities relating to design, fabrication and manufacturing of equipment took place outside India.
- Sale of equipment to unrelated Indian customers was done from outside India on a principal-to-principal basis at arm's length, and consideration was also received outside India.
- The documents and clauses of the agreement clearly stated that the equipment was sold directly by the taxpayer on an export sale basis, and the title/ ownership of equipment was transferred outside India.
- The Tribunal accepted the principle laid down in Ishikawajima-Harima Heavy Industries Limited *v.* DIT [2007] 288 ITR 408 (SC) that if title was transferred outside India, no profit arose in India.
- In connection with various acceptance tests, the Tribunal held that if the test failed, it could result only in payment of liquidated damages by the taxpayer, and hence the clause could be considered as a warranty provision. Reliance was placed on the decisions of Delhi HC in DIT *v.* LG Cable Limited [2011] 237 CTR 438 (Delhi), Delhi Special Bench in Motorola Income. *v.* DCIT [2005] 95 ITD 269 (Delhi)(SB), and of the AAR in Hyosung Corporation, *In re* (AAR) [2009] 314 ITR 343 (AAR). Deferred payment relating to an acceptance test did not have any impact on sale of goods, which was supported by the definition of "sale" mentioned under section 2(g) of the Central Sales-tax Act, 1956.

The Revenue's contention that the contract was a composite contract, and taxability could not be split into separate parts, was not accepted by the Tribunal based on the SC decision in Ishikawajma-Harima Heavy Industries Limited (*supra*). The Revenue's reliance on the AAR decision in Alstom Transport SA, *In re* [2012] 251 CTR 193 (AAR) was no longer valid as it had been overruled by the Delhi HC in Linde AG, Engineering Division *v.* DDIT [2014] 365 ITR 1 (Delhi). No PE of the taxpayer was created by sale of equipment. Income earned from supervisory activities had been attributed to supervisory PE in India, and had been considered taxable. Thus, income earned from sale of equipment was not taxable as per tax treaty provisions.

Income from supervisory activities

The Income-tax Settlement Commission, in the taxpayer's own case for earlier years, had held a profit rate of 27.5% applicable for attributing income from supervisory services. As no reason was provided by the taxpayer to deviate from this decision, the Tribunal had confirmed the rate of 27.5%.

Income from supply of design and drawings

Basic engineering packages sold by the taxpayer were largely designed on the basis of standard technologies available with it, and hence the consideration was for

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sale of products which were embedded in plants set up by Indian customers. Principles emerging from the decisions in Scientific Engineering House Private Limited *v*. CIT [1986] 157 ITR 86 (SC) and in Modern Threads (I) Limited *v.* DCIT [1999] 69 ITD 115 (Jaipur-Tribunal) were accepted by the Tribunal, and it held that income from sale of designs and drawings would be considered as business income, and not as royalty. The designs and drawings were used by Indian customers for internal business purposes, and not for commercial exploitation. Thus, the payments made by the Indian customers were for use of copyrighted articles rather than use of copyright. Hence, the taxpayer's income could only be considered as business income and not as royalty. Retaining intellectual property in designs and drawings sold by the taxpayer was similar in nature to retaining patent rights in any goods/ machinery; it did not change the character of a transaction from sale of product to license/ know-how. As the entire work in relation to designs and drawings was done outside India, sales were effected outside India, and consideration was also received outside India, the taxpayer's business income from sale of designs and drawings was not liable to tax in India under both, the Act and the tax treaty.

Interest under section 234A and 234B

Charging of interest under section 234A and 234B was consequential in nature; the TO was directed to re-compute the interest charged.

The Tribunal had passed a consolidated order in this case wherein the company's appeal for the AY 2011-12 had also been decided. Further, the Tribunal had also passed an order in the case of a group company of the taxpayer, for the AY 2010-11. In both these appeals, the issues were broadly similar.

Editor's note

This is a important decision affecting foreign Engineering, Procurement, Construction companies earning income from India. The Tribunal's observation and ruling on taxability of designs and drawings in India is extremely useful. The Tribunal has delivered this judgment based on specific sets of facts, and the decision cannot be uniformly applied to determine taxability of all offshore supply and designs and drawings in India. Before applying the decision, the facts of each case need to be carefully analysed. Further, the principle enunciated in the decision should not be construed as final as the chances of the Revenue appealing to the HC cannot be ruled out. Further it has been clarified under the Act after the amendment by the Finance Act 2012 that royalty includes consideration for any right, property or information, immaterial of its location.

Treaty or Act – which is more beneficial?

Section 206AA cannot override section 90(2) of the Act

[2015] 56 taxmann.com 1 (Pune-Tribunal)

Section 206AA of the Act would not override provisions of the tax treaty to the extent that the latter is more beneficial to a taxpayer.

Facts

The taxpayer was a company engaged in the business of manufacture, sale and export of vaccines. It made payments to various non-resident taxpayers on account of interest, royalty and FTS during the FY under consideration, and withheld taxes as per the rates prescribed in the relevant tax treaties. The tax treaty rates were used even when no PAN was provided by the recipient, and provisions of section 206AA of the Act were not invoked. During assessment, the TO held the taxpayer to be in default to the extent of short withholding of tax, being the difference between the tax rate applied as per the tax treaty, and the 20% rate under section 206AA of the Act. Aggrieved, the taxpayer filed an appeal before CIT(A). The CIT(A) concurred with the taxpayer, and held that section 206AA of the Act would override other provisions of the Act, but not the provisions of section 90(2) of the Act, which allow a taxpayer to avail the provisions of tax treaties to the extent they are more favourable than provisions of the Act. The Revenue filed an appeal before the Tribunal.

Held

The Tribunal upheld the CIT(A)'s reliance on the SC ruling in UoI *v.* Azadi Bachao Andolan and Others [2003] 263 ITR 706 (SC), wherein it had been held that provisions

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made in the tax treaties would prevail over the general provisions contained in the Act, to the extent they were more beneficial to the taxpayer. The Tribunal also observed that tax treaties entered into between India and the other relevant countries in the present context provided for scope of taxation and/ or a rate of taxation, which was different from the scope/ rate prescribed under the Act. Charging sections 4 and 5 of the Act, which dealt with the principle of ascertainment of total income under the Act, were also subordinate to the principle enshrined in section 90(2) as held by the SC in Azadi Bachao Andolan (*supra*). section 206AA of the Act was not a charging section, but was a part of the procedural provisions dealing with collection and withholding of tax, and it could not override the charging sections, *viz.* sections 4 and 5 of the Act. Reliance was placed on case of CIT *v*. Eli Lilly & Co [2009] 312 ITR 225 (SC), wherein it had been held that section 195 of the Act would apply only to sums which were otherwise chargeable to tax under the Act. Reliance was also placed on GE India Technology Centre Private Limited *v*. CIT [2010] 327 ITR 456 (SC), wherein it had been held that provisions of tax treaties, along with sections 4, 5, 9, 90 and 91 of the Act, were relevant while applying the provisions of withholding tax. Thus, upholding the CIT(A)'s order, the Tribunal held that where the tax had been withheld on the strength of the beneficial provisions of tax treaties, the provisions of section 206AA of the Act could not be invoked by the TO to insist on withholding tax @ 20%, having regard to the overriding nature section 90(2) of the Act. The tax demand relatable to the difference between 20% and the actual tax rate, on which tax was withheld by the taxpayer in terms of the relevant tax treaties, was therefore deleted.

Editor's note

Section 206AA of the Act would not be applicable to non-resident taxpayers, i.e., withholding tax rate of 20% should not be applicable where the rate prescribed under any tax treaties is lower. section 206AA of the Act is not the charging section, and cannot override section 90(2) of the Act.

Real income

No tax on consideration agreed under development agreement if not accrued or received; concept of 'real income' relevant while determining income chargeable to tax

CIT v. Chemosyn Limited [TS-73-HC-2015 (Bombay)]

In absence of 'real income', no income on account of a constructed area (to be received under the development agreement) could be subject to tax.

Facts

The taxpayer owned two plots of land. On 16 June 2006, the taxpayer entered into a development agreement with a developer for development of one of the plots. As consideration for grant of development rights, the taxpayer received INR 161.1 million and construction of 18,000 sq. ft. of built up area to be done free of cost on the second plot.

On 5 July 2007, a tripartite agreement was entered into between the taxpayer, the developer and a new buyer. Under this agreement, both plots were sold to the new buyer for INR 291.1 million. The taxpayer filed its ROI for AY 2007-08, offering INR 161.1 million to tax as capital gains. In the ROI for AY 2008-09, the taxpayer offered to tax INR 130 million (the difference between INR 291.1 million and INR 161.1 million) as capital gains. For AY 2007-08, the TO held that capital gains was payable on the market value of the 18,000 sq. ft. of construction to be carried out by the developer. The CIT(A) upheld the TO's order. However, it held that the consideration for 18,000 sq. ft. of constructed area required to be arrived at on the basis of cost of construction.

The Tribunal deleted the TO's additions and sustained those made by the CIT(A) in computation of capital gains. The dispute was regarding computation of capital gains. The Tribunal relied upon its decision in the case of Kalpataru Construction Overseas Private Limited *v*. DCIT [2007] 13 SOT 194 (Mumbai-Tribunal), and on the decision of the Bombay HC in the case of CIT *v*. Shivsagar Estates [1993] 204 ITR 1 (Bombay), to hold, on the basis of the 'real

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income' theory, that since income on account of 18,000 sq. ft. of cost of construction of area had neither accrued nor received on account of subsequent events, could not be brought to tax.

Held

On the basis of findings of fact that no income in respect of 18,000 sq. ft. of constructed area had accrued or been received, the HC held that the Tribunal's findings were not perverse or arbitrary. As a result, no substantial question of law arose warranting interference with the Tribunal's order. The HC therefore dismissed the Revenue's appeal.

Editor's note

The ruling reinforces the principle that the concept of 'real income' is important while determining taxable income. It emphasises that subsequent events may need to be taken into account in determining the accrual or receipt of income and tax liability for a particular year. However, one would need to examine whether the concept of 'real income' can be applied to defer the taxation of a consideration (for computing capital gains on development agreements) which is contingent upon future events.

Tax residency certificate

TRC sufficient evidence for accepting status of residence as well as beneficial ownership for applying India-Mauritius tax treaty

[2015] 60 taxmann.com 433 (Punjab & Haryana)

A TRC issued to a Mauritian company by the Mauritian Tax Authorities shall be sufficient evidence of its residency in Mauritius, and accordingly, the Mauritian company would be eligible for relief under the India-Mauritius tax treaty.

Facts

ABC Ltd and I Co were companies incorporated in India in 2002 and 2007 respectively. F Co1 and F Co2 were companies incorporated in Mauritius in the years 2004 and 2006 respectively, which held 66.29% and 12.75% shares in I Co respectively. During the FY 2011-12, the petitioner entered into a transaction with F Co1 and F Co2 for purchase of shares in I Co. The transfer of shares resulted in capital gains in the hands of F Co1 and F Co2, which were claimed as not liable to tax in India under the provisions of the India-Mauritius tax treaty. F Co1 and F Co2 had obtained a TRC from Mauritian Tax Authorities. Considering the provisions of the India-Mauritius tax treaty, the petitioner (i.e. the buyer) was of the view that no tax was required to be withheld under section 195 of the Act. Accordingly, the petitioner filed an application with the AAR seeking an advance ruling on the following questions:

- Whether capital gains arising in the hands of F Co1 and F Co2 would be chargeable to tax in India having regard to Article 13(4) of India-Mauritius tax treaty read with section 90(2) of the Act?
- Whether the petitioner (i.e. the buyer) was required to withhold tax under the Act while making payment of sale consideration?

AAR declined to give a ruling on the aforementioned application (after hearing the case several times) on the basis of a *prima-facie* finding that the transaction in question was designed for avoidance of income tax. Thus, the taxpayer filed an appeal in the HC submitting that the transaction was not designed for avoidance of tax and hence, relief should be granted under the India-Mauritius tax treaty.

Held

There was not a "single finding of fact" in relation to Revenue's contention that the transaction was designed for the avoidance of income tax in India. The intention to acquire the shares of I Co by F Co1 was present almost since the inception of I Co. F Co1 ran and managed I Co for over 6 years. There was nothing which suggested that the investment was only with a view to generate profit from the sale of such shares. Once a TRC had been issued by the Mauritian tax authorities, a failure to accept it would be an indication of breakdown in the faith reposed by the GoI in the Government of Mauritius. Further reliance was placed on the SC decision in UoI & another *v.* Azadi Bachao Andolan (2004) 10 SCC 1, wherein it was held that:

- Based on a harmonious reading of sections 4, 5 and 90 of the Act, provisions of a tax treaty would override provisions of the Act.

- Circulars issued by the CBDT were binding on all officers and employees employed in the execution of the Act
  - Circular No. 682/1994 reiterated the provisions of the India-Mauritius tax treaty that income derived by a Mauritian resident from alienation of shares in an Indian company would be liable to capital gains tax only in Mauritius.
  - Circular No. 789/ 2000 clarified that the TRC issued by the Mauritian Tax Authorities would constitute sufficient evidence of residency as well as beneficial ownership of the Mauritian entity for applying the tax treaty.
  - "Liable to tax" was not the same as "pays tax". Relying on the OECD Model Convention, 1977, the argument that double taxation could be avoided only when tax was actually paid in one of the contracting states could not be accepted.
  - Further while analysing the legality of 'treaty shopping' (i.e., act of a resident of a third country of take advantage of fiscal treaty between two contracting states), the SC held that if the intention of policy makers was to preclude the resident of a third State from the benefits of tax treaty between two contracting states, then a suitable limitation of benefit to that effect would have been incorporated in the tax treaty (as in the case of Indo-US tax treaty). The SC further held that entering into a treaty and terms and conditions thereof were the sovereign functions of a state, and thus, such decisions and their legality should have been left to policymakers.

The HC further brought to notice proposed sub-section 5 to section 90 (then proposed to be introduced *vide* Finance Bill, 2013) which stipulated that a TRC would be a necessary but not sufficient condition for claiming relief under the tax treaty. However, the sub-section was never implemented, since it would have affected the validity of Circular No. 789/ 2000 issued by the CBDT. The Finance Ministry, through a clarification dated 2 March 2013, also clarified that the TRC produced by a resident of a contracting state would be acceptable as evidence of residency in that contracting state, and that the ITA in India would not go behind the TRC and question the TRC holder's residential status.

Editor's note

The Punjab & Haryana HC reversed the AAR ruling in the petitioner's case and held that a TRC issued by the Mauritius Tax Authorities was sufficient evidence of residency, and accordingly, relief for capital gains tax available under the India-Mauritius tax treaty to a Mauritius resident having a valid TRC, could not be denied.

Permanent Establishment

Advertisement collection agent of a foreign broadcasting company does not create PE in India; arm's length remuneration to agents extinguishes further attribution to PE

DIT v. B4U International Holdings Limited [TS-246-HC-2015 (Bombay)]

The taxpayer's advertisement collecting agents in India did not create a dependent agent PE under the India-Mauritius tax treaty. Further, where an Indian agent had been remunerated at an ALP, nothing further was left to be taxed in the hands of the foreign enterprise.

Facts

The taxpayer was a non-resident company incorporated in Mauritius, engaged in the business of broadcasting television channels. The taxpayer appointed two Indian companies as its collecting agents in India. Its income consisted of collections from time slots given to advertisers from India through its agents. The taxpayer filed its tax return claiming that it did not have a PE in India, and therefore had no tax liability in India. The TO rejected the taxpayer's contention and held that affiliate entities were basically extensions of the taxpayer, and constituted PEs of the taxpayer in India. The CIT(A) and the Tribunal noted that the taxpayer carried out all activities from Mauritius,

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and that all contracts were concluded in Mauritius. The only activity that was carried out in India was incidental or auxiliary/ preparatory in nature, which was carried out in a routine manner as per directions of the principal, without application of mind. Hence, the Indian companies were not dependent agents of the taxpayer. The tribunal had also held that where the agent was remunerated at ALP, nothing further was left to be taxed in India.

Held

The Tribunal had rightly held that the Indian companies were not decision makers, nor did they have the authority to conclude contracts. Hence, Article 5(4) of the tax treaty was not attracted. The HC had relied upon the decisions in DIT *v.* Morgan Stanley & Co. [2007] 292 ITR 416 (SC) and SET Satellite (Singapore) Pte Limited *v.* DDIT [2008] 307 ITR 205 (Bombay) to hold that the Tribunal's conclusion was consistent with the facts, and the principles of law laid down were neither perverse nor vitiated by any error of law. The Tribunal had rightly dealt with the Revenue's alternate argument by referring to the CBDT's Circular No. 742 dated 2 May 1996 and taking 15% to be the basis for ALP.

Editor's note

In the context of taxation of foreign broadcasting companies, the issue of existence of a dependent agent on account of advertisement collection agent has been the subject matter of considerable litigation.

The HC, on interpreting the India-Mauritius tax treaty, has held that no dependent agent PE of foreign company existed in India. The judicial precedents laid down in Morgan Stanley and SET Satellite cases (Supra), that the arm's length remuneration of the agent extinguishes any further taxation in the hands of a non-resident, has been applied in this judgement.

Minimum Alternate Tax

MAT under section 115JB not payable on receipts that do not form part of total income

Shivalik Venture Private Limited v. Dy. CIT [2015] 60 taxmann.com 314 (Mumbai-Tribunal)

Capital gains arising on transfer of capital assets from holding companies to their wholly owned subsidiaries, which were not liable to tax under section 45 read with section 47(iv) of the Act, should be excluded from computation of book profits for levying MAT under section 115JB of the Act.

Facts

The taxpayer, an Indian company, was engaged in the business of building and developing properties. It had a wholly owned Indian subsidiary, SVRL. The taxpayer held a land parcel and development rights attached to it. During FY 2008-09, the taxpayer transferred a part of the development rights to SVRL, and disclosed the long-term gains on such transfer as "extra- ordinary income" in its P&L accounts for the year. The taxpayer included the following note in the Notes to Accounts:

"During the year, the company has derived a surplus over cost of acquisition of assets held by it as CWIP amounting to INR 3.0024 billion. In view of the fact that it was a capital receipt, and the transaction was not regarded as a transfer under the Act, the company interprets that since it was not in the nature of income, it did not come within purview of section 115JB.

The company interpretation on the matter of applicability to MAT on such book profits was also supported by opinion of the experts which were taken on the issue."

Section 47(iv) of the Act provided that the transfer of capital assets from companies to their wholly owned subsidiaries should not be regarded as a 'transfer' under section 45 of the Act. Consequently, the taxpayer considered that it was not liable to tax on capital gains arising on such transfer. The taxpayer also did not consider the profits on transfer of development rights to be part of 'book profits' for computing MAT under section 115JB of the Act. The TO and CIT(A) disagreed with the taxpayer's position, and included such gains as part of 'net profit' for the purpose of computing the 'book profit' under section 115JB of the Act.

Held

The Tribunal set aside the CIT(A)'s order and directed the TO to exclude the capital gains from the computation of 'book profits' on the following grounds:

- Notes to Accounts had to be considered as part of the P&L Account and had to be adjusted with the profit to arrive at the book profit:

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- Section 115JB(2) required that the P&L Account had to be prepared in accordance with Part II of Schedule VI to the Companies Act, 1956, and therefore the interpretation given to provisions of the Companies Act would be relevant.
- The Delhi HC had confirmed this view in CIT *v*. Sain Processing & Weaving Mills (P) Limited [2010] 325 ITR 565 (Delhi).
- Therefore, profits arising on transfer of capital asset by a holding company to its wholly-owned subsidiary company, as specified in the Notes to Accounts, had to be excluded while computing book profit under section 115JB of the Act.
- For making this adjustment, a specified inclusion of such adjustment in 'increase' or 'reduction' given in Explanation 1 to section 115JB of the Act was not required, as the "net profit" itself was adjusted at the source level.

- Profits from a transaction, which were not 'income' as defined under section 2(24) of the Act, should not be included in computation of 'book profit' under section 115JB of the Act.
  - Section 10 of the Act provided exemptions to certain receipts from being included in total income, which would otherwise be considered as income under section 2(24).
  - The legislature had provided similar exemptions, except for certain exclusions, from 'book profit' under section 115JB. The legislature maintained parity between "total income" and "book profit" in respect of exempted income. Extending the same logic, an item of receipt not covered under the definition of 'income' included in total income could not be included in book profit under section 115JB of the Act.
  - Section 47(iv) of the Act provided that any transfer of capital asset by a company to its wholly owned subsidiary company was not regarded as 'transfer', and therefore, gains on such transfers were not chargeable to tax under section 45 of the Act. Hence, such gains would not be covered as 'income' under section 2(24) and did not enter the computation provisions of the Act.
- The decision of the Special Bench in Rain Commodities Limited *v.* DCIT [2010] 40 SOT 265 (Hyderabad) (SB) was distinguishable and therefore not applicable.

Editor's note

The Tribunal has allowed the appeal on three grounds:

- *Profit as per P&L Account is to be adjusted for what is stated in Notes to Accounts.*
- *All exempt income, even though not covered under section 10 of the Act, which is allowed to be excluded under normal provisions of the Act, should also be allowed to be excluded from computation of 'book profit' under section 115JB of the Act.*
- *Special Bench decision is distinguishable on facts.*

In view of the SC decision in Apollo Tyres Limited v. CIT [2002] 255 ITR 273 (SC), wherein it was held that once the accounts were in accordance with Part II of Schedule VI to the Companies Act, further adjustment was allowed only for matters provide under section 115JB of the Act, this decision requires further consideration.

Portfolio management

Investment through PMS not a business activity; investment in shares using borrowed funds not relevant for characterisation of income

CIT v. Kapur Investments Private Limited [2015] 61 taxmann.com 91 (Karnataka)

- *Profit from investments made through professionally managed PMS did not mean that the taxpayer was conducting a 'business' of investment in shares; and*
- *The Act did not prohibit the taxpayer from making investments in capital assets using borrowed funds. Hence, this fact was not relevant when determining the characterisation of income earned from the transfer of shares.*

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Facts

The taxpayer, engaged in the business of finance and films, had invested in shares through a PMS, using borrowed funds. In its ROI, gains arising from the transfer of shares were offered to tax as 'capital gains'. In view of the frequency of the transactions, the TO characterised the exit gains as business income. On further appeal, the CIT(A) and the Bangalore Tribunal decided in favour of the taxpayer.

Held

The HC relied on the Delhi HC decision in Radials International *v.* ACIT [2014] 367 ITR 1 (Delhi), to hold that the investment made by the taxpayer through a PMS which may deal in the taxpayer's shares to derive maximum profits, could not be regarded as the taxpayer's business. It would only be a case of a more careful and prudent mode of investment. Thus, exit gains from transfer of shares were taxed as capital gains.

As regards the second issue, the HC held that the Act did not restrict the taxpayer from investing in capital assets by using borrowed funds. Hence, use of borrowed money could not be the determining factor for characterisation of the income. Further, the HC held that the Tribunal's findings were in conformity with the CBDT's guidelines in its Circular No. 4, dated 15 June 2007.

Editor's note

The HC has laid down an important principle, that borrowing by the taxpayer is not relevant for determining the characterisation of income from the transfer of securities.

As per the principles laid down by the CBDT in its Circular no. 4 dated 15 June 2007 and various conflicting judicial precedents for determining the characterisation of income, the total effect of all principles needs to be considered. This latest decision of the HC may serve as a guiding principle, but the facts and circumstances of each specific case should be considered to analyse the total effect of all the principles discussed in Circular no. 4 dated 15 June 2007.

Notifications/ Circulars

Dividend of foreign companies

CBDT issues circular on taxation of dividends issued by foreign companies deriving value substantially from India

Circular No. 4/2015 [F. No. 500/17/2015-FT&TR-IV] dated 26 March 2015

The CBDT has issued a circular that deals with the controversial question as to whether dividends paid by a foreign company would be taxable in India under Explanation 5 to section 9(1)(i) of the Act, if the shares derive their value substantially from the assets situated in India. The CBDT has accepted that such an extended application of the provisions of the Act may result in (an unintended) taxation of dividend income declared by a foreign company outside India.

This may cause double taxation and would be contrary to the generally accepted principles of source rules as well as the object and purpose of the amendment made by the Finance Act, 2012.

The CBDT has stated that the purpose of the amendment of section 9(1)(i) of the Act was to tax gains having economic nexus with India. Since the declaration of dividend by a foreign company outside India does not have the effect of transfer of any underlying assets located in India, such dividends would not be deemed to be income accruing or arising in India by virtue of the provisions of Explanation 5 to section 9(1)(i) of the Act, even if the shares derive their value substantially from assets situated in India.

Editor's note

This circular may be useful where dividends are paid by offshore funds to their investors/ limited partners.

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Withholding tax

Clarification on the amount of disallowance on failure to withhold tax on payments to a non-resident

Circular No. 3/ 2015 F. No. 225/201/2014-ITA.II dated 12 February 2015

According to section 40(a)(i) of the Act, while computing the income chargeable under the head 'profits or gains of business or profession', any interest, royalty, FTS or other sum chargeable under the Act, either payable in India to a non-resident (not being a company)/ a foreign company, or payable outside India, shall be disallowed on failure to comply with the withholding provisions. In other words, disallowance on 'other sum chargeable' was triggered when the taxpayer failed to withhold tax as per the provisions.

Earlier, the CBDT had issued an instruction (Instruction no. 2/ 2014 dated 26 February 2014), clarifying whether tax had to be withheld on the entire sum being remitted to a non-resident, or on only the portion representing the sum chargeable to tax, particularly if no application had been made under the Act to determine the sum chargeable to tax. The instruction clarified that the taxpayer had to be considered as a taxpayer-in-default, only after determining its compliance with reference to the 'appropriate proportion' of income determined with regard to the nature of remittance, income component, or any other fact relevant to determine such appropriate proportion of the payment.

According to the clarification issued in this circular, the amount of disallowance of 'other sum chargeable' under the disallowance provisions was interlinked with the sum chargeable to tax as provided under the Act. Thus, the 'appropriate proportion' of the sum determined as per the Instruction shall form the basis for disallowance of the 'other sum chargeable'. Further, if the taxpayer or the recipient has made an application to the TO to determine the 'other sum chargeable', then such determination shall form the basis for disallowance.

Minimum Alternate Tax

No MAT on Foreign Portfolio Investors

PIB Press Release dated 1 September 2015

The Indian Revenue authorities had proceeded to levy MAT on FPIs in the tax audit cycle for the FY 2011-12. This move of the Revenue officers had created huge concerns amongst the foreign investor community. To allay concerns of the stakeholders, the Finance Minister of India constituted a the Committee under the chairmanship of Justice A.P. Shah to examine legacy tax issues, including the issue of levy of MAT on FPIs for the period prior to 1 April 2015.

The Committee, after extensive deliberations, discussions and in-depth study, submitted its final report to the Government. The Government considered the recommendations of the Committee at length and, at a press conference held on 1 September 2015, the Finance Minister communicated its acceptance of the Committee report.

The recommendations of the Committee to the Government were:

- The Government should either amend the MAT provisions clarifying its inapplicability to FPIs; or
- The CBDT should issue a circular clarifying the above.

To give effect to the recommendations of the Committee, the Finance Minister stated that necessary amendments to the income tax law would be introduced in the next session of the Parliament. The amendment proposes to clarify that MAT provisions will not apply to FPIs that do not have a place of business/ PE in India. Pending such amendment, the CBDT would issue a circular to the Revenue officers conveying decision of the Government accepting recommendations of the Committee.

Separately, in response to a question regarding levy of MAT on foreign companies (other than FPIs), the Finance Minister clarified that the scope of the Committee's report was restricted to FPIs, and the issue of levy of MAT on other foreign companies shall be decided by the SC.

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Real Estate Investment Trusts

REITs to be eligible financial instrument under FEMA

PIB Press Release dated 6 May 2015

Background

- In order to promote funding of the infrastructure sector, the Indian Finance Minister, in his Budget speech in July 2014, proposed the introduction of REITs and a modified REITs structure, i.e. InvITs. The SEBI notified the much awaited REIT/ InvITs regulations in September 2014.
- The actual investment in REITs has not occurred, as the FDI policy, Foreign Exchange Management Act, 1999 and the regulations framed thereunder did not permit foreign investment in completed rent-yielding real estate projects. Consequently, entities registered and regulated under the REITs/ InvITs Regulations notified by SEBI were not able to access foreign investments.

Key amendment

- The press release states that the intent to introduce REITs is to reduce the pressure on the Indian banking system, which is the primary source of funding to the real estate sector, to help free up existing funds of banks and to encourage construction activities.
- The Union Cabinet, *via* a press release, has now announced its approval of REITs being considered as an eligible financial instrument/ structure under the exchange control regulations to attract long-term finance from foreign and domestic sources, including NRIs making available fresh equity to the real estate sector.

The press release only makes reference to REITs, and there is no specific mention of InvITs. This could result in uncertainties as to whether foreign investment would be allowed in InvITs.

Foreign Account Tax Compliance

Indian Government notifies rules for FATCA reporting; due date for 2014 reporting set at 31 August 2015

Notification No. 62 [F. No. 142/21/2015 TPL] dated 7 August 2015

The Indian Government signed an IGA with the US on 9 July 2015 to implement the FATCA in India. According to the IGA read with the FATCA provisions, FFIs in India are required to report tax information about US account holders to the Indian Government which would, in turn, relay that information to the US IRS.

Further, the US IRS will provide similar information about Indian citizens having any accounts or assets in the US. This automatic exchange of information is scheduled to begin on 30 September 2015.

Following the signing of the IGA on 9 July 2015, the Indian Government enacted rules relating to FATCA reporting in India.

The rules have been divided into three specific segments which deal with various aspects of the FATCA reporting regime as follows –

- Rule 114F – Definition of the various terms referred to in the rules;
- Rule 114G – Information to be maintained and reported; and
- Rule 114H – Due diligence requirement.

Editor's note

The Indian Government has quickly come out with the rules for implementation of FATCA and has notified the reporting framework and due diligence requirements.

- *Other regulators such as RBI, SEBI and IRDA are expected to come out with specific guidelines for implementation of FATCA with reference to the notification issued by the CBDT.*
- *Filing of the FATCA Report is expected to be made in .xml format similar to the tax return filing process, for which the software related modalities are expected to be notified shortly.*
- *The FIs are expected to notify their officials as Designated Director and Principal Officer respectively in-charge of FATCA implementation.*
- *Non-compliance with the FATCA requirements would attract penal provisions prescribed under the Act. Specific penalties will be levied for failure to provide a statement of financial transactions or reportable accounts. Inaccurate reporting will also attract penal provisions.*
- *FIs are also required to obtain a separate registration number from the Principal Director General of Income-tax (Systems).*

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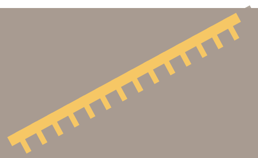
- *Portability of pre-existing mutual fund accounts under the FATCA regime needs to be implemented and watched for probable challenges.*

Importantly, the information collated by India or the US or any other country is likely to be used by the respective Revenue authorities in initiating audits. They would like to map it with the disclosures and information furnished by the taxpayer in his income-tax return. Follow on consequences about interest or penalties to the taxpayer in either jurisdictions may arise in case of non-compliance. Accordingly, the implications of the above regime needs also be evaluated carefully from an individual perspective.

Further, it is also important for the Indian FIs to have a robust implementation plan, and appropriate formal customer interactions to confirm the details shared under this regime.

Immediate reporting deadline of 31 August 2015 for the calendar year 2014 was mandated to enable the Indian Government to meet the deadline for exchange of information with the US IRS.



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Transfer Pricing

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Case Law

Reimbursement of Salary

Reimbursement of salary cost for seconded employees who are on high level managerial/executive positions is subject to withholding tax obligation

Food World Supermarkets Limited v. DDIT (International taxation), Circle-1(1), Bangalore [2015] 63 taxmann.com 43 (Bangalore-Tribunal)

Facts

The taxpayer, Food World Supermarkets Limited, is an Indian company (I Co.) engaged in the business of ownership and operation of supermarket chain in India. It needed personnel to assist with its operation in India. It approached a Hong Kong based company (F Co.), being in identical business activity to assign certain personnel to assist. The taxpayer entered into an agreement with F Co. for secondment of its 5 employees to India.

Under the agreement, the F Co. paid the salary to expatriates in Hong Kong. The taxpayer was responsible for complying with the requirements of withholding tax and reporting obligations under the Indian tax laws, on the compensation paid to the expatriate. The F Co. later raised a debit note for salary amount and the taxoayer reimbursed the same amount without withholding tax, given that the taxes on said salary income were duly deducted.

The TO held that the remittance made by the taxpayer constitute as FTS under section 9 (1) (vii) of the Act and the same is chargeable to tax on gross basis. The taxpayer was liable to withhold tax under section 195 of the Act at 10 percent. Accordingly, the TO treated the taxpayer as taxpayer- in- default for not withholding tax at source. On appeal the CIT(A) affirmed the order of the TO. Taxpayer filed an appeal before the Bangalore Tribunal.

Held

The Bangalore Tribunal examined the agreement in detail and held that the secondees are not ordinary employees but they are deputed on high level managerial/ executive positions because of their expertise and managerial skills in the field. The secondees are assigned by F Co. and there is no separate contract of employment between taxpayer and the secondees. The secondees are under legal obligation as well as employment of F Co. and assigned to the taxpayer only for a short period of time. The secondees can claim their salary only from the parent company i.e. F Co. and not from the taxpayer. Thus the expatriates were performing their duties for and on behalf of F Co.

The secondees were rendering managerial and highly expertise services to the taxpayer and the payment for such services is in the ambit of FTS defined in explanation 2 to section 9(1)(vii) of the Act. Reliance was placed on Centrica ruling of Delhi HC where identical issue was examined and held that while dealing with the definition of FTS under the tax treaty between India and United Kingdom (UK) that the services of the personnel deputed under the secondment agreement were in the nature of managerial consultancy services to the taxpayer. The definition under India – UK tax treaty as well as the definition under the Act is almost identical. Therefore, the payment made to F Co. partakes the character of FTS as per the definition of under explanation 2 to section 9(1)(vii) of the Act. The concept of income includes positive as well as negative income or nil income. In the case of payment being FTS or royalty as per section 9(1) of the Act it is irrelevant whether any profit element in the income or not.

The decision in the case of IDS Software Solutions and Abbey Business Solutions would not apply as there is judgement on identical issue in case of Centrica by Delhi HC supra. The secondment of an expatriate constitutes a service PE, however there is no treaty between India and Hong Kong and it has not been examined by the TO so, the issue was referred back to TO for proper examination of all the relevant facts as well as tax provisions to determine whether it constitute service PE in India.

Editor's Note

This judgement relies on the Delhi HC ruling in Centrica case supra and seeks to tax the reimbursement of salary cost paid by an overseas entity. However, the observations are very much based on the clauses of the agreement and accordingly, it depends upon the facts of each case whether the secondment structure results in FTS or PE etc. These rulings do call for

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the need for the Corporates to relook at their secondment structures in order to determine any risk emerging out of secondment arrangements and the steps they need to take to address them.

Capital receipts

Compensation received on denial of employment is a capital receipt and cannot be taxable

Commissioner of Income Tax-IV v. Pritam Das Narang [(2015] 61 taxmann.com 322 (Delhi)]

Facts

Taxpayer was to be employed as CEO by M/s ACEE Enterprises (ACEE). However, due to sudden change in its business plan ACEE was unable to take taxpayer on board. ACEE paid a compensation of INR 19.5 million to the taxpayer as a "one-time payment for non-commencement of employment as proposed".

The taxpayer did not offer this compensation to tax while filing the return of income. The TO rejected the claim of taxpayer on the ground that under section 17(3) (iii) of the Act receipt by the taxpayer of any sum from any person prior to his joining with such person was taxable. The TO was of the view that the condition of a pre-existing relationship of employer and employee was done away with by the use of the words "by any taxpayer from any person" introduced by the Finance Act, 2001 with effect from 1 April, 2002. The TO concluded that the payment was taxable under the head 'salary'. Additions of INR. 19.5 million were made to the returned income and penalty proceedings were also initiated.

The CIT(A) deleted the additions by concluding that the receipt in the hands of the taxpayer was *bonafide*. On appeal by the revenue, the Tribunal affirmed the order of the CIT(A) and held that the taxpayer was compensated for denial of opportunity to be employed by the prospective employer and therefore, the amount paid could not be said to be in lieu of the salary and a benefit of employment.

Held

The HC held that section 17(3)(iii)(A) of the Act pre-supposes the existence of an employment, i.e., a relationship of employee and employer between the taxpayer and the person who makes the payment of "any amount" in terms of section 17 (3) (iii) of the Act. Likewise, section 17(3)(iii)(B) of the Act also pre-supposes the existence of the relationship of employer and employee between the person who makes the payment of the amount and the taxpayer. It envisages the amount being received by the taxpayer "after cessation of his employment". Therefore, the words in section 17(3)(iii) of the Act cannot be read disjunctively to overlook the essential facet of the provision, *viz*., the existence of 'employment' i.e. a relationship of employer and employee between the person who makes the payment and the taxpayer. HC accordingly held that such compensation could not be taxed as 'profits in lieu of salary' and agreed with the view taken by CIT(A) and the Tribunal that this was a case where there was no commencement of the employment and that the offer by ACEE to the taxpayer was withdrawn even prior to the commencement of the employment. Thus, the amount received by the taxpayer was a capital receipt and could not be taxed under the head 'Profit in lieu of salary'. The HC further held that the other plea of the Revenue that the said amount should be taxed under some other head of income, including 'income from other sources', is also unsustainable. It was a capital receipt that could not be taxed as income under any other head.

Editor's Note

The provisions of clause (iii) section 17(3)(A) of the Act contemplates only taxation of joining bonus received by employee. Such provision excludes from its purview any compensation which is received due to non-commencement of employment. Any compensation received due to non-commencement of employment is a capital receipt which cannot be taxed even under any other head like income from other sources.

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Withholding tax

No Penal consequence on the taxpayer for delay in filing of return due to failure of the deductor to pay the withholding tax in time

Zulfikar Jeewanjee Moriswala v. Dy. CIT [(2015) 61 Taxmann.com 364 (Bombay)]

Facts

The taxpayer being a non-resident Indian along with other resident co-owner sold an immovable property to Vardhaman Developers Limited (Company) for a consideration of INR 90 million. The property was sold in February 2014. The company after withholding tax @ 20% paid the balance consideration to both the taxpayer and the co-owner. However, the company failed to deposit the tax with the Government treasury. The taxpayer *via* notice dated 21 July 2014 requested the company to deposit the tax with the government. It was also stated to the company that the non-deposit would preclude him from uploading the return of income for the AY 2014-15 which was due to be filed on 31 July 2014. Subsequent to it, the taxpayer could not upload his return of income.

The taxpayer also brought the aforesaid facts to the notice of the revenue [CIT (TDS)] but no action was taken by the revenue against the company. The taxpayer filed writ petition seeking a direction to the revenue to accept their return of income for the AY 2014-15.

Held

The court observed that the company has paid the TDS to the Government treasury with interest. Therefore, the court enabled the taxpayer to upload his return of income and instructed that no penal or financial consequence would visit on account of delay in uploading his return of income.

Editor's note

This ruling will bring relief to the taxpayers from penalty and interest for delay in filing of return of income where the deductor fails to deposit the tax withheld with the Government in prescribed time limit.

Salary income from stock option awards

Proceeds of stock options cannot be taxed in the hands of not ordinary resident if not related to the period of services rendered in India

Anil Bhansali v. ITO [TS-15-ITAT-2015(Hyderabad-Tribunal)]

Salary income attributable to services rendered in India is taxable in India, in case of a not ordinary resident as per the Act.

Facts

The taxpayer, an individual employed with Microsoft India (R&D), had filed his tax return for AY 2007-08 as "resident but not ordinary resident" (RNOR) in which he declared a total income of INR 22.57 million (approx.) under the head salary income. The taxpayer was granted stock option awards between August, 2002 to September, 2005 by his former employer, i.e. Microsoft, USA. His employment with Microsoft, India began with effect from 1 January 2004.

On the verification of the information available on record, the TO noticed that a perquisite amounting to INR 15.03 million (approx.) is reflecting in the tax withholding certificate issued by the employer. The employer had also withheld tax at source on the same. On subsequent verification of other details like bank statement, the TO observed that the taxpayer has received certain proceeds in foreign currency converted into INR 18.1 million (approx.) during the relevant FY. The TO further observed that such proceeds were more than the value of perquisites which was declared in the tax withholding tax certificate issued by the employer for the relevant FY. Accordingly, the TO initiated re-assessment under section 147 of the Act, by issuing a notice under section 148 of the Act.

With respect to such proceeds reflected in the bank statement, the taxpayer submitted that the stock options were vested in the FY 2006-07 and the stock awards were received in his U. S. Brokerage account. The taxpayer was RNOR in India during the FY 2006-07. The taxpayer further contended that the stock awards vested pertains to services rendered by the taxpayer in both USA and India both and the taxable portion of stock award has been computed based on period of his services rendered in India between the date of grant and vest. The remaining portion of stock award which pertains to his services rendered in USA has been claimed as exempt in the tax return filed. The taxpayer contended that income has been computed

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by taking into account the taxable income which accrue or arose in India as per the provision of the Act as well as India–USA tax treaty.

The TO, not being convinced with the explanation of the taxpayer, made an addition of the entire income related to stock option. The CIT(A) confirmed additions made by the TO. Aggrieved by the order, the taxpayer preferred an appeal before the Hyderabad Tribunal.

Held

The Tribunal observed that, in case of an individual who is RNOR in India in terms with section 6(6) of the Act, the income accruing or arising outside India shall not be included in the total income of the relevant previous year unless it is derived from a business controlled in or a profession set-up in India. On the basis of stay details submitted by the taxpayer it was held by the Tribunal that the taxpayer qualifies to be a RNOR in India for the AY 2007-08. The Tribunal further observed that "income under the head salaries" shall be deemed to accrue or arise in India if it is earned in India towards services rendered in India as per proviso of section 9(1)(ii) of the Act.

It was further observed that salary derived by a resident of USA in respect of employment exercised in USA shall be taxable in USA in light of Article 16(1) of India–USA tax treaty. Since the stock option is derived from the employment exercised in both USA and India, the income derived there from has to be apportioned based on the period of services rendered in India between the date of grant and vest.

The Tribunal observed that amount credited to the bank account are in the nature of mere remittances to India from taxpayer's post tax savings located in USA and the entire amount cannot be made taxable only because the money was received in India. The Tribunal also observed that merely because the employer withheld tax at source on the entire stock option income on a conservative basis, it alone could not lead to conclusion that the entire stock award income would be taxable in India.

The Tribunal, held that the TO and the CIT(A) failed to examine the facts properly. Hence, the matter was remitted back to the TO for fresh consideration after providing a reasonable opportunity of being heard to the taxpayer.

Editor's Note

This judgement reiterates that only that portion of income derived from stock option awarded to RNOR is taxable in India which is attributable based on the period of services rendered in India between the date of grant and vest. The balance portion of stock award income which pertains to the services rendered outside India is not taxable in India.

Capital gains

Investment in 'a residential house' suffices; need not be 'new residential house' for claiming deduction under section 54 of the Act

DCIT v. Sri Vidyasagar Dontineni [TS-51-ITAT-2015 (Hyderabad-Tribunal)]

Facts

The taxpayer, an individual, was a Managing Director of Sec Industries Private Limited. He has filed his tax return of income for the AY 2009-10 and 2010-11 declaring an income of INR 26.6 million (approx.) and INR 12.7 million (approx.) respectively. As per the tax return filed, the taxpayer declared a LTCG from sale of flats INR 7.94 million (approx.) and INR 9.91 million (approx.) for AY 2009-10 and 2010-11 respectively. The taxpayer claimed an exemption of INR 7.94 million (approx.) and INR 8.54 million (approx.) for AY 2009-10 and 2010-11 respectively on account of investments made for the construction of residential house.

During the assessment proceeding for AY 2009-10, the TO observed that INR 7.811 million (approx.) was incurred for providing amenities in the existing house which was not essential to make the house habitable. The TO further contend that investment made was not for the construction of new house and therefore disallowed the exemptions under section 54 of the Act claimed by the taxpayer and correspondingly disallow the exemption even in AY 2010-11.

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The taxpayer filed an appeal before the CIT(A) challenging the disallowance made by the TO. Based on additional evidence filed by the taxpayer, the CIT(A) held that even though there was an old structure already in existence on the land, the same was demolished to make the house habitable and further states that section 54 of the Act merely states the period by which construction should be completed and accordingly allow the exemption under section 54 of the Act to the extent the expenses incurred to make the house habitable. The revenue preferred an appeal before the Hyderabad Tribunal.

Held

It was held that, for claiming deduction under section 54 of the Act, it is **not** necessary that residential house has to be "only new residential house". The Tribunal further held that the date of commencement of construction is also not relevant for claiming exemption under section 54 of the Act. What is relevant is the date of completion of construction as well as the period of investments. Accordingly, the Tribunal concluded that the taxpayer is eligible for deduction under section 54 and confirm the order passed by the CIT(A).

Editor's Note:

This judgement reiterates that investment in purchase or construction of a 'residential house' is necessary and such house need not be a 'new residential house'. The relevance has to be given to the completion of construction and not the date of commencement of construction.

Notification/ Circulars

Administrative Charges

Reduction in administrative charges payable under the Employees' Provident Fund Scheme from 1.10 % to 0.85 %

The Ministry of Labour and Employment, Government of India through its notification dated 2 February 2015 has reduced the rate of administrative charges payable under the Employees' Provident Fund Scheme, 1952 from 1.10% to 0.85% of the pay subject to a minimum sum of INR 75 per month for every non-functional establishment (having no contributory member) and INR 500 per month for other establishments.

The administrative charges payable by the employer under Employees' Deposit linked Insurance Scheme, 1976 remained unchanged at 0.01 % of the monthly salary. However, the minimum administrative charges payable under the above scheme is set at INR 25 for non-functional establishment and INR 200 for other cases respectively.

The revised rates of administrative charges are applicable from 1 January 2015.

Editors' note

The reduction in rate of administrative charges will reduce cost incurred by companies. This is not applicable to establishments who run their own private PF trust.

TDS on Provident fund withdrawal

EPFO to deduct tax on premature withdrawal from Provident fund from 1 June, 2015

Notification No. WSU/ 6(1)2011/ IT/ Vol-IV

The Union budget 2015-16 presented by Government of India proposed to simplify the withholding tax on withdrawal from the Indian social security (provident fund). In case of premature withdrawal of INR 30,000 or more, tax will be withheld at the rate of 10% or at a maximum marginal rate where PAN is not furnished by the employee. This provision has come into effect from 1 June 2015.

The EPFO subsequently issued an internal circular instructing its field offices to deduct tax on withdrawal of the PF accumulation.

The instruction relating to the deduction of tax on PF withdrawal are summarised below:

Editor's note

Employees withdrawing accumulated PF money equal to or

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Requirement of deduction of tax	Situation	Rate of tax
Tax will be withheld at the time of payment of accumulated PF balance	• If employee withdraws more than or equal to INR 30,000 and, • 5 years of continuous services is not rendered.	If PAN submitted - 10% If PAN not submitted – 34.608%
Tax will not be withheld	• If PF withdrawn is less than INR 30,000, or • If PF is withdrawn after a period of 5 years of continuous service, or • If Form 15G/ 15H along with the PAN is submitted, or • If PF balance is transferred from one account to another, or • If PF balance is withdrawn on termination of service due to ill health of member/ discontinuation of business by employer/ completion of project/ other cause beyond the control of the member	• Already high cost of PPPs as a procurement tool can leave less funding for costs beyond infrastructure

more than INR 30,000 needs to mention their PAN in the withdrawal form to avoid higher withholding tax. Employers who manage their own private provident fund trust also need to ensure the tax is withheld in accordance with these provisions.

Income tax return forms

Government eases process of e-filing returns using EVC

Notification No. 2/ 2015 dated 13 July 3015

Taxpayers have been using digital signatures for paperless filing, or forwarding their ITR V with the CPC after e-filing their ITR. This year, Government announced an alternate way of paperless e-filing *via* EVC.

Key highlights of EVC process are summarised below -

Who can use EVC

The EVC mechanism is meant to verify the identity of the person furnishing the return of income (called 'the verifier'). The verifier can be an individual who is seeking to verify his own return or that of a Hindu Undivided Family of which he is the Karta in the ITR form nos. ITR-1, ITR-2, ITR-2A, ITR-4 or ITR-4S; or any person[1] who is seeking to verify returns filed in form nos. ITR-5 or ITR-7

Features of EVC

- The EVC is a 10 digit alpha numeric code which is unique for each PAN, and is generated for the purpose of electronic verification of the person in the e-filing website

https://incometaxindiaefiling.gov.in.

- Each EVC can be used to validate only a single return of the taxpayer, irrespective of the year or return filing type, *viz.* original or revised.
- An EVC is valid for 72 hours.

Modes of Generation of EVC

The EVC generation process may vary, depending on the risk category of the taxpayer, method of accessing the e-filing website or interface with third party authenticating entity (like banking institutions). The various methods to generate the EVC are explained hereunder.

- **Net Banking** – Several banks have registered with the income-tax department and provide direct access to

1. ITR-5 or 7 are for use by the following entities: Partnership Firm, Association of Persons, Body of Individuals, Artificial Juridical Person, Co-operative Society or local authority, Trusts and Non-Profit Organizations, etc.

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the e-filing website to a verifier through their internet banking facility. Only those taxpayers would be able to use this facility whose name appear as primary account holders and have a validated PAN (which is the tax registration number) provided as part of the KYC norms of the banks. After logging into their online bank account, the account holder is required choose to be redirected to the e-filing website, where an EVC can be generated. The EVC will be displayed on the screen and also sent to the mobile number registered with e-filing website, which can then be used to verify the return.

- **Aadhaar number** – The UIDAI, upon application and after completion of verification processes, allots a 12 digit number, i.e. an Aadhaar number to all individual applicants. A verifier can use the Aadhaar number to get his identity verified. A taxpayer using this mode has to provide his/ her Aadhaar number for linking with his/ her PAN on the e filing website. When this is done, the details such as name, date of birth, etc. as available in the PAN database are verified with details as available with the UIDAI. Upon successful verification, OT is generated and sent to the verifier's mobile number registered with the UIDAI, which can be then used to verify his/ her return. This OTP is valid for 10 minutes, or for as long as specified by the UIDAI.
- **ATM** – A verifier can generate an EVC through this mode if the verifier's bank is registered with the income-tax department. Either a Debit/ Credit card can be used for generation of EVC. This mode can be used only at ATMs of registered banks, where the option to generate an EVC will be made available. Upon selecting this option on the ATM screen, the bank will communicate this request to the e-filing website, which will generate the EVC and send it to the taxpayer's mobile number registered with the e-filing website. This EVC can then be used to verify the return.
- **Registered email and mobile number** – A verifier can use the e-filing website to generate an EVC, which will be sent to the registered email id and mobile number of the taxpayer as updated by the verifier on his on-line account on the e-filing website. This mode, however, is only available to those whose total income is INR 0.5 million or below and there is no refund claim. This option may further be restricted to taxpayers based on other risk criteria that may be determined from time to time.

For more details, one can refer to the 'e-verification of Returns – User Manual' issued by the income-tax department which explains in detail the step-wise process to generate EVC by different modes.

Editor's note

The EVC mechanism would relieve taxpayers sending signed hard copy of ITR V to the CPC, Bengaluru within 120 days of uploading of the return in the income tax website.

Those taxpayers who have already e-filed an income-tax return without using the EVC process can also use this option to e-verify the acknowledgement through the EVC process, and thus save themselves from the effort of sending a signed hard-copy acknowledgement in ITR V to the CPC, Bengaluru.

ITR Forms

Government notifies new ITR forms for the FY 2014-15

The CBDT notified ITR forms applicable for the FY 2014-15 (AY 2015-16). These return forms, originally notified on 15 April 2015, were amended after taking into account various representations made to the Government after they were first introduced. The key amendments are briefly summarised below:

- Individuals now can use the simpler return form (ITR-1) even if they have exempt income. Earlier, individuals were not allowed to use this form if they had exempt income exceeding INR 5,000. However, individuals having agricultural income exceeding INR 5,000 will still not be able to use Form ITR-1.
- As a measure of relief to individuals/ HUF who do not have income from capital gains, business or profession, foreign assets/ foreign income to be reported, or who have not claimed any relief under any tax treaty India has with other countries, a new simplified return form (Form ITR-2A) has been introduced.

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- Forms ITR-2 and ITR-2A have been made more taxpayer-friendly – they are a mere 3 pages long. Other information will be captured in schedules that are required to be filled only wherever applicable.
- Foreign nationals who qualify as ordinarily resident in India and are on business, employment or student visas are not required to report foreign assets acquired by them during those FYs in which they were non-resident of India, provided they are not deriving any income from such assets during the relevant FY.
- Details of foreign trips and expenditure thereon no longer need to be furnished. The originally notified form had required taxpayers to provide such information.
- IFS codes, name of the bank, nature of account (saving/ current) account numbers of all bank accounts have to be furnished in the returns, but not bank balances. Details of accounts that have been non-operational for over three years need not be reported.
- A new method to file the tax return electronically has been set up by using EVC. Taxpayers now have an option to provide their 12 digit unique Aadhar number in their tax return form and then, instead of sending the signed ITR-V (acknowledgement of electronically filed return) to the CPC at Bengaluru, they can authenticate their returns by using the EVC.
- E-filing of ITR is now mandatory in cases where a refund has been claimed. However, super senior citizens (aged 80 years or more) can file their return in paper form even if there is a refund or their income exceeds INR 500,000.

Editor's note

A large number of salaried taxpayers used Form ITR-1 which they were not able to use earlier where they had exempt income exceeding INR 5,000. Similarly, newly introduced Form ITR-2A eased burden on those taxpayers who have income from more than one house property, as such taxpayers earlier were required to fill Form ITR-2. Form ITR-2 as notified on 15 April, 2015 required detailed reporting requirements in relation to foreign travel which has now been done away with. Similarly, reporting of dormant bank accounts and balances in all Indian bank accounts no longer required.

Ordinarily resident taxpayers need to be more careful as they are required to provide detailed information about their overseas income/ assets in view of enlargement of the scope of reporting in Schedule FA to Form ITR-2. Such taxpayers now need to report full and accurate details about their overseas income and assets, as the Government now has greater focus on black money stashed overseas. This is more relevant now, as the Black Money Taxation Act has come into force with effect from 1 July 2015.

Foreign nationals who are ordinarily resident in India have got some relief, as they are no longer required to report those foreign assets which they had acquired when they were non-resident of India and they have not earned any income from such assets during the relevant tax year.

Interest

CBDT issues circular clarifying that no interest is chargeable on the amount of self -assessment tax paid before the due date of filing the return

Notification No. F. No. 385/ 03/ 2015-IT(B)

The CBDT has issued a circular clarifying that no interest under section 234A of the Act will be charged on the self-assessment tax paid before the due date of filing of India tax return.

Interest under section 234A of the Act is charged in case of default in furnishing return of income. The interest is charged at the specified rate on the amount of tax payable on the total income, as reduced by the amount of advance tax, TDS/ TCS, any relief of tax, deductions, and tax credit allowed under the Act. Since self-assessment tax is not mentioned as a component of tax to be reduced from the amount on which interest under section 234A of the Act is chargeable, interest is being charged on the amount of self-assessment tax paid by the taxpayer even before the due date of filing the ROI.

It has been held by the SC in the case of CIT *v*. Prannoy Roy, [2009] 309 ITR 231 (SC) that the interest under section

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234A shall be payable only on the amount of tax that has not been deposited before the due date of filing of the ITR for the relevant AY. Accordingly, the present practice of charging interest under the section 234A of the Act on the self-assessment tax paid before the due date of filing return was reviewed.

The CBDT has decided that no interest under section 234A shall be charged on self assessment tax paid before the due date of filing of return.

Editor's note

The above circular has removed the ambiguity relating to the calculation of interest under section 234A of the Act.

Black Money

Enactment of Black Money Taxation Act and rules made thereunder

Notification No. S.O. 1791(E) dated 1 July 2015

The FM presented the Union Budget for the fiscal year 2015-16 on 28 February 2015. In his budget speech, the FM acknowledged limitations under existing law and conveyed the considered decision of the current government to enact a comprehensive new law to deal specifically with undisclosed money held abroad. In fulfillment of that commitment, the Undisclosed Foreign Income and Assets (Imposition of Tax) Bill, 2015 was introduced in Parliament on 20 March 2015.

The bill was enacted on 26 May 2015 as 'the Black Money Taxation Act and has been made effective from 1 July 2015.

Any undisclosed foreign income and undisclosed foreign assets detected after 30 June 2015 will henceforth be taxed under the Black Money Taxation Act, and not under Act. Besides the stringent penalties and prosecution, the Black Money Taxation Act contained the provision of a one-time compliance opportunity to those who have undisclosed foreign assets. Where any disclosure is made under one time compliance window, the declarant is required to pay the tax @ 30% and an additional 30% as penalty. No other penalty or prosecution under the Black Money Taxation Act or the Act will be launched in such cases. Such window was available until 30 September 2015.

The key features of the Black Money taxation Act are summarised below:

Scope

- The Act extends to the whole of India and is effective from 1 July 2015.
- It provides for separate taxation in respect of undisclosed foreign income and assets (including financial interest in any entity). Such income will no longer be taxed under the Act.
- An undisclosed asset located outside India (including a financial interest in any entity) will be valued at its fair market value in the year of detection and in the manner as prescribed in the rules.
- The Black Money taxation Act covers all persons who are resident in India in accordance with the provisions of the Act. However, individuals qualifying as RNOR in India are excluded from the scope of the Black Money Taxation Act.

Rate of Tax

- Undisclosed foreign income or assets will be taxed at the flat rate of 30%.
- No exemption or deduction or set off of any carried forward will be allowed.

Penalties

- In addition to the tax payable, the following penalties will be levied.

Prosecution

Nature of default	Quantum of Penalty
Non-disclosure of foreign income and assets	300% of the tax payable
Failure to furnish a ROI before the end of the relevant AY in respect of foreign income or assets (including financial interest in any entity)	INR 1 million
If a return of income is filed but the taxpayer fails to disclose foreign income or assets (including financial interest in any entity) or furnishes inaccurate particulars of the same	INR 1 million
Other defaults such as failure to answer queries, sign statements, attend required meetings or produce books of accounts, etc.	INR 50,000 to 2,00,000
Continuing default in payment of tax (this penalty will be levied irrespective of whether the taxpayer voluntarily paid the required taxes before the levy of the penalty)	An amount equal to tax payable

Prosecution will also be initiated as outlined below for non-compliance:

Nature of offence	Punishment
Willful attempt to evade tax, penalty or interest, chargeable or impossible under the legislation	Rigorous imprisonment - 3 years to 10 years (with a fine)
Willful failure to furnish a ROI before the end of the relevant AY in respect of foreign income or assets (including financial interest in any entity)	Rigorous imprisonment - 6 months to 7 years (with a fine)
If a ROI is filed but the taxpayer fails to disclose foreign income or assets (including a financial interest in any entity) or furnishes inaccurate particulars of the same	Rigorous imprisonment - 6 months to 7 years (with a fine)
Repetition of an earlier convicted offense	Rigorous imprisonment - 3 years to 10 years (with a fine)
Willful attempt to evade payment of tax, interest or penalties	Rigorous imprisonment - 3 months to 3 years (in addition, a fine may be imposed)

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One time compliance opportunity

All resident persons (excluding RNORs) who have undisclosed foreign assets acquired from income chargeable to tax under the Act can make declaration under this compliance window. The declarant is required to pay the tax @30% and an additional 30% as penalty, and no other penalty or prosecution under the Black Money Taxation Act will be launched in such cases. The window to make disclosure in relation to undisclosed foreign assets was available up to 30 September 2015. The taxes and the penalty on such undisclosed foreign assets have to be paid on or before 31 December 2015.

Other related rules

- The provisions related to penalties and prosecution will also apply to the beneficial owners or beneficiaries of such undisclosed foreign income and assets.
- To protect persons holding foreign accounts with minor balances which may not have been reported in tax returns due to oversight or ignorance, any failure to report bank accounts with a maximum balance of up to INR 50 million (in aggregate) at any time during the year will not entail a penalty or prosecution under the Black Money Taxation Act.
- It provides for the levying of interest where a ROI has not been filed or there is a default in payment of advance tax by a taxpayer under the provisions of the Act.

Editor's note

Expatriate employees who may become ROR in India in the near future should keep track of their overseas bank accounts and other assets so that at the time of reporting of such overseas income/ assets arises, the details may be reported accurately

It is also pertinent to note that under the existing provisions, ROR individuals with bank accounts and/ or assets in a foreign country are required to file a return in India even if they do not have any taxable income. If an expatriate employee is accompanied by the spouse with overseas assets in his or her name, then such spouse is under the obligation to file a tax return in India once he or she becomes ROR in India.

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Gain arising on sale of assets by a partnership firm to a company in lieu of share allotment to partners is taxable as capital gains in the hands of the firm

Ana Labs v. DCIT [TS-800-HC-2014(Telangana and Andhra Pradesh)]

Once there is a consideration in terms of money value for the transfer of a capital asset, the capital gain tax liability arises notwithstanding that the actual consideration was paid in a different form or to a third party.

Facts

During 1995-96, Ana Labs (the taxpayer), a partnership firm, sold its assets to a company. The latter discharged the consideration for the transfer by issuing its shares to the partners of the taxpayer. In the absence of receipt of any consideration, the taxpayer did not offer any income to tax. The TO treated the transfer to be covered under section 45(4), which is a charging section for the capital gains arising from the distribution of capital assets upon dissolution of a firm. The CIT(A) also upheld the order of the TO. The Tribunal, based on the facts, held that although the sale took place before the dissolution of the firm and the provisions of section 45(4) of the Act did not apply, the transfer remained taxable under the general charging provision for capital gains, specified in section 45(1) of the Act. Subsequently, the taxpayer filed an appeal before the HC against the Tribunal order.

Held

The Tribunal found that that there was no distribution of assets upon dissolution, and the HC held that this finding did not inevitably lead to the conclusion that there was no transfer of assets made by the taxpayer. The transfer of an asset was taxable under the general charging provision for capital gains specified in section 45(1) of the Act, irrespective of whether the consideration was paid in the form of money or otherwise and irrespective of the person/party who received the consideration. The substratum for section 45(1) was existence of a consideration in money's worth and once such consideration was agreed upon, capital gain tax applied. Further, the HC, based on the facts, confirmed that this case did not involve the succession of the firm by the company.

Editor's note

This ruling reaffirms that the manner or mode of payment of consideration is irrelevant in the context of a charge to capital gain. Capital gains tax is applicable where there is a transfer of a capital asset and the value of the consideration is determined in monetary terms, irrespective of the form or recipient of the consideration. Further, the ruling has clarified that sub-section (1) of section 45 is broader and general charging section whereas other sub-sections of section 45 are cases of specific provision for computation and charge of specified gain or receipt. It is important to note that the judgement in this case was issued prior to the insertion of section 47 (xiiib) which provides, subject to certain conditions, an exemption with regard to the transaction of succession of a firm by a company.

Slump sale *v.* Itemised sale

DCIT v. Tongani Tea Co. Ltd. [TS-647-ITAT-2015(KOL)]

The sale of a tea estate by the taxpayer, involved separate values being assigned to movable property, immovable property etc., and could not be treated as slump sale under section 2(42C). Additionally, the sale was deemed taxable under section 50B merely because in the agreement the transfer was referred to as a "Going Concern".

Facts

The taxpayer was in the business of growing and manufacturing tea and owned two tea gardens. The taxpayer entered into an agreement to sell one of the tea estates as a going concern for a total consideration of INR 180 million. The sale agreement specified the consideration for land and other assets, separately. The agreement pertained to the transfer of specific assets, and not to all the assets and liabilities of the undertaking. Therefore, the taxpayer considered the sale to be an itemized sale.

The TO treated the transaction as a slump sale and computed the tax under section 50B.

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Held

The Tribunal held that the TO was erroneous in regarding the aforementioned sale as a slump sale under section 2(42C) read with section 50B, as:

- The taxpayer provided consideration for the sale of movable properties and immovable properties.
- Not all of the assets and liabilities were transferred.
- The expression, "Going Concern" was a functional qualification as far as the sale of the estate was concerned; it was insufficient for deciding the legal character of the transaction. The meaning of "Going Concern" had to be understood in light of the particular nature of the property being transferred.

Editor's note

The Tribunal has brought out the distinction between a slump sale and an itemized sale. One of the indicators of a slump sale is that the sale is of business in its entirety and on as is where is basis.

Amount received towards goodwill upon giving up a right to carry on the entire business is liable to be taxed as capital gain tax and not as business profit

Elite Orgo Chem Private Limited v. ACIT [ITA No. 2291/ Mum/2010]

Consideration towards self-generated goodwill upon transfer of an entire business and as under the terms of mutual agreement between the seller and the purchaser treated as capital in nature. The Tribunal has distinguished between the taxability of the amount received for giving up the right to carry on any activity in relation to a business vis-à-vis giving up the right to carry on a business.

Facts

Elite Orgo Chem Private Limited (the taxpayer) was an exclusive distributor in India for GN ReSound (GNRS), a Denmark-based company, since 1997. As per the terms of the agreement between the two parties, the taxpayer was to advertise and publicise GNRS products and was also under the obligation to carry out repairs and after sale services. This was the only business carried out by the taxpayer.

As for the agreement for the termination of the distribution agreement and transfer of the taxpayer's business and distribution network to GNRS (transfer agreement) entered during FY 2005-06, the taxpayer was paid a consideration of INR 111.91 million and separately an amount of INR 4.39 million for a non-compete covenant. These amounts were decided by mutual agreement between the taxpayer and GNRS.

The taxpayer offered to tax the amount received towards the non-compete agreement as business income and treated the amount of INR 111.91 million as a consideration for the assignment/transfer of goodwill as provided in different clauses of the transfer agreement.

The TO treated the amount received towards goodwill as compensating the income that the taxpayer could have earned, and thus treated it as business income under section 28(va) of the Act. On appeal, the CIT(A) upheld the TOs order. Aggrieved, the taxpayer preferred an appeal before the Mumbai Tribunal.

Held

The taxpayers' marketing skills, and selling and distribution activities constituted a very significant function of the business. Over the period of 8 years, the taxpayer developed a comprehensive network for the marketing and distribution of GNRS products by appointing various sub-distributors and engaging skilled and qualified technicians for after-sale services. This resulted in the creation of goodwill over the years on account of the marketing network and distribution, even in the absence of its own trademark.

Based on the facts that the entire business of EOPL was transferred, there was an impairment of the capital structure or profit making apparatus and relying on the principle laid out by the SC in the case of Oberoi Hotel Private Limited *v.* CIT [1999] 236 ITR 903 (SC), the Tribunal held that the receipt was in the nature of a capital receipt and was liable to capital gains tax, and could not be treated as profits and gains from business.

Editor's note

This is an important ruling where the Tribunal, based on the *facts, has treated the development of marketing skills and a distribution network over a period of time as resulting in the generation of goodwill, and the transfer thereof, resulting in the extinguishment of a source of earning income and hence a capital receipt chargeable to tax under capital gains.*

Section 50C – Not applicable to leasehold rights for 99 years

Kancast Pvt. Ltd. v. Income Tax Officer [TS-32-ITAT- 2015(Pun)]

Section 50C is triggered only when "land" or "buildings" or "both" are transferred. It does not apply when the "leasehold rights in land" are being transferred.

Facts

The taxpayer held leasehold rights in land acquired from the MIDC for a period of 99 years. The taxpayer transferred the leasehold rights for a consideration of INR 31.2 million, wherein the stamp duty value adopted was INR 57.6 million. The taxpayer contended that it was only the holder of the leasehold rights in the land, and not the owner of the land. It thereby computed its capital gains based on the consideration amount paid, which was INR 31.2 million. The TO invoked section 50C and computed the taxpayer's capital gains on the basis of the stamp duty value of INR 57.6 million. The TO rejected the taxpayers argument that it did not transfer the land in question, and contended that section 50C applied not only to land as such, but also to the leasehold rights in land, which qualified as a capital asset. The CIT(A) upheld the order of the TO.

Held

It was held that the definition of the term "land" included not only physical land but a leasehold right in land as well?

The leasehold right in land qualified as a capital asset and could be considered to be "immovable property" for the purpose of section 2(47) which deals with "transfer". However, not every kind of "capital asset" could be covered within the scope of section 50C. Only "land" or "buildings" or both could qualify as "capital assets" under section 50C. section 50C itself provided that it was a "Special provision for full value of consideration in certain cases".

Based on the facts of the case, section 50C was not applicable, as only the transfer of the leasehold rights in the land for 99 years, had taken place.

Editor's note

The Tribunal, based on facts, has treated the transfer of "leasehold rights in land" differently from land". It has also held that section 50C strictly applies to the transfer of "land" or "buildings" or both, and not to any rights associated with either of these properties.

Intention at the time of acquisition is material for determining the head of income

ACIT v a M/s Medravathi Agro Farms Pvt Ltd [TS-322-ITAT-2015(Hyd)]

Land owner's development profits split into capital gains and business profits in accordance with section 45(2) of the Act.

Facts

The taxpayer purchased some land in 2002-03. The taxpayer was incorporated with main object of agricultural activities therefore the land was shown as fixed asset and wealth tax was paid on the same. On 30 December, 2005, the taxpayer entered into a development agreement with a developer for the construction of apartments and bungalows on the land it owned. As per the agreement, 28% of the constructed area was to be allotted to the taxpayer. The taxpayer, in lieu of the transfer of its land, was then given a certain built-up area in the form of flats/ bungalows, which were subsequently sold to various buyers during FYs 2007-2008 and 2008-09.

Thirteen other group companies belonging to the taxpayer carried out similar transactions, and all of these were covered by this case.

The taxpayer divided the consideration for the sales between the land and the constructed area based on the cost of construction. The taxpayer offered that the gain on the sale of land constituted LTCG and the gain on the sale of bungalow/flat constituted STCG. For computation of STCG, the taxpayer had taken the cost to be "nil", as the same was received against the sale of land.

The TO took the view that the group companies had entered the real estate business, and systematically

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purchased adjacent lands around the same date, such that, if pooled together it created a single area of large land, before giving the land for development to the developer. The TO concluded that the income from the sale of the land as well as the constructed area was to be treated as business income.

The CIT(A) upheld the order of the TO. The taxpayer contented that the provision of section 45(2) applied and accordingly, that the total profit be divided into capital gains and business income. This argument was also rejected by the CIT(A) upon consideration of the taxpayer's intentions.

Held

The primary evidence in the form of objects belonging to the taxpayer, entries in the account books etc. showed that upon acquiring the different plots of land the group companies held by them as capital assets up to the date of the development agreement. Nothing in the group companies' records provided evidence to the contrary.

The intention of the taxpayer at the time of acquisition of land was material for ascertaining whether it was a case of stock in trade or capital asset. The conclusion of the TO and CIT(A) were based on the events that followed the development agreement, which cannot be relied upon for finding out the intention of the taxpayer at the time of the acquisition of the land.

The plots of lands in question were acquired and held by the taxpayer as capital assets up until the date of the development agreement. Therefore, it was held that the profits arising from the transfer thereof was subject to tax as capital gain and not as business income.

The profits arising from the sale of the flats and bungalows, along with the undivided share in the land, were also subject to tax in the hands of the taxpayer, partly as capital gains and partly as business income.

It was also held that capital gain and business income should be computed as per the provisions outlined in section 45(2). The Tribunal further explained the entire formula for computation of capital gain and business income with an example.

Editor's note

The Tribunal, in its ruling, emphasised that it is the intention of the taxpayer at the time of the acquisition of the asset, and not at the time of the sale/transfer of the asset, that is important. The intention of the taxpayer thus plays a key role in determining the taxability of a transaction under the head capital gains or business income.

Business Income

Non-compete fees

Arun Toshniwal v. DCIT [TS-191-HC-2015(BOM)]

The amount received under a non-compete agreement was deemed taxable as business income under the provisions of section 28(va) of the Act, despite the fact that the taxpayer had not "carried on any business" in the relevant "previous year".

Facts

On 27 May, 2008, Chemito sold one of its divisions to Thermo. *Vide* an agreement dated 2 June 2008, the Thermo entered into agreements of non-compete and non-solicitation with the taxpayer, being a Director in Chemito. In accordance with the agreements, the taxpayer agreed that he would not engage in any business or activity that was similar to those undertaken by the division, which had been sold to Thermo, for a period of 4 years. In consideration of said undertaking Thermo paid the taxpayer an aggregate sum of INR 70 million.

The TO treated the sum received as a revenue receipt that was taxable under section 28(va). The CIT(A) confirmed the order of the TO.

The taxpayer appealed to the tribunal. The latter held that the "carrying on of the business" was a *sine qua non* for section 28(i) of the Act. However, it was held that the condition of "carrying on the business" was not the only requirement for attracting the provisions of section 28(va) of the Act.

Held

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The Court was of the view that the amount received by the taxpayer was taxable under section 28(va) of the Act. It also held that it was evident that had the taxpayer not entered into an agreement of non-competition; he would have earned the amount he got in consideration from the division that was sold to Thermo. It was the sale of the division to Thermo that had deprived him of this income. Additionally, as a part of the sale consideration itself, he was required to execute an agreement of non-competition. It was held the compensation received under the said agreement was relatable to the consideration for sale of the business of the division and therefore, for these reasons also, the amount was taxable under section 28(va).

The Court relied upon the SC's decision that prior to 1 April, 2003, a non-compete fee would be a capital receipt. However, after the aforementioned date, the same amount would be a revenue receipt taxable under section 28(va).

Editor's note

The HC, has confirmed that a non-compete fee is taxable under section 28(va) of the Act.

Business Expenditure

Premium paid by company on buy-back to get rid of warring shareholder group to be considered as revenue expenditure

DCIT v. Bramha Corp. Hotels & Resorts Limited [TS-740-ITAT-2014(Pune - Tribunal)] for AY 2007-08 and CIT v. Bramha Corp. Hotels & Resorts Limited [[2015]63 Taxmann.com 13 (BOM)] for A& 2006-07

The Tribunal held premium paid on share buy-back to get rid of recalcitrant shareholder groups as revenue in nature, since expenditure was incurred out of business expediency.

Facts

Bramha Corp. Hotels and Resorts Limited (the taxpayer), was incorporated in 1987 by the Agarwal Group as its only shareholder. Subsequently, in order to ensure adequacy of funds, the Agarwal group entered into shareholders agreements with the Mac Charles (India) Limited group (Mac group) and the Gupta group.

During 2001 to 2003, the Mac and Gupta groups filed several civil and criminal cases against the Agarwal group and the taxpayer company due to certain disputes. Consequently, both groups filed a petition with the CLB and invoked sections 397 and 398 of the Companies Act, 1956. The CLB ordered the taxpayer to buy-back the shares of both the groups at a stipulated price that was over and above the face value of the shares.

The taxpayer complied with the order of the CLB and bought back its shares from the Mac and Gupta groups at a premium of INR 27.3 million and INR 54.3 million respectively. The payment of premium aggregating to INR 81.6 million was claimed as a deduction in the income return filed by the taxpayer for FY 2006-07. The TO held that the expenditure was capital in nature and rejected the claim of the taxpayer. For FY 2005-06, in a revision proceeding under section 263 of the Act, the TO had rejected a similar claim made by the taxpayer.

Aggrieved by the order, the taxpayer filed an appeal before the CIT(A), which ruled in favour of the taxpayer. The Revenue subsequently filed an appeal before the Tribunal.

Held

With regard to its ruling on the return filed for FY 2006-07, the Tribunal relied on its own previous decision (the case of the same taxpayer for FY 2005-06). It also relied on the Mumbai Bench decision in the case of USV Limited *v.* JCIT [ITA No. 376/M/2001] and Echjay Industries Limited *v.* DCIT [2004] 88 TTJ 1089 (Mumbai - Tribunal) wherein, on similar facts, it was held that since the purpose of the expenditure was to facilitate the smooth running of the business by getting rid of the recalcitrant shareholders, it was therefore incurred for purposes of business. The Mumbai Bench decision in the case of Echjay Industries Limited had also been affirmed by the Bombay HC (ITA No. 237 of 2004). Accordingly, the Tribunal ruled in favour of the taxpayer.

With regard to its ruling on the return filed for FY 2005-06, the HC relied upon the findings of the Tribunal that the excess amount was paid by the taxpayer only for the purpose of ensuring that the business ran smoothly and

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its profits increased. Above cases and on case of ACIT *v*. Chemosyn Ltd [139 ITD 68 (BOM)] held that such excess payment a revenue expenditure.

Editor's note

The Tribunal relied on various decisions, including its own decision in a previous case of the same taxpayer, where it was established that the taxpayer had not obtained any enduring benefit and the expenditure was incurred for protecting the taxpayer's business interests and was incumbent for the smooth running of the business, and thus had to be considered as revenue in nature. The decision is further strengthened by the HC order which confirmed the view for earlier year and also later Chemosyn Ltd. decision [TS -73-HC (BOM)[2015]].

Deduction 32A – Meaning of term Amalgamation

Commissioner of Income-tax, Delhi –IV vs D.C.M. Ltd [TS-779-HC-2014(Del)]

Where under a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956, 9 out of 13 of the industrial units held by the taxpayer were transferred to three newly formed companies, the same, though not compliant with section 2(1B) of the Act, was regarded as amalgamation and was therefore subject to section 32A(6) of the Act.

Facts:

During the FY 1983-84 to 1989-90, the taxpayer had claimed/availed a deduction for investment allowance under section 32A. section 32A pertained to deductions on account of investments made in purchase of new machinery, ship etc. Under a scheme of arrangement under sections 391 and 394 of the Companies Act, 1956, 9 out of 13 industrial units held by the taxpayer were transferred to three newly formed companies with effect from 1 April, 1990 ("Scheme").

Section 32A(5) of the Act provides for withdrawal of investment allowance in case the relevant asset has been sold or otherwise transferred within a period of 8 years from end of the year of acquisition. section 32A(6) of the Act provides that in case of amalgamation, the amalgamated company should continue to fulfil the conditions, thus, the benefits allowed need not be withdrawn.

The taxpayer claimed that in regard to the transfer of assets under the Scheme, section 32A(5) was not applicable.

The TO, treated the transfer of assets and liabilities, including plants and machinery as "sale or otherwise transfer" under section 32A(5) and passed an order under section 155(4A) and 154 of the Act withdrawing the benefit of investment allowance. The CIT(A) upheld the order of the TO. However, the Tribunal held that the Scheme did not result in transfer under section 32A(5). The Tribunal, taking a purposive interpretation of "otherwise transfer" used in section 32A(5) of the Act, held that the Scheme should not have been construed as violating the negative mandate which prohibited transfer, as the Scheme did not adversely affect the purpose of introduction of section 32A to promote industrial growth.

Held

The Court did not agree with the decision of the Tribunal and held that the transfer of assets under the Scheme was covered under "otherwise transfer" as per section 32A(5).

If the interpretation of the Tribunal were accepted, section 32A(6) would become redundant. It was held that since section 32A(6) carved out an exception to section 32A(5), where the Scheme was not covered under section 32A(5), the exception under section 32A(6) was not applicable.

After the above arguments had been presented, the taxpayer made the alternative argument, that the Scheme was protected under section 32A(6). In its response, the Court framed an additional question of law "Whether the scheme of arrangement/reconstruction could be regarded as amalgamation and protected under sub-section (6) to section 32A of the The Act?"

section 2(1B) of the Act defined the word "Amalgamation" for the purpose of the Act. It was held that the statutory definition should be applied when interpreting the word in any of the provisions of the Act. However, since section 2 began with the words "unless the context otherwise requires", it was held that the definition clause should be applied. This is not a strict rule and the definition clause need not be applied on account of the context in which the word "Amalgamation" is used in a particular section.

Section 32A(5) and (6) focused on the transfer of assets, namely, ship, aircraft, machinery or plant. section 32A(6), which was the relevant section for "Amalgamation", also neither spoke of transfer of all assets/liabilities nor the extinction of the amalgamating company. In fact, the sub-section stipulated that the balance investment allowance, if any, should be given to the amalgamated company, provided that the total period for allowance between the amalgamating company and the amalgamated company did not exceed the stipulated period of 8 years. This supported the view that the amalgamating company need not cease to exist. Therefore, the court held that it would not be proper to apply section 2(1B) in totality while interpreting section 32A(6).

The purpose of providing limited protection under section 32A(6) was a flexible and realistic approach for business re-organisation, which was generally treated as being tax neutral. Thus cases of amalgamation, subject to conditions, stand excluded from the rigors of section 32A(5).

The purpose and objective behind sub-section (6) to section 32A was to facilitate reconstruction and amalgamation, and not to obstruct genuine transactions of such nature. At the same time, appropriate conditions were incorporated in section 32A(6) to ensure that there could be no abuse of the conditions applicable to the amalgamating company.

The Revenue's case was that if the company had ceased to exist, all the conditions of section 2(1B) would have been complied with. That means, if the Scheme involved the merger of the taxpayer (with remaining assets/liabilities) with a fourth company, the Scheme would have been compliant with section 2(1B). Thus, it is case of a selection of an incorrect taxable event due to lack of foresight about the objection that could be raised. This would not be in consonance with the objective behind the introduction of section 32A(6).

The Court held that the Act was a living Act and not a relic. The principle of updating the construction of an Act was premised on the doctrine that Acts were always speaking and were intended to apply over a period of time. Therefore, it was not correct that the language of a statute had to always be construed in as it was construed at the time that the Act in question passed. Thus, there was a need to interpret statues with reference to contemporary understanding.

The Court rejected the Revenues' contention that the Scheme resulted in a "transfer" as defined under section 32A(5) and held that the benefit under section 32A(6) was not available as Scheme did not comply with section 2(1B) compliant. The Court also held that in order for section 32A(6) to apply, it was not necessary that the scheme of amalgamation had to postulate a complete merger of the company, and that part or partial merger would equally constitute amalgamation.

The taxpayer would be entitled to protection under section 32A(6), if the conditions specified therein as well as clauses (ii) and (iii) of section 2(1B) of the Act were satisfied, and remanded the case only to examine compliance with such conditions.

Editor's note

It is important to note that the ruling in this case was given prior to the introduction of section 2(19AA) of the Act, and other provisions dealing with demerger. It is also important to note that the court framed an additional question of law on a new ground and decided the matter on that new ground.

MAT

Capital receipt credited to Profits and Loss account is part of MAT computation

B&B infotech Ltd. v. ITO [TS-643-ITAT-2015(Mum)

Capital receipt arising on remission of principal amount payable to bank, if credited to the P&L account the same cannot be removed from computation of MAT profit in absence of specific provision in 115JB for such removal.

Facts

During the FY 2005-06, the taxpayer got remission of the principal amount payable to a bank on account of a one-time settlement. The taxpayer credited this amount to its P&L account and in its "Notes to Accounts" disclosed that the remission was a capital receipt. When the taxpayer filed its ROI, it stated that it had "nil" income, and excluded the remission amount in the computation of MAT profit.

The TO re-opened the assessment to tax the remission of liability under MAT provisions.

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Held

The remission of loan liability was credited to the P&L account in accordance with Schedule VI of the Companies Act, and in compliance with the mandatory Accounting Standards (AS 5). Any disclosure made in the "Notes to Account" could not change the P&L account prepared in accordance with Schedule VI of the Companies Act.

Profit in the P&L account was not open to adjustment by the TO or the taxpayer while they computed the "book profit" under section 115JB. The only exception was the permissible adjustment provided under the Explanation to section 115JB. It was undisputed that the amount in question did not fall in the ambit of the Explanation and therefore, it was held that the amount in question could be excluded from the computation of the "Book Profit" under section 115JB.

Editor's note

This Tribunal has relied on the SC decision in the case of Apollo Tyres [255 ITR 274(SC)] and reconfirmed the possibility of limited adjustment in cases of computation under section 115JB. The decision in the case of Shivalik Ventures, was distinguished on the basis that the amount in question was not credited to the P&L account.

Computation of quantum of expenditure relatable to exempt income that is reduced from book profits under the provisions of MAT

DCIT v. Sobha Developers [TS-35-ITAT-(Bangalore - Tribunal)]

Section 14A read with Rule 8D is a reasonable method for arriving at the quantum of expenditure to be adjusted for computing book profits under section 115JB where the taxpayer has accepted similar disallowance under the normal provisions of the Act.

Facts

Sobha Developers' (the taxpayer) total income for AY 2008-09 was determined by applying the provisions of section 115JB of the Act, since the tax under the normal provisions was lower due to exempt income from dividends on units of mutual funds and share of income from a partnership.

For the purpose of calculating MAT profits, the TO in accordance with Explanation 1(f) to section 115JB(2) of the Act added an expenditure of INR 2.464 million to the "book profits". The quantum of expenditure was determined as per section 14A of the Act read with Rule 8D of the Rules, and was accepted by the taxpayer as an adjustment to income under the normal provisions of the Act. There were no direct expense attributable to the earning of exempt income, and the disallowance made under normal provisions was only for indirect interest expenses and other expenses by invoking the provisions of Rule 8D. On appeal, the CIT(A) agreed with the taxpayer's contention that the amount disallowed under section 14A could not be applied, and that adjustments to "book profits" for MAT in the absence of any direct expenses attributable the earning of exempt income, could not be made. The Revenue preferred an appeal before the Tribunal.

Held

The expression "expenditure relatable" used in Explanation 1(f) to section 115JB of the Act and the expression "expenditure incurred by the taxpayer in relation to" used in section 14A of the Act applies to both direct and indirect expenditure. Where the taxpayer has accepted the disallowance of quantum of expenditure determined by the TO under section 14A read with Rule 8D, while computing income under normal provisions of the Act, the same amount could be adopted in computing the "book profits" under section 115JB.

Editor's note

This ruling clarifies that both direct and indirect expenditure relatable to exempt income need to be adjusted when determining the "book profits". The computation mechanism specified in Rule 8D of the Rules provides a reasonable basis for determining the quantum of expenditure to has to be added to the "book profits" for MAT purposes, where the taxpayer has not been able to satisfy the TO regarding the quantum.

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Losses

Applicability of section 72A of the Act on amalgamation of a company having more than one undertaking with another company.

CIT vs. KBD Sugars and Distilleries Limited [TS 630-HC [2015]]

As per section 72A of the Act, the amalgamating company should be engaged in the business for more than 3 years. It is not required that amalgamating company should have commenced the business 3 years prior to the date of amalgamation.

Facts

M/S Shree Vani Sugars and Industries Limited (amalgamating company) amalgamated with the taxpayer, M/S KBD Sugars and Distilleries Limited (amalgamated company) w.e.f. 1 March 2005. The amalgamating company was engaged in two business undertakings *viz.*

- Manufacturing of sugar since 1984.
- Generation of power – setting up commenced in 2000 and generation commenced on 8 September 2003.

In the return for AY 2006-07 the taxpayer claimed set-off of losses of INR 213 million pertaining to the amalgamating company. The TO allowed the set-off of INR 178 million related to the sugar manufacturing undertaking and rejected set-off of INR 35 million pertaining to the power generation undertaking as the amalgamating company had commenced its power generation business less than 3 years before the amalgamation. section 72A allows the carrying forward of losses of the amalgamating company only if the amalgamating company was engaged in the business in question for a minimum period of 3 years.

Held

The Court held that where section 72A was concerned, the term "commencement of business" was different from the term "engaged in business". The commencement of a business could be from the date of the start of production, whereas a company setting up a business would "engaged in the business" from the time that it was set up. In this case, though amalgamating company had commenced power generation within the period of 3 years prior to the amalgamation, the business set-up process had commenced more than 3 years prior to the amalgamation and therefore, the court allowed the losses related to the power generation undertaking to be set-off.

The Court also held that section 72A(2) provides for the carry forward of losses of the amalgamating company as a whole and not losses of a specific undertaking thereof. Accordingly, the amalgamating company should have been in the business for more than 3 years and not any specific division thereof. Therefore, the Court held that since the amalgamating company was in business since 1984, set-off of losses could be permitted.

Editor's note

Two principle emerges from this decision (a) for computation of 3 years, the period commencing from the setting up of the business is relevant and not the period from date of commencement of production and (b) the test of "being engaged in business" need to be applied to the amalgamating company and not to any division thereof.

Section 79 of the Act is not triggered if there is no change in beneficial ownership

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The benefit of carry forward and the set-off of business losses for "previous years" shall be available if 51% of the control and voting power of the Company remains unchanged

Facts:

The shares in AMCO Power Systems Limited (APSL) (the taxpayer) were entirely held by AMCO Batteries Limited (ABL) up until the AY 2000-01. Thereafter, 45% of the shareholding was transferred to AMCO Properties and Investments Limited (APIL), a wholly-owned subsidiary of ABL in the AY 2001-02. In the AY 2002-03, ABL further transferred 49% of its remaining 55% shares to Tractors and Farm Equipments Limited (TAFE). As a result of the above transactions, the shareholding now stood as follows:

- ABL = 6%
- APIL = 45%
- TAFE = 49%

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In its return for the AY 2003-04, the taxpayer had claimed for set off of the losses pertaining to earlier years.

The taxpayer contended that that even though there was a change in the shareholding, 51% of the voting power continued to be beneficially held by ABL through its wholly-owned subsidiary, APIL, and therefore, section 79(a) of the Act could not be triggered.

The TO contended that since the shareholding and voting power of ABL was reduced below 51%, it is not in compliance with section 79(a) of the Act and denied the set off of the losses incurred in the AYs 2002-03 and 2003-04.

Held

The submission of the taxpayer that not less than 51% of voting power is beneficially held by the person who beneficially held not less than 51% shares carrying voting rights, section 79(a) should not trigger has force.

Although the shareholding of ABL was reduced to 6% in the year in question, its wholly-owned subsidiary APIL owned 46% of the shareholding. Since ABL was the holding company, and owned 100% of the shares in APIL, the voting power of ABL could not be said to have been reduced to less than 51% because together, both the companies had the voting power of 51%.

Since, there was no change in control of the taxpayer, section 79(a) was not applicable and the taxpayer was allowed the benefit of carry forward and the set-off of losses.

Editor’s note

This ruling clarifies that even the indirect holding of voting power through a wholly-owned subsidiary should be considered for the purpose of section 79. As long as control remained with the company in the year it incurred the losses, and remains in the year it applies for the set-off, section 79 would not be triggered even if the shareholding per se falls below 51%. It is important to note that placing reliance only on voting power and ignoring the actual changes in the shareholding does not seem to be suggested in the provisions of section 79.

Set-off of short-term capital loss

ACIT v. Mac Charles India Limited (TS-105-ITAT-2015 -Bangalore-Tribunal)

STCL is taxable at concessional rate and can be set-off against other STCG regardless of the difference in tax rates.

Facts

The taxpayer had sold listed equity shares on market, which were taxable at a concessional rate under section 111A of the Act. The sale of the shares, partly resulting in STCG and partly in STCL. The taxpayer had also sold other capital assets resulting in STCG that were taxable at the normal rate of 30%. In computing the tax liability, the taxpayer first set off the STCL against the STCG taxable at the normal rate. According to the TO, STCL arising from the sale of equity shares, taxable at a concessional rate, should be first set-off against STCG taxable at concessional rate and balance against STCG on the transfer of other capital assets chargeable at the normal rate and therefore, disallowed the claim of set-off proposed by the taxpayer.

Held

section 70(2) of the Act provides that STCL could be set off against STCG from any capital assets. Hence, the taxpayer had the unqualified option of setting off any STCL against any STCG.

Thus, the Tribunal ruled in favour of the taxpayer and held that it was inappropriate to deny the taxpayer a legitimate right simply because it resulted in a lower tax burden for the taxpayer.

Editor’s Note

This judgement has clarified that the choice pertaining to the set-off of any type of STCL against any other type of STCG lies with the taxpayer.

Long-term capital loss arising from the sale of listed shares allowed to be set-off

Raptakos Brett & Co Ltd v. DCIT [TS-326-ITAT-2015(Mum)]

Set-off of LTCL on sale of shares (where security Transaction Tax (STT) is paid) against the long-term capital gain on the sale of land.

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Facts

The taxpayer was a pharmaceutical company, which had suffered LTCL resulting from the sale of shares and mutual fund units (where STT was paid). The LTCL was set-off against the LTCG on the sale of land.

The TO disallowed the set-off claiming that since LTCG on sale of shares (where STT is paid) is exempt under section 10(38) of the Act, and since income included loss, such a loss could not be allowed to be set-off. The CIT(A) confirmed the order of the TO.

Held

The concept of income as including loss was only applicable when the entire source of income was exempt and not in cases where only one particular stream of income was exempt. section 10(38) of the Act excludes the income arising from transfer of Long-term capital assets being equity share or equity fund which is chargeable to STT, and not entire source of income from capital gains, arising from transfer of shares.

Therefore, the LTCL on sale of shares, for which STT had been paid, was allowed to be set-off against the LTCG on the sale of land.

Editor's note

The Tribunal held that only if an entire source of income is completely exempt from taxation, will the set off-of loss = be disallowed. However, if the exemption applies only to a part of the source of income and/or is subject to fulfilment of some conditions, loss from such source of income will be allowed to be set-off and carried forward.

Companies Act

A RD is entitled to raise tax objections even when the ITA have not

Casby CFS Private Ltd. In re. (2015 /56/Taxmann.com/263/ Bombay)

RD was entitled to raise tax-related objections with regard to a scheme of amalgamation even though the ITA raised no objections in relation to this scheme.

Facts

A scheme of amalgamation of Casby CFS Private Limited with Casby Logistics Private Limited was filed with the HC on 21 March 2014 with a retrospective appointed date of 1 April 2008. The ITA had not objected to the scheme. However, the RD contended that the idea behind propounding the scheme with a retrospective appointed date was with a view to evade capital gains tax and other provisions relating to revised returns, tax demands and assessment proceedings under the Act. The HC directed the RD to refer to the ITA with regard the objections raised. The ITA informed the RD that it supported the objections that it had raised.

Held

The Court could interfere with the decision or commercial wisdom of the shareholders, where it was satisfied that the scheme had been framed to contravene the provisions of any law.

The RD was bound by duty to inform the HC of any provision in the scheme that was in contravention of any law, including the Income-tax laws. The RD had the necessary *locus standi* and statutory recognition under sections 394 and 394A of the Companies Act, 1956 to represent and comment on a scheme. The HC was required to consider the findings of the RD.

Where the ITA has not raised any objections, the RD cannot be prevented from raising such objections pertaining to the Income-tax laws as he may deem fit.

The HC sanctioned the scheme on specific conditions that the tax

It also ruled against the petitioner thereby upholding the RDs entitlement to voice his apprehensions before the Court pertaining to the the provisions of the Income-tax laws, despite the fact that no objections were raised by the ITA. It also held that the ITA should address the income-tax issues raised by the RD in accordance with the provisions of law and without being influenced by the observations made in the order and appointed date fixed thereunder.

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Editor's Note

This decision is relevant for companies proposing to undertake a merger scheme as it enhances the scope of the RD and empowers him to raise objections to the Scheme from an income-tax perspective, irrespective of whether the ITA has raised any objections or not.

Securities and Exchange Board of India (SEBI)

SEBI has no Locus in Scheme matters under sections. 391 and 394 of the Companies Act

LSI-739-HC-2015(Bom)

Facts

This case involved two schemes of amalgamation. The first scheme involved the merger of Isika with City Pulse, both unlisted public companies, and was approved by the court *vide* order dated 27 August 2010. Post-amalgamation City pulse was renamed Isikan.

The second scheme was sanctioned by the court *vide* order dated 17 June 2011 and was amended vide order dated 22 June 2011. The second scheme was a composite Scheme that involved firstly, the demerger of an undertaking of NFCL, a company listed on the stock exchange, into NOR; secondly, the merger of NFCL (after the aforementioned demerger), and Isikan (as renamed) into KFL (100% subsidiary of NFCL –renamed NFCL). Both NORL and KFL (renamed NFCL) were then listed on the stock exchange. NFCL approached SEBI for an exemption under Regulation 19(2)(b) from the requirement of creating an IPO for the purpose of listing the shares. According to SEBI, this was the first time that it got chance to pursue the financials of Isikan Limited.

SEBI applied to the court to recall/review and/or set aside the order dated 17 June 2011 sanctioning the second scheme, and on 22 June 2011, amending the second scheme. The application was based on various allegations including the allegation of intangible assets of Isikan to be fictitious and that there was inflated valuation of such intangibles, allegation of larger number of shares to the promoters pursuant to such inflated valuation and suppression of facts. During the hearing, SEBI provided two alternative approaches to set right the damage resulting from the issuing of a large number of shares, by modifying the Scheme under the provisions of section 392 of the Companies Act, 1956.

Held

SEBI had no *locus standi* in the case of Scheme matters under section 391-394 of the Companies Act, 1956. section 392 of the Companies Act, 1956 expressly provides that modifications to a Scheme can only be made for ensuring that the Scheme works properly and that such modifications cannot alter the basic fabric of the scheme. Suggesting alternative solutions would amount to imposing a new commercial bargain on the shareholders and other stakeholders, to which they had not consented, and would not fall within the scope of section 392

All other allegations were rejected.

Therefore, there is no question of granting relief to SEBI as prayed for and the appeals were disposed of with cost.

Editor's note

The HC has reconfirmed that the decision in the case of SEBI v. Sterlite Industries Limited [2003(113) Company cases 273(Bom)] holding that SEBI has no locus to intervene in the Scheme matters under section 391-394 of the Companies Act, 1956 is good law. The Court has also referred to the SEBI Circular No. 5 dated 4 February 2013, which prescribes revised requirements in Scheme matters. However, the Court has not commented upon the same.

Regulatory update

The Companies Act, 1956

Companies Deposit Rules Amended: Loans from Relativs of Directors Allowed

The MCA has issued a notification dated 15 September, 2015 to amend the Companies (Acceptance of Deposit) Rules, 2014 (the Rule) as follows:

Securities and Exchange Board of India (SEBI)

- In Rule 2(1)(c)(viii), the definition of "deposit" now excludes any amount received from a director or "a relative of the director of a Private Company", subject to the condition that such person shall furnish a declaration that the amount being deposited, is not from funds acquired by him through borrowing or accepting loans or deposits from others, and the company shall disclose the details of the money so accepted in the Board's report.
- In Rule 3, the words "paid-up share capital and free reserves", will be replaced by the words "paid-up share capital, free reserves and securities premium account".

The above amendment will increase borrowing limits and enhances the ability of companies to accept deposits. Companies are now also allowed to raise loans from directors and their relatives, and these will not be considered to be "deposits", which otherwise requires pursuing detailed process for accepting the same.

Editor's Note:

The above changes are positive in nature, and will go a long way in helping businesses fulfil their funding requirements. These new measures are in line with the earlier provisions of the Companies Act, 1956.

Important amendments to the Companies (Amendment) Act, 2015

The Companies (Amendment) Act, 2015

- Requirement of minimum paid-up capital for companies

  As per the Companies Act, 2013, private and public companies had a minimum paid-up capital requirement of INR 0.1 million and INR 0.5 million respectively. This requirement no longer exists.

- **Related Party Transactions**

  As per section 188(1) of the Companies Act, 2013, no contract or arrangement can be entered into that exceeds the specified limits, except with the prior approval of the company by a special resolution passed by non-related shareholders. The special resolution requirement was amended by non-related shareholders, which means that only an ordinary resolution by non-related shareholders in now required. In addition, transactions between a company and its wholly-owned subsidiary are exempted from the aforementioned requirement.

  Further, the Audit Committee now has the power to give omnibus approvals for related party transactions subject to prescribed conditions.

- **Writing off past losses/depreciation before declaring dividend for the year**

  The amendment to section 123(1) of the Companies Act, 2013 provides that no company shall declare dividend unless carried-over previous losses and depreciation not provided in the previous year or years are set off against the profit of the company for the current year.

- **Loan/Guarantee by holding company to/for subsidiary company**

  As per section 185(1) of the Companies Act, 2013, no company shall advance a loan to any of its directors or to any other person in whom the director is interested, or give any guarantee or provide any security in connection with any loan taken by the director or such other person. The amendment to this section provides that the provisions should not apply to any loan/ guarantee by the holding company to the subsidiary company, if the loans are to be utilised by the subsidiary company for its principal business activities.

SEBI

Summary of Informal Guidance

- SL and IL were both promoter group companies that held shares in Elder Pharma Limited ("EL") for more than 3 years. Mr. Alok and Dr. Anuj were promoters of EL and held shares in EL for more than 3 years. ACL is equally held by Mr. Alok and Dr. Anuj and forms part of the promoter group, however, ACL is not holding any shares in EL. It is proposed the transfer of shares from SL and IL to Mr. Alok, Dr. Anuj and ACL. It was contended that if the transferees had collectively held shares for more than 3 years, that constituted as sufficient compliance with the requirement set down by Regulation 10(1)(a)(ii). SEBI has taken the view that the exemption of inter-se promoter transfer under Regulation 10(1)(a)(ii) can only be made available if each of the Transferors as well as the Transferees satisfies the condition of being a promoter group for 3 years prior to proposed Transfer.

- In the case of Geogit BNP Paribas Financial Services Ltd. (Geogit), two promoters Mr. and Mrs. C. George held 21.15% of the shares in Geogit, and all of the promoter groups together with the PACs held 64.31% of the shares in the company. One of the Directors of Geogit, Mr. Punnoose George (who was part of the Promoter Group until 6 May, 2006) held 4.27% of the shares in Geogit, and intended to enter into a shareholder's agreement with Mr. C. George for supporting each other in all matters that came up before the board and general body of Geogit. Geogit had approached SEBI to ascertain whether entering into the proposed agreement would trigger provision of Regulation 3(1) to the takeover regulation. SEBI opined that pursuant to the agreement, Mr. Punnoose George would become PAC as well as a part of the Promoter Group and would not be subject to Regulation 3(1) of the. Additionally, SEBI opined that, as Mr. Punnoose George would exercise control along with Mr. C. George and other members of the Promoter Group, the proposed agreement would result in changes with regard to the control of Geogit, and that Regulation 4 of the Takeover Regulations would then be applicable.
- One of the promoters of Future Lifestyle Fashions Ltd. (FLFL), which was listed on 1 October, 2012, proposed to transfer its shareholding during the FY 2014. The acquirer had held shares in FCEL for more than 3 years prior to 2012 and was allotted shares in FLFL upon the demerger of an undertaking of FCEL. With regard to the question of whether the transaction would be Inter-se promoter transfer exempt under Regulation 10(1)(ii), SEBI opined that since the company was listed for less than 3 years, neither the transferor nor the transferee could comply with the condition of being disclosed as promoters for at least 3 years. Therefore, it was held that the transaction was not exempt under regulation 10(1)(ii).

Takeover Regulation

SEBI *vide* its notification dated 24 March 2015 amended the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011. As per the amendment an acquirer making an open offer under Regulation 3 to 5 to make delisting offer in accordance with the SEBI (Delisting of Equity Shares) Regulations, 2009 provided that the acquirer declares his intention to delist in the detailed public announcement.

If the delisting offer is successful, the acquirer should complete the acquisition of shares only after making an announcement pertaining to the success of the delisting offer.

If the delisting offer fails, the acquirer can continue with the open offer. However, in such a case the interest on the offer price needs to be increased by 10% for the period starting from the date of payment as per the open offer and date of actual payment.

In case a competing offer is made, the acquirer cannot delist the security.

Listing Regulation

SEBI vide its notification dated 2 September, 2015 issued the Securities and Exchange Board of India the listing Regulation, 2015

The regulations relating to (a) the ordinary resolution for related party transactions and (b) the disclosure of class of shareholders and condition for reclassification came into operation on 2 September 2015. All other regulations came into operation on 1 December 2015.

Primarily, the obligations and disclosure requirements which were hitherto provided under listing agreements are consolidated in the listing Regulation. SEBI has issued a uniform listing agreement format, to be used by all companies for listing all types of securities. The same format is to be used for new listings of securities. The uniform listing agreement format is simple and runs into two pages only. Any company that has listed any of its securities on the stock exchange is required to execute a fresh listing agreement with the concerned stock exchange within 6 months from the date of notification, i.e., before 1 March 2016.

Structuring for companies

Mergers and acquisitions

Though the listing Regulation is primarily composed of existing provisions pertaining to listing agreements, there is a major difference between the authority of a listing agreement, which is a contractual arrangement between a stock exchange and a company, and the listing Regulation, which is a part of the statute directly governed by SEBI.

Some of the important provisions added to the listing Regulation, are as follows:

- Relaxation is provided to listed companies with capital less than INR 100 million and net worth less than INR 250 million, from the applicability of the provisions related to the board of directors, committees, related party transaction etc. However, such companies are required to comply with all the provisions within 6 months of the date from which either of the above limits are crossed.
- The shares of Promoter Groups must be in dematerialised form.
- Provisions relating to the reclassification of a Promoter as a public and professionally managed company without an identifiable promoter.
- Provisions relating to the review of the annual report by the stock exchange and the qualified audit report review committee.
- Filing of Annual information Memorandum.
- Penal provisions for the violation of the listing Regulation, which includes imposition of fines, suspension of trading and freezing of the promoter groups holdings.
- Provisions relating to in-principle approval for listing from stock exchange shall not be applicable to securities issued pursuant to a Scheme approved by the Stock Exchange.
- Disclosure of any material event or information. A list of deemed material even is provided in the regulation. On 9 September, 2015, SEBI issued a circular providing guidance on what details are to be disclosed and how to determine when an event can be said to have occurred.

Update on Tendering of Shares through Stock Market Mechanism

SEBI *vide* its Notification dated 24 March, 2015, amended the SEBI (Buy Back of Securities) Regulations, 1998, the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 and the SEBI (Delisting of Equity Shares) Regulations, 2009 to allow the tendering of shares by the shareholders through the stock exchange mechanism for acquisitions proposed under those regulations.

Subsequently *vide* the circular dated 13 April, 2015 SEBI issued a detailed procedure for the above tendering process. The circular is applicable to all the Public Announcements made after 1 July, 2015. However, in case an acquirer or any person acting in concert with the acquirer is not eligible to acquire shares through the stock exchange due to operation of any other law, they can follow the existing "tender offer method".

Stock exchange having nationwide terminals should provide a separate window for acquisition of shares as above ("Acquisition Window").

Delisting Regulation

On 24 March 2015, SEBI amended the SEBI (Delisting of Equity Shares) Regulation, 2009. Some of the important amendments made to the Regulation are as follows:

- Promoter/Promoter Group selling shares of the company is not allowed to propose delisting for next 6 months.
- The Acquirer/Promoter/Promoter Group as the case may be, proposing the delisting is not allowed to sell shares of the company until the completion of the delisting process.
- The delisting process timelines are revised and reduced.
- Provisions enabling SEBI to grant exemption from the strict enforcement of regulations, upon receiving an application from acquirer/promoter, are inserted.
- Companies with paid-up capital of up to INR 100 million and net worth of up to INR 250 million on last day of preceding FY are allowed to delist without following the

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exit opportunity process, but must follow the simpler process. Earlier, the limit for paid up capital was INR 10 million.

- The delisting offer is considered successful only if (i) Post-offer, the promoter shareholding reaches at least 90% of issued capital, excluding the shares held by the custodian against ADR/GDR and (ii) at least 25% of the public shareholders holding shares in dematerialised form have participated.

  Pre-amendment the delisting offer was considered successful if post-offer the promoter shareholding reached (i) at least 90% of issued capital, excluding the shares held by the custodian against ADR/GDR or (ii) the aggregate percentage of the pre-offer promoter holding plus 50% of the offer size.

Insider Trading Regulation

On 15 January 2015 SEBI notified the SEBI (Prohibition of Insider Trading) Regulations, 2015 (“2015 regulation”) repealing the SEBI (Prohibition of Insider Trading) Regulations, 1992. The 2015 Regulations were published in the Official Gazette on 15 January 2015. The 2015 Regulations has come into force with effect from 15 May 2015 (120 days from the date of publication in the Official Gazette)

In addition to broadening the definitions of UPSI, insider and connected persons Regulations, 2015 also impose graver penalties for company officials involved in the selective exchange of price-sensitive information. Some of the important changes brought in by the 2015 Regulation are as follows:

- The 2015 Regulation prohibits any communication of UPSI, whereas the 1992 Regulation prohibited only the communication resulting in trade.
- Enables an insider to get his trading plan pre-sanctioned by the compliance officer, such plan when implemented, generally would not be considered insider trading. Such plans are required to be disclosed to the public and can be acted upon only after 6 months of the public disclosure. Once approved the insider shall mandatorily have to implement the trading plan, without any change.
- The threshold for continual disclosure for specified persons is revised to aggregate trade value of INR 1 million.
- In regard to non-specified persons, a company is empowered to call for the information.

Security Contract Regulation Rules

On 25 February 2015 the Ministry of Finance notified the Securities Contract (Regulation) (Amendment) Rules, 2015 thereby amending the definition of “Public Shareholding” to include listed ADR/GDR where the holder has the right to issue voting instructions and to exclude shares held in the employee benefit scheme trust. The Regulation also provides that in case a public shareholding goes below the threshold limit of 25% as a result of the above, the company shall increase the public shareholding to 25% within 3 years from the date of notification of relevant regulations.

Finance Act 2015

Clarification regarding indirect transfers (applicable from FY 2015-16)

The following clarifications have been made with regard to the applicability of the indirect transfer tax provisions. These clarifications are as follows:

- The term “substantially” means at least 50% of the fair value of all assets (tangible/intangible) owned by the company/entity, on the specified date and exceeding INR 100 million. The computation of the fair value of assets should not include the reduction of liabilities, if any, in respect of the asset. “Specified date” means (i) the date on which the accounting period ends prior to the date of transfer or (ii) the date of transfer, if book value of assets is higher by 15% as compared to the book value on date in (i). The mechanism for determining the book value is prescribed separately.
- An additional 5% voting/control threshold has been prescribed for determining the applicability of the indirect transfer tax provisions.

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- Where all the assets owned by a transferor are not located in India, the income of the non-resident transferor, accrued from the transfer of shares outside India shall be only such a part of the income as is reasonably attributable to assets located in India. Thus, the taxation of gains will be on a proportional basis, and the method of determination of proportionality will be provided for in the rules.
- Subject to specified conditions, the indirect transfer of shares arising from the amalgamation or demerger of foreign companies is exempted under the heading of capital gains.
- Reporting obligations required to be complied with by the Indian entity furnishing information relating to the off-shore transaction.

Rental income earned by REITs

- Pass-through status will now be provided to REITs in respect of income earned from the renting, leasing or letting out any real estate asset owned directly by the REITs. Thus, the rental income will be exempt in the hands of REITs.
- On distribution of rental income, REITs are now required to withhold tax at 10% in the case of resident unit-holders and at the applicable tax rates in the case of payment to non-residents. Tax would not be required to be withheld under section 194-I of the Act, by the tenants on payment of rental income to the REITs.

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Case law

Inter-company outbound loans

Delhi HC upholds Tribunal ruling - TPO not empowered to restructure transaction; agreed commercial terms to be respected in determining arm's length interest rate charged, Indian PLR not applicable for foreign currency loans

CIT v. Cotton Naturals (India) Private Limited [2015] 55 taxmann.com 523 (Delhi)

The first HC judgement regarding the manner of determining the arm's length interest rate for outbound loans denominated in a foreign currency. The Delhi HC has reconfirmed certain established principles, and provided direction on tax authorities' powers to restructure transactions and interpretation of global guidance in this regard.

Facts

The taxpayer was engaged in the business of manufacture and exports of rider apparels, and had advanced a loan with an interest rate of 4% per annum, to its AE in the US. The AE was a subsidiary responsible for the distribution and marketing of the taxpayer's products. The taxpayer had granted the loan, denominated in a foreign currency, to its AE during the FY 2002–2003 in order to enable it to meet its working capital requirements so that it could continue conducting its business activities smoothly. The taxpayer contended that the interest rate was determined on an arm's length basis, on the basis that the rate was comparable to the export packing credit rate obtained from independent banks in India. Confirming the order of the TPO and factoring in the DRPs directions, the TO recomputed the arm's length rate of interest in line with domestic PLR in India, being the taxpayer's opportunity return on the funds if deployed in the domestic market. The Tribunal2 ruled in favour of the taxpayer, and the Revenue subsequently filed an appeal before the HC.

Held

While the HC agreed with some of the principles laid down in the past on the subject matter by various Tribunals, it also provided direction on certain important additional factors regarding comparability and international guidance. The key principles from the HC Ruling are as follows:

2. Cotton Naturals (India) Private Limited v. DCIT (ITA No. 3265/Del/2011, ITAT Delhi).

- Commercial expediency needs to be recognised, and the transaction cannot be restructured
  - The HC found that the TPO had viewed the transaction concerning the foreign currency l in isolation, and that the commercial relationship between the taxpayer and its AE was not take into consideration. Thus, the HC relied on the Bangalore Tribunal ruling in the case of Logix Micro Systems Limited3 and held that the TPO had stepped into the shoes of the taxpayer and restructured the transaction in order to determine the maximum return it could earn on the loan amount from other sources. By ignoring the commercial expediency of the transaction, the TPO had acted beyond his role, which was restricted to determining the arm's length nature of the transaction as it was originally undertaken.
  - In making the above judgement, the HC relied on the ruling in EKL Appliances Limited4, and referred to its own previous ruling in Sony Ericsson Mobile Communications India Private Limited5. The HC also relied on the UN Model Double Taxation Convention between Developed and Developing Countries. Various Tribunals have dealt with the issue of commercial expediency in the past (including outside the context of financial transactions), and the courts have frequently ruled in favour of the taxpayers.
- Guidance on comparability
  - Comparability analysis to be undertaken in line with Rule 10B and Rule 10C of the Rules
  - The HC stated that since incorporating subsidiaries outside India for the purpose of undertaking functions such as marketing and distribution was a prevalent practice among multinational companies, Rule 10B and 10C of the Rules were applicable in carrying out a comparability analysis. Accordingly, the comparison had to be with what an independent entity would pay under identical circumstances, and not with the choices that were available to the

    taxpayer for earning the maximum returns by re-

3 Logix Micro Systems Limited v. ACIT (ITA No. 423/Bang/2009, ITAT Bangalore).
4. CIT v. EKL Appliances Limited [2012] 209 Taxman 200 (Delhi HC).
5. Sony Ericsson Mobile Communications India Private Limited v. CIT (ITA No. 16/2014).

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structuring the transaction. The HC thus reiterated that when applying the arm's length principle the interest rate needs to be benchmarked from the borrower's perspective (along with the terms of the loan such as currency, tenure etc.) and that the parameters should be consistent for inbound and outbound loans.

In applying the Rules, the HC went a step further and observed that a comparability analysis required that the data used belong to the FY in which the international transaction took place. Since the advancing of the loan in the current case took place in the FY 2002–2003, only data from this period was usable. The payment of interest (which was also an international transaction) would depend on the year in which the grant of the loan took place. The HC did not provide detailed guidance with regard to this matter as no mention of the issue occurred during the proceedings.

The HC also stated that it was erroneous to apply the Reserve Bank of India's (RBI) Master Circular for determining the arm's length rates, since these were special schemes floated by the RBI to encourage and facilitate exports.

– ***Indian lending rate v. foreign currency lending rate***
The HC stated that the arm's length interest rate had to be the market-determined rate applicable to the currency in which repayment of the loan would take place. In this respect, the HC referred to Klaus Vogel's recommendation on the Double Taxation Conventions (Third Edition), a position that various Tribunals had accepted in the past.
Guidance on the Indian Administration's viewpoints expressed in the United Nations Practical Manual on Transfer Pricing for Developing Countries (Manual) –
The HC agreed with the systematic steps for determining the arm's length interest rate on loans as outlined in the Manual, which stipulate the examination of loan agreements, terms, credit rating of the lender and the borrower, and comparable third party arrangements with suitable adjustments. However, it disagreed with the Indian Administration's specific viewpoint on the use of PLR for outbound loans being contrary to accepted international tax jurisprudence.

PwC Observations

Besides recognising important global best practices in the financial transactions domain pertaining to the determination of interest rates, the HC, through this judgement, has provided critical direction to a wider universe of taxpayers by adjudicating that restructuring transactions is not within the power of tax authorities and highlighting the relevance of commercial relationships in determining ALPs.

Transfer pricing has been an area that has seen significant tax litigation in India. Hence, this judgement will go a long way towards guiding and providing clarity to taxpayers, and is a step forward in the evolution of transfer pricing in the domain of financial transactions and beyond.

Coverage of international transactions

Bangalore Tribunal rules on the coverage of international transaction to even include an arrangement

TS-366-ITAT-2015(Bang)-TP

In a recent ruling the Bangalore Bench of the Tribunal, following the findings made in the taxpayer's own previous case for AY 2009–2010[6] has:

- *Upheld that the transaction between the taxpayer (A) and the Indian third party (B Limited) was "a concerted action or arrangement" between the taxpayer and its foreign entity (F Co), which was apparently intended and framed in such a manner as not to attract the provisions of Section 92B of the The Act;*
- *Upheld that the transaction between the taxpayer and the Indian third party could not be subject to the provisions of the TP regulations, as it did not result in any base erosion. However, the transaction which involved the import of raw materials by B Limited from F Co, would be* subject to the *transfer pricing regulations because of the possibility that it could result in base erosion;*
- *Upheld that the taxpayer in respect of the transaction*

6. Novo Nordisk India Private Limited v. DCIT (ITA No 122/Bang/2014, ITAT Bangalore).

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of import of raw materials by B Limited from F Co was acting as a manufacturer and not a distributor, since it was considered that the Indian third party was acting as a contract manufacturer for the taxpayer, given that the taxpayer was completely in charge of the overall manufacturing process;

- *Upheld that the subvention fee received by the taxpayer to ensure arm's length operating margin should not be subjected to ALP determination and should be set-off against the transfer pricing adjustment; and*
- *Directed the TPO to determine the ALP for the manufacturing and trading segment separately, after evaluating the facts of the case and determining the most appropriate method.*

Facts

The taxpayer, an indirect subsidiary of F Co, was primarily engaged in the sale of drug formulations, drug delivery systems and other specified pharmaceutical products (together referred to as, "formulations") in India.

These formulations were imported directly by the taxpayer from F Co ("imported formulations") as well as sourced locally from a third party manufacturer i.e. B Limited ("locally purchased formulations").

The transaction flow between F Co, B Limited and the taxpayer with respect to the locally purchased formulations was as follows:

- B Limited purchased the raw materials from F Co;
- B Limited then used the technical knowledge provided by the taxpayer and the aforementioned raw materials to manufacture the formulations, free of charge;
- B Limited then supplied the formulations to the taxpayer for sale in the Indian market.

In the transfer pricing study report, the taxpayer claimed in Form 3CEB that the purchase of raw materials by B Limited from F Co was an international transaction.

The taxpayer characterised itself as a "distributor" in respect of both imported and locally purchased formulations. The international transactions carried out with regard to the import of formulations, purchase of raw materials by B Limited from F Co, payment of quality testing fees and receipt of subvention fee were aggregated under the "distribution segment" as they were closely linked transactions. The net operating margin arrived at was 2% on sales. The taxpayer applied the TNMM using comparable pharmaceutical distributors and concluded that all its aforementioned international transactions that formed part of the distribution segment were at arm's length.

However, the TPO contended that the arrangement between the taxpayer, F Co and B Limited with respect to locally purchased formulations did in fact constitute a manufacturing activity and could not be characterised as a distribution activity. Thus, he conducted a fresh comparability analysis for Indian manufacturers and determined that the arm's length operating margin at 8.26% on total sales, by applying the TNMM method. While applying the aforementioned margin, the TPO did not consider the fact that the total sales were not entirely composed of purchased products from B Limited (in fact more than 61% of the total purchases by the taxpayer were finished products imported from group companies). Furthermore, the TPO had also applied the PSM in respect of the aforementioned arrangement. Aggrieved by the order of the TPO, the taxpayer filed its objections with the DRP.

During the course of the proceedings before the TPO/DRP, the taxpayer argued that the provision of Section 92B(2) of the Act was applicable only in cases where at least one of the parties was a non-resident, whereas in the current case, both B Limited and the taxpayer were residents. Furthermore, F Co and B Limited were not AEs and hence, the transaction pertaining to the supply of raw materials to B Limited did not fall within the definition of an international transaction. The DRP issued the directions, in principle, upholding the order of the TPO. Aggrieved by the DRP's directions, the taxpayer preferred an appeal before the Tribunal.

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Held

Applicability of Indian Transfer Pricing Regulations to the arrangement between the taxpayer, F Co and B Limited

With regard to this issue, the Tribunal, following the findings made in the taxpayer's own case for AY 2009–2010, held that:

- The sum and substance of all the agreements was the supply of raw materials by F Co to the taxpayer, to enable the latter to manufacture finished formulations and sell them in India. All the agreements between the taxpayer, B Limited and F Co refer to each other and specifically incorporate the terms of one agreement into the other. It was a "concerted action or arrangement", brought out in a "form" which was framed in a manner so as not to attract the provisions of Section 92B of the Act. Since one of the parties to the transaction was a non-resident, the conditions specified in Section 92B(1) of the Act was satisfied and there was no necessity to look at the provisions of Section 92B(2) of the Act.
- The judicial precedents[7] relied upon by the taxpayer were distinguished based on facts. The Tribunal stated that the concept of a transaction between two "residents" who were AEs being regarded as an "international transaction" was implicit in the scheme of transfer pricing provisions in India, if it impacted or eroded the tax base in India. The amendment to Section 92B(2) of the Finance Act, 2014 was inserted only by way of abundant caution. It was made with a view to clarify the position that by entering into a series of transactions with third parties who were not AEs, one could not claim that the transfer pricing regulations would not apply, if in reality and in substance, transactions were with related parties, at least one of whom was a non-resident.
- The application of PSM as the most appropriate method required reconsideration since the taxpayer was not given an adequate opportunity before the lower authorities to make submissions on the same.

Import of formulations directly from F Co as well as sourced locally from B Limited not closely linked

With regard to this issue, the Tribunal, following the findings made in the taxpayer's own case for AY 2009–2010, held that:

- While the sale of imported products was a trading activity, the purchase of raw material by B Limited from F Co for supply of formulation to the taxpayer was in the nature of manufacturing activity undertaken by the taxpayer. Thus, taking different parameters into consideration was a requirement for determining the ALP of the two transactions. The two transactions had no connection whatsoever and hence, needed to be evaluated individually.
- The payment of quality testing fees by the taxpayer to F Co constituted a completely different transaction from those mentioned above, and having no connection whatsoever their evaluation could take place independently.

In view of the above, the Tribunal set aside the matter to the files of the TPO/DRP with the following directions:

- The TPO/DRP had erred in characterising both the activities (i.e. the sale of imported products and locally procured from B Limited) as manufacturing activities instead of using the segmental profitability.
- The subvention fee claimed by the taxpayer from F Co to sustain its business operations, had to be set off against any potential transfer pricing adjustment, i.e. the receipt of subvention was not separately subject to the ALP test.

PwC Observations

- The Tribunal did not confine itself to the legal/contractual arrangement, and looked at the entire arrangement while adjudicating the matter. It interpreted the definition of transaction as including an "arrangement", while coming to the conclusion that the supply of raw materials by F Co to B Limited was covered within the purview of international transactions under section 92B(1) of the Act. The Tribunal, on careful consideration of all the agreements decided

7. Swarnandhra IJMII Integrated Township Development Private Limited *v.* DCIT – ITA No. 2072/Hyd/2011 order dated 31.12.2012 and Kodak India Private Limited *v.* ACIT – ITA No. 7349/Mum/2012 order dated 30.4.2013.

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that the agreements when read together, showed that an agreement emerged between F Co and the taxpayer pertaining to the supply of raw materials. This was an important observation on part of Tribunal, as it re-emphasised the need to look at the substance of a transaction while evaluating the applicability of TP regulations.

- The Tribunal reiterated the fundamental principle that TP regulations apply to both residents as well as non-residents, provided that the tax base in India has been impacted or eroded. Thus, the base erosion principle has been emphasised here.
- The Tribunal looked at the substance of the entire arrangement and re-characterised the taxpayer as a "manufacturer" instead of a "distributor" with respect to the international transaction pertaining to the import of raw materials by B Limited from F Co. Thus, looking at the substance of the entire arrangement is required for defining the characterisation of parties to the transaction.
- The Tribunal held that subventions received by taxpayers could be set off against the transfer pricing adjustments, and are not required to be separately benchmarked, which is a welcome pronouncement for taxpayers, since some TPOs tend to view subventions as being non-operational, leading to increased litigation.

Berry Ratio

Use of the "Berry ratio" as a PLI upheld

Marubeni Itochu Steel India Private Limited v. DCIT [2015] 60 taxmann.com 464 (Delhi - Trib.)

In a recent ruling, the Delhi Bench of the Tribunal, placed extensive reliance on the ruling made by the same bench in the case of Mitsubishi Corporation India Private Limited (Mitsubishi)[8], and did the following:

- *Upheld the use of the "Berry ratio" as a PLI.*
- *Rejected the TPO's re-characterisation of the taxpayer's service activity as a trading activity.*
- *Rejected the TPO's contentions pertaining to the attribution of additional returns on account of location savings, and certain supply chain and human intangibles owned/developed by the taxpayer.*

Facts

The taxpayer's business, an Indian subsidiary of a Japanese general trading company (Sogo Shosha[9]) dealing in steel, comprised of:

- Provision of support services – entailed the taxpayer rendering facilitation, and liaising services to its group companies for purchase/sale of goods from/into India; and
- Trading – the purchase of steel products (based on confirmed orders) from group companies for re-sale in India.

In the TP documentation maintained by the taxpayer, TNMM was selected as the most appropriate method using the operating profit/value added expenses (OP/VAE) and OP/Sales as the PLI with regard to the provision of support services and the trading segment respectively.

During the transfer pricing assessment, the TPO accepted that the international transactions pertaining to the trading segment were at arm's length. However, with regard to the provision of support services segment, the TPO re-characterised the service activity as a trading activity; included the value of the goods on which the taxpayer had earned service income in the cost base; applied OP/total operating costs as the PLI; and re-computed the ALP, thereby making a transfer pricing adjustment. The TPO was of the view that:

- Rule 10B(1)(e)(i) of the Rules did not prescribe the use of value added costs/value added expenses as a cost base for computing the net profit margins– accordingly the taxpayer's claim concerning the use of the Berry ratio was not accepted;
- the commission business of the taxpayer was equivalent to the trading business;
- The existing cost-plus model of the taxpayer did not compensate it for the unique intangibles developed by it, such as supply chain management and human assets s; and

8. Mitsubishi Corporation India Private Limited *v.* DCIT (ITA No. 5042/Del/11, ITAT Delhi).

9. Sogo Shosha companies are general trading companies, which deal in diverse range of products, linking the buyers and sellers and performing the role of trade intermediaries.

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- the compensation model did not remunerate the taxpayer for location savings

Aggrieved by the TPO's order, the taxpayer filed its objections with the DRP. The DRP issued directions, which in principle, upheld the TPO's order; but directed the TPO to include the correct "Free on Board" value of goods for the purpose of computing the adjustment for the international transactions. Aggrieved by the DRP's directions, the taxpayer preferred an appeal before the Tribunal.

Held

Permissibility of the "Berry ratio"

The Tribunal, relied on the ruling of the same bench in the case of Mitsubishi[7], and upheld the use of the "Berry ratio" as a PLI.

In the case of Mitsubishi[7], the Tribunal had made the following observations:

- With respect to the contention of the Revenue that use of the "Berry ratio" was not permitted under Rule 10B(1)(e)(i) of the Rules, the Tribunal ruled that the PLI computation methodology set out in the Rules was illustrative and not exhaustive as it ended with the phrase, "or having regard to any other relevant base". In a situation like the taxpayer's, where the significant functions and risks pertaining to inventories were not undertaken, the cost of inventory became irrelevant, and only the value added expenses needed to be considered in the cost base for computing the PLI.
- The Tribunal rejected the TPO's contention that the differences in cost classifications precluded the application of the Berry ratio, by relying upon the co-ordinate bench ruling made in the case of GAP International Sourcing India Private Limited. It further added that the TPO had not brought forward any specific issues with regard to cost classifications, which could have hampered the appropriateness of selecting the Berry Ratio as the PLI.
- The Revenue had contended that the taxpayer had a high number of current assets. While the Tribunal agreed with the principle that the "Berry ratio" was only applicable in a situation where the current assets were not significant, it ruled that in the taxpayer's case, the TPO had not been able to demonstrate that the taxpayer had significant current assets.

Our observation

The acceptance of the "Berry ratio" as a PLI is indeed a welcome step, in keeping with the fundamental principle of TP that the arm's length remuneration should be consistent with the functions performed, risks assumed and assets employed. This reinforces that the use of the "Berry ratio" by taxpayers for determining the arm's length remuneration for distributors and agents undertaking limited functions and bearing limited risks in connection with inventory handled, is the correct approach.

Re-characterisation of service activity as a trading activity

The Tribunal, relying on the Delhi HC (the jurisdictional HC) Ruling in the case of Li & Fung India Private Limited[10] and on the Ruling in the Mitsubishi case[7], rejected the re-characterisation of the taxpayer's services activity as a trading activity.

The Delhi HC, in the case of Li & Fung[9], had held the following:

- Under the Indian TP regulations, for TNMM to be applicable, the net margin realised from international transactions had to be calculated only with reference to the cost incurred by the taxpayer, and not that incurred by any other related or third party.
- Rule 10B(1)(e) of the Rules did not enable consideration or imputation of cost incurred by third parties or unrelated enterprises in computing the taxpayer's net profit margin for application of the TNMM.
- It was not open to the revenue authorities to reconstruct the taxpayer's financial statements by including the cost of products incurred by the AE, in respect of the services rendered, in its reconstructed financial statements, and then computing hypothetical trading profit.

Our observation

In adjudicating this issue, the Tribunal has relied on the principle laid down by the jurisdictional HC. In this case, the taxpayer painstakingly brought out the differences in the functional profile of a service provider *vis-à-vis* a distributor, before the Tribunal, on account of which

10. Li & Fung India Private Limited *v.* CIT [2014] 361 ITR 85 (Delhi).

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the TPO's re-characterisation was ascertained as being fallacious. While the Tribunal did not discuss this aspect of the case while adjudicating the matter, we would like to reinforce the fact that the characterisation of a taxpayer would follow its functional profile. Hence, it was not correct to re-characterise the service provider as a distributor without taking cognizance of the difference in the functional profile of the two, that is, the service provider and the distributor.

Existence of intangibles in the nature of supply chain and human assets

The Tribunal, relied upon the same bench's ruling in the case of Mitsubishi[7], and rejected the TPO's contentions that the taxpayer owned supply chain management intangibles and human assets by observing that the TPO could neither infer nor assume the use of intangibles. Rather, the demonstration of the same was required on the basis of cogent materials. In the current case, the TPO could not substantiate that the taxpayer's activity had resulted in the development or use of unique intangibles, which had an impact on determining the ALP.

In the Mitsubishi case[7], the same bench of the Tribunal held that:

- Any comparable involved in a similar activity would essentially use similar intangibles, and accordingly, an adjustment could not be made in the case of routine intangibles.
- While a trained workforce was, indeed, an intangible asset, it also constituted a routine intangible inasmuch as anyone pursuing a business activity would develop a trained workforce for carrying out that activity.
- For an intangible to have had an impact on the determination of the ALP, not only should the intangible have existed, but it should have also been a unique intangible, which provided an edge to the business in which it was used.

Our observations

The Tribunal has laid down a great principle with regard to the impact intangibles haves on the determination of the ALP. It is only the non-routine or unique intangible which has an impact on the determination of the ALP. Comparables make use of routine intangibles, and the return attributable to the same is embedded in the profit margin reflected by such comparables. This does not call for additional return. It is only in the case of unique intangibles, that one needs to ascertain the additional return attributable to such unique intangibles. Thus, unless it is demonstrated based on facts that the taxpayer is using non-routine intangibles, an automatic claim for additional returns attributable to such intangibles cannot be made.

Location savings

On this issue too, the Tribunal relied on the Mitsubishi India decision[7] and concurred with the view that the adjustment pertaining to locational savings was unwarranted.

In Mitsubishi India's case[7], the same bench of the Tribunal, agreed to the four steps process advocated under the OECD report titled "Guidance on TP Aspects of Intangibles", but observed that:

- Neither had the TPO followed the aforementioned steps, nor had he demonstrated any concrete findings with regard to the existence of any location savings.
- In the "*Sogo Shosha*[8]" business model, where the service provider only acted as a facilitator, there may, in fact, be no location savings for the service provider. With regard to the procurement of goods, location savings, if any, would arise for the AEs actually purchasing the goods, and not for the taxpayer assisting such purchases by way of acting as an intermediary. Further, these savings may eventually be derived by the ultimate customer.

Our observation

The Tribunal rejected the contention of location savings on the basis that the TPO could not substantiate this argument with facts. However, the Tribunal did not discuss the fact that as long as the comparables were also operating in similar conditions, there could not be any additional return attributable to location savings. The comparables would have benefitted from location savings in a similar manner and hence, the return earned by comparables would include the return for location savings, thereby resulting in no further attribution of return towards location savings. Taxpayers could also rely on this economic argument to defend the issue of location savings.

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PwC Observations

The fact that the Tribunal has reiterated the principles emerging out of the Mitsubishi ruling[7] with regard to the use of the "Berry ratio" as a PLI is a welcome move. This reinforces the fundamental TP principle that the arm's length return should be commensurate with the functions performed, assets employed and risks assumed by the taxpayer. Thus, in the case of distributors and agents who undertake limited functions and bear no significant risks with respect to inventory, and do not deploy any unique intangibles, the use of the "Berry ratio" could be an appropriate PLI for determining the arm's length remuneration. Internationally, use of the "Berry ratio" is quite frequent, especially for determining the remuneration for distribution functions. The acceptance of this PLI by the Indian judiciary would result in a boost with regard to the use of this PLI by Indian taxpayers.

In applying the "Berry ratio", one needs to lay great emphasis on the functional similarity of the comparables identified *vis-à-vis* the tested party, identifying comparables not deploying or developing any unique intangibles, similarity in the cost classifications since any variation in the same could distort the comparability, etc. This calls for a detailed and exhaustive comparability analysis.

Notwithstanding the above, this ruling, however, lays down an important judicial precedent, that the use of the "Berry ratio" as a PLI is appropriate in some cases.

Functional Analysis

Mere super profits/losses cannot be criterion for rejecting a comparable; circumstances for using "multiple year data" explained

Chryscapital Investment Advisors (India) Private Limited v. DCIT [2015] 56 taxmann.com 417 (Delhi)

Recently, the Delhi HC emphasised that functional analysis was the key comparability criterion, and inter alia, held that:

- *The mere earning of high profits/losses could not be a reason for the exclusion of a company as a comparable; and*
- *For the purpose of comparability analysis, the use of data of multiple years was permissible, but only when such data had an influence on the TP of the transaction under consideration.*

Facts

- The taxpayer was a private limited company, engaged in providing investment advisory services on a cost-plus mark-up basis to its AE. TNMM was used, as it was the most appropriate method for determining the ALP of the international transaction under consideration.
- The taxpayer selected four companies as comparables and computed the operating margin of these comparables by using "multiple year data". In this regard, the taxpayer relied on Rule 10B(4) of the Rules.
- During the course of the TP assessment, the TPO made an adjustment to the taxpayer's income on account of the following:
  - the addition of two new companies with abnormal profits [*viz.* Brescon Corporate Advisors Limited (Brescon) and Keynote Corporate Services Limited (Keynote)] to the set of comparable companies selected by the taxpayer;
  - the fact the TPO computed the operating margin of the set of comparable companies using single year data by stating that the taxpayer did not furnish any detail as to how the data of earlier years had an impact on the profits of the taxpayer in the relevant AY, or on the comparables;

The DRP and the Tribunal confirmed the approach adopted by the TPO. Aggrieved, the taxpayer preferred an appeal before the HC.

Held

The Court set aside the matter to the file of the DRP for the examination of the facts pertaining to the comparable companies (i.e., Brescon, Khandwala and Keynote), and held that:

- Rule 10B of the Rules provided sufficient guidance and clarity on the principles applicable for determination of the ALP, and that functional analysis (functions performed, assets employed, risks assumed, contractual terms, market/geography, competition, terms of contracts etc.) was the key for comparability analysis.
- It was necessary to attempt to eliminate/adjust for dissimilarities (between the comparable and the tested transaction), which have a material impact on the

price. In the event that there could be no elimination/adjustment, the exclusion of the comparable had to take place.

- The mere fact that an entity made extremely high profits/losses did not, *ipso facto*, lead to its exclusion from the list of comparables for the purposes of determining ALP. In such circumstances, an enquiry had to be carried out under Rule 10B(3) of the Rules, to determine whether the material differences between the taxpayer and the comparable under consideration could be eliminated/adjusted.
- While determining the comparability of transactions, “multiple year data” could only be included in the manner provided in Rule 10B(4) of the Rules, that is, prior years’ data could be considered if such data could be shown to have an influence on the determination of the TP with regard to the international transaction under consideration.
- As a general rule, it was not open to the taxpayer to rely upon “multiple year data”. Wide fluctuation in the profit margins of comparables from year-to-year *per se* did not justify the need for using “multiple year data”.
- Proviso to Rule 10B(4) of the Rules, read together with the sub-rule, did not prescribe the use of an arithmetic mean of 3 years (i.e., current year and two prior years) of a given comparable to obviate an apparent volatility in the data, as it would lead to assigning equal weight to the data for each of the three years, which was against the mandate of Rule 10B(4) of the Rules.
- Use of the word “shall” in Rule 10B(4), and the word “may” in the proviso, implied that the data of the current year was of primary consideration as opposed to the previous year’s data.
- Given that India is not a member of the OECD, the OECD Guidelines[11] only had persuasive status and did not have any legal effect. As the Act and the Rules were adequate, the reliance on OECD Guidelines[10] was considered unwarranted.

11. Transfer Pricing Guidelines for Multinational Enterprises and tax Administrations issued by the Organisation for Economic Co-operation and Development (OECD).

PwC Observations

The HC stressed that functional comparability is the key criterion for the selection of comparables, and has also endorsed the need for making appropriate adjustments to eliminate material differences between the comparables and the tested transaction.

The HC’s view on non-exclusion of comparable companies merely on account of earning super profits/loss is in line with the view taken by the Special Bench (SB) of the Tribunal in case of Maersk Global Centres (India) Private Limited[12]. In such cases, the HC has emphasised the need for undertaking a detailed analysis in such cases, to figure out the reasons for the differences and make adjustments to eliminate them.

The HC has laid down the principle that the taxpayers need to use single year data for the purpose of benchmarking, unless it is demonstrable that the prior years’ data will have an influence on the determination of the ALP. However, it is pertinent to note that at the time of preparation of transfer pricing documentation, the data for the current year is seldom available in the public domain. Therefore, it is a practical challenge for the taxpayers to use the current year data for the purpose of comparability analysis; the HC did not address this practical aspect in its ruling.

The Finance Ministry has taken note of this problem, and the 2014 Budget had proposed to amend the transfer pricing regulation to allow the use of multiple year data. Such an amendment is a welcome measure that would definitely provide a significant relief to taxpayers tackling this practical challenge.

Marketing Intangibles

Delhi HC rules on marketing intangibles in the case of distributors

[2015] 55 taxmann.com 240 (Delhi)

For several taxpayers in India, the Revenue authorities alleged incurring of “excess” AMP, thereby creating a marketing intangible for the AE. The AE was required to compensate the taxpayer for such brand building services along with a mark-up. The measurement of the “excess” took place with respect to the AMP expenditure of comparable companies.

12. Maersk Global Centres (India) Private Limited *v.* ACIT [2014] 43 taxmann.com 100 (Mumbai-Tribunal)(SB).

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This rationale, applied by the Revenue authorities, was largely upheld by the Special Bench (SB) in the case of LG Electronics[13] *(LG ruling), which was consequently applied to several interveners in that case who were parties to the proceedings before the SB, and was later followed in the cases of many other taxpayers.*

The appeals before the Delhi HC were filed by various affected taxpayers (most of whom were interveners before the SB) against the Division Bench rulings in their respective cases, wherein essentially the ratio of the LG ruling was applied regardless of their individual fact pattern.

The HC recently announced its ruling in respect of marketing intangibles in the case of taxpayers who were engaged in the import, marketing and distribution of their AEs branded products.

The HC, in its ruling, provided guidance on the appropriate approach towards the issue of marketing intangibles in cases where the taxpayers have been characterised as distributors. The HC held that it was not obligatory to subject the AMP to a "bright line" test and consider non-routine AMP as a separate transaction. The HC concluded that the function of marketing and distribution were closely connected, and hence could be bundled together to determine the ALP. Furthermore, upon testing the bundled transaction under either TNMM or RPM with appropriate comparables, the conclusion reached was that the transactions were at arm's length, and there was no need to bifurcate and look at AMP as a separate transaction.

In detail

The HC considered the following 2 broad sets of facts for distributor taxpayers:

Scenario 1

The taxpayers adopted the TNMM as the most appropriate method to justify the ALP on the import of finished goods. The TPO accepted the TNMM. However, the TPO alleged that by incurring "excess" AMP, the taxpayer had contributed to brand building for the AE. The TPO used the "bright line"[14] test to determine the "excess" AMP. A transfer pricing adjustment was made in accordance with the "excess", along with a mark-up of 15%. The DRP accepted the TPO's approach, but granted partial relief by reducing the mark-up from 15% to 12.5%. The Tribunal followed the SB's LG ruling and upheld the TPO's and DRP's orders, against which, the taxpayer filed an appeal before the HC.

Scenario 2:

The only difference between the scenario described below, and *Scenario 1* was that the taxpayers considered the RPM to justify the ALP of the international transaction pertaining to the import of finished goods. Furthermore, the taxpayer had also paid royalty to its AE, which was justified at ALP based on the Comparable Uncontrolled Price Method (CUP).

The HC adjudicated on the following common questions of law:

Whether the additions suggested by the TPO on account of the AMP, was beyond its jurisdiction and "bad in law", as the TO made no specific reference to the retrospective amendment to section 92CA of the Act by the Finance Act, 2012?

The HC, on careful analysis of section 92CA(2B) of the Act, held:

- After insertion of section 92CA(2B) of the Act, w.e.f. 1 June, 2002, full effect needed to be given to the said provision and there was no case to negate or curtail the retrospective effect. The retrospective amendment had a negative effect and led to consequences that could not be unwritten or erased.
- If, during the course of the proceedings, a TPO came to a conclusion that there was an international transaction for which the taxpayer had not furnished a report under section 92E, the TPO could go into the question of ALP and apply the provisions of Chapter X. No specific reference in respect of such a hidden/unknown international transaction was required under section 92CA (1) of the Act.

The HC agreed with the LG ruling, and answered the aforementioned question in favour the Revenue.

Whether the AMP incurred by the taxpayer in India could be treated and categorised as an international transaction under section 92B of the Act?

13. LG Electronics India Pvt Ltd *v.* ACIT [2013] 29 taxmann.com 300 (Delhi-Tribunal)(SB).
14. Bright line applied by the TPO is the arithmetic mean of the AMP/ Sales ratio of comparable companies.

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The HC held that:

- It had to reject the contention that the AMP was not an international transaction. There seemed to be an inconsistency in the taxpayers' submission with regard to this aspect because, in most previous cases, the taxpayers submitted that the international transactions that took place between them and the AE included the cost/value of the AMP incurred in India.
- The question was not whether the taxpayer had incurred the AMP in India. The arm's length determination pertained to providing adequate compensation to the taxpayer for performing functions of marketing and incurring non-routine AMP in India. The quantum of expenditure paid by the taxpayer to third parties in India while incurring the AMP was not in dispute and not relevant to arm's length pricing or determination.

The HC seems to have accepted the stand taken in the LG ruling that a transaction did exist, whereby the taxpayer incurred AMP towards the promotion of the brand, legally owned by the AE.

Whether, under Chapter X of the Act, a transfer pricing adjustment can be made by the TPO in respect of expenditure treated as AMP, and if so, under what circumstances?

The HC held that the principles laid out in Chapter X did not artificially broaden, expand or deviate from the concept of "real income", that is, profits arrived at on commercial principles, subject to the provisions of the Act. The profits and gains report had to be true and correct, and neither under- nor over-stated. The ALP sought to correct the distortion and shifting of profits, to tax the actual income earned by a taxpayer. Thus, the outcome was that the profit, which would have accrued had arm's length conditions prevailed, was brought to tax.

The HC then proceeded to examine the appropriate circumstances for carrying out an evaluation of the AMP, detailed below.

Scenario 1: Taxpayers using TNMM

- TNMM could be effective and reliable when applied to closely linked or continuous transactions. It would be inappropriate to proceed with the arm's length computation methods with a pre-conceived supposition of singularity as a statutory mandate. The clubbing of closely linked transactions (including those that were continuous) was deemed permissible and not out rightly rejected.
- Aggregation of closely linked transactions, or segregation by the taxpayer, had to be tested by the TPO in terms of the four clauses stipulated in section 92C(3) of the Act, read with the Rules.
- The strength of the TNMM is that transactional differences have less of an effect on net profit indicators in comparison to some other methods. This method has proved to be more tolerant to functional differences between controlled and uncontrolled transactions, as compared to gross profit margins. Yet net profit could potentially be volatile, primarily for 2 reasons. Firstly, factors that do not affect gross profit margin and prices could influence net profit indicators due to variations in operating expenses or vice-versa. This could include variation in the AMP. The other factors include the taxpayers' competitive position in the form of price and margins. In some cases, eliminating or computing the effect of these factors may prove difficult. The difficulties in applying or accepting TNMM arise as a result of the complexity of functions and each party to the transaction(s) makes valuable unique contributions.
- In case the tested party was engaged in a single line of business, there was no bar or prohibition from applying the TNMM at the entity level. In fact, when transactions were inter-connected, a combined consideration could be the most reliable means of determining the ALP. There were often situations where it was not possible to adequately evaluate closely linked and connected transactions on a separate basis. On the other hand, segmentation could be mandated when controlled bundled transactions are not adequately compared on an aggregate basis.
- complex entities, or where one of the entities was not a "plain vanilla distributor", TNMM had to be applied when necessary, and could factor in comparables with or without adjustments. Otherwise, TNMM should not be adopted or applied on account of it being an inappropriate method. The use of the words, "plain vanilla distributor" did not mean plain vanilla situations, but value additions with each party making valuable unique contributions.

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- TNMM would not be the most appropriate method where there were considerable value additions by the subsidiary AEs.
- It would not be appropriate and proper to apply the TNMM where the taxpayer was engaged in manufacturing activities and distribution and marketing of imported and manufactured products, as inter-connected transactions. The import of raw material for manufacture could possibly be an independent international transaction *vis-à-vis* marketing and distribution activities or functions.
- In explaining that the segregation of AMP as an independent international transaction would be irrational and unsound, the HC provided the below example:

Particulars	Case 1	Case 2
Sales	1,000	1,000
Purchase Price	600	500
Gross Margin	400 (40%)	500 (50%)
Marketing, Sales Promotion expenses	50	150
Overhead expense	300	300
Net profit	50 (5%)	50 (5%)

In case 2, a distributor having significant marketing functions incurred substantial expenditure on AMP, three times more than in case 1, but the purchase price being lower, the taxpayer got adequately compensated and therefore, no transfer pricing adjustment was required.

If the AMP in case 2 was INR 50, that is, identical to case 1, and AMP of INR 100 was incurred as a separate transaction, the position in case 2 would be as follows:

Particulars	Case 2
Sales	1,000
Purchase Price	500
Gross Margin	500 (50%)
Overhead expenses	300
Marketing expenses	50
Net profit	150 (15%)

It was obvious that this would not be the correct method of computing the ALP. The purchase price adjustments/set off would be required to arrive at the ALP, if segregation of the AMP is as an independent international transaction takes place. The position may be worse for the taxpayer, if the TPO makes an addition of INR 100 and adds 15% mark-up thereto. This position was not acceptable as it was irrational and unsound.

The HC summarised the guidance on the use of TNMM as follows:

TNMM is typically applied when the related parties are engaged in a continuous series of transactions and one of the parties controls intangible assets for which the ALP/return is not easy to determine. It is favourable to apply TNMM when one party is performing routine marketing, distribution and other functions that do not involve control over intangible assets, as it allows appropriate return to the party controlling unique or difficult to value intangible assets.

Where the TPO had accepted and adopted TNMM, but then chose to treat a particular expenditure such as AMP as a separate international transaction without bifurcation/segregation, invariably, as demonstrated in the above example, this would lead to unusual and inconsistent results, since AMP was the cost or expense, and was not diverse. It was factored into the net profit of the inter-linked transaction. A comparison of a horizontal item without segregation would be impermissible.

Scenario 2: Taxpayers using RPM:

- It would be wrong to assert and accept that gross profit margins under RPM would not inevitably include AMP. The gross profit margins could remunerate an AE performing the marketing and selling functions. This had to be tested and examined without any assumption against the taxpayer.
- An external comparable should perform similar AMP functions. Similarly the comparable should not be the legal owner of the brand name, trade mark, etc. In case a comparable did not perform AMP functions in the marketing operations, or a function which was performed by the tested party, the comparable would have to be discarded. Comparable analysis of the tested party and the comparable would include reference to

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AMP. In case of a mismatch, adjustments could be made to ensure that the result was reliable and accurate. Otherwise, RPM should not be adopted.

- If on analysis of comparables including AMP, gross profit margins matched or were within the specified range, no TP adjustment was required. Routine or non-routine AMP would have no material and substantial effect on the gross profit margins where the tested party and the comparable undertook similar AMP functions.

Relevance of Brand and Brand building

In relation to Brand and Brand building, the Delhi HC held as follows:

- There was a line of demarcation between development and exploitation. The development of a trademark or goodwill took place over a passage of time and was a slow, ongoing process. In cases of well-recognised or known trademarks, the trademark was already recognisable. Expenditure incurred for promoting product(s) with a trademark pertained to the exploitation of the trademark rather than the development of its value.
- There were many examples where brand building occurred without incurring substantial advertisement or promotion expenses, and also cases where, in spite of extensive and large scale advertisements, the creation of brand values did not take place. Therefore, to assert and profess that brand building was equivalent to AMP would be largely incorrect.
- Reputed brands did not go in for advertisement with the intention to increase the brand value, but to increase sales and thereby earn larger and greater profits.
- Reputed and established brands tend to have value and goodwill. However, a new brand/trade-mark/trade name would be relatively unknown. This fact was referred to, not to make a comparison between different brands, but to highlight that these were relevant factors that could affect the function undertaken, and should be duly taken into consideration with regard to the selection of comparables, or when making subjective adjustments, and thereby, for computing the ALP as well.
- Routine or day-to-day marketing or sale promotion expenses, even when excessive and exorbitant, could not amount *per se* to “brand building” expenses.
- It would be incorrect to treat advertisement as being equivalent or synonymous with “brand building”, for the latter in the commercial sense referred to several facets and components, primarily the quality and reputation of the product or name, which was acquired gradually and silently over time.
- The above arguments failed to incorporate the fundamental principle of international taxation and Chapter X of the Act, which state that the foreign AE and the taxpayer were 2 separate tax centres and taxable entities, respectively. Profits or enhanced profits consequent to a higher manufacturing turnover would be subject to tax in the hands of the foreign AE, whereas higher profits as a result of increased turnover relatable to distribution and marketing functions would be taxed in the hands of the taxpayer.
- The Revenue’s argument was general in nature and adopted a universal and ubiquitous approach through the contention that increased turnover would not benefit the taxpayer. Additionally, the argument was sceptical and conjectural.

Thus, the HC provided substantial guidance on how the taxpayer and TPO should approach the issue on marketing intangibles. Further, it highlighted the fault in the revenue’s interpretation that AMP was directly attributable AE’s brand building. In addition, the HC has given credence to the taxpayer’s argument that there was a benefit to the taxpayer from the increase in sales, which the Revenue could not ignore.

Whether the Tribunal was right in directing that fresh benchmarking/comparability analysis should be undertaken by the TPO by applying the parameters specified in paragraph 17.4 of the order dated 23.01.2013 passed by the SB in the LG ruling?

The HC held as follows:

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Bright Line Test

- The LG ruling mandated that each case where an Indian subsidiary of a foreign AE incurred AMP expenditure had to be subjected to the "bright line test" on the basis of comparables, as mentioned in paragraph 17.4 of the ruling. Accordingly, any excess expenditure beyond the bright line was seen as a separate international transaction of brand building. Such a broad-brush universal approach was unwarranted and amounted to judicial legislation.
- The list of parameters for ascertaining comparables in applying the "bright line test" in paragraph 17.4, and thereafter, the assertion in paragraph 17.6 that a comparison could be only made by choosing comparable of domestic cases not using any foreign brand, was contrary to the Rules. It amounted to writing and prescribing a mandatory procedure or test, which was not stipulated in the Act or the Rules.
- Applying the "bright line test" on the basis of the parameters prescribed in paragraphs 17.4 and 17.6 of the LG ruling would amount to adding and writing words into the statute and the Rules. It would also result in the introduction of a new concept, which had not been recognised and accepted in any international commentary, or as per the general principles of international taxation accepted and applied universally.
- There was nothing in the Act or Rules to hold that it was obligatory for the AMP to be subjected to "bright line test" and the non-routine AMP as a separate transaction to be computed in the manner as stipulated.
- Relied on the illustrations made by the Australian Tax Office (ATO) on various scenarios of distributors, such as simple independent distributors, distributors with marketing rights and entrepreneur distributors.
- Relied on the India chapter in the United Nations Manual on TP in para. 10.4.8.15 and held that when a subsidiary entity engaged in distribution and marketing incurred AMP expenses, the question was to ascertain whether the subsidiary AE entity was adequately and properly compensated for undertaking the expenditure. Such compensation could be in the form of lower purchase price, no or reduced payment of royalty, or by way of direct payments to ensure adequate profit margins. This ensured proper payment of taxes and curtailed avoidance or lower taxes of the Indian subsidiary as a separate juristic entity.
- There could not be any assumption against the taxpayer when ALP by applying TNMM was accepted, to infer that the purchase price did not account for and subsume AMP incurred by the taxpayer.
- The TPO had to examine the question of whether the taxpayer was performing functions of a pure distributor, or was performing both distribution and marketing functions. In case of the latter, he had to ascertain whether the TP took into consideration the marketing function, which would include AMP functions. This would ensure that the transaction price was adequate, and hence cause no loss of revenue. When the distribution and marketing functions were inter-connected and reliable, and comparables were available, the computation of ALP as a package could take place, if required and necessary, by making adequate adjustments.
- Where the TPO came to the conclusion that it was not possible to compute ALP without segregating and dividing distribution and marketing, or AMP functions, he could = proceed after providing a justification and adequate reasons. At that stage, he would have apportioned the price received or the compensation paid by the foreign AE towards distribution and marketing, or AMP functions. The TPO could then apply an appropriate method and compute the ALP of both independently, and even apply separate methods. This would have to be in accordance with the provisions of the Act and the Rules, and the general principles of international taxation accepted and applied universally.
- In determining the ALP it was important to examine the benefits of the AMP expenditure, and to determine whether the taxpayer received share of excess profits related to local marketing intangibles in the form of enhanced profitability.
- The HC disagreed and did not accept the Revenue's position that the exercise to separate routine and non-routine AMP or the brand building exercise by applying

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"bright line test" of non-comparables. In all cases, costs or compensation paid for AMP would be "NIL", or at best, would mean the amount of compensation expressly paid for AMP. Further, in a specific case, this criterion, and even zero attribution, could be possible, where revealed and required by the facts.

- The HC referred to the fact that the Revenue relied on the rulings in the case of DHL[15] and GlaxoSmithKline[16] and on paras 6.36 to 6.39 of the OECD Guidelines. It held that the aforementioned references did not support the recognition of the "bright line test" and non-routine AMP, as a separate international transaction that was subject to arm's length pricing. However, where the Act or the Rules did not devise or enacted a contrary provision, reliance on OECD Guidelines or the UN TP Manual should not be discarded or ignored without adequate justification. Otherwise, it would amount to denial of the benefit and advantage of the study, and the dexterous and deliberated elucidations made in the extant OECD Guidelines or the UN Transfer Pricing Manual, would become redundant and superfluous. The Act and the Rules were supreme, but the OECD Guidelines or the UN TP Manual could supplement it and constitute a valuable and convenient commentary on the subject. They were not binding, but surely their rationale and articulation required consideration, if not acceptance, when warranted.
- There was no material or justification provided for holding that no independent party would incur AMP expenses beyond the "bright line" AMP expenses. It would be incongruous and presumptuous to contend, without any data or good reason, that the execution of the transactions for distribution and marketing between the foreign enterprise and the independent enterprise, did not take place. Commercial entities would likely seek appropriate margins to incur AMP expenses, while earning net profit as per market conditions.

Economic v. legal ownership

- Economic ownership of a trade name or trademark was accepted in international taxation as one of the components or aspects for determining TP. The question of economic ownership only arose in the case of long-term contracts, and where there was no negative stipulation denying it. When pleading economic ownership, the taxpayer must be able to provide proof in order for his plea to be accepted.
- Determining whether an arrangement was long-term with regard to economic ownership, or short-term, should ordinarily be based upon the conditions existing at the start of the arrangement, and not on whether the contract was subsequently renewed. However, it was open to the taxpayer to place evidence, including affirmation from the brand owner AE, that at the start of the arrangement, it was accepted and agreed that the contract would be renewed.
- Economic ownership of a brand was an intangible asset, just as legal ownership. Undifferentiated, economic ownership brand valuation was not done from moment to moment, but would be mandated and required if the taxpayer assessed was deprived, denied or transferred economic ownership. This could happen upon termination of the distribution-cum-marketing agreement, or when economic ownership got transferred to a third party. TP valuation, therefore, would be mandated at that time. The international transaction would then become a matter of TP and be subjected to tax.

Decision in the case of Maruti Suzuki and order of SC

The LG ruling had incorrectly inferred that the legal principles and directions issued by the HC in the case of Maruti Suzuki (which the SC sent back for re-examination to the TPO) would continue to be binding *decidendi* and had attained finality, *vis-à-vis* the tax authorities and the Tribunal.

Marketing or selling expenses

- The distribution and marketing exercise required the transfer/sale of goods to third parties, be it sub-distributors or retailers. This transaction was in the nature of sale of goods for consideration. The marketing or selling expenses like trade discounts, volume discounts, etc., offered to sub-distributors or retailers, were not in the nature and character of

15. DHL Corp *v.* Commissioner, T.C. Memo 1998-461, 1998 Tax Ct. Memo LEXIS 461,76 T.C.M. (CCH) 1122, T.C.M. (RIA) P98461 (T.C. 1998).
16. Canada *v.* Glaxo Smithkline Inc. 2012 SCC 52, with docket No. 33874, dated 18.10.2012.

"brand promotion". They were not directly reflective of "brand building" exercises, but had a live link and direct connection with marketing, and increased volume of sales or turnover. The brand building connection was too remote and faint. To include and treat direct marketing expenses like trade or volume discount or incentive as "brand building" exercises would be contrary to common sense and would be highly exaggerated.

- Expenses in the nature of selling expenses had an immediate connection to the price/consideration payable for the goods sold. They were not incurred for publicity or advertisement. Direct marketing and sale-related expenses or discounts/concessions could not form part of the AMP.

Order of Remand

After laying down the above principles, the HC remanded the matter back to the Tribunals for *de novo* consideration, as the legal standards/ratio accepted by the Tribunal was erroneous. The Tribunal needed to ascertain the facts based on the legal ratio laid down by the HC in this decision. Further, the HC directed the Tribunals to endeavour to dispose off the appeals, as opposed to remanding them to the TPO. The Tribunal was required to ascertain whether the gross/net margin would duly account for AMP. If it did, the taxpayer's appeal had to be accepted. Only where there was a doubt or another view was plausible, would a remand to the TPO be justified.

PwC Observations

Key insights

The issue of marketing intangibles is concerned with the fundamentals of economics and TP. The HC, in its order, has not only provided clarity on the legal aspects dealt with in the LG ruling, but has also put forth fact-specific conclusions in the cases of the distributors dealt with therein.

The HC has appreciated that the issue of marketing intangibles requires an in-depth factual analysis, depending upon the FAR profile of each taxpayer and its AEs. The HC dismissed a common dictum, which would apply across the board as per the LG ruling. Having said that, we have provided our analysis of the key observations made by the HC, below.

Although the HC has ruled in the case of distributors, since it has dealt with the legal principles in its ruling, there could be merit in borrowing and leveraging on the HC's conclusions, in the case of licensed manufacturers as well. Our specific analysis in this regard is as follows:

- The HC has held that brand building is not equivalent to advertisement and sale promotion. In the context of licensed manufacturers, this would be relevant, as the brand value not only consists of the trademark or trade name but also includes the contribution of infrastructure, knowledge, ability to compete, etc. Also, the HC's clarification that routine or day-to-day marketing or sale promotion expenses, even when excessive and exorbitant, would not amount *per se* to "brand building" expenses is relevant.
- The "bright line test" is not stipulated and mandated in the Act or the Rules. This observation by the HC could also have applicability to licensed manufacturers as this negates the observations made in the LG ruling, which was in the context of a licensee.
- The HC has dealt with the issue of Economic *v.* Legal ownership, and in doing so has provided sanctity to the concept of economic ownership *per se*. Although dealt with in the context of distributors, the concept of economic ownership is far more relevant for licensed manufacturers.
- The HC has referred to and placed reliance on the global guidance available (OECD, ATO, US IRS, etc.) This is a welcome observation, because globally, this issue is in the context of distributors and not licensed manufacturers.

The HC has placed emphasis on the relevance of the intensity of the AMP function, in regard to choosing potential comparables. However, the HC has not provided specific guidance on how to measure the intensity of the functions.

Concluding remarks

The issue around marketing intangibles is highly factual, depending upon the FAR profile of each taxpayer, for which

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a common dictum could not have been laid down on merits of the issue, applying to taxpayers across the board. The resolution on merits for licensed manufacturers is far from over, as facts pertinent to licensed manufacturers have not been dealt with by the HC. Nonetheless, taxpayers who are licensed manufacturers are advised to follow correct approach in line with fundamentals of TP, and leveraging upon relevant legal principles laid out in this ruling.

The HC ruling gives the distributor community a reason to cheer. Further, the HC ruling will go a long way in boosting the confidence in the Indian judiciary as the guiding force for laying down the right principles on the subject of transfer pricing.

Conduct *v.* Contract

Functional/risk profile rather than solely contractual arrangement decide the ALP of international transactions

[2015] 53 taxmann.com 253 (Kolkata - Tribunal)

In a recent ruling, the Kolkata Bench of the Tribunal held that the overall business model and functional and risk allocation in the transactions between AEs had to be given consideration, rather than solely relying on contractual arrangements for determining the ALP of the transactions.

Facts

The taxpayer was engaged in the business of rendering IT services. During the AYs 2005–2006 and 2006–2007, the taxpayer entered into international transactions with its AEs, *viz.* “I2A” and “I2B” respectively.

The taxpayer and its AEs operated under a global delivery model for IT services, wherein the allocation of functions and revenues was defined under a Master Service Agreement (MSA). The MSA stated that the AEs would provide marketing and administrative services to the taxpayer. The business was conducted under the following two revenue sharing models, based on the contracting preference of customers:

Model 1 - customer contracts entered into directly with the taxpayer. In such cases, the taxpayer retained 75% of the revenues and paid 25% to the AEs for marketing and administrative support, as account management charges; and

Model 2 - customer contracts entered into with the AEs. In such cases, the AEs raised invoices on the customer and the taxpayer raised back-to-back invoices on the AEs for its 75% revenue share.

Hence, under both the models, the AEs retained 25% of the revenue for the marketing and administrative support services provided to the taxpayer.

The taxpayer had prepared and maintained a Transfer Pricing Report for computing the ALP of its international transactions, wherein the AEs were the tested parties, selected for justifying the ALP of the transactions. The TPO however, made adjustments in relation to the account management charges paid by the taxpayer to its AEs under Model 1 (above). He was of the view that under Model 2, AEs bore greater risk as compared to Model 1, where the customers entered into contracts directly with the taxpayer. Due to this purported risk differential, the TPO reduced the 25% revenue share paid to the AEs for account management services under Model 1, to 13% and 15% for both the AEs respectively. Aggrieved, the taxpayer appealed before the CIT(A).

The CIT(A) accepted that in both the business models, the taxpayer undertook and assumed significant and analogous functions and risks, and consequently undertook full responsibility for the delivery of IT services to the customer. The CIT(A) also agreed that under both the above scenarios, the functional and risk profiles of the AEs remained the same as they did not have the technical competencies and financial capabilities to bear any loss arising from bad debts or delivery failure, and would need to revert to the taxpayer in case any such events occurred. Aggrieved, the Revenue appealed before the Tribunal.

Held

Representatives for Revenue and the taxpayer reiterated their arguments before the Tribunal. The taxpayer contended that the TPO had accepted the revenue split of 25:75 to be at arm’s length for one of the models. The taxpayer further contended that if under both the business models, the taxpayer and its subsidiaries performed the same functions and assumed the same risk, then no adjustment was warranted to the ALP of the other model merely based on the contention that the customer contracts were entered into by different parties.

The Tribunal considered the various arguments and ruled in favour of the taxpayer, thereby upholding the CIT(A)'s order and deleting the TP adjustment. The key observations made by the Tribunal were:

- The Tribunal took cognisance of the taxpayer's global business model and the economic substance underlying the two business models. It noted that the two contracting models were optically different, but the functional and risk profile of the taxpayer and its AEs remained the same in both models, which was evident from the conduct of the parties.
- The Tribunal elaborated on the true conduct of the parties, and the fact that irrespective of the contracting model, the taxpayer's technical expertise was the key factor, and the local presence of the AEs could hardly influence customers to award a contract. The Tribunal observed that in the structure of both the contracts, the risk profiles of the taxpayer and the AEs remained the same, since the AEs did not have the financial or technical wherewithal to bear the direct risks arising out of the contracts, and that the same would eventually pass on to the taxpayer.
- The Tribunal referred to the guidance provided in the UN TP Manual[17] on the topic of "conduct of parties", wherein it was clearly mentioned that any examination of risk allocation between AEs must be done in light of the conduct of the parties. The Tribunal also noted the relevant commentary in the OECD TP Guidelines[18]; Chapter 9 (Business Restructuring)[19] wherein the issue of risk allocation between AEs had been discussed in the light of factors such as (a) the conduct of the parties; (b) ability to control the risk; and (c) financial capability to bear the risk.
- In light of such authoritative guidance, the Tribunal noted that the taxpayer had the adequate capital and technical expertise to bear the risks arising from deficiency in services, which neither I2A nor I2B possessed. Thus, even if a customer raised a claim directly against I2A/I2B, such risk would eventually pass on to the taxpayer, because I2A/I2B lacked the technical expertise or financial capability to manage or bear such risks.
- On the issue of risk quantification based on which the TPO had arbitrarily determined the revenue sharing ratio of 15% or 13%, the Tribunal held that such ad hoc adjustment was without any basis, and ought to be rejected. It also noted that such ad hoc reduction in revenue share of the AEs from 25% to 15% or 13% would result in a loss for the AEs (being the tested parties carrying lesser risks), which was an absurd outcome that was not in compliance with the arm's length standard.

Based on the above determinations and observations, the Tribunal rejected the TPO's allegation of a risk differential between the two business models, and any consequential risk adjustment. Hence, the Tribunal rejected the Revenue's appeal on this ground.

PwC Observations

This ruling deals with the very important topic of risk allocation and substance, which is gaining significant attention in the world of cross-border taxation. The case also shows an emerging trend in Indian TP audits, wherein the Revenue is going beyond classical issues like selection of TP methods or comparables, and seeking to challenge the intra-group pricing policy/contractual arrangements to make TP adjustments.

In the present case, the taxpayer succeeded in explaining and defending the true substance of the intra-group relationships based on functional conduct and risk allocation, rather than placing stand-alone reliance on the contractual arrangements. Though the Revenue's *ad hoc* approach of making a pricing adjustment based on purported risk differential was rejected, taxpayers can refer to this case to ensure that:

17. United Nation Practical Manual on Transfer Pricing, 2012.
18. OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.
19. Para 9.29, 9.30 of OECD Transfer Pricing Guidelines.

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- for any intra-group business dealings, the contractual arrangements (i.e. the "form") are fully aligned with the true conduct (i.e. the "substance") of the parties;
- adequate documentation underlying the business transaction is maintained to explain the conduct of the parties and the commercial rationale, before the Revenue and appellate authorities;
- that proper internal control mechanisms and check points are maintained to avoid or correct any misalignment between form and substance in intra-group dealings.

Location Savings

Tribunal negates location savings adjustment – taxpayer had no unique advantage, operated in "perfect competition", and was benchmarked against local comparables

[2015] 54 taxmann.com 88 (Mumbai - Trib.)

The taxpayer was engaged in contract manufacturing for its AEs and provided contract research and development services to its AEs. The AEs compensated the taxpayer for these transactions based on the total operating cost plus arm's length mark-up. The TPO made an adjustment on account of locations savings purportedly accruing to AEs, owing to the transfer of these activities from the US (location of the AE) to India. The Tribunal negated the adjustment citing several reasons, including the following:

- *The taxpayer as well as the AEs operated in a perfectly competitive market, and the taxpayer did not have exclusive access to factors leading to location-specific advantages. Therefore, the taxpayer did not have any unique advantage, and no super profit arose in the entire supply chain.*
- *Where local market comparables were available and used, specific adjustment for location savings was not required. Any benefit/advantage to the AE was irrelevant if the PLI of the taxpayer was within the range of comparables.*
- *The Indian chapter of the United Nations TP (UN TP) manual (which amongst other issues also discusses location saving) simply represented a view of Indian tax administration and was not binding on Appellate authorities.*

Facts

- The transactions with AEs, that is, contract manufacturing for AEs and provision of contract research and development services, were benchmarked separately taking local comparables. TNMM was adopted as the most appropriate method.
- The primary adjustment made by the TPO was on account of locations savings owing to the transfer of activities from USA to India[20], which, as per the TPO, accrued to AEs on both the above mentioned transactions. The TPO made the adjustment based on articles[21] available in the public domain, which contained an analysis of costs undertaken in different jurisdictions. The TPO concluded that there was a significant reduction in costs in India *vis-à-vis* those in the USA. Based on this, location savings were computed and thereafter allocated equally between the taxpayer and the AE because in the TPO's view, the taxpayer and the AE had similar bargaining power owing to their individual strengths. In doing so, the TPO relied on certain international judicial precedents, and on the Indian tax administration's position, articulated in the UN TP Manual.
- The Revenue authorities sought certain information from the taxpayer relating to the cost of production in the US, AE's competitors in the US (i.e., whether they had similar facilities in India for costs savings), the selling prices of AEs *vis-à-vis* selling prices of taxpayer to AEs, etc., which the taxpayer partly submitted. Revenue authorities alleged that the taxpayer did not submit enough details, and assumed that the impact of savings was not passed on to the ultimate consumers/ distributors.

Held

- Revenue authorities were unable to substantiate their adjustments from any authenticated/global material. Furthermore, non-submission of records could not form the basis for adjusting the ALP on bold assertions

20. This was substantiated by the TPO by referring to the Form 10K (annual report) of AEs.
21. Contract manufacturing: Indian Generic Pharmaceuticals Market-A Snapshot; Contract R&D: Clinical Trial Magnifier Vol. 1:6 Jun 2008.

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alone[22]. Therefore, one of the reasons for making the ALP adjustment had no basis.

- The taxpayer as well as AEs operated in a perfectly competitive market, and the taxpayer did not have exclusive access to factors, which could have led to location-specific advantages. As a result, no super profits arose in the entire supply chain. Thus, the taxpayer had no unique advantage over competitors.
- Comparables selected by the taxpayer were local Indian comparables that operated in similar economic circumstances as the taxpayer. Where local market comparables were available, specific adjustment for location savings was not required[23].
- The articles relied upon by the TPO were web articles and not accepted by any forum, reliance on them could thus not be treated as acceptable. Furthermore, these articles were published in 2012, whereas the taxpayer's case related to the FY 2008–2009, and thus interpolation could not be taken into consideration, unless specified.
- The TPO calculated the cost savings of AEs on the basis of articles which provided an analysis of costs undertaken in different jurisdictions. If at all this aspect was to be considered, it had to be in the context of the taxpayer, and not the AE. This was because the taxpayer was the tested party, and the international transaction had to be tested by comparing the same with uncontrolled comparable transactions, and not in the context of the AE. Therefore, financial results of the AE were not relevant, and any benefit/advantage to the AE was irrelevant if the PLI of the taxpayer was within the range of comparables[24].
- International judicial precedents (case law) relied upon by the TPO related to fiscal years 1970 and 1980 when the economic scenario was completely different primitive) as compared to the current economic scenario. Further, in those cases, taxpayers were not operating in a perfectly competitive market, unlike the taxpayer in the current case. Those taxpayers instead operated in monopolistic economic situations and there were intangibles held by, or transferred to them.
- The TPO incorrectly relied on the UN TP manual, which simply provided a view of the Indian tax administration and was not binding on appellate authorities.
- Facts remaining the same, no adjustment was made in the preceding AY on account of location savings, and therefore, the TPO's approach was inconsistent[25].
- Method followed by the TPO in making the adjustment was not prescribed by the provisions of the Act, and hence his computation was based on an incorrect method.

Based on the above, the Tribunal concluded that the TPO erred in making the adjustment on account of location savings, and eventually negated the same.

PwC Observations

- In the absence of any local guidance available on the issue of location savings, it is reassuring to note that the Tribunal, in this ruling has largely echoed the principles emanating from prevailing international guidance with regard to this issue. In fact, the Tribunal has dismissed the reliance placed on the Indian Chapter of the UN TP Manual, which is probably only an articulation of the views of the Indian tax administration on location savings. Much to the relief of taxpayers, the Tribunal has clarified that these views are not binding on appellate authorities.
- Taxpayers have been persistently arguing with Revenue authorities that the presence of a unique locational advantage is one of the pre-conditions to a location savings adjustment. The Tribunal, in this ruling, has not only explained this matter, but also ratified this argument, which is certainly a noteworthy precedent. Although not addressed in this decision, it may be worthwhile to highlight that even where a taxpayer

22. Reliance placed on decision in case of UCB India Pvt. Ltd. *v.* ACIT [2009] 124 TTJ 289 (Mumbai-Tribunal).
23. Reliance placed on ruling in case of GAP International Sourcing (India) Pvt. Ltd. *v.* ACIT [2012] 149 TTJ 437 (Delhi-Tribunal) and OECD Guidance on Transfer Pricing Aspects of Intangibles (released pursuant to Action 8 of OECD/G20 BEPS Project). Tribunal noted that G-20 countries had given their concurrence to this position, and India was a part of G-20.
24. Reliance placed on decision in case of Syscom Corporation Ltd *v.* ACIT [2013] 35 taxmann.com 600 (Mumbai-Tribunal).

25. Tribunal cited the decisions in cases of McCann Erickson India Pvt Ltd *v.* ACIT [2012] 24 taxmann.com 21 (Delhi-Tribunal) and Brintons Carpets Asia Pvt Ltd *v.* DCIT [2011] 12 taxmann.com148 (Pune-Tribunal), which the taxpayer had relied upon in this context.

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does have access to a unique local advantage, location savings may, in theory, arise but not actually materialize if, based on a factual analysis, it is established that the advantage has been passed on to the customers.

- The Tribunal has also reiterated the precedent set by the decision in case of GAP International Sourcing (India) Private Limited[22] that the need for a location savings adjustment is in the first place negated if the taxpayer meets the benchmark set by local market comparables.
- In the instant case, the Tribunal has shelved the adjustment as no location savings arose. However, even if it is established in any taxpayer's case that location savings did in fact arise, the eligibility of the taxpayer to retain or share in the location savings (or rent) would need to first be evaluated. That would be a function of the bargaining power of the parties involved, which would in turn depend upon their characterisation, functions performed, risks assumed, and assets (especially intangibles) owned and utilised. Thereafter, the question of quantifying the taxpayer's share in the location savings (or rent) would need to be answered, which would depend upon its relative contribution.
- Notably, the Tribunal has clearly discouraged the use of material by Revenue authorities, not authenticated by any forum, even though it may be available in the public domain. This is certainly a welcome verdict, and will have widespread applicability.
- The Tribunal has once again propagated and upheld the rule of consistency where facts have remained unchanged. Given that Tribunals have now repeatedly concurred with this, it would certainly be worthwhile for taxpayers (whose facts have not changed) to persevere with arguments around consistency, especially at the ground level, so as to at least avert any new adjustments transpiring on a year-to-year basis.

Circulars/Notifications

Dispute Resolution Panel

Dispute Resolution Panel - Mechanism restructured

CBDT Order No.1/2015 & 5/2015 and CBDT Notification No. 1/2015 & 91/2014

The CBDT has restructured the composition, jurisdiction and control of the DRPs across the country. It is a welcome initiative.

As a result, now:

- There will only be five Panels across the country – two each in Delhi and Mumbai, and one in Bengaluru;
- These Panels shall now comprise of Commissioners stationed at the respective Panel locations making them available all the time. They will also hold charge of respective Panel Members as their main charge and responsibility, unlike as an additional charge and responsibility in the past. This change will:
- address the long standing issue pertaining to the conflict of interest arising out of Panel Members holding dual responsibilities;
- ensure regular hearings and disposals, evenly spread out across the year; and
- provide more time for hearings and discussions in each case, unlike the cramped hearings in the past.

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The details regarding the constitution of the Panels and their respective jurisdictions are as follows:

Dispute Resolution Panel	Name of Member (*)	Headquarters	Jurisdiction	Eligible taxpayer having principal office in jurisdiction mentioned in adjacent Column
DRP-1, Delhi	1. Sanjay Puri 2. Dr Simmi Gupta 3. Raj Tandon	Delhi – subordinate to Principal Chief Commissioner of Income-tax (International Taxation).	National Capital Territory of Delhi	Cases starting with letters “A” to “P” of the alphabet, numerals, special characters and symbols.
			States of Rajasthan, Haryana, Punjab, Himachal Pradesh, Jammu and Kashmir and Union territory of Chandigarh	All Eligible taxpayer(s).
DRP-2, Delhi	1. Ashwani Kumar 2. Rajiv Sinha 3. Yogesh Kumar		National Capital Territory of Delhi	Cases starting with letters “Q” to “Z” of the alphabet.
			States of Uttar Pradesh, Uttarakhand, West Bengal, Jharkhand, Bihar, Odisha, Sikkim, Assam Arunachal Pradesh, Meghalaya, Manipur, Mizoram, Nagaland, Tripura and Union territory of Andaman and Nicobar Islands	All Eligible taxpayer(s).
DRP-1, Mumbai	4. Neena Singh Pandey 5. Hemant Jawahar Lal 6. Naresh Kumar Balodia	Mumbai – subordinate to Chief Commissioner of Income-tax (International Taxation) (West Zone), Mumbai.	Municipal Corporation of Greater Mumbai and Navi Mumbai, districts of Thane and Raigarh in the State of Maharashtra	Cases starting with letters “A” to “L” of the alphabet.
			Rest of the State of Maharashtra	All Eligible taxpayer(s).
DRP-2, Mumbai	7. Yeshwant U Chavan 8. Sanjay Singh 9. B Senthil Kumar		Municipal Corporation of Greater Mumbai and Navi Mumbai, districts of Thane and Raigarh in the State of Maharashtra	Cases starting with letters “M” to “Z” of the alphabet, numerals, special characters and symbols.
			States of Gujarat, Madhya Pradesh, Chhattisgarh and Union territories of Daman and Diu and Dadra and Nagar Haveli.	All Eligible taxpayer(s).

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DRP, Bengaluru	1. Yalavarti Rajendra 2. Jahanzeb Akhtar 3. S K Ambastha	Bengaluru - subordinate to Chief Commissioner of Income-tax (International Taxation) (South Zone), Bengaluru.	States of Karnataka, Tamil Nadu, Andhra Pradesh, Telangana, Kerala, Goa and Union territories of Puducherry and Lakshadweep	All Eligible taxpayer(s).

* They currently hold additional charge, of which they are likely to be relieved off in due course.

Safe Harbour Rules

CBDT announces "Safe Harbour Rules" for Specified Domestic Transactions of Government electricity companies

CBDT Notification No. 11/2015 [F.No. 142/7/2014-TPL] dated 4 February, 2015.

The CBDT has introduced "Safe Harbour Rules" for specified domestic transactions (SDTs) undertaken by Government companies engaged in the business of generation, transmission or distribution of electricity ("eligible taxpayer"). The Safe Harbour Rules are applicable to "eligible SDTs" that are undertaken by an "eligible taxpayer". The SDTs comprise of –

- Supply of electricity by a generating company; or
- Transmission of electricity; or
- Wheeling of electricity.

The transfer price declared by the taxpayer in respect of eligible SDTs shall be accepted by Income-tax-authorities provided that the tariff in respect of the supply of electricity, transmission of electricity or wheeling of electricity, as the case may be, is determined by the appropriate commission, as per the provisions of the Electricity Act, 2003. In order to opt for the Safe Harbour Rules in respect of eligible SDTs, the eligible taxpayer must furnish Form 3CEFB to the TO. Such an application is required to be furnished on or before the due date for the furnishing of returns, for the relevant AY, provided that ROI is furnished by taxpayer on or before the date of furnishing Form 3CEFB. The furnishing of Form 3CEFB, in respect of eligible SDTs undertaken during FYs 2012–2013 and 2013–2014, had to take place on or before 31 March 2015.

APA

APA rollback rules announced

CBDT Notification No.23/2015 dated 14 March, 2015

The introduction of provisions in the Act concerning APAs, took place with effect from 1 July 2012, vide Finance Act, 2012. At the time, these provisions did not include rollback rules. The Act incorporated the provision to provide for a rollback mechanism with effect from 1 October 2014, vide Finance Act 2014. However, there were no detailed rules provided at the time.

The CBDT recently introduced detailed rules explaining the rollback provisions and the procedure for giving effect to them. Apart from that, the CBDT has made another key amendment, wherein pre-filing consultation has become optional for the taxpayer.

In detail

The key rollback provisions are as follows:

Rollback of the agreement

- The rollback of an APA is available for the rollback years. The definition of a "rollback year" is any "previous year" that falls within the period of the four "previous years", preceding the first "previous year" covered in the APA (i.e., the regular APA).
- For example, if the applicant files an APA application on or before 31 March 2015, covering a period of up to 5 years from FY 2015–2016 to FY 2019–2020 and applies for a rollback, the rollback years can cover the period from FY 2011–2012 to FY 2014–2015.

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- Similarly, if the applicant has filed an APA application covering a period of five years from FY 2013–2014 to FY 2017–2018 and applies for a rollback, the rollback years can cover the period from FY 2009–2010 to FY 2012–2013.
- For the rollback years, the agreement may:
  - provide for determining the ALP; or
  - specify the manner in which the ALP shall be determined.
- Necessary conditions for availing rollback:
  - The international transaction under consideration should be the same as the international transaction that is subject to the regular APA;

    Observation: In cases where an applicant contends that a transaction does not constitute an international transaction as defined under section 92B of the Act, but the Revenue contends that it does - then, in such cases, going by this condition, it appears that the applicant may not be able to make use of the rollback provisions for such transactions.
  - Filing the ROI and Form 3CEB for the relevant rollback years before the due date.
  - The Rollback application should cover all the rollback years (i.e., the years falling within the period of the 4 previous years) in which the international transaction has taken place.

    Observation: This provision suggests that where there is a period of 4 years, classified as Y1, Y2, Y3 and Y4 and the transactions have taken place in only Y1 and Y2 only, then the rollback would apply for Y1 and Y2; it may not be possible for the applicant to be selective in this regard. It may, however, be noted that the prescribed Form26 includes the option of employing a somewhat contrary position, which would allow the applicant to select either Y1 or Y2, as long as reasons were provided. However, it is difficult to ascertain from a joint reading of the provisions and the Form, whether it is possible to selectively apply for rollback.
- Rollback provisions will not be applicable, in respect of an international transaction, if:
  - the Tribunal has passed an order disposing off an appeal relating to the determination of the ALP of the international transaction, at any time before the signing of the APA agreement; or
    Observation: This implies that even if the disposition of the applicant's appeal for any of the rollback years by the Tribunal or any lower tax authority thereof, is pending, as of the date of the agreement, the applicant will be entitled to the rollback provisions. However, it is important to note that the condition is that of "disposition" of appeal, which apart from resulting in a positive outcome, could lead to the matter being "set aside" or an adverse decision. In a case where the matter has been "set aside", although the Tribunal would have technically "disposed off" the case, it appears that the applicant may not be able to benefit from the rollback provisions. Even in a case where there is an adverse decision, it seems that the applicant may still not be able to benefit from the rollback provisions. However, in this regard, there seems to be a conflict in the Rules[27] itself, which requires that the applicant withdraw an appeal pending before the HC before furnishing a modified ROI in respect of a rollback year following the signing of the APA. This in effect implies that the applicant can avail rollback even after the Tribunal has disposed off the matter and the same is pending before the HC or for that matter even ruled upon by the HC.
  - The application of the rollback provision has the effect of reducing total income or increasing loss as declared in the ROI.

    Observation: For example, an Indian company (I Co.) has a cost-plus arrangement in the rollback years with its AE for cost-plus 20%. Then a rollback would not be available for a mark-up of say 18% (or any mark-up of less than 20%) as that will have an impact of reducing total income of the I Co. As a corollary, it follows that an applicant should be able to seek a rollback to agree a mark-up of 20%, in order to mitigate the risk of the said mark-up being potentially increased by the Revenue authorities in TP audits.

26. Point 8 of Form 3CEDA.

27. Sub-rule (4) to Rule 10RA of the Rules.

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- The manner of determining the ALP in the rollback years with respect to any particular international transaction will be the same as that followed in the regular APA.

  Observation: The elements of a rollback agreement could include – first, the determination of the ALP, or second, the manner in which the ALP shall be determined. The rollback rules provide for consistency in the latter. However, the rollback rules have no effect in respect of the former.

  For example, if an Indian company is a distributor, an agreement pertaining to the manner of determining the ALP could be reached based on the RPM. However, the appropriate margin that the applicant should achieve may differ for the rollback years vis-à-vis the period covered by the regular APA.
- The fee for applying for a rollback is an additional amount of INR 0.5 million (approximately USD 8,000), which is to be accompanied by an application in the prescribed Form 3CEDA.
- Timelines for applying for rollback:
  - Where the regular APA application has been filed before 1 January 2015, the application for rollback can be filed on or before 31 March 2015, or the date on which the agreement was entered into, whichever is earlier.

    For example, if an APA application was filed on 31 March 2013, then rollback could be applied for by 31 March 2015. However, if the regular APA agreement was entered into on 20 March, 2015, rollback may be applied for, on or before 20 March, 2015.
  - In case the regular APA has already been entered into before 1 January 2015, the last date of filing Form 3CEDA will be 31 March 2015, and the regular APA may be revised accordingly.
  - In case the regular APA application is to be filed by the applicant in future, Form 3CEDA has to be filed along with Form 3CED.

Observation: From the above, it is not clear as to what would be the deadline for applying for rollback in the case of applicants who have filed APA applications during the period from 1 January, 2015, to date. However, given that the deadline for filing an APA application for FY 2015–2016 is 31 March, 2015, it seems reasonable to assume that the deadline for applying for rollback in the above situation ideally ought to be 31 March, 2015.

Procedure for giving effect to a rollback

- The applicant is required to file a modified ROI for all the rollback years by the applicant, along with the proof of payment of any additional tax liability borne as a consequence of the rollback agreement.
- If for a rollback year, there is any appeal pending before the CIT(A), or the Tribunal or the HC on the issue which is the subject matter of the rollback provision, then such an appeal would need to be withdrawn by the applicant before furnishing the modified ROI.

  Similarly, pending appeals filed by the assessing officer or the principal commissioner or commissioner would need to be withdrawn within three months of filing of the modified ROI by the applicant.
- In case giving effect to the rollback provision of an agreement for any rollback year, on account of failure on the part of the applicant, takes place, then the agreement shall stand cancelled.

  Observation: A reading of this provision suggests that if the rollback does not go into effect, owing to a failure on part of the applicant, then the regular APA could be subject to cancellation. Applicants therefore would need to think through potential impediments to ensure that the rollback goes into effect (for example –they would need to obtain regulatory approval, provide details of cost incurred/margin earned by overseas tested parties, etc.) before entering into the agreement for rollback years.
- The Form 3CED has been revised and the applicant would now need to mention therein whether it is requesting a rollback or not and attach Form 3CEDA (i.e., rollback application form).

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PwC Observations

Largely, the provisions seem to be in line with the rollback rules that exist in other countries. However, there are some creases that require ironing, so as to make the rollback provisions workable, and they are as follows:

- There is a need for guidance with regard to how due-diligence will be conducted in relation to rollback, that is, whether the APA authorities would draw reference from the analysis undertaken for the regular APA, or would they analyse the rollback years on a standalone basis.
- The period of 15 days (the date of pronouncement of the rollback provisions, i.e., 16 March 2015 to 31 March 2015) is too lean a time frame for companies to decide and apply for rollback. An extension of the time frame in this regard would be welcome.
- The provision which suggests that if the rollback cannot be given effect to owing to a failure on part of the applicant, then the regular APA would also stand cancelled, seems like a very stringent provision; a relaxation on this front is required in order to not deter companies from applying for a rollback.
- Clarity is required on whether or not the selective application of rollback is permissible within the block of the four "previous years".
- Clarity is required on whether or not an applicant can avail rollback even after the Tribunal has disposed off the matter, especially in cases where the applicant has preferred an appeal to the HC or in cases that have been "set aside".
- Clarity is required on whether or not rollback provisions would be available in a case where an applicant does not believe that the transaction is an international transaction, as defined under section 92B, but the Revenue contends it to be so. In such a case the condition of filing Form 3CEB for that transaction would not be met.
- Clarity is required on whether an applicant would be given relief from penalties/interest arising from a higher than actual return agreed in the APA for rollback years. For example, if the applicant actually earned returns of 15% in the rollback years, and has agreed to a higher return of 20% *vide* the APA rollback provisions—then, clarity would be required on whether in such cases, penalties/interest would be levied/charged in respect of the additional tax liability arising on account of the higher than actual return.

The much awaited rollback rules will provide certainty for applicants for a period of nine years, which was earlier five years. Further, simplification of the APA process has resulted from making pre-filing optional for the applicant. These steps quite apparently evidence the Government's intention towards curbing, controlling and resolving the growing number of transfer pricing disputes in India and providing certainty in regard to tax laws to corporate entities.

CBDT provides clarifications on APA rollback provisions

CBDT Circular No.10/2015, dated 10 June 2015

The introduction of provisions in the Act on APAs took place with effect from 1 July 2012, vide Finance Act, 2012. The Act incorporated the provision to provide for a rollback mechanism with effect from 1 October, 2014, vide Finance Act 2014. Thereafter, in March 2015, the CBDT announced detailed rules explaining the rollback provisions and the procedure for giving effect to them (the Rules).

Subsequent to the notification of the Rules, the CBDT received several requests for clarifications regarding certain matters. To address these, the CBDT issued clarifications in a "Question and Answer" format.

In detail

The clarifications provided by the CBDT are as follows:

- Rollback provisions will be available even in the case of a revised ROI or return filed under section 139(5) of the Act, because the revised return will have the effect of replacing the original return. However, rollback provisions will not be available for a return filed under section 139(4) of the Act, because the return would not have been filed within the specified due date.
- As per the Rules, the rollback provisions are only applicable to the "same" international transaction to which the APA applies. It has been clarified that "same" implies transactions that are of the same nature, and undertaken with the same AE. Additionally, the underlying FAR of the transaction

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should not be "materially" different, that is, there should be no material change in the underlying facts and circumstances, which could result in an APA with significantly different terms and conditions.

- An applicant has to choose all the four years for rollback, unless: (a) the applicant did not undertake the relevant international transaction in any of the 4 years; or (b) the applicant fails to meet the prescribed rollback conditions for any of the 4 rollback years. In such cases, the applicant can still apply for rollback for other rollback years.

  (Observation: The CBDT has clarified that it is a requirement that the international transaction is undertaken with the same AE. However, it may be possible that the same international transaction, for a variety of reasons, was later undertaken with a different AE. This should not be the reason for prohibiting the applicability of the rollback provisions to the international transaction, so long as the international transaction is the same. It is imperative to note that the relevant Rule only refers to the "same international transaction" and not to the "same AE".

- Rollback provisions shall not be available in case a Tribunal has decided the matter on ALP determination of an international transaction for which rollback has been applied, unless the matter has been set aside by the Tribunal for fresh consideration by lower authorities, with full discretion.

  (Observation: This would imply that even in cases where a Tribunal has disposed of a matter by providing directions to lower authorities for deciding on the matter, rollback provisions would not be available because of the lack of "full discretion" available to the lower authorities.)

- Rollback provisions would be available where the application of rollback is effected in a manner such that the returned income or loss does not reduce or increase, respectively; that is, the rollback benefit would be limited to the extent of declared income, and not beyond. For example, if the returned income is INR 100, after TP adjustment the income amount would increase to INR 120, and the application of the rollback provisions would result in a reduction of the amount to INR 90. The rollback for that year would then be determined according to the declared income of INR 100, which would be treated as the final income for that year.
- If the rollback provisions have not gone into effect in accordance with the prescribed rules, then in such cases the entire APA agreement would stand cancelled.

  (Observation: Although the requirements for giving effect to the rollback provisions are largely procedural, applicants need to exercise great caution in this regard as failure to do so would jeopardise their entire APA agreement.)

- If the MAP has been concluded for any rollback year for a particular international transaction, then rollback provisions would not be available for that particular international transaction in that particular year. However, if MAP is pending for any rollback year, then, at the applicant can opt to proceed with either MAP or a rollback application for that year.
- ALP could differ for different years – however, the manner of determining the ALP as per the rollback provisions would need to be the same as that agreed in the APA (e.g., choice of method, comparability analysis and tested party).
- LP for rollback years would be agreed after full examination of facts, including validating critical assumptions. Accordingly, a compliance audit for the rollback years would be required to check if the agreed price or methodology has been applied in the modified ROI.
- An applicant can withdraw its rollback application, and still maintain the APA application for future years. However, it cannot accept the rollback results without accepting the APA for future years. In case of withdrawal, there will be no refund issued with regard to the fee for filing a rollback application.

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- Already concluded APAs (i.e., finalised before 14 March 2015) may be revised to include rollback provisions.
- For already concluded APAs, the time to file the modified ROI for all the rollback years shall commence from the date of signing the revised APA incorporating the rollback provisions.
- In case of a merger or demerger, only the entity that applied for an APA, or entered into one, would be eligible for rollback provisions. For example:
  - If A, B and C merge to form C, and C is the APA applicant, then only C would be eligible for rollback provisions – while A and B would not be.
  - If A and B merge to form a new company C, and C files an APA application, then neither A nor B would be eligible for rollback provisions.
  - If A has applied for or entered into an APA, and subsequently demerges into A and B, then only A will be eligible for rollback provisions, as B did not exist during the rollback years.

PwC Observations

Within 3 months of announcing the Rules and receiving subsequent requests for clarifications, the Government has issued the much-needed answers to various questions. The responsiveness of the Government in providing clarity to taxpayers is undoubtedly laudable. The clarifications issued are apparently quite clear, crisp and accord reasonable flexibility to the Rules. Needless to say, the clarity provided will go a long way in deterring disputes.

Although ambiguities on several aspects no longer exist, some areas remain ambiguous. It is imperative that the APA authorities take these areas into consideration when reviewing APA/rollback applications or during negotiations:

- Despite clarifying that rollback provisions shall not be available once a Tribunal has decided the matter, unless it has been set aside for fresh consideration by lower authorities, the Government has still not clarified whether rollback provisions would be available in a case where the taxpayer or Revenue before the HC contests a Tribunal order. From a conjoint reading of the Rules, it appears that rollback provisions would be available in such cases.
- One of the pre-conditions for being eligible for the rollback provisions is that the international transaction for which rollback is being applied should have been reported in Form 3CEB by the due date. Given the expansive powers of the TPO under Section 92CA subsections (2A) and (2B) to examine even those transactions which have not been reported – it may have been worthwhile for the CBDT to clarify that even if the transaction is not reported in Form 3CEB, the taxpayer would be eligible for rollback.

Further, although not expressly clarified, there is an expectation that the resolution pertaining to rollback applications could have a persuasive effect on the "stay of demand" petitions filed before Tribunals and any other appellate authorities in respect of any of the rollback years. There is also an expectation that penalty provisions would be judiciously applied when an APA and a rollback is negotiated with the Government.

In conclusion, it is fair to state that with the introduction of the rollback provisions, the prescription of rollback rules, and the fast-paced subsequent issue of clarifications, the Government has taken a positive leap towards meeting its stated "on-ground" objectives of building trust, enhancing taxpayer confidence and providing taxpayers with sought after certainty.

Range and Multiple years

CBDT prescribes final rules pertaining to the use of "arm's length range" and "multiple year data"

CBDT Notification No.83 of 2015, dated 19 October 2015

The CBDT recently issued the final rules to give effect to the use of "multiple year data" and the "range concept", introduced in the Finance Act, 2014. These rules would be applicable to international transactions and SDTs that are entered into by taxpayers on or after 1 April 2014.

In detail

Use of multiple year data

- Is applicable only in cases where RPM, CPM or TNMM is selected as the most appropriate method.
- For each comparable, the data has to relate to the current year. In case such data is not available at the

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time of furnishing the ROI, the data from up to two preceding FYs may be used.

(Observation: If current year is Year 0 and the FY preceding it is Year 1, and the year prior to Year 1 is Year 2, then it is worth noting that the rules do not envisage a situation wherein a the selection of a comparable only occurs if it has data relating to Year 2.)

- Current year data, if available during assessment, shall be used.

  (Observation: This is not in line with contemporaneous documentation requirements and the requirement that documentation should exist up until the due date for filing the ROI *[Rule 10D(4)], especially if additional comparable(s) are added during assessment. This would lead to uncertainty as to the basis of ALP determination, and may even result in penal consequences for taxpayers. Owing to this uncertainty over which the taxpayer has no control, penalty provisions, as they currently exist, may need modification).*

- If the selection of a comparable takes place on the basis of preceding year data, but does not pertain to the current year for qualitative or quantitative reasons, then such a comparable would need to be rejected from the data set.
- When using multiple year data, the data for each comparable shall be the weighted average of the selected years. An illustration explaining the computation is provided below:

	Year 0	Year 1	Year 2	Total	OP/TC for the comparable would be 900/5400 = 16.7%
Operating profit	250	300	350	900	
Total cost	1700	1800	1900	5400	

Application of range

- The "range concept" shall be applicable when: (a) the most appropriate method is either CUP Method, RPM, CPM, or TNMM; and (b) there are at least six comparables. Where it is not possible to fulfil these conditions, the "arithmetic mean" shall continue to apply, as before, along with the tolerance range benefit.

  (Observation: Specifying the number of comparables may lead to a situation where the taxpayer uses the range for setting a TP, but may have to apply the arithmetic mean at the time of the assessment. Such situations could lead to a fair amount of ambiguity, uncertainty and reconciliation difficulties for taxpayers and jeopardize their transfer pricing documentation and price setting.)

- Once the arrangement of the values in a data set is in ascending order, the arm's length range would constitute the data points lying between the 35th and 65th percentile of the data set.
- If the transaction price falls within the range, then the same shall be deemed to be the ALP. If the transaction price falls outside the range, the ALP shall be taken to be the Median of the data set.
- The computation mechanism of range, is explained by way of illustrations below (as reproduced from the final rules):

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Illustration 1: Where the data set comprises seven data points (arranged in ascending order), and the percentiles computed are not whole numbers.

Percentile	Formula	Result	Value to be selected
35th	Total no. of data points in dataset*35% = [7 * 35%]	2.45	3rd value*
65th	Total no. of data points in dataset*65% = [7 * 65%]	4.55	5th value*
Median	Total no. of data points in datasets*50% = [7 * 50%]	3.50	4th value*

** Value referred to here is the place value in the data set as arranged in ascending order.*

Illustration 2: Where the data set comprises 20 data points (arranged in ascending order), and the percentiles computed are whole numbers.

Percentile	Formula	Result	Value to be selected
35th	Total no. of data points in dataset * 35% = [20 * 35%]	7.00	Mean of 7th & 8th value
65th	Total no. of data points in dataset * 65% = [20 * 65%]	13.00	Mean of 13th & 14th value
Median	Total no. of data points in dataset * 50% = [20 * 50%]	10.00	Mean of 10th & 11th value

PwC Observations

Largely, the provisions seem to provide clarity in relation to the use of multiple year data and the application of the range concept. The CBDT's intention to reduce TP litigation is clearly visible. The reduction of the minimum number of comparables required for availing the range, from 9 to 6; a relative broadening/widening of the range from 40th - 60th percentile to 35th – 65th percentile; allowing the use of the range in case of CUP Method are all undoubtedly positive measures emerging from the final rules. Having said that, going forward, the Government may have to consider the following aspects:

- Since there is no alignment between the use of the 35th–65th percentile with globally followed practices, the Competent Authorities of other countries may not find this acceptable during a bilateral APA, multilateral APA or a MAP negotiation.
- APA authorities may need to consider how to facilitate a reconciliation between the application of "range" in the regular APA years *vis-à-vis* use of "arithmetic mean" in the rollback years.

Implementation of TP Provisions

CBDT issues revised and updated guidance for the implementation of TP provisions

CBDT Instruction No.15 of 2015, dated 16 October, 2015

The CBDT issued Instruction No. 15 of 2015 on 16 October, 2015. This instruction (new instruction) replaces Instruction No. 3 of 2003 (old instruction) issued by the CBDT on 20 May, 2003. The purpose of the old instruction was to provide guidance to TPOs and TO concerning the operationalising of the transfer pricing provisions and to ensure procedural uniformity. However, due to a number of legislative, procedural and structural changes carried out over the last few years, the CBDT is replacing the old instruction with the new one in order to provide updated and adequate guidance on international transactions. The new instruction mentions that similar guidance is also under consideration by the CBDT for SDTs.

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In detail

The guidelines contained in the new instruction are either:

- Similar to the ones in the old instruction; or
- Have simply been updated based on the current relevant provisions of the Act and the Rules; or
- Entirely new, that is, did not exist in the old instruction or are a modified version of the old instruction, and are not in either the Act or the Rules as they currently stand.

We have focused on the third category of changes made in the new instruction [i.e., the new guidelines], and have summarized each change below:

- There is now no requirement of selecting or referring a case for TP scrutiny on the basis of the value of international transaction(s), because the selection of transfer pricing cases for scrutiny now takes place on the basis of risk parameters. The only exception to this would be in a case where the TO comes to know that the taxpayer has entered into an international transaction(s), but has either not filed an Accountant's Report (AR) under section 92E of the Act, or not declared the transaction(s) in its AR. In such a case, irrespective of the value of the international transactions, the TO may refer the matter to the TPO after giving the taxpayer an opportunity to present its case first. It is important to note that the new instruction specifically mentions that this guidance would also apply in case of SDTs.
- • Where the taxpayer has filed an AR, the TO can (as he could earlier), on the basis of the details provided in the AR, arrive at a *prima facie* belief that referring to the TPO is necessary. However, in a few situations, before making a reference to the TPO[28] or determining ALP on his own[29], the TO must, as a jurisdictional requirement, record that he is satisfied (after giving the taxpayer the opportunity to be heard) that there is an income or the potential of an income arising and/or being affected on the determination of ALP. These situations are as follows:
  - where the taxpayer has not filed an AR, or has not declared one or more international transactions in the AR, but the international transaction(s) come to the notice of the TO, or
  - where the taxpayer has declared the international transaction(s) in the AR, but has made certain qualifying remarks to the effect that the said transaction(s) are not international transactions, or they do not impact the income of the taxpayer.

  If the taxpayer raises no objections with regard to the applicability of Chapter X (sections 92 to 92F) of the Act, then the TO's view would be sufficient for referring the issue to the TPO. However, where any objections are raised by the taxpayer with regard to the applicability of Chapter X of the Act, then such objections will be considered and specifically dealt with.
- If a TPO is the rank of an Additional/Joint Commissioner of Income-Tax (CIT), then he has to obtain approval of the jurisdictional CIT (TP) before passing the TP assessment order. On the other hand, if a TPO is the rank of a Deputy/Assistant CIT, then he has to obtain the approval of the jurisdictional Additional/Joint CIT before passing the TP assessment order.
- The jurisdictional CIT (TP) can assign a limited number of important and complex cases, not exceeding 50, to the Additional/Joint CIT (TPOs) working in the same jurisdiction. The framing of the appropriate guidelines will take place for the selection of such important and complex cases.

PwC Observations

Risk based selection of cases for transfer pricing audits (from "quantity" to "quality")

The option of selecting cases for transfer pricing scrutiny based on risk parameters is not an on-ground reality yet. However, the fact that this has been explicitly stated in the new instruction indicates that the next round of selection of cases is likely to be risk based.

28. Under section 92CA(1) of the Act.
29. Under section 92C(3) of the Act.

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So far, the selection of cases, based on a monetary threshold has led to a significant number of cases being selected for transfer pricing audits. As a result, the focus had shifted from a quality investigation to quantity investigations, the repercussions of which are evident in cumbersome audits, both for taxpayers and revenue authorities.

Therefore, the introduction of risk based scrutiny is a very rational step taken by the Indian Government towards streamlining the TP audit process. With such an enormous dispute resolution burden, coupled with the growing number of pending cases and already strained Revenue resources, risk based selection of cases for transfer pricing audits is undoubtedly called for. Revenue authorities will now hopefully spend less time and money on audits, and end up doing justice to audits, which are in fact "worth it". Further, the judiciary will now be able to spend its time effectively and only on "meaningful" cases, and the Government will in fact be able to collect "real" revenues.

Taxpayers can now focus their energy on high risk areas, and deploy their own risk assessment techniques in order to strengthen their documentation and defence files, which will allow them to effectively manage compliance.

However, the choices and transparency around risk parameters will determine how the implementation of this policy change takes place on the ground.

The introduction of the selection of cases that are risk based, for transfer pricing audits also indicates India's intention to adopt Action 13 of the OECD's Base Erosion and Profit Shifting project, that is, Transfer Pricing Documentation and CbCR. This is because one of the articulated purposes of CbCR is to provide assistance in risk assessment.

Whatever the driving factor is, the selection of cases based on risk assessment is a significant positive measure that is in line with "best practices" followed globally. Moreover, it will surely have the effect of boosting investor confidence, and demonstrating India's commitment to attracting foreign investment.

Situations in which TO must record his satisfaction before reference to TPO

The CBDT acknowledges that there could be situations where taxpayers either do not file an AR, or do not declare a transaction(s) in their AR, or declare the transaction with qualifying statements to the effect that the transaction itself is not an international transaction, or that no income arises therefrom. To address these situations, the CBDT has put the onus on the TO to record why he believes that the international transaction(s) impacts, or has the potential to impact, income. This would provide the taxpayer with an additional opportunity to present its position, and may prevent the occurrence of unwarranted litigation, provided that TOs are given sufficient guidance, as such issues have, in the past, been highly debated at higher judicial fora.

From a reading of the instruction, it is apparent that the CBDT appreciates that the applicability of Chapter X (Sections 92 to 92F) of the Act would come into play only where an international transaction has an impact on, or has the potential to impact, income. This is undoubtedly a very rational and appropriate legal approach adopted by the CBDT, and will serve as a reminder for the tax authorities that transfer pricing does not go beyond the fundamentals of taxation. On an overall basis, this approach also ties in with the underlying intent of the Indian TP regulations, that is, avoiding "erosion of the tax base" in India.

Notably, this is also in line with the HC decision in the case of Vodafone (pronounced in October 2014[30]), wherein the HC had held that if an international transaction did not give rise to income under the Act, no occasion to apply Chapter X of the Act could arise.

That the TO is required to record his satisfaction, where a taxpayer has declared an international transaction in the AR, with qualifying remarks indicates that in scenarios where the taxpayer contends non-applicability of Chapter X, it may be advisable to provide a note in the AR stating the taxpayer's position on such transactions. However, to make this workable, the online AR format would need modification so as to provide for additional notes.

30. Vodafone India Services Pvt Ltd *v.* UOI - WP No.871 of 2014, TS-308-HC-2014(BOM)-TP, [2014] 50 taxmann.com 300 (Bombay), [2014] 368 ITR 1 (Bombay), [2014] 271 CTR 488 (Bombay), [2015] 228 Taxman 25 (Bombay), 2014-TII-19-HC-MUM-TP.

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The fact that the onus has been put on the AO to record why he believes that an international transaction impacts or has the potential to impact income, provides evidence for the fact that the Indian Government is invoking a system of checks and balances in order to avoid the arbitrary use of authority by first level assessing officers. This may also prevent taxpayers from being saddled with unnecessary adjustments and protracted litigation thereafter, at least on issues relating to applicability or otherwise of Chapter X *per se*. This is yet another welcome move by the Government, which will have the effect of invigorating the investment climate in India.

Limiting the number of cases per TPO

Limiting the number of important and complex cases handled by each TPO is undoubtedly a laudable step taken by the Indian Government, as the large number of cases handled by TPOs has probably deterred them from delving into the merits of each case. This could have led to "batch processing" of cases without proper application of thought, leading to unsustainable TP adjustments at higher judicial fora.

However, that said, 50 cases (for senior rank TPOs) may still be a large number, particularly given the fact that these 50 cases would be important/complex in nature.

Further, even for junior rank TPOs, it would be important to prescribe a reasonable upper limit per TPO, in line with international norms (as TPO's counterparts in certain developed jurisdictions handle far less cases on an annual basis).

Concluding thoughts

Overall, the issuance of the new instruction reflects the Indian Government's line of thinking and philosophy on the different aspects discussed above, and clearly reflects the political will to control the volume of disputes, better utilise the Revenue's resources, and enhance international perception and investor confidence. However, having said that, on-ground implementation and execution remain to be seen.

Analysing tax issues
Corporate tax

Assessing personal tax
Personal taxes

Structuring for companies
Mergers and acquisitions

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Taxing of goods and services
Indirect taxes

Following the rule book
Regulatory developments

Taxing of goods and services

Indirect taxes

Case law

VAT/Entry tax

Work station/cubicle used to sit in and operate a computer classified as an accessory to the computer and not as furniture

2015-TIOL-385-HC-KAR-VAT

The Karnataka HC allowed the input tax credit of VAT paid on work stations. The court observed that since the purpose of a work station or cubicle was for sitting and operating a computer, it qualified as an accessory to the computer/computer peripherals, which meant that it did not fall under the definition of "furniture," which is for convenience or decoration.

Transactions constitute inter-state sales, where an inextricable connection between the inter-state movement of goods and the purpose of sale exists

Commissioner of Commercial Taxes v. Desai Beedi Company (2015-TIOL-21-SC-CT-LB)

The SC held that in order for transactions to constitute inter-state sales, the movement of goods from one state to another has to have an inextricable connection to the purpose of sale. Where a sale transaction concludes in one state, the mere transport of goods from that state to another cannot result in an inter-state sale.

A contract for the printing of an annual report as per the instructions of a client deemed a works contract and not a sale

Heritage Printers v. The Joint Commissioner of Commercial Taxes (2015-TIOL-608 (HC)-Mad-CT)

The Madras HC held that a contract for the printing of annual reports as per the instructions of the customer was a works contract, and did not qualify as a sale of printed materials. The Court observed that where the finished goods supplied to a particular customer were not commercial commodities—in the sense that the sale of such goods in the market to any other person could not occur—the transaction was a works contract.

Sodexo meal vouchers qualify as "goods," and subject to octroi

Writ Petition No. 5653 of 2010 with Writ Petition No. 7503 of 2013)

The Bombay HC held that Sodexo meal vouchers qualified as "goods" within the meaning of the Maharashtra Municipal Corporations Act, and as "printed material" would be subject to octroi at a rate of 2%. The Court further observed that the paper vouchers were capable of being sold, delivered and possessed, and that they could not be equated with either lottery tickets or electromagnetic waves.

Supply of medicines during provision of medical services not subject to VAT

(2015) 57 taxmann.com 44 (Punjab and Haryana))

The Punjab and Haryana HC held that the supply of drugs, medicines, implants, stents and valves was integral to medical services/procedures, and that the element of supply was not severable from the procedure and advice so as to allow the inference of a sale. Therefore, the Court held that the supply was not liable to VAT, and that the sub-clauses outlined under article 366(29A) of the Constitution did not cover hospital services.

Acceptable to file declaration forms after completion of assessment; not necessary to file the forms at the same time as the returns

Weir BDK Valves v. The Assistant Commissioner of Commercial Taxes (TIOL-1547-HC-KAR-VAT)

The Karnataka HC, relying on the SC decision in the case of the State of Himachal Pradesh v Gujarat Ambuja Cements (2001-121-STC-273), held that it was possible to file declaration forms at a stage subsequent to the completion of assessment, and that it was not necessary to file the forms at the same time as the returns.

Taxing of goods and services
Indirect taxes

The implementation of customized software carried out under a separate service contract not subject to VAT

2015-TIOL-2106-HC-KAR-VAT

The Karnataka HC held that VAT was not payable on the consideration charged for the implementation of customized software under a separate service contract. The Court observed that the implementation of software was a post-sale activity, undertaken to integrate the software with the banking system.

Goods supplied under a turnkey contract not eligible for in-transit sales exemption under Section 6(2) of the Central Sales Tax (CST) Act

TS-507-HC-2015(TEL & AP)-VAT

The Andhra Pradesh HC held that the supply of goods in a turnkey contact was not eligible for the CST exemption made available for in-transit sales under Section 6(2) of the CST Act, as the sale of the goods had taken place after the incorporation of the goods into the project. However, the HC accepted the assessee's alternative argument that supplies in turnkey contracts were inter-state sales falling u/s 3(a) and the mere fact that goods delivered and appropriation took place within the state is inconsequential, if the parties' envisaged movement of goods from one state to another and such movement is an incident of the contract of sale.

Exemption from CST available, provided that the sale occasioned the export of goods outside India

PVC Leathers, Paper Mills Ltd. v. State of Tamil Nadu (TS-476-HC-2015 (MAD)-VAT)

The Madras HC held that the sale of goods to the purchaser's branch office in Chennai, pursuant to an export order executed by the head office in Bombay, was eligible for exemption from CST under Section 5(3) of the CST Act. The Court observed that it was immaterial whether the branch office or head office issued the declaration in Form H, so long as the sale had occasioned the export of goods outside India.

Central Excise

The CBEC does not have the right to issue circulars that incorporate directions contrary to the decisions of the Tribunal

Karamchand Appliances Private Ltd v. UOI (2015 (318) ELT 221)

The Delhi HC held that the CBEC had no right to issue a circular that incorporated directions that were contrary to the decision of the Tribunal, and that the Revenue department had the option to move either the HC or the SC in order to challenge or contest the correctness of the Tribunal's decision.

Excise duty payable on intermediate products that come into existence during the manufacture of exempted products

2015 (319) ELT 406

The SC held that excise duty was payable on transmission assemblies that came into existence as intermediate products during the manufacture of exempted tractors. Since such products were known in the market as distinctive products, the fact that not a single sale of the transmission assemblies has been made by the appellants was deemed irrelevant.

Performance bonus received after the clearance of goods not includible in the assessable value

Vishwakarma Refractories P Ltd v. CCE (2015 (320) ELT 622)

The Bangalore Tribunal held that a performance bonus received after the clearance of goods was not includible in the assessable value.

Generation of fly ash during the burning of coal deemed to not amount to manufacture

Mettur Thermal Power Station v. CBEC (2015-TIOL-1948-HC-MAD-CX)

The Madras HC held that the "fly ash" generated during the burning of coal did not involve any manufacturing activity; hence, it did not fall under the purview of excisable goods and was not subject to excise duty. However, bricks made from fly ash were subject to excise duty, as they qualified as a manufactured product.

Taxing of goods and services
Indirect taxes

The transfer of advance licence in favour of the assessee for duty free import of raw material held to constitute additional consideration

CCE v. Indorama Synthetics (I) Ltd (2015-TIOL-190-SC-CX)

The SC held that the transfer of an advance licence by a buyer in favour of the assesse for the duty free import of raw material constituted additional consideration. Hence, the monetary value of the licence was includible with regards to valuation, specifically in terms of Rule 6 of the Customs Valuation Rules.

Valuation of physician samples distributed free of cost to be based on the cost plus method

Biochem Pharmaceuticals Ind. Ltd. v. CCE (2015 (322) ELT 808)

The SC held that the valuation of physician samples distributed free of cost would be based on the cost of production and not on the value of the same goods sold in the market.

CENVAT reversal not applicable on non-excisable items that emerge during the manufacture of excisable goods

Union of India v. DSCL (2015 (322) ELT 769)

The SC held that the bagasse that emerged as a waste product during the manufacture of sugar was a non-excisable item, even after the introduction of Explanation to Section 2(d) effective from 16 May, 2008, and therefore reversal of the credit under Rule 6(3) of the CENVAT credit rules was not applicable to such waste products.

The difference between the sales tax payable and the sales tax paid at NPV of the deferred taxes under the Package Incentive Scheme cannot constitute additional consideration

CCE v. Uttam Galva Steels Ltd (2015-TIOL-2242-CESTAT-MUM)

The Mumbai Tribunal held that the difference between the sales tax collected from the customers and the sales tax paid to the state authorities at NPV of deferred taxes under the Package Incentive Scheme cannot constitute additional consideration. The payment of sales tax at NPV (which is less than what was originally payable), cannot be adjusted to the amount that was actually payable at the time and place of removal, particularly when under Sales Tax Law, such a payment is considered as deemed payment of the sales tax payable.

Service Tax

Lease rent from "lease in perpetuity" held liable to service tax

Greater Noida Industrial Development Authority v. CCCE and Ors (2015-TIOL-1008-HC-ALL-ST)

The Allahabad HC held that if a sovereign/public authority provided a service, which was not in the nature of statutory activity, for a consideration, the same would be liable to tax so long as the activity undertaken fell within the scope of taxable services. Accordingly, the court also held that the lease rental received by the appellant for allotting plots for business/commercial purposes would be liable to service tax under "renting of immovable property services."

The HC further held that since the applicable provisions did not carve out any distinction between a lease that was short-term and one that was long-term or "in perpetuity," the rental income would be subject to tax, irrespective of the tenure of the lease.

Indivisible works contracts executed before 1 June 2007, not subject to service tax

TS-437-SC-2015-ST

The SC reversed the judgment of the CESTAT 5-member bench and held that indivisible works contracts that existed before 1 June, 2007, could not be taxed under any other category.

Customs/FTP

SAD not applicable on stock transfer of goods by an EOU to DTA unit

2015 (315) ELT 303

The Mumbai Tribunal held that an exemption from SAD was available for the stock transfer of goods from an EOU to a DTA, since there was no possibility of exemption from the sales tax levied by the state government on the sale of such goods in the DTA. Accordingly, the condition of SAD exemption notification was fulfilled. The Revenue department had contended that exemption from SAD was not available, since the levying of sales tax on inter-unit transfers could not take place.

Taxing of goods and services
Indirect taxes

Arbitrary loading of 1% of the CIF value as “loading, unloading and handling charge” unsustainable where the actual charges are ascertainable

2015-TIOL-79-SC-CUS

The SC of India held that arbitrary loading of 1% of CIF value as “loading, unloading and handling charge” was unsustainable where the actual charges were ascertainable.

Exemption/concession of CVD on fulfilment of condition of non-availment of CENVAT credit on raw material available on imported goods

2015-TIOL-74-SC-CUS

The SC of India held that the exemption/concession of excise duty was applicable to imported goods, provided that CENVAT credit on raw material had not been availed.

Customs duty not applicable on software downloaded electronically through the Internet; licence fee included in the value of goods imported to the extent that the customer pays the charges

2015-TIOL-1766-CESTAT

The Tribunal held that no Customs duty was chargeable on software downloaded electronically through the Internet, and the licence fee could only be included in the value of goods physically imported to the extent that the customers were charged, and the charges paid to the overseas company, on account of it being a condition of sale.

The DGFT held that export obligation was fulfilled by exporter for the exempted goods; the same was not binding on Customs Authorities

CC v. Pennar Industries Ltd and Anr (2015-TIOL-162-SC-CUS),

The SC of India held that even though the DGFT had held that the exporter of exempted goods was responsible for fulfilling the export obligation, this mandate was not binding on the Customs Authorities.

Customs duty deemed payable only on the quantity received in India

Mangalore Refinery and Petrochemicals Ltd. v. CC. (2015-TIOL-199-SC)

The SC of India held that Customs duty was payable only on the quantity that was received in India, and not on the quantity exported from the suppliers’ countries.

Royalty not includible in the value of imported goods when it is not a condition of the sale of the imported goods

CC v. Can-Pack India Pvt Ltd. (2015-TIOL-201-SC-CUS-LB)

The SC of India held that where an agreement for the purchase of raw material stipulated that the importer had the freedom to procure the material from any person—provided desired standards were maintained—royalty was not includible in the calculation of the value of the imported goods, since it did not qualify as a condition of sale for imported goods.

Circulars and notifications

Service tax and excise

Circular regarding the issuance of SCN and closure of proceedings

Circular F. No 137/46/2015-Service Tax dated 18 August, 2015

The Board has provided the following clarifications in the context of the discoveries/observations made through audits, investigations and scrutiny:

- In cases involving fraud, suppression of facts etc.:
  - Where an assessee pays the service tax/excise duty, interest and reduced penalty equal to 15% of the tax, then the assessee can request a waiver of a written SCN.
  - Where the assessee provides a written request for the waiver of a written SCN, the 30-days period to deposit reduced penalty is computed from the date of receipt of the waiver request by the Department.
- In cases not involving fraud, suppression of facts etc.:
  - Where an assessee pays the tax along with the interest within 30 days of the issuance of the SCN or before the issuance of the SCN, then no penalty is payable and the proceedings will have reached a conclusion.
- Furthermore, the conclusion of proceedings against the assessee requires the approval of an officer equal in rank to an officer who is competent enough to adjudicate such cases.

Taxing of goods and services

Indirect taxes

Withdrawal of Education Cess and Secondary and Higher Education Cess

Education Cess and Secondary and Higher Education Cess on excise duty and service tax have been withdrawn.

Service Tax

Levy of Swachh Bharat Cess

The Swachh Bharat Cess came into effect on 15 November, 2015; and will be levied at the rate of 0.5% on the value of all taxable services.

Grant of partial refund of accumulated CENVAT credit to service exporters on provisional basis

Circular No. 187/6/2015-Service Tax dated 10 November 2015

The CBEC has issued a circular that requires the payment of 80% of the amount of CENVAT credit eligible for claim of a refund by service exporters, on a provisional basis, subject to submission of a certificate from a statutory auditor/ Chartered Accountant for corporate/non-corporate assessees. The scheme is applicable only for the refund claims filed on or before 31 March 2015, and does not cover any refund claim, which is then subject to review in terms of any remand by a higher authority.

VAT/CST/Profession Tax/Entry Tax

Haryana restricts input tax credit on inputs used for inter-state sales

(Notification No 22/ST-1/H.A.6/2003/S.59/2015, dated 7 September 2015)

Where the sale of locally purchased goods takes place on an inter-state basis, or such goods are used in the manufacture of other goods and those manufactured goods are sold on an inter-state basis, input tax credit shall be allowed. However, the credit will apply only to the extent of the amount of tax actually paid for the purchase of such goods, or the tax payable on the sale of such goods on an inter-state basis, whichever is lower.

Customs/FTP

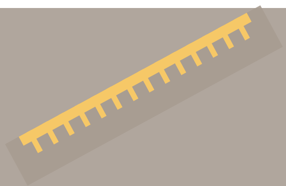
Introduction of FTP 2015–2020

The FTP 2015–2020 replaced the FTP 2009–2014 and came into effect on 1 April, 2015. Among other measures, the new policy has consolidated multiple different schemes such as Focus Market Scheme, Focus Product Scheme etc. in a new scheme called the Merchandise Exports from India Scheme; Served from India Scheme has been replaced by Services Exports from India Scheme. These schemes have their own respective conditions.

Importers and Exporter given the option of filing combined commercial invoice-cum-packing list

Circular No. 1/2015-Customs dated 12 January 2015

The Central Government, in order to simplify custom procedures, has provided importers/exporters with the option of filing a combined commercial invoice-cum-packing list, provided it contains the specified fields of normal packing list.



Analyzing tax issues
Corporate tax

Assessing personal tax
Personal taxes

Structuring for companies
Mergers and acquisitions

Pricing appropriately
Transfer Pricing

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Regulatory developments

FDI

Liberalisation of FDI norms in regard to the Construction Development Sector

(Press note No. 10 (2014 series) dated 03 December 2014)

The Government has notified the following amendments to the FDI policy *vide* Press Note 10 of 2014.

- ***Lock-in/ Exit***
  A lock-in period for investments linked to completion of project or development of trunk infrastructure (roads, water supply street lighting, drainage and sewerage) whichever is earlier. Thus, the three-year lock-in subsequent to the last date of investment has now been removed.
- ***Affordable housing parameters***
  Minimum 40% FAR/ FSI (Affordable Housing FSI) to be utilised for dwelling units that have a floor area of maximum 140 square metres (as against 60% FAR/ FSI and a carpet area of maximum 60 square metres, as specified in an earlier press release in October 2014). 25% of Affordable Housing FSI to be utilised for dwelling units that have a floor area of maximum 60 square metres (as against 35% FSI and carpet area of 21–27 square metres as specified in an earlier press release in October 2014).
- ***Minimum area development***
  In case of combination project, minimum development of 20,000 square metres of floor area will be required.

Mapping of sector specific FDI policy with NIC code

(Press Note 1 of (2015 series) dated 05 January 2015)

With the objective of improving ease of doing business in India, the Government has mapped the activities listed in Chapter VI of the Consolidated FDI Policy with the National Industrial Classification, 2008

FDI in Pharmaceuticals sector

(Press Note 2 (2015) dated 06 January 2015 and A.P. (DIR Series) Circular No. 70 dated 02 February 2015)

Under the extant FDI Policy, FDI of up to 100% is permitted under the automatic route for greenfield projects as well as the Government approval route for brownfield projects (i.e., existing companies) in the pharmaceuticals sector.

With effect from 21 January 2015 *vide* Press Note 2 (2015 Series) issued by the DIPP, FDI up to 100% under automatic route is permitted in manufacturing of medical devices which was earlier deemed to be classified within the ambit of the pharmaceutical sector.

As per this Press Note, medical devices would mean:

Any instrument, apparatus, appliance, implant, material or other article, which used alone or in combination, including the software, intended by its manufacturer to be used specially for human beings or animals for one or more of the specific purposes of –

- diagnosis, prevention, monitoring, treatment or alleviation of any disease or disorder;
- diagnosis, monitoring, treatment, alleviation of, or assistance for, any injury or handicap;
- investigation, replacement, modification or support of the anatomy or of a physiological process;
- supporting or sustaining life;
- disinfection of medical devices;
- control of conception;

Any instrument, apparatus, appliance, implant, material or other article which does not achieve its primary intended action in or on the human body or animals by any pharmacological or immunological or metabolic means, but which may be assisted in its intended function by such means.

An accessory to such an instrument, apparatus, appliance, material or other article;

a device which is reagent, reagent product, calibrator, control material, kit, instrument, apparatus, equipment or system whether used alone or in combination thereof intended to be used for examination and providing information for medical or diagnostic purposes by means of in vitro examination of specimens

Following the rule book

Regulatory developments

Foreign investment in the Pension Sector

(Press note No. 4 (2015 series) dated 24 April 2015)

In pursuance of enactment of the IRDA Act, 2013, the Government has allowed FDI of up to 49% in the Pension sector, wherein up to 26% is permitted under the automatic route; however, FDI beyond 26 % will require Government approval. Such investments are subject to the conditions outlined in the PFRDA Act, 2013.

Review of the investment limit for cases requiring prior approval of the FIPB/ CCEA

(Press note No. 6 (2015 series) dated 03 June 2015)

The investment limit for review of FDI approval cases by the FIPB in-charge (Minister of Finance) has increased from INR 2000 crores to INR 3000 crores. Proposals with total equity inflow of more than INR 3000 crores would require consideration by the CCEA.

Review of FDI policy on Investments by NRIs, PIOs and OCIs

(Press note No. 7 (2015 series) dated 03 June 2015)

The government had decided to amend the definition of "NRI" as contained in the FDI policy Investments by NRIs under schedule 4 of FEMA (Transfer or issue of Security by Persons Resident Outside India) Regulations will now be deemed to be domestic investments, i.e., shall be considered as being at par with the investments made by residents.

An "NRI" is defined as an individual resident outside India who is a citizen of India or is an "OCI" cardholder within the meaning of section 7 (A) of the Citizenship Act, 1955. "PIO" cardholders registered as such are deemed "OCI" cardholders.

Introduction of Composite Caps for Simplification of Foreign Direct Investment policy to attract foreign investments

(Press note No. 8 (2015 series) dated 30 July 2015)

The Union Cabinet on 16 July 2015 decided to approve the introduction of composite caps in FDI policy for attracting foreign investments by simplifying the FDI regime. The DIPP, Ministry of Commerce & Industry, GoI has issued this Press Note introducing composite caps in the FDI policy for various sectors.

The key conditions outlined in the press note are as follows: Composite caps include all types of foreign investments (direct and indirect) regardless of whether the said investments have been made under Schedule 1 (FDI), 2 (FII), 2A (FPI), 3 (NRI), 6 (FVCI), 8 (QFI), 9 (LLPs) and 10 (DRs) of FEMA. Total foreign investment (as defined above), direct and indirect, in an entity shall not exceed the sectoral/ statutory cap prescribed for a particular sector. The aggregate FII/ FPI/ QFI investment, individually or in conjunction with other kinds of foreign investment, shall not exceed the sectoral/ statutory cap.

Portfolio investment, up to aggregate foreign investment level of 49 % or sectoral/ statutory cap, whichever is lower, will not be subject to either government approval or compliance of sectoral conditions, provided such investment does not result in transfer of ownership and/or control of Indian entities from resident Indian citizens to non-resident entities.

In sectors under Government approval route, foreign investment resulting in the transfer of ownership and/ or control of Indian entities from resident Indian citizens to non-resident entities will be subject to Government approval. However, such transfer of ownership and/or control of Indian entities, which are operating in sectors under the automatic route but with conditionalities will be have to comply with these conditionalities; no government approval will be required.

Review of existing policy on Partly Paid Shares and Warrants

(Press note No. 9 (2015 series) dated 30 July 2015)

The Government has decided to allow Partly Paid Shares and Warrants as eligible capital instruments for the purpose of FDI policy. As per the revised policy, "Capital" means equity shares; fully, compulsorily and mandatorily convertible preference shares; fully, compulsorily and mandatorily convertible debentures and warrants.

Equity shares issued in accordance with the provisions of the Companies Act shall include equity shares that have been partly paid. Preference shares and convertible debentures shall be required to be fully paid, and should be mandatorily and fully convertible. Further, "warrant" includes a Share Warrant issued by an Indian Company in accordance to provisions of the Companies Act, as applicable.

Following the rule book

Regulatory developments

An Indian company may issue warrants and partly paid shares to a person resident outside India subject to terms and conditions as stipulated by the Reserve Bank of India in this behalf, from time to time.

FDI up to 100% in White Label ATM Operations under Automatic Route

(Press note No. 11 (2015 series) dated 01 October 2015)

The GoI has decided to allow Foreign Investment of up to 100% in White Label ATM Operations, under the Automatic route vide the aforementioned Press note.

Foreign Exchange Management Act (FEMA)

Issue of shares under Employees Stock Options Scheme and/or sweat equity shares to persons residing outside India

(A.P. (DIR Series) Circular No. 4 dated 16 July 2015)

In terms of Regulation 8 of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000, an Indian company can issue shares under the Employees' Stock Option (ESOP) Scheme, by whatever name called, to its employees or employees of its JV or Wholly owned overseas subsidiary/ subsidiaries who are resident outside India, directly or through a Trust, provided that the scheme has been drawn in terms of regulations issued under the SEBI Act, 1992 and face value of the shares to be allotted under the scheme to non-resident employees does not exceed 5% of the paid up capital of the issuing company.

The RBI has now decided to also allow an Indian company to issue "employees' stock option" and/or "sweat equity shares" to employees/ directors or employees/ directors of its holding company or JV or wholly owned overseas subsidiary/ subsidiaries who are resident outside India, provided that:

- The scheme has been drawn in terms of either regulations issued under the Securities Exchange Board of India Act, 1992 or the Companies (Share Capital and Debentures) Rules, 2014 notified by the Central Government under the Companies Act 2013, as the case may be.
- The "employee's stock option"/ "sweat equity shares" issued to non-resident employees/ directors under the applicable rules/ regulations are in compliance with the sectoral cap applicable to the said company.
- Issue of "employee's stock option"/ "sweat equity shares" in a company where foreign investment is under the approval route shall require prior approval of the FIPB of GoI
- Issue of "employee's stock option"/ "sweat equity shares" under the applicable rules/ regulations to an employee/ director who is a citizen of Bangladesh/ Pakistan shall require prior approval of the FIPB of GoI.

Reporting under FDI Scheme on the e-Biz platform

(A.P (DIR Series) Circular No. 77, Circular No. 95 and Circular No. 9 dated 12 February 2015, 17 April 2015 and 21 August 2015, respectively)

RBI under the aegis of the e-Biz project of the GoI has enabled the online filing of the following returns with the RBI (in addition to the manual filing facility):

- **ARF** – Used by Companies for reporting the foreign direct investment (FDI) inflow to RBI;
- **FCGPR Form** – Used by Companies for reporting the issue of eligible instruments to overseas investors against the aforementioned FDI inflow;
- **Form FC-TRS –** Used by Companies for reporting transfer of instruments *viz.* shares, convertible debentures, partly-paid shares and warrants from a person resident outside India or vice-versa

Through the eBiz portal, a business user can download eForms, upload attachments, make payments online and submit forms for processing by the department. Upon submission, the business user shall be provided with a copy of the receipt along with an acknowledgement, which could then be saved/ printed for tracking the status. In addition, the user shall also receive important notifications through SMS alerts. Upon issuance of the certificate/ clearance, the user may download it using the eBiz platform. This platform, thus, represents a transformational shift in the Governments' service delivery approach, which has gone from being department-centric to customer-centric through a single window portal.

Following the rule book

Regulatory developments

Depository receipts scheme

(A.P. (DIR Series) Circular No. 61 dated 22 January 2015)

The Central Government has notified a new scheme for investments under ADR/ GDR called the "Depository Receipts Scheme, 2014" (DR Scheme). The DR Scheme shall replace the existing guidelines of the Foreign Currency Convertible Bonds and Ordinary shares (through the Depositary Receipt Mechanism) Scheme, 1993 with the exception of the extent relating to foreign currency convertible bonds.

Some of salient features of the new scheme are as follows:

- **Eligible security** – The securities in which a person resident outside India is allowed to invest under Schedule 1, 2, 2A, 3, 5 and 8 of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000 shall be eligible securities for issue of DR.
- **Investment cap** – The aggregate of eligible securities, which may be issued or transferred to foreign depositories and along with eligible securities already held by persons resident outside India, shall not exceed the total limit on foreign holding of such eligible securities under the FEMA regulations.
- **Pricing norms** – The eligible securities shall not be issued to a foreign depository at a price less than the price at which they are issued to domestic investors.
- **End use** – If the issuance of the depository receipts adds to the capital of a company, the issue of shares and utilisation of the proceeds shall have to comply with the relevant conditions laid down in the regulations framed and directions issued under FEMA, 1999.
- **Reporting compliances** – The domestic custodian shall report the issue/ transfer of sponsored/ unsponsored depository receipts as per the DR Scheme 2014 in Form DRR within 30 days of close of the issue/ program.

Foreign investment in India by FPI

(A.P. (DIR Series) Circular No. 71, 72 and 73 dated 3 February, 5 February and 6 February 2015 respectively)

Currently, all investments in Government bonds by registered FPIs need to be made with a minimum residual maturity of 3 years.

The RBI now requires that all future investments by an FPI in any type of debt instrument (including amortised debt instruments) will to be made within the minimum residual maturity period of three years. In addition, investment in debt instruments having a minimum residual maturity period of 3 years and over with an optionality clause exercisable within 3 years will not be allowed.

FPIs shall not be allowed to make any further investment in the liquid money market, mutual fund schemes and commercial papers. There will be no-lock in period and FPIs can sell the securities (including those presently held with less than 3 years residual maturity) to domestic investors.

Reinvestment of the coupon received on existing investments in Government securities will now be kept outside the current limit of investment (USD 30 billion) for investment by FPIs in Government securities.

Annual Return on FLA Return – Reporting by Limited Liability Partnerships

(A. P. (DIR Series) Circular No. 22 dated 21 October 2015)

The RBI has decided that all LLPs that have received FDI and/or made FDI abroad (i.e., overseas investment) in the previous year(s) as well as in the current year, shall submit the FLA return to the Reserve Bank of India by 15 July every year, in the prescribed format by entering "A99999AA9999LLP999999" against CIN in the FLA Return.

Following the rule book

Regulatory developments

ODI

Overseas Direct Investments by proprietorship concern/ unregistered partnership firm in India

(A.P. (DIR Series) Circular No. 59 dated 22 January 2015)

RBI has prescribed complying with the following revised terms and conditions for considering the proposal of ODI, by a proprietorship concern/ unregistered partnership firm in India, by the Reserve Bank under the approval route:

- The proprietorship concern/ unregistered partnership firm in India is classified as "Status Holder" as per the FTP issued by the Ministry of Commerce and Industry, GoI from time to time;
- The proprietorship concern/ unregistered partnership firm in India has a proven track record, i.e., the export outstanding does not exceed 10% of the average export realisation of the preceding 3 years and a consistently high export performance;
- The Authorised Dealer bank is satisfied that the proprietorship concern/ unregistered partnership firm in India is KYC compliant, engaged in the proposed business and has turnover as indicated;
- The proprietorship concern/ unregistered partnership firm in India has not come under the adverse notice of any Government agency like the Directorate of Enforcement, Central Bureau of Investigation, Income-tax Department, etc. and does not appear in the exporters' caution list of the Reserve Bank or in the list of defaulters to the banking system in India; and
- The amount of proposed investment outside India does not exceed 10% of the average of last 3 years' export realisation or 200% of the net owned funds of the proprietorship concern/ unregistered partnership firm in India, whichever is lower.

Creation of charge on overseas and domestic assets

(A.P. (DIR Series) Circular No. 54 dated 29 December 2014)

The RBI has now permitted creation of charge under the automatic route as follows:

- Creation of charge for securing the funded and/or non-funded facility to be availed of by Indian investee company or by its group companies/ sister concerns/ associate concerns or by any of its overseas JV/ WOS/ SDS (irrespective of level) on shares in overseas JV/ WOS/ SDS (irrespective of level) in favour of a domestic or overseas lender
- Creation of charge for securing the funded and/or non-funded facility to be availed of by the JV/ WOS/ SDS (irrespective of level) of the Indian party on the domestic assets of an Indian party or its group companies/ sister concerns/ associate concerns, including the individual promoters/ directors in favour of an overseas lender

The aforesaid liberalisation is permitted subject to compliance with prescribed conditions, including a key condition that the loan/ facility availed by the overseas entity needs to be utilised only for its core business activities overseas, and not for investing back in India.

Exports & Imports

Export of Goods and Services – Period of Realisation

(A.P. (DIR Series) Circular No. 37 dated 20 November 2014)

Exporters, including the units located in SEZs, EHTPs, STPs and BTPs, Status Holder Exporters, and EOUs are required to realise and repatriate proceeds in connection with export of goods/ software/ services to India within a period of 9 months from the date of export.

Export and Import of Indian Currency

(A.P. (DIR Series) Circular No. 63 dated 22 January 2015)

In terms of Regulation 8 of Foreign Exchange Management (Export and Import of Currency) Regulations, 2000, a person is allowed to take or send out of India to Nepal or Bhutan and bring into India from Nepal or Bhutan, currency notes of GoI and RBI for any amount in denominations up to INR 100/-.

RBI has now allowed an individual to carry to Nepal or Bhutan, currency notes of Reserve Bank of India denominations above INR 100/-, i.e., currency notes of INR 500/- and/or INR 1000/- denominations, subject to a limit of INR 25000/-.

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Extant Commercial Borrowing

ECB – Parking of ECB proceeds in rupee term deposits

(A.P. (DIR Series) Circular No. 39 dated 21 November 2014)

Indian borrowers are now permitted to park ECB proceeds (raised under the automatic or approval routes) in term deposits with AD Category-I banks in India for a maximum period of six months pending utilisation for permitted end uses, subject to certain specified conditions, *viz.,* term deposit is kept unencumbered and will be liquidated as and when required.

Pre-liberalisation, ECB proceeds meant for Rupee expenditure were immediately credited to the Rupee accounts of the borrower.

ECB Policy – Security for ECBs

(A.P. (DIR Series) Circular No. 55 issued on 1 January 2015)

The RBI has permitted that AD bankers may be allowed to create a charge on specified asset classes in order to secure the ECB being raised by borrower. This would be applicable only where there is a security clause in the loan agreement and the appropriate NOCs have been obtained, where necessary, and subject to specific conditions.

ECB Policy – Simplification of procedure

(A.P. (DIR Series) Circular No. 64 issued on 23 January 2015)

In a move to ensure easier and simpler procedures, the RBI has delegated its powers and has permitted the AD Bankers to look into the following matters pertaining to ECBs raised under the automatic and approval route:

- Modifications to drawdown and repayment schedules of ECB, which may be triggered by changes in the average maturity period or the all-in-cost ceilings
- Reduction of the amount of ECB or an increase in the all-in-cost of ECB pursuant to ensuring the such changes are out into effect during the tenure of the ECB and are in conformity with applicable ceilings/ guidelines
- Permit changes in the name of the lender of the ECB after satisfying themselves with the legality of the transactions
- Transfer of ECB from one company to another (under a scheme of reorganization – merger/ demerger) post ensuring that the acquirer company of ECB is an eligible borrower
- Such changes made to the ECB should be reported to the RBI (Department of Statistics and Information Management) in the revised form 83 and must also be reflected in the ECB 2 return.

ECB Policy – Review of all-in-cost ceiling

(A.P. (DIR Series) Circular No. 80 issued on 3 March 2015)

Continuation of the all-in-cost ceiling as specified under paragraph 2 of A.P. (DIR Series) Circular No. 99 dated 30 March 2012 (provided in the table below).

Average Maturity Period	All-in-cost over 6 month LIBOR*
Three years and up to five years	350 bps
More than five years	500 bps
* for the respective currency of borrowing or applicable benchmark	

Such ceiling rates would be applicable until 31 March 2015 and would be subject to review thereafter.

Trade Credits – Review of all-in-cost ceiling

(A.P. (DIR Series) Circular No. 81 issued on 3 March 2015)

Continuation of the all-in-cost ceiling as specified under paragraph 4 of A.P. (DIR Series) Circular No. 28 dated 11 September 2012 (provided in the table below).

Maturity period	All-in-cost ceilings over 6 months LIBOR*
Up to one year	350 basis points
More than one year and up to three years	
More than three years and up to five years	
* for the respective currency of credit or applicable benchmark	

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Such ceiling rates would be applicable until 31 March 2015 and would be subject to review thereafter.

ECB Policy – Denomination in INR

(A.P. (DIR Series) Circular No. 103 issued on 21 May 2015)

Recognised non-resident ECB lenders can now extend loans in Indian rupees to the Indian borrower. This would be implemented through the lender's overseas bank entering a swap arrangement with an AD Category-I bank in India. The steps for obtaining the swap rate for a rupee denominated ECB has been detailed in the aforesaid circular.

ECB Policy – Issuance of rupee denominated bonds overseas

(A.P. (DIR Series) Circular No. 17 issued on 29 September 2015)

The RBI has put in place a framework for facilitating rupee denominated borrowing from overseas. Some of the highlights of the same include:

- Eligible borrowers include corporate bodies, REITs, InvITs.
- Recognised investors include any investor from a financial action task force complaint jurisdiction.
- Have a minimum maturity period of 5 years
- Have an all-in-cost ceiling rate commensurate with the prevailing market
- Under the automatic route, an amount of ECB for USD 750 million annually and any amount exceeding the same would require approval from the RBI.

Miscellaneous

Liberalised Remittance Scheme

(A.P. (DIR Series) Circular No. 106 dated 01 June 2015)

RBI has increased the limit for resident individuals for any permitted current or capital account transaction (or a combination of both) from USD 125,000 to USD 250,000 per FY. If an individual has already remitted any amount under the LRS, then the applicable limit for such an individual will see a reduction from the present limit of USD 250,000 for the FY by the amount already remitted. The permissible capital account transactions by an individual under LRS are:

- Opening of foreign currency account, abroad with a bank;
- Purchase of property abroad;
- Making investments abroad;
- Setting up Wholly owned subsidiaries and JV abroad;
- Extending loans including loans in Indian Rupees to Non-resident Indians (NRIs) who are relatives, as defined in the Companies Act, 2013.

Further, all the facilities (including private/ business visits) for release of exchange/ remittances for current account transactions, available to resident individuals under Para 1 of Schedule III to the Foreign Exchange Management (Current Account Transactions) Rules, 2000, as amended from time to time, shall now be subsumed under the overall limit of USD 250,000. However, for emigration, and expenses in connection with medical treatment abroad and studies abroad, individuals may avail of the exchange facility for an amount in excess of the overall limit prescribed under the LRS, if it is so required by a country of emigration, medical institute offering treatment or the university respectively. Gift in Indian Rupees by resident individuals to NRI relatives as defined in the Companies Act, 2013 shall also be subsumed under the LRS limit.

Further, persons other than resident individuals can make remittances for the following additional purposes within the limit of USD 250,000 only. Any additional remittance in excess of the said limit for the following purposes shall require prior approval of the Reserve Bank of India:

- Donations for educational institutions;
- Commissions to agents abroad for sale of residential flats/ commercial plots in India;
- Remittances for consultancy services;
- Remittances for reimbursement of pre-incorporation expenses.

Remittance of salary

(A.P. (DIR Series) Circular No. 62 dated 22 January 2015)

In terms of Regulation 7(8) of the Foreign Exchange Management (Foreign Currency Account by a person resident in India) Regulation, 2000, a citizen of a foreign State, resident in India, being an employee of a foreign

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company or a citizen of India, employed by a foreign company outside India and in either case on deputation to the office/ branch/ subsidiary/ JV/ group company in India of such foreign company may open, hold and maintain a foreign currency account with a bank outside India and receive the whole salary payable to him for the services rendered to the office/ branch/ subsidiary/ JV/ group company in India of such foreign company, by credit to such account, provided that income tax chargeable under the The Act is paid on the entire salary as accrued in India.

RBI has clarified that the said facility shall also be available to an employee who is deputed to a group company in India. In addition, the term "company" in the aforementioned regulation will include "Limited Liability Partnerships" as defined in the LLP Act, 2008.

Acquisition/ transfer of immovable property – Prohibition on citizens of certain countries

(A.P. (DIR Series) Circular No. 83 dated 11 March 2015)

In terms of Regulation 7 of the Foreign Exchange Management (Acquisition and Transfer of immovable property in India) Regulations, 2000, no person being a citizen of Pakistan, Bangladesh, Sri Lanka, Afghanistan, China, Iran, Nepal or Bhutan without prior permission of the Reserve Bank shall acquire or transfer immovable property in India, other than lease, not exceeding five years.

RBI has now decided to include Macau and Hong Kong in the list of countries, which are prohibited from acquiring/ transferring immovable property in India.

RBI Clarification – Non-resident guarantee for domestic non-fund based facilities

(A.P. (DIR Series) Circular No. 56 dated 6 January 2015)

The RBI has clarified that a resident subsidiary of a multinational company can hedge its Forex exposure through permissible derivative contracts on the strength of guarantee of its non-resident group entity.

REITs to be eligible financial instrument under FEMA

(Press Release dated 06 May 2015 issued by GoI)

Background

- In order to promote funding of the infrastructure sector, the Indian Finance Minister in his Budget speech in July 2014 had proposed the introduction of REITs and a modified REITs structure, i.e., InvITs. The SEBI notified the much awaited REIT/ InvITs regulations in September 2014.
- The actual investment in REITs has not occurred as the FDI policy, the Foreign Exchange Management Act, 1999 and the regulations framed thereunder did not permit foreign investment in completed rent-yielding real estate projects. Consequently, entities registered and regulated under the REITs/ InvITs Regulations notified by SEBI were not able to access foreign investments.

Key amendment

- The press release states that the intent behind introducing REITs is to reduce the pressure on the Indian banking system– which is the primary source of funding to the real estate sector, to help free up existing funds of banks and to encourage construction activities.
- The Union Cabinet, *via* a press release, has announced its approval of REITs being considered as an eligible financial instrument/ structure under the exchange control regulations for attracting long-term finance from foreign and domestic sources including NRIs. This move will make fresh equity available in the real estate sector
- The press release only refers to REITs, and there is no specific mention of InvITs. This could result in uncertainties as to whether foreign investment would be allowed in InvITs.
- Following this press release, the government will issue a formal circular/ notification amending the law. It is important to note that foreign investment is permitted in both, REITs and InvITs.

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Regularisation of assets held abroad by a person resident in India

(A.P. (DIR Series) Circular No. 18)

The GoI has enacted Black Money Act on 26 May 2015 to address the issue of undisclosed assets held abroad. It provides for the separate taxation of "income and assets acquired abroad" and "income not disclosed but chargeable to tax in India".

For this purpose, the RBI has issued the Foreign Exchange Management (Regularization of assets held abroad by a person resident in India) Regulations, 2015 notified though Notification *No. FEMA 348/2015-RB dated 25 September 2015 vide G.S.R. No. 738 (E) dated 25 September 2015.*

It is clarified that:-

- No proceedings shall lie under the Foreign Exchange Management Act (FEMA) against the declarant with respect to an asset held abroad for which taxes and penalties under the provisions of the Black Money Act have been paid.
- No permission under FEMA will be required to dispose of the asset so declared and bring back the proceeds to India through banking channels within 180 days from the date of declaration. In case the declarant wishes to hold the asset so declared, she/he may apply to the Reserve Bank of India within 180 days from the date of declaration if such permission is necessary as on date of application. The Reserve Bank of India will deal with such applications as per extant regulations.
- In case such permission is not granted, the asset will have to be disposed of within 180 days from the date of receipt of the communication of refusal from the Reserve Bank, or within such extended period as may be permitted by the Reserve Bank and the proceeds brought back to India immediately through the banking channel.

Remittance of Assets

(A.P. (DIR Series) Circular No. 43 Dated 02 December 2014)

The RBI has amended the Foreign Exchange Management (Remittance of Assets) Regulations, 2000 with respect to the submission of "NOC" to the Income-tax department for tax payments. In line with this circular, the requirement of submitting a NOC at the time of closure of Liaison offices/ Branch offices of foreign companies in India stands deleted as per Master Circular No. 7/ 2015–2016 on Establishment of Liaison/ Branch/ Project offices in India by Foreign Entities.

Sectoral updates

Aerospace and Defence

FTP

The FTP 2015–20, released by Commerce Minister Mrs Nirmala Sitharaman on 01 April 2015, provides a framework for increasing exports of goods and services as well as generation of employment and increasing value addition in the country. The focus of the new policy is to support both the manufacturing and services sectors with a special emphasis on improving the "ease of doing business" in India.

Some of the key highlights of the policy and initiatives taken in relation to the defence sector are as follows:

- Validity of NOC for items falling in the categories of defence, military store, aerospace and nuclear energy shall be 24 months from the date of issue or authorization, or co-terminus with the contracted duration of the export order, whichever is more.
- A list of military stores requiring a NOC from the Department of Defence Production has also been notified by DGFT (http://dgft.gov.in/exim/2000/NOT/NOT13/not11513.pdf). A committee has been formed to create ITC (HS) codes for industrial licenses issued by the DIPP.
- The extension of the validity of SCOMET export authorisation from 12 months to 24 months.
- Authorisation for repeat orders will be considered on an automatic basis subject to certain conditions.
- Simplification of the verification process for EUC where a SCOMET item is being exported under Defence Export Offset Policy.

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DPP

Smaller defence deals brought under the ambit of "integrity pact"

The GoI recently amended the DPP to bring contracts of the value of INR 20 crore and more under the ambit of the "integrity pact"— a binding document in which the government promises that it will not accept bribes during the procurement process, and bidders promise not to offer bribes.

As per the earlier provisions of the DPP 2013, an integrity pact was required to be signed between the government department and the bidders for all procurement schemes over INR 1000 million. However, going forward, the bidders will be required to sign an integrity pact for providing equipment worth INR 200 million or more to the GoI.

Flexibility to OEMs in relation to nomination/ change in Indian Offset Partners

The MoD addressed a long-standing demand of OEMs by providing flexibility in relation to the nomination or change in offset partners, post the signing of the contract. The amendment in the DPP 2013 has been made with retrospective effect.

Earlier, OEMs were required to provide details pertaining to IOP-wise work share and specific products at the time of bid submission. Through this amendment, OEMs will now have the option to furnish these details to the DOMW, either at the time of seeking offset credits or one year prior to the actual discharge of offset obligations. However, they run the risk of incurring a penalty in case they are found to be ineligible for any reason. Resultant re-phasing, if any, also carries a risk of 5% enhancement in offset obligations.

Further, the Secretary (Defence Production) has been empowered to approve any changes in IOPs and products. Earlier, this required an approval from the Defence Minister based on the recommendations of the DPB.

ERV in Defence contracts

The MoD has recently amended the DPP-2013 by extending the benefit of ERV to Indian vendors under all procurement categories of capital acquisition. Under the earlier provisions, the ERV provision was applicable for rupee contracts with Indian vendors in "Buy (Global)" cases only. ERV was, however, not applicable earlier in cases categorised as "Buy (Indian)", except for DPSUs, in *ab-initio* single vendor cases or when nominated as a Production agency.

The move is expected to benefit defence vendors, particularly domestic vendors who import large quantities of components for products they make and sell to the Indian armed forces.

Industrial License (IL)

With a view to attract investments in the defence sector, the GoI has recently liberalised the industrial licensing regime *vide* issue of Press Note 10 of 2015 dated 22 September 2015, Press note 5 of 2015 dated 27 April 2015 and Press note 9 of 2014 dated 20 October 2014.

The key highlights of these press notes are as follows:

Increase in validity period of Industrial License –

The initial validity of ILs for the defence sector has increased from 7 years to 15 years, and is further extendable up to 18 years for existing as well as future licenses. However, in case a license has already expired, the licensee has to apply for a new one. This measure is being implemented to further promote ease of doing business, in view of the long gestation period of defence contracts.

Removal of stipulation of annual capacity in the Industrial License –

Press note 9 of 2014 stipulates the deregulation of the annual capacity for defence items for Industrial License. However, the licensee shall submit half-yearly production returns to the DIPP, and the Department of Defence Production in the prescribed format (to be notified separately).

Sale of Defence items to Government entities without approval of MoD

The Licensee shall be allowed to sell defence items to Government entities under the control of the Ministry of Home Affairs, state governments, PSU and other valid defence licensed companies without prior approval of the Department of Defence Production. However, for sale of items to other entities, prior permission would be required from the MoD.

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Broadcasting updates

First stage of Phase III FM Radio channel auctions

The MIB had approached the TRAI in December 2014, for its recommendations on reserve price for auction of FM Radio channels in 264 new cities as per Phase III. The TRAI in this regard, issued a consultation paper inviting comments from stakeholders by 25 February 2015.

After taking the comments into consideration, the TRAI released recommendation papers on 24 March 2015 in which it outlined the various approaches for valuation of FM Radio Channels.

In the recommendation paper, the reserve price for FM radio channels was fixed at 80% of the valuation for 253 cities and INR 0.5 million for the remaining 11 cities included in the “Others” category, which have a population of less than 0.1 million in the border areas of Jammu and Kashmir (J&K) and the North East (NE) region.

The First stage of the Phase III FM auctions was came to a successful conclusion after 125 rounds, that lasted 32 days, and offered 135 channels in 69 cities.

Phase III of cable TV digitisation

Phase I and II of cable digitisation has been completed. Phase III of digitisation, will cover all the remaining urban areas in the country and is scheduled for completion by 31 December 2015. Rural areas will be covered in Phase IV, which has to be completed by 31 December 2016. In order to receive TV services in urban areas after 31 December 2015, it is essential that:

- Multi-system operators and cable operators carry only digital encrypted signals; and
- Every cable subscriber has a set top box,

Recommendation on Regulatory Framework for Platform Services

The TRAI had issued a recommendation paper dated 19 November 2014, on the Regulatory Framework for Platform Services. In the recommendation paper, the TRAI has recommended that the regulatory framework ought to apply to all DPOs providing Platform Services (PS) irrespective of the mode of distribution.

In addition, recommendations have been provided for a regulatory framework for ground-based broadcasters, who are providing local-channels to the cable operators, with the intention to ensure that the regulatory framework established is comprehensive in its coverage of all program content that is available to TV subscribers. While providing its recommendations, the TRAI has also defined the term PS, as programs transmitted by DPOs exclusively to their own subscribers and does not include Doordarshan channels and registered TV channels. PS will not include foreign TV channels not registered in India.

Direction to Multi System Operators

The TRAI issued a direction to Multi System Operators on 04 November 2015, to provide a copy of the inter-connection agreement to cable operators:

- within 15 days, in respect of all inter-connection agreements entered into, prior to the date of issue of this direction; and
- which may be entered into after the issue of this direction within 15 days of signing the agreement and furnish compliance report within 21 days of issue of this direction

Consultation on the draft Telecommunication (Broadcasting and Cable) Services (Fourth) (Addressable Systems) Tariff (Amendment) Order, 2015

The TRAI has issued a consultation paper on the draft Telecommunication (Broadcasting and Cable) Services (Fourth) (Addressable Systems) Tariff (Amendment) Order, 2015. One of the amendment provides that if a multi-system operator, or direct to home operator, or internet protocol service provider or HITs operator provides broadcasting services or cable service to its subscribers, using a digital addressable system, and offers pay channels or pay channels and free to air channels as part of a bouquet; the a-la-carte rate of such pay channels forming part of a bouquet and the rate of such bouquet shall be subject to the following conditions, namely:

- the *a-la-carte* rate of a pay channel forming part of a bouquet shall not exceed 2 times its RIO rate offered by the broadcaster for addressable systems; and

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- the sum of a-la-carte rates of all the channels in the bouquet shall not exceed three times the bouquet rate.

Consultation paper on Tariff issues related to Commercial Subscribers

The TRAI has issued a consultation paper dated 14 July 2015, on Tariff issues related to Commercial Subscribers. The paper highlights the following issues:

- Is there a need to define and differentiate between domestic subscribers and commercial subscribers and if yes, what should be the basis or criterion?
- Is there a need to review the existing tariff framework (both at wholesale and retail levels) for TV services provided through addressable systems and non-addressable systems in order to cater to commercial subscribers?
- Is there is a need to have a different tariff framework for commercial subscribers (both at wholesale and retail levels)? If yes, then what should be the suggested tariff framework?
- What practical mechanism can be implemented so as to ensure transparency and accountability in the value chain?
- Is there a need to engage broadcasters in the determination of retail tariffs for commercial subscribers on a case-to-case basis?
- How can a TV signal feed provided for commercial purposes, be prevented from being misused for commercial purposes?

Telecom Sector

Consultation Paper on Compensation to the consumers in the event of dropped calls

(Press release no. 48/ 2015 issued by TRAI dated 04 September 2015)

The TRAI has released a consultation paper is response to the rising number of complaints by consumers on the issue of "dropped calls" and the deteriorating quality of phone services. The TRAI had conducted tests in Mumbai and New Delhi and found the Call Drop Rates to be higher than the permissible limits for most of the TSPs.

In the consultation paper, the TRAI invited stakeholders to comment the various possible methods for compensating the consumers for call drops by 28 September 2015. The methods under consideration are as follows:

- Provision for not charging for the dropped calls
  - Consumers should not be charged for a call that gets dropped within five seconds
  - In addition, if the call is dropped any time after 5 seconds, the last pulse of the call (minute/ second) which got dropped should not be charged.
- Provision of providing credit to the consumers for dropped calls
  - Credit of talk-time in minutes/ seconds, or
  - Credit of talk-time in monetary terms.

Guidelines on Spectrum Sharing

Source – Press information Bureau

The Government had approved the principle of spectrum sharing in 2012. The Government has now released guidelines for spectrum sharing, with the view of improving spectral efficiency and quality of services,

This step will increase spectrum efficiency for both operators, as capacity to carry telecom traffic is not in linear proportion to the sum of their spectrum holding, but is much larger than the sum of the traffic capacities of individual service provider.

Salient features of the norms for spectrum sharing, among other things, shall include:

- Access service providers in a LSA would only be allowed to share spectrum
- Sharing would be allowed only if both the licenses are having spectrum in the same band
- Spectrum Leasing would not be allowed
- Breach of terms and conditions of the license or revocation/ termination of license by the licensor would render the licensee ineligible to share spectrum
- Spectrum sharing would be allowed in following scenarios:

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- Where both sharing entities possess spectrum, for which the market price has been paid
- Where both sharing entities have administratively allotted spectrum
- Sharing of spectrum shall be permitted only after spectrum charges for liberalizing the administratively allocated spectrum are paid
- Both licenses will be individually and collectively responsible for complying with sharing guidelines, including interference norms
- Sharing will be restricted to sharing by only 2 licenses subject to condition that there will be at least 2 independent networks provided in the same band
- SUC rate for each of the licenses post-sharing shall increase by 0.5 % of AGR

Recommendations on "Introducing VNOs in telecom sector"

(Press Release No. 30/ 2015 issued by TRAI dated 01 May 2015)

VNOs are service delivery operators, who with the help of infrastructure providers provide telecom services to end users/ customers. VNOs can provide any or all telecom services, which are being provided by the existing TSPs.

The salient features of the recommendations are:

- VNO be introduced through proper "licensing framework" in the Indian Telecom Sector.
- The VNOs should be permitted for all segments of Voice, Data and Video as well as for all services notified in the UL.
- For introduction of VNO in the sector, there should be a separate category of license namely UL (VNO). Like UL authorisation, only pan-India or service area-wise authorisations may be granted under a UL (VNO) license.
- Duration for VNO licenses should be 10 years, extendable by 10 years at a time.
- There should not be a restriction on the number of VNO licensees per service area. Also there should be no restriction on the number of VNOs parented by an NSO

Consultation paper on Regulatory Framework for OTT services

(Press Release No. 22/ 2015 issued by TRAI dated 27 March 2015)

TSPs offer online content through applications and services, which are accessible over internet, and ride on operators' networks offering internet access services.

OTT services are rendered through the infrastructure of TSPs infrastructure, which provides fixed and mobile telephony. OTT service providers not only use TSPs infrastructure to provide services but also provide traditional services which are offered by TSPs and also other e-commerce sites etc.

The TRAI has released its "Consultation paper on Regulatory Framework on OTT services", which covers the views of the service providers and OTT providers, as well as all related issues (including Net Neutrality) and the regulation of OTTs (communication and non-communication).

The important issues highlighted in the paper are as follows:

- Policy and regulatory environment and need for regulation;
- Current Policy dispensation for OTT players *vis-à-vis* TSPs;
- Security concerns of OTT players providing communication services;
- Issues related to security, safety and privacy of the consumer;
- Issues arising because of "net-neutrality";
- Network discrimination and traffic management practices;
- Non-price-based discrimination of services and ensuring transparency to consumers
- Pricing related issues, including differential pricing for data services;

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Telecommunication Mobile Number Portability (Sixth Amendment) Regulations, 2015

(Press release No. 15/ 2015 issued by TRAI dated 25 February 2015)

To facilitate Full MNP (PAN India Portability) within 6 months in the country w.e.f 3 May 2015, the TRAI has issued a 6th Amendment to the Telecommunication Mobile Number Portability Regulation, 2009.

In addition to facilitating Pan-India Portability, the amendment provides for changes in the porting process as well. The changes made after the amendment to the MNP License Agreement on 3 September 2014, are as follow:

- The service provider (Donor Operator) from whom the post-paid subscriber has ported out, has to give a notice within a period of 30 days of due date of payment of its outstanding bill. After a lapse of 60 days from the due date of payment of the outstanding bill, the Donor Operator will not be entitled to raise non-payment disconnection requests with the Recipient Operator.
- For a post-paid subscriber who has defaulted payment to the Donor Operator, the Donor Operator will request the Recipient Operator to disconnect the ported number. The Recipient Operator in turn will give a notice of 15 days for making such payment, failing which the outgoing services for such subscriber will be debarred for a period of 15 days. In case the subscriber fails to make payment within these 15 days, his mobile number will be disconnected permanently by the Recipient Operator.
- In the case of a mobile number, which has been disconnected due to any reason, the time period for returning to the original service provider has been reduced from 90 days to 60 days. This step has been taken to effectively utilise the numbering resources.

Clarifications/ Reconsideration of Recommendations on "Valuation and Reserve Price of Spectrum: 2100 MHz Band"

(Press Release No. 05/ 2015 issued by TRAI on 15 January 2015)

The TRAI has issued this press release in response to the DoTs request for clarification pertaining to the TRAI's recommendations on the Valuation and Reserve Price of Spectrum: 2100 MHz Band.

The TRAI has now made the following clarifications:

- There is no change in the reserve prices for spectrum in the 2100 MHz bands from what were recommended earlier
- The whole purpose of clubbing the 2100 MHz band spectrum along with spectrum of other bands for auction in February 2015 will be defeated if sufficient spectrum is not made available in the 2100 MHz band. A split auction of 2100 MHz (one in February 2015 and remaining, say, in December 2015 after availability from Defence) will artificially increase the market price of 2100 MHz in February 2015 because of the severe supply constraint. The 15 MHz of spectrum in the 2100 MHz spectrum being vacated by MoD should be auctioned in view of the in-principle agreement reached with MoD, even if it is not available immediately.
- The Authority reiterated that in the upcoming auction of 2100 MHz band spectrum, an auction-specific cap should be placed that no bidder would be permitted to bid for more than 2 blocks in an LSA if 3–4 blocks are available in that LSA.

Recommendation on "Definition of Revenue Base (AGR) for the Reckoning of LF and SUCs"

(Press Release No. 03/ 2015 by TRAI dated 06 January 2015)

TRAI released its Recommendations after receiving comments and counter-comments from stakeholders on 15 September 2015 and 22 December 2014, respectively. The TRAI *suo-moto* felt the need to review the definition of Revenue, license fee rate etc., after taking note of disputes between licensor and licensees on the definition of Gross Revenue (GR) and Accumulated Gross Revenue under licenses granted by the DoT for different telecom services.

Salient features of the recommendations are as follows:

- LF and SUC should continue to be computed based on Adjusted Gross Revenue.
- Gross Revenue shall comprise revenue accruing to the licensed entity by way of all operations/ activities and inclusive of all other revenue/ income on account of interest, dividend, rent, profit on sale of fixed assets, miscellaneous income etc., without any set-off for related items of expense.

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- The concept of ApGR has been introduced. ApGR would be equal to total Gross Revenue of the licensee as reduced by:
  - Revenue from operations other than telecom activities/ operations as well as revenue from activities under a license/ permission issued by Ministry of Information and Broadcasting;
  - Receipts from the USO Fund; and
  - Items of "other income" as listed in the "positive list"
- The AGR then would be arrived at by deducting pass through charges from the ApGR. The existing definition of pass through charges (i.e., deductions) under different licenses to arrive at the AGR for the computation of LF and SUC, now includes access charges paid by TSPs providing international calling card services and toll-free charges.
- SUC should be levied on the AGR of telecom services, which use access spectrum in operations or providing services.
- Share of USO levied in the LF should be reduced from the present 5% to 3% of the AGR for all licenses with effect from 1st April 2015. With this reduction, the applicable uniform rate of license fees would decrease to 6% (from the present 8%) of the AGR *viz.* the 3% rate of LF that currently directly accrues to the Government will not change.
- IP-I services may not be brought under the licensing regime
- Immediate steps should be taken by the DoT to introduce a system of LfDS w.e.f. 1st April 2015 and to develop an e-portal for submission of LF and SUC by 1st April 2016.

Insurance

From the increase in the FDI limit to creating avenues for foreign reinsurers, the Indian insurance sector has witnessed significant developments in the past one year. The key developments are set out below:

Increase in FDI limit from 26% to 49%

The Insurance Laws (Amendment) Act, 2015 read with (Press note NO. 3 (2015 series))

The Insurance Laws (Amendment) Act, 2015 brought about major reforms in the Insurance Sector. One of the key amendments includes the enhancement of the FDI limit from 26% to 49%. However, it is pertinent to note that FIPB approval is required for increasing the foreign equity beyond 26%. In addition, other insurance intermediaries would also be covered within the ambit of the said limit of 49%, i.e., the foreign investment limit of 49% will now also be applicable to other insurance intermediaries such as web aggregators, Insurance Marketing Firms, etc.

Requirement of Indian ownership and control for Indian Insurance companies and intermediaries

IRDA Guidelines on "Indian owned and controlled"

The Insurance Laws (Amendment) Act, 2015 amended the definition of the term "Indian Insurance Company" to state that the Indian Insurance companies should be Indian owned and controlled in such manner as may be prescribed.

On 19 October 2015, the IRDA released guidelines for Indian insurance companies in order to bring more clarity to the requirement of Indian ownership and control. The guidelines prescribe mandatory compliance with the aforementioned requirement, and also require that the insurance companies report to the IRDA by 18 January 2016. The key features of these guidelines are listed below:

- They apply to Indian Insurance Companies that do not intend to increase their current foreign stake as well as to insurance intermediaries.
- The guidelines also lay down various criteria to ensure Indian control of Indian insurance companies which includes the following:
  - Majority of directors to be nominated by Indian promoter(s)/ investor(s).

Following the rule book

Regulatory developments

- Key Management Persons to be appointed through the Board of Directors/ Indian promoters/ Indian investors. However, Key Management Person(s) excluding the CEO may be nominated by the foreign investor provided that the appointment of such Key Management person is approved by the Board of Directors, wherein majority of the directors excluding independent directors are the nominees of Indian promoter(s)/ Indian investor(s).
- Control over significant policies to be exercised by the Board.
- Quorum shall be defined as the presence of majority of the directors. The right of a foreign investor's nominee to constitute a valid quorum is a protective right and would not tantamount to control so long as the presence of nominees of Indian promoter(s)/ investor(s) are also mandatorily taken into account for the purposes of quorum.
- Chairman (if has a casting vote) – to be nominated by the Indian promoters/ Indian investors

Foreign reinsurers permitted to open Indian Branch offices

IRDA (Registration and Operations of Branch Offices of Foreign Reinsurers other than Lloyd's) Regulations, 2015

Definition of the term "insurer" was amended vide the Insurance Laws (Amendment) Act, 2015, to include "the branch of a foreign reinsurer". The IRDA, on 30 October 2015, released the regulations for "Registration and Operations of Branch Offices of Foreign Reinsurers", thereby opening the path for foreign reinsurers to approach IRDA for registration of branch offices in India. Listed below are the key provisions contained in the regulations:

- As per the said regulations, the foreign reinsurer may apply under any of the following two categories:
  - Category I – those with the order of preference of cessions at par with the Indian Reinsurer(s) and minimum retention of 50%.
  - Category II – Others – minimum retention of 30%
- The regulations also prescribe the eligibility criteria for the foreign reinsurers, which, among other things, states that the foreign company should have been engaged in the reinsurance business for at least 10 years, a minimum net-owned funds of INR 50 billion and a minimum credit rating which has is characteristic of financial security for the last 3 years.
- The two-stages IRDA registration process, order of preference for cessions by Indian insurers to the reinsurers, annual fee requirement, time limit for commencement of business, etc. and other operational aspects have also been laid down by the said regulations.

The regulations also specify other operational aspects for such branch offices, which include the functions that cannot be outsourced, requirement of IRDA approval for opening additional offices, appointment, reappointment, removal, managerial remuneration payable to CEO, CFO and Chief Underwriter, other IRDA regulations to be complied with, etc.

Revised regulations for Corporate Agents

IRDA (Registration of Corporate Agents) Regulations, 2015

The IRDA, on 15 September 2015, released revised regulations for registration of Corporate Agents. These regulations shall come into force from 01 April 2016. The key highlights of the amended regulations are as follows:

- As per these regulations, a corporate agent may have arrangements with a maximum of three life, general and health insurers each, to solicit, procure and service their insurance products.
- Application for registration can be made under any one of the following categories:
  - Corporate Agent (Life)
  - Corporate Agent (General)
  - Corporate Agent (Health)
  - Corporate Agent (Composite)

Following the rule book

Regulatory developments

- It is pertinent to note that an applicant or its group entities ordinarily may be granted one certificate of registration provided that the group does not have any other insurance intermediation. However, an application for a corporate agency registration where any member of the applicant is already engaged in insurance intermediation, including the corporate agency, shall be considered on merits and with no conflict of interest.
- Validity – Registration, once issued, shall be valid for a period of 3 years from the date of its issue

Note

- *The Reserve Bank of India has issued a Circular dated 30 November 2015 outlining the new framework for ECBs, replacing the existing guidelines issued about a decade ago. The overarching principle of the new framework has been to liberalise and encourage long term ECBs denominated in foreign currency, and ECBs denominated in INR. For this purpose, these ECBs have been segregated from other ECBs as separate "Track II" and "Track III" respectively under the new framework. Further, there have been various amendments made in respect of other ECBs that have average maturity of less than 10 years.*
- *The DIPP has released Press Note No. 12 dated 24 November 2015 liberalising the FDI Policy in 15 major sectors of the Indian economy. Changes introduced in the policy include increase in sectoral caps, bringing activities under automatic route and easing of conditions for foreign investment. The 15 sectors in which liberalization took place include Construction Development Sector, Manufacturing and trading sector, Broadcasting Sector, Defence sector, Plantation sector, Civil Aviation Sector, Banking sector, LLPs, NRI investments etc.*

Annexures

Articles

PwC Thought Leadership Articles

Sn	Particulars of Articles/ TL Publication	Where published	Date of publication	Author names
1	The ‘Other Method’-A flexible recourse	BCAJ	08 January 2015	Darpan Mehta and Sujay Thakkar
2	New Tax ICDS convergence with IND-AS - Need of the hour	Taxsutra	15 January 2015	Vishal J Shah
3	Transfer Pricing and Customs - Part I	Taxsutra	22 January 2015	Darpan Mehta, Niren Shethia, Abhay Saboo
4	The Depository Receipt Scheme, 2014 - Tax Aspects Missing	Business World	28 January 2015	Sunil Gidwani
5	DAS - Dealing with tax aspects	Broadcase and CableSat	01 February 2015	Milan Shah
6	Welcoming DRP Revamp - 10 Suggestions to make it work	Taxsutra	04 February 2015	Kuntal Sen and Raju Vakharia
7	Budget must boost infrastructure	The Financial Express	05 February 2015	Nikhil Rohera
8	We do not expect much change in income tax rates	Business Standard	07 February 2015	Kuldip Kumar
9	Correct the duly structure for manufacturing	The Financial Express	10 February 2015	Pramod Banthia , Kunal Wadhwa , Siddharth Garg
10	TARCs critical recommendations - A step towards tax reforms - Part I	Taxsutra	10 February 2015	Sanjay Tolia and Ruhi Mehta
11	High hopes from Budget FY 16	The Financial Express	14 February 2015	Dinesh Supekar
12	Budget 2015 - Going to the MAT	Money Control	14 February 2015	Sandip Mukherjee
13	TARCs critical recommendations - A step towards tax reforms - Part II	Taxsutra	15 February 2015	Sanjay Tolia and Ruhi Mehta
14	Position on reporting International transaction	International Taxation	16 February 2015	Kanchun Kaushal, Dhanesh Bafna, Anusha Singh
15	Rely on just MAT	The Financial Express	19 February 2015	Rahul Garg
16	Stimulating SEZs	The Financial Express	20 February 2015	Kiran D Mehra
17	Budget 2015 - TP litigation issues need to be addressed	Moneycontrol.com	21 February 2015	Darpan Mehta and Sujaty Thakkar
18	What We Want From Budget 2015	The Economic Times Wealth	23 February 2015	Kuldip Kumar
19	Budget 2015 – Expectations of the Financial Services Industry	Taxsutra	23 February 2015	Gautam Mehra
20	Union Budget 2015 - Laying the ground work for GST	Taxsutra	23 February 2015	Satish S and Hitashree Chhabria
21	Budget must fix GST timelines	The Financial Express	26 February 2015	Vivek Mishra
23	Taxation in Sync with Key Ideas?	The Economic Times	27 February 2015	Ketan Dalal
24	Union Budget 2015 Tax Alignment with Key Themes?	The Economic Times	27 February 2015	Ketan Dalal
25	Falling Oil Prices, Rising Budget 2015 Expectations	Taxsutra	27 February 2015	Satish S and Jyoti Shukla
26	Jaitley presents a watershed budget	Mint	01 March 2015	Shyamal Mukherjee , Prerna Mehndiratta
27	More Options to Save though Tax Slabs Stay the Same	The Economic Times	01 March 2015	Kuldip Kumar

Sn	Particulars of Articles/ TL Publication	Where published	Date of publication	Author names
28	Budget 2015: More options to save though tax slabs stay the same	The Economic Times	01 March 2015	Kuldip Kumar
29	Emphasis on tax compliance, GST rollout:pet projects get their dues	Business Standard	02 March 2015	Pramod Banthia , Kunal Wadhwa , Siddharth Garg
30	Investment-friendly measures for industry, infra development	Business Standard	02 March 2015	Kaushik Mukherjee
31	Budget will curb tax litigation	The Financial Express	03 March 2015	Rahul Garg
32	Few hits, few misses	The Financial Express	07 March 2015	Dinesh Supekar
33	Taxation of Indirect Transfers - need for further clarity	Taxsutra	11 March 2015	Pavan Kakade and Puneet Putiani
34	Needed: Tax clarity for lease premium	The Financial Express	13 March 2015	Kamal Abrol , Amit Singhal
35	Tax compliance is still a nightmare	The Hindu Business Line	17 March 2015	Pallavi Singhal
36	MANY HITS, A FEW MISSES	BW Businessworld	23 March 2015	Ketan Dalal
37	Retrospective Amendments-Testing the Waters	The Firm	06 April 2015	Ajay Rastogi
38	REIT/ InvIT....Still-born, a second time?	Hindustan Times	08 April 2015	Vivek Mehra
39	Transfer Pricing and Customs - Part II	Taxsutra	10 April 2015	Darpan Mehta and Abhay Saboo
40	Real estate trusts may remain stillborn	The Hindu Business Line	11 April 2015	Vivek Mehra
41	Conceptual clarity versus piecemeal relief	The Financial Express	23 April 2015	Saurabh Upadhyay
42	MAT on FIIs-Conceptual clarity versus piecemeal relief	Financial Express	23 April 2015	Saurabh Upadhyay
43	Using CUP in commodity transactions benchmarking - Part I	Taxsutra	24 April 2015	Kunj Vaidya and Chandrakumar S
44	MAT on FIIs - Strom in a Tea-cup	Taxsutra	27 April 2015	Nitin Karve
45	MAT on FPIs-It's a bleak past but bright future	Economic Times	28 April 2015	Anish Sanghvi
46	B2B e commerce can power "Make in India"	Business Today	30 April 2015	Akash Gupta
47	Taxation of Cross-Border Services - Certain controversies	IFA Compendium	30 April 2015	Radhakishan Raval and Geeta Bhatia
48	A path to transfer pricing certainty	The Financial Express	01 May 2015	Dhaivat Anjaria
49	RNR should be in the range of 20-24%	The Financial Express	12 May 2015	Gautam Khattar , Vimal Pruthi , Aayush Bhargava
50	New FTP hits India s infra plans	The Financial Express	12 May 2015	Amit Bhagat , Sahil Sood
51	RNR should be in the range of 20-24 percent	Financial Express	12 May 2015	Gautam Khattar, Vimal Pruthi and Aayush Bhargava
52	Reader's corner	Business Standard	24 May 2015	Kuldip Kumar
53	ICDS-III relating to Construction Contracts	The Chamber's Journal	25 May 2015	Vishal J Shah and Kunal Mehta

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54	Withholding tax on remittances to non-residents - PAN dilemma!	Taxindiainternational.com	25 May 2015	Rakesh B Jain and Anuj Singhal
55	Pulling the MAT	The Financial Express	28 May 2015	Suresh V Swamy , Deepa Purswani , Shivam Tiwari
56	Is tax rebate for plastic money a good idea?	Financial Express	01 July 2015	Kuldip Kumar
57	Availment of foreign tax credit and issues involved	International Taxmann	01 July 2015	Pavan Kakade and Puneet putiani
58	Does NPS score over other pension products	Financial Chronicle	06 July 2015	Hitesh Sharma and Risha Parekh
59	Tax relief on fees for technical services	Financial Express	17 July 2015	Shailesh Monani and Gaurish Zaoba
60	Section 40(a)(i) - Is new always better?	Taxsutra	24 July 2015	Nitin Karve
61	Taxability under the provision of the DTAA between India and relevant countries	The Chamber's Journal	01 August 2015	Nikhil Rohera and Faizan Nursu
62	Tax Issues for foreign airline companies	The Chamber's Journal	01 August 2015	Chandresh Bhimani and Rakesh B Jain
63	How the change in Capital gains tax impacts investors	Financial Chronicle	03 August 2015	Shuddhasattwa Ghosh
64	Life after Indian HC decision on Marketing Intangibles	Bloomberg BNA	13 August 2015	Sanjay Tolia, Ruhi Mehta and Rackesh kotak
65	SC upholds NR oil and gas service providers claims	International Taxmann	19 August 2015	Chandresh Bhimani and Gaurish Zaoba
66	BEPS 8 - Hard to value intangibles	International Taxmann	19 August 2015	Pavan Kakade and Chahat Mahajan
67	POEM - Change in India tax residency test	Bloomberg BNA	26 August 2015	Ravindra Agrawal and Tarla Shah
68	Interchange fees witness justice	Taxsutra	31 August 2015	Abhishek A Rastogi, Rashmi Deshpande
69	Taxation of e-commerce transactions - A host of unanswered questions	Taxsutra	02 September 2015	Poonam Prabhu and Kruti Shah
70	Analysis of BEPS Action 15 – Developing a Multilateral Instrument to modify Bilateral Tax Treaties	International Taxation	16 September 2015	Pavan Kakade and Mehul Jain
71	CCAs Newer Dimension	International Taxation	16 September 2015	Arun Saripalli, Anuja Talukder and Sumin Mehta
72	How Income tax is affecting business	BusinessLine on Campus	18 September 2015	Pavan Kakade and Puneet Putiani
73	Mission Possible : Making waste-to-energy work in India	Power Today, National	01 October 2015	Umesh Agarwal
74	Claim of Residency and Eligibility under the India-Mauritius Tax Treaty	Bloomberg BNA	01 October 2015	Ravindra Agrawal and Tarla Shah
75	HC's Rampgreen ruling - A silver lining to comparables identification jigsaw	Taxsutra	01 October 2015	Kanchun Kaushal, Anand Kankani, Deven Shah
76	BEPS - A dramatic change in Global Tax policy landscape	Mint	05 October 2015	Sanjay Tolia
77	E- Commerce and Pharmacies add to the right formulation	Financial Chronicle	19 October 2015	Sandeep Ladda

Sn	Particulars of Articles/ TL Publication	Where published	Date of publication	Author names
78	Financial transactions in Transfer Pricing	International Taxation	20 October 2015	Dinesh Supekar and Bhavik Timbadia
79	Analysis of BEPS Action Plan 3 – Strengthening CFC Rules	International Taxation	20 October 2015	Pavan R Kakade and Puneet Putiani
80	Tax notice for limited scrutiny is not scary	Financial Chronicle	20 October 2015	Vineet Agarwal
81	Tax Residency certificate - An Indian perspective	International Taxation	20 October 2015	Shailesh Monani, Chandresh Bhimani and Gaurish Zaoba
82	BEPS - An India Perspective	The Financial Express	23 October 2015	Hitesh Sawhney
83	Unified regulator for equity & commodities market - A Tax Spin to SEBI-FMC Merger!	Taxsutra	28 October 2015	Sunil Gidwani
84	Does India Need Mandatory Disclosure Rules?	The Firm CNBC	16 November 2015	Rahul Garg
85	GA sector cries for succour to tap huge potential	Financial Chronicle	20 November 2015	Dhiraj Mathur
86	Tax rules you must know if you work abroad	Financial Chronicle	01 December 2015	Gireesh Shetty
87	Why India’s most important tax reform is still stuck in parliament	Quartz India	14 December 2015	Gautam Khattar

Alerts

PwC India Tax Insights

Sn+A2:D35	Date	Issue	Ruling/ Notification/ Circular
1	7 January 2015	Roadmap for Ind-AS implementation	MCA press release on 02 January 2015 on the roadmap for implementation of Ind-AS
2	9 January 2015	Non-compete fees re-characterised as consideration for transfer of shares - Vodafone test applied for tax planning *v.* tax evasion	[2014] 52 taxmann.com 425 (Delhi)
3	9 January 2015	Dispute Resolution Panel - Mechanism restructured	
4	13 January 2015	Tribunal invokes MFN clause to bring the 'make available' condition into the India-Sweden tax treaty	[2014] 52 taxmann.com 211 (Pune-Tribunal)
5	15 January 2015	Entire salary of Indian residents on deputation to group company/ LLP and foreign citizens on employment with LLP in India can be credited to foreign bank account	
6	15 January 2015	Tribunal deletes location savings adjustment - taxpayer had no unique advantage, operated in 'perfect competition', and was benchmarked against local companies	[TS-3-ITAT-2015(Mumbai-Tribunal)TP]
7	20 January 2015	Functional/ risk profile rather then solely contractual arrangement decide the arm's length price of international transactions	[2015] 53 taxmann.com 253 (Kolkata-Tribunal)
8	28 January 2015	Amount received by non-resident from its Indian franchisees towards reimbursement of international sales and marketing expenses is royalty/ FIS as per India-US tax treaty	[TS-4-ITAT-2015(Mumbai-Tribunal)]
9	5 February 2015	Social Security Agreement between India-Norway comes into force with effect from 1 January 2015	http://www.epfindia.com/Circulars/Y2014-15/IWU_SSA_Norway_36198.pdf
10	6 February 2015	CBDT announces Safe Harbour Rules for Specified Domestic Transactions of Government electricity companies	CBDT Notification No. 11 /2015 [F.No. 142/7/2014-TPL] dated 4 February 2015
11	17 February 2015	Applicability of withholding tax depends on nature of underlying transaction - reimbursement mechanisms through agents to be ignored	[TS-31-ITAT-2015(Mumbai-Tribunal)]
12	28 February 2015	Income from rendering of marine logistic services taxable under section 44BB of the Act	[ITA No.107/ Del/ 2012, AY 2008-09, ITAT Delhi]
13	16 March 2015	No tax on consideration agreed under development agreement if not accrued or received; concept of 'real income' relevant while determining income charegable to tax	[TS-73-HC-2015(Bombay)]
14	17 March 2015	APA roll back rules announced	CBDT Notification No.23/2015 dated 14 March 2015
15	18 March 2015	Delhi HC rules on marketing intangibles in the case of distributors	[2013] 29 taxmann.com 300 (Delhi-Tribunal)(SB)
16	19 March 2015	Short-term capital loss taxable at concessional rate can be set off against other STCGs regardless of tax rate differential	TS-105-ITAT-2015(Bangalore-Tribunal)]
17	23 March 2015	Clarification of foreign direct investment norms in the construction development sector	Clarification to Press Note 10 of 2014

Sn+A2:D35	Date	Issue	Ruling/ Notification/ Circular
18	27 March 2015	CBDT issues circular on taxation of dividends issued by foreign companies deriving value substantially from India	CBDT Circular No. 4/ 2015 dated 26 March 2015
19	31 March 2015	Substantiating cost essential for deduction under cost allocation arrangements	[TS-120-ITAT-2015(Delhi-Tribunal)]
20	1 April 2015	Highlights of the Foreign Trade Policy 2015-2020	http://commerce.nic.in/MOC/foreign_trade_policy2.asp
21	2 April 2015	Section 206AA cannot override section 90(2) of the Act	[TS-158-ITAT-2015(Pune-Tribunal)]
22	10 April 2015	Regional Director can raise income-tax related objections in merger scheme though tax authorities raised no objections; tax authorities not bound by appointed date fixed by scheme	[TS-152-HC-2015(Bombay)]
23	13 April 2015	Delhi HC upholds Tribunal ruling - TPO not empowered to restructure transaction; Agreed commercial terms to be respected in determining arm's length interest rate charged, Indian PLR not applicable for foreign currency loans	[TS-117-HC-2015(Delhi)]
24	4 May 2015	Nearly superprofits/ losses cannot be criterion for rejecting a comparable; circumstances for using multiple year data explained	[TS-173-HC-2015(Delhi)-TP]
25	6 May 2015	Finance Bill, 2015 passed in Lok Sabha - Changes in tax proposals explained	
26	6 May 2015	Rental income from property assessable under the head 'profits and gains o business or profession'	[TS-238-SC-2015(Supreme Court)]
27	7 May 2015	GST Constitution Amendment Bill has been passed by the Lok Sabha	
28	8 May 2015	REITs to be eligible financial instrument under FEMA	
29	8 May 2015	Advertisement collection agent of a foreign broadcasting company does not create PE in India; arm's length remuneration to agents extinguishes further attribution to PE	[TS-246-HC-2015(Bombay)]
30	15 May 2015	Finance Act, 2015 has received the assent of the President of India	
31	20 May 2015	Rate of service tax to be 14% effective from 1 June 2015	Notification No. 14, 15 and 16 of 2015-Service tax dated 19 May, 2015 & Notification No. 14/2015-central excise dated 19 May, 2015
32	22 May 2015	CBDT prescribes draft scheme for use of "Arm's Length Range" and "Multiple Year Data"	F. No. 134/11/2015-TPL
33	31 May 2015	Simplified IT Return Forms announced and deadline for filing returns extended	PIB Press Release dated 31 May 2015
34	1 June 2015	Recommendations on the Draft Scheme of the proposed rules for computation of ALP - "range" concept and "multiple year data"	
35	11 June 2015	CBDT issues guidelines on condonation of delay in filing claim for refund/ carry forward of losses	CBDT Circular No. 9/2015
36	12 June 2015	CBDT provides clarifications on APA rollback provisions	CBDT Circular No. 10/2015
37	12 June 2015	Investment through porfolio management services not a business activity; investment in shares using borrowed funds not relevant for characterisation of income	TS-318-HC-2015(Karnataka)]

Sn+A2:D35	Date	Issue	Ruling/ Notification/ Circular
38	18 June 2015	FinMin approves 2 Committees to suggest GST rates and monitor IT preparedness	
39	23 June 2015	Government notifies new income tax return forms for the financial year 2014-15	CBDT Notification Number 49/2015 dated 22 June 2015
40	30 June 2015	Off-shore supply of equipment and design and drwaings not taxable in India	[TS-349-ITAT-2015 (Kolkata-Tribunal)]
41	7 July 2015	Government notifies valuation rules and timelines for one-time compliance window under Black Money Taxation Act	Notification No. G.S.R. 529 (E) dated 2 July 2015
42	7 July 2015	GST Bill update: line-up to Monsoon session of the Upper house	
43	9 July 2015	Services inextricabily linked to prospecting, extraction or production of mineral oil eligible for presumptive taxation under the Act	[2015] 59 taxmann.com 1 (Supreme Court)
44	10 July 2015	Government issues clarifications in form of FAQs on one time complainace window scheme of the Black Money Taxation Act	Circular No. 13 of 2015 dated 06 July 2015
45	10 July 2015	Agreement on Social Security with Austria enters into force on 1 July 2015	EPFO Circular No. IWU/7(7)2010/Austria dated 6 July 2015
46	10 July 2015	FATCA Update - India and United States sign Inter Governmental Agreement (IGA) on FATCA	
47	14 July 2015	Government eases process of e-filing returns using EVC	Notifcation No. 2/2015 dated 13 July 2015
48	17 July 2015	Marketing and other support services not taxable as FIS where the 'make available' test is not satisfied; where dependent agent PE is remunerated at arm's length, no further amount is taxable	[TS-386-ITAT-2015 (Bangalore-Tribunal)]
49	22 July 2015	GST Bill update: Select committee submits report to Rajya Sabha	
50	29 July 2015	Transaction of unregistered development agreement not regarded as a 'transfer' under 2(47)(v); on subsequent cancellation of development agreement, expected income cannot be taxed on hypothetical basis	[TS-414-HC-2015 (Punjab & Haryana)]
51	30 July 2015	GST Bill update: Union Cabinet approves amendments to the GST Constitution Amendment Bill	
52	3 August 2015	Use of Berry ratio as PLI upheld	ITA No. 761/DEL/2015
53	4 August 2015	Social Security Agreement between India-Canada comes into force with effect from 1 August 2015	EPFO Circular dated 31 July 2015
54	11 August 2015	FATCA Update: Indian Government notifies rules for FATCA reporting; due date for 2014 reporting set at 31 August 2015	
55	25 August 2015	Consultation paper released by SEBI for amendments to SEBI (Infrastructure Investment Trusts) Regulations	SEBI issued consultation paper on 20 August 2015
56	25 August 2015	Bangalore Tribunal rules on the coverage of international transactions to even include an arrangement	ITA No. 146/Bang/2015

Sn+A2:D35	Date	Issue	Ruling/ Notification/ Circular
57	2 September 2015	No MAT on Foreign Portfolio Investors	"http://finmin.nic.in/reports/ReportonApplicabilityofMinimumAlternateTax%20onFIIsFPIs.pdf http://finmin.nic.in/press_room/2015/PressonApplicabilityofMinimumAlternateTax_onFIIsFPIs.pdf"
58	2 September 2015	TRS sufficient evidence for accepting status of residence as well as beneficial ownership for applying India-Mauritius tax treaty	[TS-484-HC-2015(Punjab & Haryana)]
59	8 September 2015	Minimum Alternate Tax under section 115JB not payable on receipts that do not form part of Total income	[ITA No. 2008/Mum/2012]
60	9 September 2015	Income earned by a taxpayer through 'on-site' software development work eligible for exemption under section 10A	[TS-497-HC-2015(Karnataka)]
61	11 September 2015	Government issues another set of FAQs on one time compliance window scheme of the Black Money Taxation Act, 2015	Circular No. 15 of 2015 dated 3 September 2015
62	11 September 2015	Karnataka High Court holds that no VAT is applicable on software implementation	[TS-481-HC-2015(Karnataka)-VAT]
63	16 September 2015	Facility Sharing Arrangements between Group Companies not to qualify as 'Real Estate Business' under the FDI Policy	DIPP File No.: No.12/15/2009-FC-1 dated 15 September 2015
64	16 September 2015	Companies Deposit Rules Amended - Loans from Relatives of Dirctors Allowed	
65	23 September 2015	CBEC issues a circular stating that SC judgments override circulars and instructions issued by the CBEC	(Civil Appeal No. 4022 of 1999)
66	26 September 2015	Government provides immunity under FEMA in respect of assets declared under one-time compliance scheme of the Black Money Taxation Act	RBI Press Release : 2015-2016/754
67	30 September 2015	Supreme Court disposes off the Castleton's SLP against AAR Ruling on MAT	
68	8 October 2015	Issue of reports of committees on business processes to be followed in GST regime for registration, payment of tax and refunds for circulation	
69	19 October 2015	CBDT's revised and updated guidance for implementation of TP provisions	CBDT Instruction No. 15 of 2015 dated 16 October 2015
70	21 October 2015	CBDT prescribes final rules for use of 'arm's length range' and 'multiple year data'	CBDT Notification No. 83 of 2015 dated 19 October 2015
71	23 October 2015	Draft business processes for returns	
72	30 October 2015	Carry-forward and set-off of unabsorbed losses permissible even if shareholding changes by more then 49%, so long as there is no change in control of company	[TS-607-HC-2015(Karnataka)]

Sn+A2:D35	Date	Issue	Ruling/ Notification/ Circular
73	30 October 2015	CBEC issues a notification allowing the service providers to utilise CENVAT credit of education cess and secondary and higher education cess against output service tax liability in specified cases	Notification No. 22/2015-Central Excise (N.T.) dated 29 October 2015
74	6 November 2015	CBEC notifications giving effective rate and date of levy of Swachh Bharat Cess	Notification No. 21/2015-Service Tax dated 6 November 2015
75	6 November 2015	Transfer of unabsorbed losses permissible if amalgamating company in business for three or more years even if business units engaged for less than three years; Activities for setting up of business also construed as "engaged in business"	[TS-630-HC-2015(Karnataka)]
76	13 November 2015	Major Reforms in Foreign Direct Investment Policy	"http://dipp.gov.in/English/policies/fdi_review_10112015.pdf"
77	13 November 2015	CEBC issues circular to grant partial refunds to service exporters	Circular No. 187/6/2015 - Service Tax dated 10 November 2015
78	17 November 2015	Capital receipt credited to P&L account is part of book profit for MAT purposes	[TS-643-ITAT-2015(Bangalore-Tribunal)]
79	19 November 2015	Transfer as a 'Going Concern' not determinative of 'Slump Sale'	[TS-647-ITAT-2015(Kolkata-Tribunal)]
80	20 November 2015	Regulations enabling foreign investment in investment vehicles (including AIFs, REITs and InvITs) notified	Notification No. FEMA 355/2015-RB
81	21 November 2015	Government releases proposed roadmap to phase-out deductions under Income-tax Act	
82	23 November 2015	IRDAI regulations for issue of other forms of capital	F. No. IRDAI/Reg/20/110/2015 dated 13 November 2015
83	26 November 2015	Liberalisation of FDI Policy	Press Note No. 12 dated 24 November 2015
84	1 December 2015	Exempt capital gains excluded from 'accumulated profit' for deemed dividend; deemed dividend provisions cannot be applied to non-shareholder family members	[TS-669-ITAT-2015(Kolkata-Tribunal)]
85	2 December 2015	ECB Policy - New Framework	ECB Policy – Revised Framework published vide A.P. (DIR Series) Circular No. 32 dated 30 November 2015
86	3 December 2015	Upfront premium received for leasing out land on BOT basis taxable on receipt basis	[TS-674-ITAT-2015(Bangalore-Tribunal)]
87	3 December 2015	SEBI notifies new Listing Regulations	CIR/CFD/CMD/16/2015
88	4 December 2015	Draft model GST law made available	
89	4 December 2015	Key recommendations of the panel on GST rates	
90	14 December 2015	Delhi HC rules on marketing intangibles in the case of licensed manufacturers	ITA No. 110/2014 & 710/2015
91	16 December 2015	Safe Harbour Rules - Recommendations	

Alerts

PwC India Newsletters

India Spectrum

Sn	Issue
1	PwC Newsletter: India Spectrum - December - January 2015

Customs, FTP and WTO

Sn	Issue
1	PwC Newsletter: Customs, FTP and WTO - January 2015
2	PwC Newsletter: Customs, FTP and WTO - February 2015
3	PwC Newsletter: Customs, FTP and WTO - March 2015
4	PwC Newsletter: Customs, FTP and WTO - April 2015
5	PwC Newsletter: Customs, FTP and WTO - May 2015
6	PwC Newsletter: Customs, FTP and WTO - June 2015
7	PwC Newsletter: Customs, FTP and WTO - July 2015
8	PwC Newsletter: Customs, FTP and WTO - August 2015
9	PwC Newsletter: Customs, FTP and WTO - September 2015
10	PwC Newsletter: Customs, FTP and WTO - October 2015
11	PwC Newsletter: Customs, FTP and WTO - November 2015

Indirect Taxes

Sn	Issue
1	PwC Newsletter: Indirect taxes - January 2015
2	PwC Newsletter: Indirect taxes - February 2015
3	PwC Newsletter: Indirect taxes - March 2015
4	PwC Newsletter: Indirect taxes - April 2015
5	PwC Newsletter: Indirect taxes - May 2015
6	PwC Newsletter: Indirect taxes - June 2015
7	PwC Newsletter: Indirect taxes - July 2015
8	PwC Newsletter: Indirect taxes - August 2015
9	PwC Newsletter: Indirect taxes - September 2015
10	PwC Newsletter: Indirect taxes - October 2015
11	PwC Newsletter: Indirect taxes - November 2015

Tax Treaties

List of Tax Information Exchange Agreements (TIEAs)

Sr No	Country	Notification No. and Date	Date when signed	Date of coming into force
1	Argentina	Notification No. 22/2013 [F.NO. 504/3/2010-FTD-II]/SO 824(E), dated 22-3-2013	21 November 2011	28 January 2013
2	Bahamas	Notification No. 25/2011 [F.NO. 503/6/2009-FTD-I], dated 13-5-2011	11 February 2011	01 March 2011
3	Bahrain	Notification No. 44/2013[F.No.501/03/1994-FT&TR-II]/SO 1766(E), dated 19-6-2013	31 May 2012	11 April 2013
4	Bermuda	Notification No. 5/2011 [F. NO. 503/2/2009-FTD-I], dated 24-1-2011	07 October 2010	03 November 2010
5	Belize	Notification No. 3/2014 [F. No. 503/4/2012-FTD-I], dated 7-1-2014	18 September 2013	25 November 2013
6	British Virgin Islands	Notification No. 54/2011 [F.NO. 503/10/2009-FTD-I], dated 3-10-2011	09 February 2011	22 August 2011
7	Cayman Islands	Notification No.61/2011[F.NO.503/03/2009-FTD-I]/S.O. 2902(E), dated 27-12-2011	21 March 2011	08 November 2011
8	Gibraltar	Notification No. 28/2013 [F. No. 503/11/2009-FTD-I]/S.O. 924(E), dated 01-04-2013	01 February 2013	11 March 2013
9	Guernsey	Notification No. 30/2012 [F. NO. 503/1/2009-FTD-I]/SO 1782(E), dated 9-8-2012	20 December 2011	11 June 2012
10	Isle of Man	Notification No. 26/2011 [F.NO. 503/01/2008 - FTD-I], dated 13-5-2011	04 February 2011	17 March 2011
11	Jersey	Notification No. 26/2012 [F. NO. 503/6/2008-FTD-I]/S.O. 1541(E), dated 10-7-2012	03 November 2011	08 May 2012
12	Principality of Liechtenstein	Notification No. 30/2014[F.No.503/4/2009-FTD-I], dated 6-6-2014	28 March 2013	01 April 2013
13	Liberia	Notification No. 32/20012-FT&TR-II [F.NO. 503/02/2010-FT&TR-II]/SO 1877(E), dated 17-8-2012	03 October 2011	30 March 2012
14	Macau, China	Notification No.43/2012[F.No.503/04/2009-FT&TR-II]/SO 2427(E), dated 10-10-2012	03 January 2012	16 April 2013
15	Monaco	Notification No.43/2012[F.NO.503/04/2009-FT&TR-II]/SO 2427(E), dated 10-10-2012	31 July 2012	27 March 2013
16	San Marino	Notification No.63/2015 [F.No.500/02/2003-FTD-I] SO 2192(E), dated 12-8-2015	Signed on 19 December 2013	29 August 2014
17	St. Maarten		Signed on 27 October 2012	00 January 1900

List of Social Security Agreements

Sr No	Country	Date when signed	Date of coming into force
1	Belgium	03 November 2006	01 September 2009
2	Czech Repulic	09 June 2010	01 September 2014
3	Denmark	17 February 2010	01 May 2011
4	Finland	12 June 2012	01 August 2014
5	French Republic	30 September 2008	01 July 2011
6	Germany (On Social Insurance)	08 October 2008	01 October 2009
7	Hungary	03 February 2010	01 April 2013
8	Korea	19 October 2010	01 November 2011
9	Luxembourg	30 September 2009	01 June 2011
10	Netherlands	22 October 2009	01 December 2011
11	Norway	29 October 2010	01 January 2015
12	Switzerland	03 September 2009	29 January 2011
13	Sweden	26 November 2012	01 August 2014

List of Social Security Agreements

Sr No	Country	Notification
1	Afghanistan	GSR 514(E), dated 30.09.1975
2	Ethiopia	GSR 8(E), dated 04.01.1978 as corrected by Notification No. GSR 159(E), dated 02.03.1978
3	Iran	GSR 284(E), dated 28.05.1973
4	Lebanon	GSR 1552 and 1553, dated 28.06.1969
5	Maldives	SO 34(E), dated 10.01.2011 by Notification No. 3/2011
6	Pakistan	GSR 792(E), dated 29.08.1989
7	Peoples Democratic Republic of Yemen	GSR 857(E), dated 12.08.1988
8	SAARC Countries	SO 34(E), dated 10.01.2011 by Notification No. 3/2011

List of Double Taxation Avoidance Agreements

Sr No	Country	Notification No. and Date	Date when signed	Date of coming into force
1	Albania	Notification No. 2/2014 [F. No. 501/1/2003-FTD-I]/SO 47(E), dated 7-1-2014	08 July 2013	04 December 2013
2	Armenia	Notification No. GSR 800E, dated 8-12-2004	31 October 2003	09 September 2004
3	Australia	Notification No. GSR 60(E), dated 22-1-1992	25 July 1991	20 December 1991
4	Austria	Notification No. GSR 682(E), dated 20-9-2001	08 November 1999	05 September 2001
5	Azerbaijan		20 November 1988	01 April 1990
6	Bangladesh	Notification No. GSR 758(E), dated 8- 9-1992	27 August 1991	27 May 1992
7	Belarus	Notification No. GSR 392(E), dated 17-7-1998	27 September 1997	17 July 1998
8	Belgium	Notification No. GSR 632(E), dated 31-10-1997, as amended by Notification No. SO 54(E), dated 19-1-2001. Earlier agreement was entered into vide GSR 323(E), dated 6-6-1975 which was later amended by GSR 321(E), dated 2-3-1988.	26 April 1993	01 October 1997
9	Bhutan	NOTIFICATION NO. 42/2014 [F.NO.503/4/2004-FTD-II], dated 5-9-2014	04 March 2013	17 July 2014
10	Botswana	Notification No. 70/2008-FTD, dated 18-6-2008	08 December 2006	31 January 2008
11	Brazil	Notification No. GSR 381(E), dated 31-3-1992	26 April 1988	11 March 1992
12	Bulgaria	Notification No. GSR 205(E), dated 9-5-1996	26 May 1994	23 June 1995
13	Canada	Notification No. SO 28(E), dated 15-1-1998. Earlier agreement was entered into vide GSR 1108(E), dated 25-9-1986, as amended by GSR 635(E) dated 24-6-1992. Circular No. 638, dated 28-10-1992 dealt with this agreement.	11 January 1996	06 May 1997
14	China (People's Republic of China)	Notification No. GSR 331(E), dated 5-4-1995	18 July 1994	21 November 1994
15	Croatia	Notification No.24/2015 [F.NO.501/09/1995-FTD-I], dated 17-3-2015	12 February 2014	Not yet in force.
16	Chinese Taipei (Taiwan)		12 July 2011	12 August 2011
17	Colombia	Notification No.44/2014 [F.NO.501/3/99-FTD-II], dated 23-9-2014	13 May 2011	07 July 2014
18	Cyprus	Notification No. GSR 805(E), dated 26-12-1995	13 June 1994	21 December 1994
19	Czech Republic	Notification No. GSR 811(E), dated 8-12-1999	01 October 1998	27 September 1999
20	Denmark	Notification No. GSR 853(E), dated 25-9-1989	08 March 1989	13 June 1989
21	Egypt (United Arab Republic)	Notification No. GSR 2363, dated 30-9-1969	20 February 1969	30 September 1969
22	Estonia	Notification No. 27/2012 [F.NO.503/02/1997- FTD-1]/SO NO. 1677(E), dated 25-7-2012	19 September 2011	20 June 2012
23	Ethiopia	Notification No. 14/2013 [FT & TR-II/F. No. 503/01/1996-FT&TR-II], dated 21-02-2013	25 May 2011	01 April 2013
24	Fiji	NOTIFICATION NO.35/2014 [F.NO.503/11/2005-FTD-II], dated 12-8-2014	30 January 2014	15 May 2014

Sr No	Country	Notification No. and Date	Date when signed	Date of coming into force
25	Finland	Notification No. 36/2010 [F. NO. 501/13/1980-FTD-I], dated 20-5-2010	15 January 2010	19 April 2010
26	France	Notification No. 9602 [F. No. 501/16/80-FTD], dated 6-9-1994, as amended by Notification No. SO 650(E), dated 10-7-2000	29 September 1992	01 August 1994
27	Georgia	Notification No. 4/2012[F.NO.503/05/2006-FTD.I], dated 6-1-2012	24 August 2011	08 December 2011
28	Germany	Notification No. SO 836(E), dated 29-11-1996. Earlier an agreement was entered with Federal German Republic vide GSR 1090, dated 13-9-1960 and vide GSR 107(E), dated 2-3-1990 and agreement was entered with German Democratic Republic.	19 June 1995	26 October 1996
29	Greece	Notification No. GSR 394, dated 17-3-1967	11 February 1965	17 March 1967
30	Hungary	Notification No. GSR 197(E), dated 31-3-2005	03 November 2003	04 March 2005
31	Iceland	Notification No. S.O. 241(E), dated 5-2-2008	23 November 2007	21 December 2007
32	Indonesia	Notification No. GSR 77(E), dated 4-2-1988	07 August 1987	19 December 1987
33	Ireland	Notification No. 45/2002 [F. No. 503/6/99-FTD], dated 20-2-2002	06 November 2000	26 December 2001
34	Israel	Notification No. GSR 256(E), dated 26-6-1996	29 January 1996	15 May 1996
35	Italy	Notification No. GSR 189(E), dated 25-4-1996. Earlier agreement was entered into vide GSR 608(E), dated 8-4-1986	19 February 1993	23 November 1995
36	Japan	Notification No. GSR 101(E), dated 1-3-1990, as amended by Notification Nos. SO 753(E), dated 16-8-2000 (w.r.e.f. 1-10-1999), SO 1136(E), dated 19-7-2006, w.r.e.f. 28-6-2006 and SO 2528(E), dated 8-10-2008, w.e.f. 1-10-2008	07 March 1989	29 December 1989
37	Jordan	Notification No. GSR 810(E), dated 8-12-1999	20 April 1999	16 October 1999
38	Kazakhstan	Notification No. GSR 633(E), dated 31-10-1997	09 December 1996	02 October 1997
39	Kenya	Notification No. GSR 665(E), dated 20-8-1985	12 April 1985	20 August 1985
40	Korea, (Republic of)	Notification No. GSR 111(E), dated 26-9-1986, as amended by GSR 986(E), dated 20-12-1990	19 July 1985	31 August 1986
41	Kuwait	Notification No. SO 2000(E), dated 27-11-2007	15 June 2006	17 October 2007
42	Kyrgyz Republic	Notification No. GSR 75(E), dated 7-2-2001	13 April 1999	10 January 2001
43	Latvia	NOTIFICATION NO.12/2014 [F.NO.503/02/1997-FTD-I], dated 5-3-2014	18 September 2013	01 April 2014
44	Libya	Notification No. GSR 22(E), dated 1-7-1982	02 March 1981	01 July 1982
45	Lithuania	Notification No. 28/2012 [F. No. 503/02/1997-FTD-1], dated 25-7-2012	26 July 2011	10 July 2012
46	Luxembourg	Notification No. 78/2009 [F. No. 503/1/96-FTD-I], dated 12-10-2009	02 June 2008	09 July 2009
47	Macedonia		17 December 2013	12 September 2014
48	Malaysia	Notification No. 07/2013 [F. No. 506/123/84-FTD-II], dated 29-1-2013	29 Jauary 2013	01 April 2013

Sr No	Country	Notification No. and Date	Date when signed	Date of coming into force
49	Malta	Notification No. 34/2014 [F. No. 504/06/2003-FTD-I], dated 5-8-2014	05 August 2014	01 April 2015
50	Mauritius	Notification GSR No. 920(E), dated 6-12-1983	24 August 1982	06 December 1983
51	Mexico	Notification No. 86/2010 [F. NO. 503/4/91-FTD-I], dated 26-11-2010	10 September 2007	01 February 2010
52	Mongolia	Notification No. SO 635(E), dated 16-9-1996	22 February 1994	29 March 1996
53	Montenegro	Notification No. 4/2009 [F.NO. 503/1/1997-FTD-I]/S.O. 96(E), dated 7-1-2009	08 February 2006	23 September 2008
54	Morocco	Notification No. GSR 245(E), dated 15-3-2000	30 October 1998	20 February 2000
55	Mozambique	Notification No. 30/2011-FT&TR-II [F.NO.501/152/2000-FT&TR-II], dated 31-5-2011	30 September 2010	28 February 2011
56	Myanmar	Notification No. 49/2009-FT & TR-II [F. NO. 504/10/2004-FT & TR-II], dated 18-6-2009	02 April 2008	30 January 2009
57	Namibia	Notification No. GSR 196(E), dated 8-3-1999	15 February 1997	22 January 1999
58	Nepal	Notification No. 20/2012 [F.NO.503/03/2005-FTD-II], dated 12-6-2012	27 November 2011	16 March 2012
59	Netherlands	Notification No. GSR 382(E), dated 27-3-1989 as amended by Notification No. SO 693(E), dated 30-8-1999 and Notification No. 2/2013, dated 14-1-2013	30 July 1988	21 January 1989
60	New Zealand	Notification No. GSR 314(E), dated 27-3-1987, as amended by GSR 477(E), dated 21-4-1988 and GSR 37(E), dated 12-1-2000	17 October 1986	23 December 1986
61	Norway	Notification No. 24/2012 [F.NO. 505/3A/81-FTD-I], dated 19-6-2012	02 February 2011	20 December 2011
62	Oman	Notification No. SO 563(E), dated 23-9-1997	02 April 1997	03 June 1997
63	Philippines	Notification No. GSR 173(E), dated 2-4-1996 and as amended by Notification No. SO 125(E), dated 2-2-2005	12 February 1990	21 March 1994
64	Poland	Notification No. GSR 72(E), dated 12-2-1990	21 June 1989	26 October 1989
65	Portuguese Republic	Notification No. GSR 542(E), dated 16-6-2000, as corrected by Notification No. SO 673(E), dated 25-8-2000 and GSR 597(E), dated 20-9-2005	11 September 1998	30 April 2000
66	Qatar	Notification No. GSR 96(E), dated 8-2-2000	07 April 1999	15 January 2000
67	Romania	Notification No. GSR 80(E), dated 8-2-1988	08 March 2013	16 December 2013
68	Russian Federation	Notification No. 10677 [F. No. 501/6/92-FTD], dated 21-8-1998. Earlier agreement was entered into vide GSR 812(E), dated 4-9-1989, as amended by GSR 952(E), dated 30-12-1992.	25 March 1997	11 April 1998
69	Saudi Arabia	Notification No. 287/2006-FTD [F.No. 501/7/91-FTD], dated 17-10-2006	25 January 2006	01 November 2006
70	Serbia and Montenegro	Notification No. 5/2009 [F.No. 503/1/797-FTD-1]/S.O. 97(E), dated 7-1-2009	08 February 2006	23 September 2008
71	Singapore	Notification No. GSR 610(E), dated 8-8-1994 as amended by Notification SO 1022(E), dated 18-7-2005	24 January 1994	27 May 1994
72	Slovenia	Notification No. GSR 344(E), dated 31-5-2005	13 January 2003	17 February 2005

Sr No	Country	Notification No. and Date	Date when signed	Date of coming into force
73	South Africa	Notification No. GSR 198(E), dated 21-4-1998	04 December 1996	28 November 1997
74	Spain	Notification No. GSR 356(E), dated 21-4-1995	08 February 1993	12 January 1995
75	Sri Lanka	Notification No. 23/2014 [F.NO.503/8/2005-FTD-II]/SO 956(E), dated 28-3-2014	22 January 2014	01 April 2014
76	Sudan	Notification No. GSR 723(E), dated 1-11-2004	22 October 2003	15 April 2004
77	Sweden	Notification No. GSR 705(E), dated 17-12-1997. Earlier agreement was entered into vide GSR 38(E), dated 27-3-1989.	24 June 1997	25 December 1997
78	Switzerland	Notification No. GSR 357(E), dated 21-4-1995, as amended by Notification No. GSR 74(E), dated 7-2-2001, 62/2011, dated 27-12-2011 w.e.f. 1-4-2012	02 November 1994	29 December 1994
79	Syria	Notification No. 33/2009-FTD-II [F.NO. 503/7/2005-FTD-II], dated 30-3-2009	06 Februray 1984	25 June 1985
80	Tajikistan	Notification No. 58/2009 [FT & TR-II [F.No. 503/10/95-FT & TR-II], dated 16-7-2009	20 November 2008	10 April 2009
81	Tanzania	Notification No. 8/2012 [FT & TR-II/F. No. 503/02/2005-FTD-II], dated 16-2-2012	27 May 2011	12 December 2011
82	Thailand	Notification No.88/2015 [F.No.503/5/2005-FTD-II], dated 1-12-2015	29 June 2015	13 October 2015
83	Trinidad & Tobago	Notification No. GSR 720(E), dated 26-10-1999	08 February 1999	13 October 1999
84	Turkey	Notification No. SO 74(E), dated 3-2-1997	31 January 1995	01 February 1997
85	Turkmenistan	Notification No. GSR 567(E), dated 25-9-1997	25 February 1997	07 July 1997
86	Uganda	Notification No. GSR 666(E), dated 12-10-2004	30 April 2004	27 August 2004
87	Ukraine	Notification : GSR 24(E), dated 11-1-2002	07 April 1999	31 October 2001
88	United Arab Emirates	Notification No. GSR 710(E) [No. 9409 (F. No. 501/3/89-FTD)], dated 18-11-1993, as amended by Notification No. SO 2001(E), dated 28-11-2007. Earlier agreement was entered into vide GSR 969(E), dated 8-11-1989.	29 April 1992	22 September 1993
89	United Kingdom	Notification No. GSR 91(E), dated 11-2-1994	25 January 1993	26 October 1993
90	United States	Notification No. GSR 990(E), dated 20-12-1990.	12 September 1989	18 December 1990
91	Uruguay	NOTIFICATION NO. 53/2013 [F.NO.500/138/2002-FTD-II]/SO 2081(E), dated 5-7-2013	08 September 2011	01 April 2014
92	Uzbekistan	SO No. 2689(E), dated 7-11-2012	29 July 1993	25 January 1994
93	Vietnam	Notification No. GSR 369(E), dated 28-4-1995, as amended by Notification No. 9860 [F.No. 503/7/91-FTD], dated 12-9-1995	07 September 1994	02 February 1995
94	Zambia	Notification: No. GSR 39(E), dated 18-1-1984	05 June 1981	18 January 1984

Glossary

AAR	Authority for Advance Ruling
AD	Authorised Dealer
ADR	American Depository Receipts
AE	Associated enterprise
AIC	All-in-cost
ALP	Arm's length price
AMP	Average Maturity period
AOP	Association of persons
AY	Assessment year
APA	Advance pricing agreement
BO	Branch office
BT	Business trust
BPO	Business process outsourcing
CBDT	Central Board of Direct Taxes
CBED	Central Board of Excise and Customs
CCDs	Compulsorily convertible debentures
CENVAT	Central value added tax
CESTAT	Customs, Excise and Service Tax Appellate Tribunal
CIB	Central information branch
CIC	Core investment companies
CIT	Commissioner of Income-tax
CIT(A)	Commissioner of Income-tax (Appeals)
CCIT	Chief Commissioner of Income-tax
CSS	Cabinet Committee on Security
CUP	Comparable uncontrolled price
DDT	Dividend distribution tax
DIPP	Department of Industrial Policy and Promotion
DoDP	Department of Defence Production
DRP	Dispute resolution panel
DTA	Domestic tariff area
ECB	External commercial borrowings
EDLI	Employees' Deposit Linked Insurance Scheme, 1976
EOU	Export oriented unit
EPC	Engineering Procurement Construction
EPF	Employees' Provident Fund
EPS	Employees' Pension Scheme
ESOP	Employees stock option plan
FAR	Functions assets and risks
FDI	Foreign direct investment
FEMA	Foreign Exchange Management Act, 1999
FII	Foreign institutional investor
FIPB	Foreign Investment Promotion Board
FIRC	Foreign inward remittance certificate
FMV	Fair market value
FPI	Foreign Portfolio Investors
FTS	Fees for technical services
FTWZ	Free trade and warehousing zone
FVCI	Foreign Venture Capital Investor
FY	Financial year
GDR	Global Depository Receipts
GSM	Global System for Mobile Communications
HC	High court
HO	Head office
IL	Industrial license
IPR	Intellectual property right
IT	Income-tax
IT	Information technology
ITES	Information technology enabled services
IRDA	Insurance Regulatory and Development Authority
InvIT	Infrastructure Investment Trusts
JV	Joint venture
KPO	Knowledge process outsourcing
KYC	Know your customer
LC	Letter of credit
LIBOR	London Inter Bank Offered Rate
LLP	Limited liability partnership
LO	Liaison office
LRS	Liberalised remittance scheme
LTCG	Long-term capital gains
MCA	Ministry of Corporate Affairs
MTSO	Money transfer service operators
MoD	Ministry of Defence
MoU	Memorandum of understanding
NIC	National Industrial Classification
NRI	Non-resident Indian

NoC	No objection certificate
NPA	Non-performing asset
OECD	Organisati0n for Economic Cooperation and Development
ODI	Outbound investment
PE	Permanent establishment
PF	Provident fund
PLI	Profit level indicator
PO	Project office
PPP	Public-private partnership
PSM	Profit split method
QFI	Qualified Foreign Investor
RBI	The Reserve Bank of India
RD	Regional director
RoE	Return of Equity
RoI	Return of income
REIT	Real estate investment trust
RSU	Restricted stock units
SAD	Special additional duty of customs
SAR	Stock appreciation rights
SB	Special bench of Income-tax Appellate Tribunal
SC	Supreme court
SEBI India	The Securities and Exchange Board of
SEZ	Special economic zone
SHA	Shareholder's agreement
SPV	Special purpose vehicle
STT	Securities transaction tax
The Act	The Income-tax Act, 1961
The Rule	The Income-tax Rules, 1962
The tax treaty	Double taxation avoidance agreement
The Tribunal	The Income-tax Appellate Tribunal
TDS	Tax deducted at source/ withholding tax
TNMM	Transactional net margin method
TO	Tax officer
TP	Transfer pricing
TPO	Transfer pricing officer
TRC	Tax residency certificate
UN	United Nations
ULIP	Unit-link insurance plan
VAT	Value added tax
Vienna Convention Treaties	Vienna Convention on the Law of
WOS	Wholly owned subsidiary

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