# The Chamber's Journal

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**The Chamber of Tax Consultants**

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## GST Part III

## Industry Specific Analysis

**Other Contents**

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- Other Laws
- Best of the Rest
- Indirect Taxes
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# Editorial

The exit of United States of America from the Paris Accord reinforces one point that USA may claim to be world leader in a mono-polar world but it shirks responsibility of a leader. The mess created in the Middle East, as it walked into a sovereign country in search of weapons of mass destruction. This irresponsible act has made the people of that region witness eternal mass destruction. Same thing happened with the allegedly waged war against terrorism post 9/11. By pulling out of Paris Accord, they finally declared, please don't expect any responsible behaviour from us.

This issue of the Chamber's Journal brings out the Special Story dealing with the impact of GST on several industries. Eminent professionals have contributed to this issue. As Richard Hooker English Theologian of 16th century states "change is not made without inconvenience even from worst to better." We have taken the demonetisation in the same spirit. We will brace with the migration to GST also in the same manner. The roll out of GST from 1st July, 2017 is good news but the business and industry is skeptical. There is uncertainty as the tax rate schedule is out, the interpretation notes are awaited. The transitional provisions for traders are still at the draft stage. The fate of area based exemption is not known. Small and medium sizes enterprises have their own doubts. This lack of clarity floods the tax consultants with queries. Tax consultants have tried to familiarise themselves with the new tax regime at the cost of their vacation. The GST has posed challenges to IT professionals also. The last minute changes in the return format/API's posing are making their lives even more difficult.

As per Peer Vilayat Khan, in "Awakening : A Sufi experience" At one end is the dimension of our being i.e. transient and evanescent are continually changing and transforming through a process of evolution. At the other end of this pendulum is that part of consciousness that remains immortal, unchanged. This our whole being could be said to be continuity of change – just as it's never the same water that passes under the bridge while at the same time it's the same river. The laws will keep changing, the uncertainty in tax law's is a certainty.

The Chamber's Journal Committee decided to bring three Special Stories on GST with a view that if a man will begin with certainties, he shall end in doubts – but if he will be content to begin with doubts, he may end in certainties (Francis Beacon).

I thank all the contributors to this issue for sparing their valuable time for the Chamber's Journal.

K. GOPAL
Editor

# From the President

Dear Members,

My journey of communicating with you is coming to an end as this is my last communication as President of this august organisation, "The Chamber of Tax Consultants".

At the end of my term, Chamber will complete 90th year and will enter 91st year. Nine decades have passed and Chamber is becoming younger day by day in terms of its thought process, innovative ways of thinking and geographically spreading its wings across India. The Chamber's activities are continuing with more and more vigour and velocity.

**It is now time for me to share my views and experiences. It is also an occasion for me to revisit the strong roots and high values upon which Chamber was formed.** It was a great privilege for me to be at the helm of affairs of Chamber in its landmark 90th year.

In my first Speech on 4th July, 2016, when I took over the reigns of Chamber as President, I shared **my vision for the year 2016-17** viz. to deliver quality programmes, to make more representations on varied laws and legislations, to bring digital transformation, to introduce qualitative changes in Journal, to bring out more publications, to celebrate 90th year of Chamber by unique knowledge spreading activities to increase visibility and, finally, to bring better Governance and Transparency in administration.

I am happy to share that I was able to achieve almost all the initiatives that I had envisaged at the last AGM. This year Chamber has witnessed:

(i) Taking many new and bold initiatives, like starting International Tax Journal, webinars and other digital transmissions;

(ii) Initiating maiden ventures, like holding first Moot Court Competition, certificate course on Ind-AS, intensive study group on Ind-AS, standalone programme outside Mumbai, participation of various media agencies and so on;

(iii) Organising many mega and unique programmes, in Mumbai, Delhi, Pune, Jamnagar like Public Meeting on Demonetisation, Budget Talk 2017, Seminar on GST;

(iv) Making record number of representations before various authorities, including Parliamentary Standing Committee and

(v) Initiation of process of filing Writ Petition challenging notified ICDS.

**I believe that a leader should always have a vision and a conviction**. Carrying on any activity, without vision, becomes directionless and may not yield desired results. It was the above vision that constantly guided me to move forward and remain focused throughout my tenure.

## SOCIAL RESPONSIBILITY

**Chamber is always conscious of its responsibilities towards the society.** This year Chamber has undertaken various social activities within the domain of its object of providing education. The Chamber has donated funds for pursuing educational object in the State of Jammu & Kashmir and Uttarakhand and has reconstructed classrooms for a School at Uttarakhand. **Pursuing this lone object itself has given me immense inner satisfaction.**

## 90TH YEAR CELEBRATIONS

90th Year celebration was inaugurated by holding a first lecture meeting, which was addressed by Hon'ble Shri Justice R. V. Easwar, former Judge of Delhi High Court and former President of ITAT and Shri Dinesh Vyas, Senior Advocate.

**The year was buzzed with various activities throughout the year** which included, among other, coming out with various publications, special issue of Journal as well as International Taxation magazine. The Annual Report of Chamber for year 2016-17 gives, in detail, highlights of various activities of Chamber for the year.

**Chamber could undertake such all round activities because it has a vibrant and dedicated team.** Chairmen, Co- Chairmen, Advisors, Council Members, Past Presidents and every single core – committee member of Chamber were of great support to me, without which it would not have been possible to undertake so many activities. **The zeal and enthusiasm of Team Chamber is unstoppable as can be seen from the activities of the Chamber for the month of June 2017.** Its support have been the greatest asset for me as well as Chamber. I believe, it is for a President to know how to make use of such invaluable and intangible assets. In my view there is nothing like Non Performing Committee. **We all should realise one thing that organisation like us runs on a human value based system, where emotions and sentiments of people are attached to it.**

I have mentioned about some of the accomplishments. **At the same time, I also would like to touch upon future challenges,** as we all know changes are taking place in every sphere and taxation and allied laws are not an exception to this. **As we have witnessed this year, the velocity with which changes are happening is very fast, if we do not change ourselves with the time then we will be left behind.** *It is our ability to adapt to changes and proactively make changes in our learning process that will make a crucial difference in our professional life.*

Innovations are entering into human activities and one cannot function without technology. **We are entering into an era of digital brains.** We all know google has set up Deep Mind Lab for the **Artificial Intelligence (AI)** research community. Soon we will be moving

to such a time where it will be difficult to imagine an era without computers, e-mail or mobile phones. Experts in Adult education estimate what we learn will be obsolete a decade from now. *To say that we live in a changing world understates the pace and the scope of ongoing changes.*

**To succeed today we must be in a constant state of adaptation – continuously unlearning old and relearning new ones i.e., learn, unlearn and relearn**

That requires continuous upgrading our knowledge, challenging old paradigms and 'relearning' what is now relevant is in the present scenario.

**Hence, it is need of an hour to constantly improve ourselves and change with changing time and avoid using the same old rigid pattern of functioning.** Chamber also need to think differently and use innovative features for dissemination of knowledge. **Innovations and creativity should be new mantra to be followed.** It needs to create more branches to further spread its arms geographically. More amount needs to be spent on technology, for example, to have high technical studio which can connect to various members across India at the same time and can have two way transmission process. **Chamber needs to be a trend setter and innovative.**

**Young minds are always bubbling with new ideas** and Chamber needs to generate and tape new ideas. It needs to develop young generation within its ambit with the vision of seniors and develop them as good leader.

**I have a feeling of accomplishment for putting best of my efforts but at the same time there is still a lot to be done.**

I would like to make a special mention of dedicated staff members of Chamber who have always supported Chamber in all its endeavours. Manager Hitesh, Accountant Manisha,Vaishali, Tarlika, Monica, Anand, Suresh, Rajan all have worked hard to the best of their abilities. My Best Wishes to all of them.

With the sense of great gratitude, one last time through this communication, **I salute the spirit of each one of you and wish you and Chamber great years of education ahead.** The time has now come for me to make transition from present to history with a promise that I shall always be available for any services which Chamber may require.

Good Bye

**HITESH R. SHAH**
*President*

# Chairman's Communication

Dear Readers,

The Reserve Bank of India in its recent Monetary Policy has kept the interest rate unchanged. Though decision of the RBI in not reducing the interest rate is hailed by the Captains of the Industry, it has not gone well with the top Economists and the Finance Ministry. But RBI Governor has asserted Central Bank's independence and has taken policy decisions which is more suited in the current economic scenario. Problem of NPA continues to haunt the Indian Banking Industry. Recent inspection of two of the private banks by the RBI has found huge divergence in the NPA figures disclosed by these banks and those ascertained by the RBI. The problem of NPA has become so grave that RBI has formally invoked PCA (Prompt Corrective Action) on three banks. The Banking Industry is thus passing through one of its worst phases and something drastic and immediate will have to be done by the Government to bring it back on track.

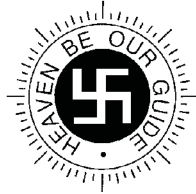
Count down for implementation of GST from July 1, 2017 has started. Though many still feel that Government is not fully geared up for implementation of GST, the Government appears to be determined in implementing GST from July 1, 2017. However experts still feel that there are some areas where there would be lot of challenges and therefore even if GST is implemented from July 1, 2017, initial few months are going to be challenging for business community as well as for professionals.

The Committee had decided to come out with the Special Issue on GST in three parts. But considering the fact that lot of changes in law were being made by the Government even before its implementation, we thought that the issues should be brought when there is reasonable clarity on the law. The rates of GST having been notified, the impact of GST on various industries is now almost clear. Therefore, Part III of the GST series is on Industry specific analysis and there could not have been better month than June for this issue.

My colleagues in the Committee CA Mandar Telang, CA Kush Vora and CA Janak Vaghani have put in lot of efforts in designing this issue as well as for overall co-ordination . But for their efforts, this issue as well as the previous two issues would not have been possible. Sincere appreciation for their efforts.

I thank and compliment all the authors for agreeing to write articles and sparing their valuable time and sharing their knowledge on such an important subject despite their very busy schedule.

**VIPUL K. CHOKSI**
*Chairman* – Journal Committee




## The Chamber of Tax Consultants

# Vision Statement

The Chamber of Tax Consultants (The Chamber) shall be a powerhouse of knowledge in the field of fiscal laws in the global economy.

The Chamber shall contribute to the development of law and the profession through research, analysis and dissemination of knowledge.

The Chamber shall be a voice which is heard and recognised by all Government and Regulatory agencies through effective representations.

The Chamber shall be pre-eminent in laying down and upholding, among the professionals, the tradition of excellence in service, principled conduct and social responsibility.

Niraj Bagri, Partner, Dhruva Advisors, LLP
Pankit Shah, Principal, Dhruva Advisors, LLP

# Impact Study on Manufacturing Sector and Traders (SMEs) including Job Work

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

Goods and Services tax ('GST') is the biggest tax reform the country has witnessed since independence.

The GST framework will subsume majority of indirect taxes levied by Central and State Governments like Central Excise Duty, Service Tax, State Value Added Tax, Central Sales Tax, Entry Tax, Purchase Tax, Entertainment Tax, Luxury Tax etc.

GST will have a business-wide impact on the entire chain of operations like procurement, manufacturing, sales and pricing, finance, information technology, supply chain, warehousing etc.

## Concept of "supply" and levy of tax under GST

The term "supply" has been defined to include all forms of supply such as sale, transfer, barter, exchange, licence, rental, lease or disposal made for a consideration by a person in the course of business and includes other identified transactions.

*(Refer Section 9 and Section 7 of Central Goods and Services Tax Act, 2017 and respective State Goods and Services Tax Act, 2017).*

All intra-State supplies of goods or services or both except supply of alcoholic liquor for human consumption, petroleum products and natural gas will attract GST.

## Traders and manufacturers get a level playing field under GST

– Currently, purchase of goods attracts excise duty and VAT/CST. Traders are not entitled to claim credit of excise duty on subsequent sale resulting in cascading of taxes and increased tax cost. GST would eliminate such cascading effect of taxes and would provide seamless credit across value chain.

– Also, 'trading' is regarded as an "exempted service" and hence traders are not entitled to claim credit of Excise and Service tax paid on procurement of goods and services. However, with multiple indirect tax subsuming into GST, traders would be eligible to claim full credit (including capital goods) as currently available to a manufacturer, subject to prescribed conditions.

– With the concept of manufacturing been done away under GST regime, traders would now be at par with manufacturers.

## Guiding principles for determining inter-state and intra-state supply

The determination of nature of supply as an inter-state and intra-state supply is based on the location of supplier and place of supply. Below table explains the criteria and its taxability:

| Particulars | Location of supplier & Place of supply | **Taxability** |
|---|---|---|
| | | |
| Same State / Union Territory (UT) | Yes | **CGST/ SGST** |
| | No | **IGST** |

*(Refer Sections 7, 8, 10 and 12 of IGST Act)*

**Local / Inter-state supply of goods**

Where the supply involves movement of goods (whether by the supplier or recipient or by any other person), the place of supply shall be location where the movement terminates for delivery to the recipient.

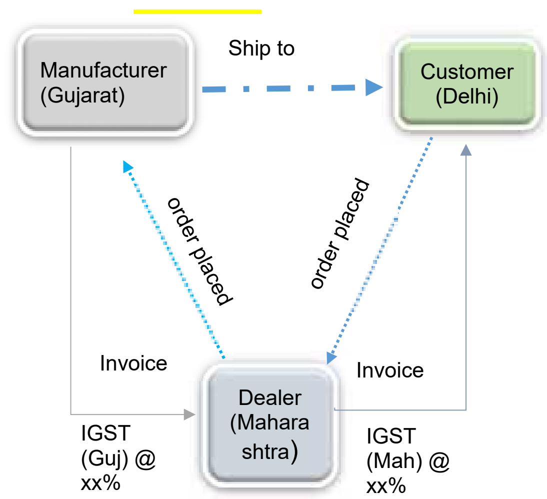
If the location of supplier and place of supply are in the same state, then, such transaction of supply should attract CGST and SGST, else IGST, at applicable rate.

*(Refer Section 10(1)(a) read with Section 7(1) or Section 8(1), as applicable)*

**'Bill to Ship To' transaction**

Transaction Flow

1. Customer places order on Dealer (in Maharashtra) for delivery of goods in Delhi
2. The dealer in-turn places order on Manufacturer in Gujarat for delivery at Delhi
3. Manufacturer delivers the goods to the dealer in Delhi




*Transaction between supplier (manufacturer) and third party (dealer)*

Where the goods are delivered by the supplier to a recipient or any other person on the direction of a third person, before or during the movement of goods (either by way of transfer of documents of title to goods or otherwise), it shall be deemed that the said third person has received the goods and the place of supply of such goods shall be the principal place of business of such person.

The principal place of business of the dealer being in Maharashtra and the location of supplier in Gujarat, the said transaction should be an inter-state supply. Accordingly, IGST should be charged by the supplier.

*Transaction between third party and recipient*

The place of supply should be the location of the goods where the movement terminates for delivery to the recipient (i.e. customer in Delhi).

Since the dealer is located in Maharashtra and place of supply is in Delhi, the transaction should be regarded as inter-state supply liable to IGST.

*(Refer Section 10(1)(b) and 10(1)(a) read with Section 7(1)(a) of IGST Act)*

At this juncture, it is also important to understand the concept of composite supply and mixed supply.

**What is a Composite supply?**
Composite supply means a supply of two or more taxable supplies of goods or services or both or any combination thereof, which are naturally bundled and supplied in conjunction with each other in the ordinary course of business, one of which is a principal supply.

The term 'principal supply' has been defined to mean the supply of goods or services which constitutes the **predominant element** of a composite supply and to which any other supply forming part of that supply is ancillary.

*Illustration* – Where goods are packed and transported with insurance, the supply of goods, packing materials, transport and insurance is a composite supply and supply of goods is a principal supply.

The tax liability on a composite supply shall be determined by treating all supplies to be a supply of such principal supply.

**Thus, basis the above, sale of goods on Ex-works or FOR basis would be regarded as a composite supply wherein sale of goods is the principal supply and other supplies (packing material, freight, insurance) are ancillary to it. In such case, GST on other supplies shall apply basis the rate applicable on such goods.**

However, the challenge lies in characterisation of the transaction as composite supply and identifying as to which supply is the 'principal supply' and other as ancillary especially in cases where the transaction involves supply of goods and services like a painting job, repair activity etc. and both can play an equally dominant role. Further, the complexity compounds when the said supply of goods and services are made from different States by the supplier to the client.

*(Refer Sections 2(30) and 2(90) read with Section 8 of CGST Act)*

**What is a mixed supply?**
Mixed supply means two or more individual supplies of goods or services, or any combination thereof, made in conjunction with each other by a taxable person for a single price where such supply does not constitute a composite supply

*Illustration* – A supply of a package consisting of canned foods, sweets, chocolates, cakes, dry fruits, aerated drinks and fruit juices when supplied for a single price is a mixed supply. Each of these items can be supplied separately and is not dependent on any other. It shall not be a mixed supply if these items are supplied separately.

The tax liability on mixed supply shall be determined treating a supply of such particular item which attracts the highest rate of tax.

It may perhaps be prudent to charge separate consideration for different constituents of the supply to avoid everything being charged at the highest rate.

## Taxability of Branch Transfer

Section 7(1)(a) of CGST Act levies tax on forms of supply such sale, transfer etc. when made for a consideration in the course or furtherance of business. Further, as per clause (c) of the said section read with Schedule I and Section 25(5) of CGST Act, supply of goods or services or both between distinct persons when made in the course or furtherance of business shall be **deemed to be supply** even

1 *Business vertical means a distinguishable component of an enterprise that is engaged in the supply of individual goods or services or a group of related goods or services which is subject to risks and returns that are different from those of the other business verticals.*

if made without consideration. The provisions identify establishment of the same legal entity when located in different States as distinct persons i.e. transactions between head office and branch or between two branch offices. Thus, all inter-state branch transfers would attract IGST at applicable rate. Further, the provisions allow an entity to obtain separate registration within the state / UT for each business vertical[1], subject to such conditions as may be prescribed. Further, SEZ unit of an entity is also required to obtain separate registration and DTA and SEZ unit of the same entity would be regarded as distinct persons. Thus, if entity holds separate registration within the same State / UT, then, transactions within the State/UT between different registrations shall also be liable to CGST & SGST/UTGST, as applicable.

The payment of taxes at various stages will lead to higher working capital requirement.

The valuation of such transaction shall be as per Rule 2 of Determination of Value of Supply as under:

(a) the 'open market value' (OMV) of such supply. The term 'open market value' *of a supply of goods or services or both means the full value in money, excluding the Integrated Tax, Central Tax, State Tax, Union Territory Tax and the cess payable by a person in a transaction, where the supplier and the recipient of the supply are not related and price is the sole consideration, to obtain such supply at the same time when the supply being valued is made*

(b) if OMV is not available, then, the value of supply of goods or services of like kind and quality;

(c) if value is not determinable under clause (a) or (b), then, the value shall be –

  (i) 110 per cent of cost of production or manufacture or cost of acquisition of such goods (under Rule 4) or

  (ii) Residuary method using reasonable means consistent with the principles and general provisions of Section 15 and these rules.

However, if the goods are meant for **further supply,** then, the value shall be at the *option* of the supplier be 90 percent of the price charged for like kind and quality by the recipient to his customer (not being a related party).

Further, it also provided that where the recipient is eligible for full input tax credit, then, the value declared shall be **deemed to be the OMV** of such goods.

Hence, it is important that businesses undertake a detailed supply chain study and reassess the requirement of warehouses, inventory holding period and its impact on working capital requirement of the company.

## Treatment of goods return

In case of goods return, the supplier of goods is required to issue credit note containing necessary details to the recipient.

This credit note should be disclosed in the monthly return but not later than September following the said financial year of supply or date of furnishing the annual return, *whichever is earlier.* For example, credit note for supplies made during FY 17-18, should be issued not later than September 2018 and before filing of annual return for FY. 2017-18.

It is also relevant to note that the framework of the proposed legislation empowers and requires the seller to initiate all transactions and accordingly the credit note issued by the seller would be considered and disclosed in the GST return and issuing debit note/credit note by purchaser will not be recognized in the GST return.

## Valuation – Inclusions and exclusions

Section 15 of CGST Act deals with value of goods or services.

As per the said section, the value of goods shall be the **transaction value** which is the price actually paid or payable for the said supply when supplier and recipient are **not related** and **price is the sole consideration.**

*Plus*

- Any taxes, duties, cesses, fees and charges leviable under any law other than CGST, SGST, UTGST and GST Compensation cess, if charged separately by the supplier
- Any amount payable by supplier but incurred by the recipient and **not included** in the price;
- **Incidental expenses**, including commission and packing, charged by the supplier and any amount charged for anything done by the supplier in respect of the said supply **at the time of, or before delivery** of goods thereof
- Interest or late fee or penalty for delayed payment of any consideration for any supply. Thus, whether GST shall apply on interest component when the supply itself is exempted / non-taxable? ***Under the current provisions, of Central Excise, Service tax, VAT / CST, no tax is payable on interest recovered for delayed payment of consideration.***
- Subsidies directly linked to the price excluding subsidies provided by Central and state governments.

*Less*

- Discounts given before / at the time of the supply;
- Discounts given after the supply, if it is established by the agreement entered before the supply, linked to relevant invoices and provided input tax credit has been reversed by the recipient

## Free samples

The transaction of issuing free samples shall not be regarded as a supply. As per Section 7(1) of CSGT Act, supply includes a transaction made for a consideration by a person in the course or furtherance of business. Since the samples are issued without any consideration (on free basis), the transaction does not qualify as supply.

However, as per Section 17(5)(h) of CGST Act, input tax credit shall not be available on goods disposed of by way of free samples.

The rationale for disallowing the credit attributed to such free samples is not clear. Even though samples are given for free its cost is already a part of cost of goods sold. Hence, there should not be any reason why the credit attributable to supply of free samples should be denied.

## Imports and Exports

*Import of goods*

Section 2(10) of IGST Act defines the term "import of goods" with its grammatical variations and cognate expressions, meaning bringing into India from a place outside India.

As per proviso to Section 5(1) of IGST Act, there shall be levied an IGST on goods imported into India in accordance with the provisions of Section 3 of Customs Tariff Act, 1975 (CTA) on the value as determined at the time of import under Section 12 of the Customs Act, 1962. Further, as per Section 11 of IGST, the place of supply of imported goods shall be the location of the importer.

Thus, going forward, an importer shall be liable to pay Basic Customs duty (BCD), IGST,

Customs Cess and GST Compensation Cess (if applicable) on import of goods into India.

At this juncture, it is important to refer to Sections 3(7) and (8) of CTA which prescribes for levy of IGST. The relevant extract of the said provision reads as under:

*(8) For the purposes of calculating the integrated tax under sub-section (7) on any imported article where such tax is leviable at any percentage of its value, the value of the imported article shall, notwithstanding anything contained in Section 14 of the Customs Act, 1962, be the aggregate of –*

*(a) …..*

*(b) Any duty of customs chargeable on that article under Section 12 of the Customs Act, 1962, and* ***any sum chargeable on that article under any law for the time being in force as an addition to, and in the same manner as, a duty of customs,*** *but does not include the tax referred to in sub-section (7) or the cess referred to in sub-section (9).*

On a closer reading of Section 3(8) of The Taxation Laws (Amendment) Act, 2017, it appears that the said provision provides for levy of IGST on –

– Value of goods

– BCD and

– Any sum chargeable on that article under any law for the time being in force as an addition to and in the same manner as a duty of Customs

– But does not include IGST and GST Compensation Cess.

The said provision does not provide for exclusion of Customs Cess but specifically provides for inclusion of any sum chargeable on the imported goods under any law for the time being in force.

Hence, there seems to be a circular reference getting created in calculating IGST and Customs Cess (since it would be computed on BCD and IGST) unless specifically exempted/clarified by the Government.

Whilst the literal interpretation suggests that there is an anomaly, it is also relevant to mention that similar provision also exists under the current law. However, the Government has clarified the manner of computation of duty by way of illustration at the time of introduction of Customs Cess (i.e. Education Cess) *vide* D.O.F. No. 334/3/2004 - TRU dated 8th July, 2004 wherein CVD does not include education cess and hence no dispute has arisen on this issue till date.

It is also important to note that the concept of Sale in the course of import (SICOI) as existed under Section 5(2) of CST law has now been done away under GST regime.

*Export of goods*

*Direct exports*

Section 2(5) of IGST Act defines the term "export of goods" with its grammatical variations and cognate expressions, means taking goods out of India to a place outside India.

As per Section 7(5) of IGST Act, supply of goods shall be treated as in the course of inter-state trade or commerce when the supplier is located in India and the place of supply is outside India. Further, as per Section 11(b) of IGST Act, the place of supply of goods exported from India shall be the location outside India.

Exports are regarded as zero-rated supplies under Section 16 of IGST Act and the registered person making such supplies shall have the option of exporting either –

– On payment of IGST and claiming refund **or**

– Supplying under bond / Letter of Undertaking subject to fulfilment of conditions and procedures as may be prescribed.

*Penultimate exports*

It is important to note that there is no concept of penultimate export under GST as it existed under the CST law. Accordingly, the sales made to an exporter should either be an inter-state or intra-state supply, as the case may be.

*Deemed exports*

As per Section 147 of CGST Act, the Government may notify certain supplies of goods as deemed exports –

– Where the supplies do not leave India;

– Payment for such supplies is received in INR or convertible foreign exchange; and

– Such goods are manufactured in India

## Taxability of High Seas Sales

Section 5(2) of the CST Act granted exemption on sale or purchase of goods in the course of import into the territory of India only if the sale or purchase either occasions such import or is effected by a transfer of documents of title to the goods before they cross the customs frontiers of India. Such transactions are regarded as deemed import transactions.

Whereas under the proposed legislation, Section 7(2) of CGST Act states that supply of goods imported into the territory of India till they cross the customs frontiers of India, shall be treated to be a supply of goods in the course of inter-state trade or commerce. Thus, the exemption erstwhile available on high seas sale has been done away and it appears that such transactions could now be subjected to IGST. Separately, such transactions could also be liable to Customs duty in terms of proviso to Section 5(1) of IGST Act. In such case it needs to be examined whether it would result in the same transaction getting taxed twice as high seas sale and import?

The term "India" has in turned been defined under Section 2(56) of CGST Act. India means *the territory of India as referred to in Article 1 of the Constitution, its territorial waters, seabed and sub-soil underlying such waters, continental shelf, exclusive economic zone or any other maritime zone as referred to in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976, and the air space above its territory and territorial waters.*

Basis the above, the jurisdiction of India is up to 200 nautical miles from the baseline. Hence, it could be argued that any sales executed beyond 200 nautical miles may be outside the purview of GST.

Before concluding, in order to substantiate the transaction as high seas sales, it would also be imperative for businesses to now demonstrate as to where had the sale transaction taken place whether within or beyond 200 nautical miles.

Hence, on an overall basis, businesses would certainly have to re-look at their procurement pattern and examine whether high seas sale is still a viable option!!

## Transaction with SEZ developer / units

**Supplies to SEZ**

As per Section 7(5) of IGST Act, supply of goods or services or both to / by a SEZ developer / unit shall be treated as a transaction in the course of inter-state trade or commerce and accordingly liable to IGST. The provision creates a deeming fiction and irrespective of place of supply and location of supplier whether intra-state or inter-state, such supplies are liable to IGST. Further, as per Section 16 of IGST, such sales are regarded as zero-rated supplies and the supplier may supply such goods either by paying IGST and claiming refund or supply under bond / Letter of Undertaking without payment of IGST, subject to fulfillment of other conditions / procedures as may be prescribed.

**Supplies by SEZ units to DTA**

As noted above, as per Section 7(5) of IGST Act, supply of goods or services or both by a SEZ developer / unit shall be treated as a transaction in the course of inter-state trade or commerce and accordingly liable to IGST. Also, such transaction should also be treated as "import" in the hands of buyer attracting customs duty. The buyer of the goods (or SEZ unit on the basis of authorization from buyer) would file the Bill of Entry for home consumption and pay customs duty as per value arrived in terms with the provisions of Customs Act (refer Section 30 of SEZ Act read Rule 48 of SEZ Rules). Thus, in the absence of any specific exemption, IGST could be levied twice on such supplies firstly, by the SEZ supplier as per IGST Act and secondly paid by the importer as a part of Customs duty. Similar situation also exists under the current law. To obviate double taxation, SAD is exempted if VAT / CST is chargeable on supply of goods by SEZ to DTA (refer Notification no. 45/2005 – Cus dated 16 May 2005)

**Supplies by SEZ unit to another SEZ unit**

As already noted above, as per Section 7(5) of IGST, supplies by one SEZ unit to another SEZ unit (whether in the same state or otherwise), shall be deemed to be an inter-state transaction liable to IGST, at applicable rate. The said supply should be treated as zero rated supplies and accordingly, the SEZ unit may choose to supply such goods either by charging IGST and claiming refund or supply under bond / Letter of Undertaking without payment of IGST, subject to fulfillment of other conditions / procedures as may be prescribed

## Supplies from North-East and Hill States

Currently, procurements are undertaken by various pharmaceuticals and FMCG companies from North-East and Hill states as the said units are covered under area based exemption under Central Excise and also attracts a concessional VAT / CST rate on sale of manufactured products.

Going forward, the supplies from such states should also attract CGST&SGST or IGST, as applicable, on sale of manufactured products. While the GST charged by such manufacturers should be available as credit to the buyers, the same could increase their overall purchase price especially where sale price to end customer is regulated by the authorities.

Whether the central and state governments would give refund, the extent of refund etc is still under discussion.

While the specifics are being debated, businesses may choose to initiate the dialogue with their vendors for re-negotiating the prices if taxes are refunded. Further, the said manufacturers would also now be eligible to claim input tax credit of tax paid on purchase of goods and services. Thus, this would further lower the cascading effect of tax in the current cost structure.

## Anti-profiteering provisions – a new weapon in the arsenal to tackle inflation

Section 171 of CGST Act, 2017 is relevant in this regard. In terms of the said provisions -

– Any reduction in rate of tax on any supply of goods or services;

– Benefit of input tax credit

shall be **passed on** to the recipient by way of **commensurate** reduction in price of goods and services.

The Central Government may on recommendation of GST Council constitute an Authority to examine the aforesaid and whether it has resulted in commensurate reduction of prices of goods or services. There have been considerable apprehensions as to whether these measures would result in increased scrutiny by the department. The Government has been assuaging the concerns by stating that these

provisions are created as anti-inflationary measure. Further, the functions of the Authority may be handled by an independent agency like Competition Commission of India or the members of the committee could be appointed from the trade and industry so that this does not result into an Inspector Raj again.

Internationally experience suggests that introduction of GST has resulted into inflation and therefore the government is more cautious on this front. The intent of the said provision is to act as a watchdog in ensuring that no businesses should generate profit out of reduction in tax rate or increased credit.

Thus, it is important that businesses undertake detailed financial impact analysis covering current tax structure, procurement pattern and supply chain so as to identify additional tax credit and rate reduction, if any, and accordingly determine their pricing policy in order to be compliant with the provisions of anti-profiteering. It is a subjective matter and hence detailing is required. Also, there could be situation where credits have increased but at the same time overall working capital requirement has also increased due to applicability of GST on stock transfers resulting in increase in the overall cost structure and sale price of the product.

While the intent is noble, it is also critical that Government provides clear guidance on operations of these provisions so that the provision can be complied with in letter and spirit.

## Key Transitionary provisions

1. ***Carry forward of closing credits (Section 140(1) of CGST Act)***
   - Filing of returns for past months with appropriate disclosure of closing CENVAT credit / input tax credit;
   - Application in Form GST TRAN-1 to be submitted on the Common Portal within 60 days of appointed day specifying tax / duty / CENVAT Credit to be carried forward

2. ***Unavailed CENVAT Credit on capital goods which has been carried forward (Section 140(2) of CGST Act)***
   - Entitled to claim the unavailed (i.e., balance 50%) CENVAT Credit on capital goods under the GST regime;
   - Application in Form GST TRAN-1 to be submitted on the Common Portal within 60 days of appointed day;
   - The amount of duty or tax already availed or utilised and yet to be availed or utilised till the appointed day should be specified for every item of capital goods

3. ***Eligibility of ITC on goods used for providing exempt services, manufacture of exempt goods if such supplies become taxable under GST? (Sections 140(3) and (4) of CGST Act)***

   Yes. Credit of eligible duties (including Excise duty, CVD, SAD) and taxes in respect of inputs held as stock on the appointed day shall be available subject to the following conditions:

   - Such inputs are used or intended to be used for making taxable supplies under GST
   - Supplier **passes on** the benefit of such credit by way of reduced prices to the customers;
   - The credit is eligible under the provisions of GST Act;
   - The Company should have document evidencing payment of duty under the existing law;

– The document should not be issued earlier than twelve months preceding the appointed day;

– Further, the Application in Form GST TRAN-1 should be submitted on the Common Portal within 60 days of appointed day mentioning the details of tax or duty and stock held on appointed day

**4. *Would the credit under point 3 above be available in cases where the supplier does not possess the document evidencing payment of duty? (Sections 140 (3) and (4) of CGST Act)***

Yes, credit eligible subject to following conditions:

– Credit shall be allowed @ 40% of the CGST payable;

– Credit shall be allowed only after the payment of CGST as above;

– This scheme shall be available for 6 tax periods from appointed day i.e. goods must be sold within 6 months from appointed day;

– Such goods are not wholly exempt from Excise duty under the existing law;

– Such goods are not NIL rated goods under the existing law;

– Documents for procurement of goods are available;

– Statement in specified format (yet to be notified) should be submitted at the end of each tax period indicating details of supplies of such goods effected during the tax period;

– The stock of such goods should be stored in a manner that they are easily identifiable;

– The credit allowed shall be shown in the electronic credit ledger on the common portal

***There is an expectation that the amount of 40% may undergo a change for goods covered under 28% due to various representations made.***

**5. *Pendency of Declarations forms / certificates (second proviso to Section 140 of respective SGST Bill / Act read with Draft Transitional rules)***

The carry forward of ITC would be restricted to the extent of declaration/ certificates outstanding for more than 3 months as on the effective date (i.e., 1 July 2017). This will result into additional cash outflow and working capital requirement as taxes in the GST regime would need to be paid without using these restricted credits. The amount of these restricted credit would only be available as refund if the same is provided to the department later. This would entail an immediate review of status of pending forms and speedy collection of the same.

**6. *Other transition issues***

*IT framework challenges*

The industry is facing several challenges on IT front as the entire framework requires a complete overhaul in a shorter time frame which is being experienced as an uphill task. The systems are required to be mapped with new configurations on taxability, credits, tax masters, logics etc. so that appropriate reports are drawn for the system and returns can be filed with the assistance of GST Suvidha Provider (GSP). The Company needs to ensure that

current systems are compatible with GSP utility.

*Compliances under GST*

Timely compliances under GST would be of paramount importance. Since the entire eco-system is technology driven it would be critical that corporates fulfill their obligations so that value chain remains intact till the last customer.

*E-way Bills*

The government has introduced draft rules for E-way bills. Every registered person who causes movement of goods in excess of ₹ 50,000/- is required to generate an E-way Bill. The e-way bill generated under CGST/SGST provisions of any state should be valid in other states. The way bills would be required for all inter-state and intra-state movement of goods. There is a possibility that compliance of E-way bills be postponed to a later date.

*Supply chain re-engineering*

The Companies would have to undertake detailed supply chain analysis right from souring to distribution considering purchase pattern, inventory holding period, number of warehouses and assess the extent of re-engineering required from GST perspective

## Closing comments

The Government has done a phenomenal job in bringing the much-awaited law to last mile - a law which has remained for more than a decade in discussion / deliberations.

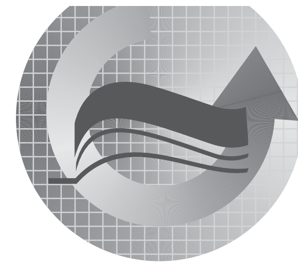
On a macro level, the framework of the proposed legislation provides a level playing field to the India Inc and lives up to the ideology of creating 'One Nation One Tax', eliminating state borders, seamless credit chain, removes cascading effect of taxes, simplification of procedures through technology enabled solutions and last and most important bringing businesses to main stream economy which would boost tax collections and improve GDP.

The recent swiftness showcased by the Government in terms of releasing draft rules, formats of returns, resolution on various contentious issues, fitment of rates for goods and services reinforces the commitment of introducing GST from 1st July 2017 which on a standalone basis is indeed remarkable.

However, GST being a transactional level tax, if looked upon in a little detail, one could find that there still remain quite a few areas which requires immediate attention (including anti-profiteering provisions) and if not addressed at this stage could haunt the industry. The recent clarification from CBEC provides an assurance that the issues flagged by the trade and industry are being examined and would be clarified before the rollout date.

We are hopeful that the industry would be granted adequate time for smooth transition to the GST regime.

> We are what our thoughts have made us; so take care about what you think. Words are secondary. Thoughts live; they travel far.
>
> — *Swami Vivekananda*



CA Sandesh Mundra

# Impact Study on Real Estate including housing societies

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

Real Estate sector in India has been identified as one of the key sectors by the Government. Government has even set ambitious targets under the low cost housing segment and has left no stone unturned to incentivise the developers in multiple ways. At the same time the consumers have been empowered by the implementation of Real Estate Regulation Act, 2016.

GST will no doubt increase the compliance burden of the industry by indirectly tracking all the transactions and bringing them in the public domain. It will be very interesting how the Government plans to demystify the large maze of data that would now be available to them by way of regular online returns being filed by the developers and builders.

India is on the cusp of developing into a country where a lot of things have to be set right. Multiple and complex indirect taxes being one of them. So the paradigm shift from the current mess into a cleaner GST would give way to a better system. At the same time it would see some new issues being born out of this shift.

The below study is an effort on our part to assess the impact of GST on various issues connected with the real estate sector. The following issues have been taken up by us for this impact study:

1. Basic overview of the new tax regime under GST
   - a. The past
   - b. Scheme of taxation under GST
   - c. Valuation
   - d. Time & place of supply
   - e. Exemption
2. Impact on Ongoing projects
3. Anti-profiteering clause
4. Joint Development Projects
5. Redevelopment and Slum Rehabilitation Projects
6. Input Tax Credit
7. Leasing of properties
8. Other collections and charges
9. Maintenance of housing societies

**Unless otherwise stated "Act" means The Central Goods and Services Tax Act, 2017**

## 1. Basic overview of the new tax regime under GST

### a. The Past

Well, it all began with the verdict of **Hon' Karnataka High Court in the matter of K. Raheja Corporation** which treated a developer as a works contractor to tax the transfer of property in goods while constructing the real estate property. **The law laid down by the Hon'ble Supreme Court in K. Rahejas' case (141 STC 298) was a subject matter of challenge before the Hon'ble Supreme Court in the case of *Larsen and Toubro Limited & Another vs. State of Karnataka & Another.*** However the same was upheld in the year 2013 which paved the way for all the states in the country to start recovering indirect taxes in the form of VAT from the builders.

The Hon'ble Supreme Court while delivering the judgment however made a very critical remark that in such cases the position of works contract would only arise from the date the agreement is being entered into with the prospective customer.

As far as service tax is concerned, In the Finance Act, 2010, an Explanation was added w.e.f. 1-7-2010, which meant that any construction of a complex by a builder during or after construction shall be deemed to be service taxable under the Act. This came with an exception that if no sum is received from the prospective buyer before the grant of completion certificate by the authority, then it would not be service taxable under the act.

Thus, by a 'deeming provision', an activity which was not a 'service' as per Court decisions and CBE&C's own earlier circulars became 'deemed service' for the purpose of levy of service tax.

### b. Scheme of taxation under GST law:

Works contract as well as sale of under-construction property have been classified as a 'service' under Schedule II to the Act. This is the most positive sign for the construction and real estate sector as this would take care of major valuation related issues dealing with splitting the total agreement into value towards material and labour.

As far as construction of complex is concerned a significant change that is now visible is that apart from the requirement of completion certificate from the competent authority there is also a reference of "first occupation" as an alternative option. This would suggest that the moment first occupation (though may be illegal) is proved by anyone, any subsequent bookings would not be subjected to GST. However the said term has been left undefined under the act leaving a scope for ambiguity and confusion, hence it may be advisable to issue suitable clarification with regard to the same.

The Government during the discussions at the 14th GST Council Meeting on 19th May, 2017 has released a draft document containing the rates at which services would be taxed under GST. Two relevant entries in the said list are as below :-

| Sr. No. | Description of Services | GST Rate |
|---|---|---|
| 1 | Construction of a complex, building, civil structure or a part thereof, intended for sale to a buyer, wholly or partly. [The value of land is included in the amount charged from the service recipient] | 12% With Full ITC but no refund of overflow of ITC |
| 2 | Composite supply of Works Contract as defined in clause 119 of section 2 of CGST Act | 18% With Full ITC |

One can thus conclude that effectively a 33% abatement has been considered for the purpose of land. The issue that arises is whether the constitutional validity of the rate structure can be challenged just like the several challenges under the current regime (more recently the case of Suresh Kumar Bansal at Delhi High Court). However according to the author the chances of such a situation arising seem to be low mainly on account of two reasons :-

a) Wider definition of service under the constitution so as to include everything other than goods,

b) Land and construction when clubbed together may be treated as a mixed supply with land also be subjected to same rate as the construction of complex.

Besides what is interesting to note is that 12% rate allows full ITC without any refund of overflow. This would suggest that the Government foresees a situation where the developer would be paying Input taxes at 18% and 28% which may lead to excess Input Tax credit balances. Such taxes would only be available for set off against the future projects. Besides it may also lead to a situation where the restructuring takes place whereby all the purchases at 28% are routed through the contractors in order to avoid payment of higher taxes in Inputs. A contractor when subsumes such purchases would only be charging 18% on his gross billing.

### c. Valuation

Also as far as the valuation is concerned it may be relevant to note the provisions of Section 15(2)(a) of the Act which talk about inclusion of any taxes, duties, cesses, fees and charges levied under any other law (other than GST) while discharging the GST liability.

Now the issue is whether stamp duty and registration charges collected from the buyer would also be subjected to GST or not? Looking to the language of the law, such charges are thus bound to be taxed leading to a cascading effect.

Besides, free of cost supplies by the developer to the contractor would not be liable to GST as there is no provision within the valuation framework (both act and rules) to cover such issues.

### d. Time and Place of Supply on Real Estate Sector

Developers would be covered under Continuous Supply of Service, implying that the milestones for payment as decided in the Agreement to sale would become the Time of Supply. Utmost care is thus required that the payments are actually received as per the pre-decided milestones.

This has to be done by defining the events in such a way that the time difference between date when tax liability is due and the date of receipt of payment are reduced to the shortest period.

Place of supply for services in relation to immovable property would be the location of the immovable property. There may be possible issues where a single contract is entered into for provision of services related to immovable properties across two or more States. For example, in case of services from an architect, a single contract may be entered into with the vendor, for which consolidated invoices may be raised at one location. Under GST, since immovable property may be located in more than one State, the place of supply would be each such State where the immovable property is located, and hence, there may be a requirement for the vendor to raise separate invoices (for which separate contracts may also be required).

### e. Exemptions

The Government during the discussions at the 14th GST Council Meeting on 19th May, 2017 has released a draft document containing the list of service tax exemptions which are to be continued under GST. Two relevant entries in the said list are as below :-

| Sr. No. | Description of Services |
|---|---|
| 1 | Services provided by way of pure labour contracts of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration of a civil structure or any other original works pertaining to the Beneficiary-led individual house construction / enhancement under the Housing for All (Urban) Mission/Pradhan Mantri Awas Yojana (PMAY); |
| 2 | Services by way of pure labour contracts of construction, erection, commissioning, or installation of original works pertaining to a single residential unit otherwise than as a part of a residential complex; |

The way these exemptions have been drafted, they would simply be redundant as a developer would never enter into pure labour contracts with a prospective customer.

Hence practically none of the existing exemptions related to low cost housing, slum rehabilitation have been grand fathered under GST.

## 2. Impact on Ongoing Projects – Transitional Issues

Ongoing projects are those where completion certificate is not received. There are several issues which may be faced during the transitional period. Some of these are as below :-

### Availability of Tax credits stipulated *vide* Section 140 for ongoing projects

Government has prescribed a rate of 12% for payment of GST on Real estate projects. This rate would apply not only to projects which are launched after the GST implementation date but also those projects which are ongoing as on the implementation date. This would suggest that whatever input tax credit stream that is available to new projects should also be available to ongoing projects.

The only challenge is that the ongoing projects will carry a legacy of work done prior to GST regime where the various costs incurred have been subjected to old taxes like VAT, Excise, CST, Service Tax, Octroi, Entry Taxes etc. Bare reading of the fine print does not make the life comfortable. Let's look at various transitional provisions incorporated to smoothen the availability of past credits

As per Section 140(1) the Act, existing taxpayers shall be eligible to carry forward credits which are carried forward in the past returns subject to eligibility under the GST regime. Section 140(2) permits carry forward of unavailed capital goods CENVAT credit not carry forwarded in the returns.

Section 140(3) and Section 140(6) are the most critical sections applicable to registered taxable persons availing benefit of service tax abatement in case of construction of complex, building, etc. or paying VAT under the simplified composition schemes under the State VAT Act respectively. These provisions however use the words "credit of eligible duties in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day". The doubt that surfaces in the minds based on this clause is whether the stock of Work-in-Progress of the under-construction property could be termed as a stock of semi-finished goods when construction of complexes have been deemed to be a service under Schedule II of the Act. Well the fact that there is a same GST rate for both new and ongoing projects would suggest that intention of the law is not to block these credits. At this stage it would be noteworthy to refer to the case of *ALA Chemicals vs. CCE (2011)-TIOL-940-CESTAT –MUM – Held in CEA, 1944* that where work-in-progress goods and semi-finished goods are

not defined – common parlance meaning should be used – goods which do not attain finality are called as work-in-progress/semi-finished goods/intermediate goods – Benefit of remission available u/r. 21 of CER, 2002.

However there are certain bottlenecks in the Act which may prevent a free flow of the CENVAT Credits despite doing the bravery of assuming WIP to be the semi-finished goods as referred to above :

a) Possession of documents evidencing the payment of duties.

It is very likely to be the case that goods are procured from a vendor who is not registered under the excise laws and hence proper documents would not be available leading to lapse of the excise credits.

b) Documents should not be earlier than 12 months immediately preceding the appointed day.

The above restriction of 12 months would hit a developer very hard who may have a substantial amount of Work-in-progress where the procurement of raw materials like cement and steel may have taken place prior to 12 months. Thus we are talking of a scenario where the rate of GST would be applicable at 12% with a presumption by the Government that the developer is availing all the credits. However the transitional credits are being blocked by such restrictive clauses thereby leading to inflationary tendencies.

The only way out would be to allow a 5% transitional rate without credits which should go as representation to the Government.

**Taxability of ongoing projects stipulated *vide* Sections 142(10) and 142(11)**

Section 142 of the GST Bill provides for transition provisions for works contract/ periodic supplies as under:

> *'(10). Save as otherwise provided in this Chapter, the goods or services or both supplied on or after the appointed day in pursuance of a contract entered into prior to the appointed day shall be liable to tax under the provisions of this Act.*
>
> *(11)(a). notwithstanding anything contained in section 12, no tax shall be payable on goods under this Act to the extent the tax was leviable on the said goods under the Value Added Tax Act of the State;*
>
> *(b) notwithstanding anything contained in section 13, no tax shall be payable on services under this Act to the extent the tax was leviable on the said services under Chapter V of the Finance Act, 1994;*
>
> *(c) where tax was paid on any supply both under the Value Added Tax Act and under Chapter V of the Finance Act, 1994, tax shall be leviable under this Act and the taxable person shall be entitled to take credit of value added tax or service tax paid under the existing law to the extent of supplies made after the appointed day and such credit shall be calculated in such manner as may be prescribed.'*

The goods and/or services supplied on or after the appointed day in pursuance of a projects entered into prior to the appointed day shall be liable to tax under the provisions of this Act. Hence the unexecuted portion of the project would be subjected to GST after the appointed day and no grandfathering mechanism is being followed here.

Further Section 142(11)(c) above creates a very interesting situation. The intention of the Government seems to be to avoid double taxation. Let's study it with an example

M/s XYZ a developer is in the process of completing a project which has just 6 units. Each of these units has achieved a 50% completion except the sample house purchased by Customer ABC which is at 90% completion.

| Name | Agreement Value | Extent of Supply or % Completion | Value on which VAT is Paid (in % terms up to appointed day) | Value on which Service Tax is Paid (in % terms up to appointed day) | Balance Agree-ment value to be subjected to CGST and SGST | Value out of (E) already suffered Service Tax and now subjected to CGST | Value out of (E) already suffered VAT and now subjected to SGST | Excess ST Paid | Excess VAT Paid |
|---|---|---|---|---|---|---|---|---|---|
| | **A** | **B** | **C** | **D** | **E** | F= A*(D-B) | G = A*(C-B) | I = F*4.5% | J = E*1% |
| ABC | 1,00,000 | 90% | 90% | 90% | CGST 10,000 SGST 10,000 | 0 | 0 | 0 | 0 |
| PQR | 1,00,000 | 50% | 100% | 90% | CGST 50,000 SGST 50,000 | 40,000 | 50,000 | 1,800 | 500 |
| SEA | 1,00,000 | 50% | 0% | 50% | CGST 50,000 SGST 1,00,000 | 0 | 0 | 0 | 0 |
| CBA | 1,00,000 | 50% | 20% | 20% | CGST 80,000 SGST 80,000 | 0 | 0 | 0 | 0 |
| RQP | 1,00,000 | 50% | 100% | 40% | CGST 60,000 SGST 50,000 | 0 | 50,000 | 0 | 500 |
| AES | 10,00,000 | 50% | 100% | 100% | CGST 5,00,000 SGST 5,00,000 | 5,00,000 | 5,00,000 | 22,500 | 5,000 |

Some critical observations from the above working table are as below :-

1. The presumption taken is that the phrase "extent of supply" as referred in the Section 142(11)(c) would mean the stage of physical construction (Extent of Supply or % Completion).
2. As long as VAT and Service Tax are paid in tune with the % completion, there are no overlapping taxes. (Customer ABC)
3. As long as the % completion is more than the % values on which VAT and Service Taxes have been paid, there are still no overlapping taxes. (Customer CBA)

4. The moment the % values on which VAT and Service Tax have been paid both of which exceed the % completion, the provisions of Section 142(11)(c) seem to be triggered. (Customer PQR, AES).

5. If only Service Tax has been paid and VAT has not been paid in a case, then the provisions of Section 142(11)(c) do not seem to be attracted. Instead provisions as referred to in Section 142(11)(b) would be attracted giving the necessary relief by ensuring no charge of CGST on the same value. (Customer SEA). However a recent Notification No. VAT. 1517/C.R.57/ Taxation-1 dated 26-5-2017 issued under the Maharashtra VAT Act would ensure that such a scenario does not arise.

6. The excess service tax & VAT paid would be available as a credit, however instead of giving the credit on an actual basis the Government has chosen to prescribe rules for the same which may either lead to some losses or even gains.

## 3. Anti-Profiteering

Anti-profiteering provisions have been introduced in GST in order to ensure that the business passes on the benefits of reduction in tax incidence of goods and services or both to the consumers on account of benefit of input tax credits. The intention of the Government is mainly to target the B2C segment catering to the consumer goods to avoid any kind of inflation in the life of a common man after the implementation of GST. Although the author believes, with the kind of competition that exists in the Indian markets, it may not be practical for the industry to keep with itself the benefits arising out of GST. The market will force all the players to offer the best pricing to lure the customers.

Section 171 of the Act speaks about passing to the recipient the benefits both on account of Output and Input Taxes by way of commensurate reduction in the prices. Interestingly, the emphasis here is not on profits earned pre-GST or post-GST but on the impact of taxes.

Let's look at a case how one would like to pass the benefits of credit benefits. A simple formula could be as below:

| Particulars/Taxes | Impact on Collection |
|---|---|
| Post GST Credit inefficiency under current regime | 5,00,000 |
| Less : Post GST Credit inefficiency under GST regime | 1,00,000 |
| Improvement in credit efficiency | 4,00,000 |

Note – Credit Inefficiency denotes the loss of Input Tax Credits

In case of developers the credit efficiencies can be distributed by passing on these benefits by offer of discounts/credit notes as it may be difficult to reduce the agreement values which are subject to strict watch of the stamp duty authorities unless there are specific circulars from these authorities to cater to this particular issue faced by the real estate sector.

It may be interesting to note what would happen in cases where the customers have made the complete down payment towards the agreement value. In such cases actual payments would have to be made by the developers to the customers by way of refunds to comply with this provision.

Further Distribution of benefits amongst the customers would again be challenging on the part of the developers due to multiple options being practically available. This is due to lack of proper clarity from the Government. Whether benefits gained are to be passed on at the entity level or on a project level basis? Question further arises as to whether the benefits are to be passed to all the customers for a particular project or only to those customers from whom outstanding amount is still due on the appointed

date. Clarification on these crucial aspects are expected from the Government very soon.

It will also be interesting to note the manner in which the Government goes around to monitor the compliance of this clause looking to huge volume of work involved.

## 4. Joint Development Agreements

In the real estate sector, it is a common practice for land owner and developers to come together and develop or redevelop a property. In such a case, the land owner contributes the land and the developer uses his expertise of construction/development of a project. The constructed property is sold together by the land owner and developer. There can be various revenue sharing options as stated below depending on the levels of risks involved:-

**Models**

1. Fixed monetary consideration to land owner
2. Allotting free units out of constructed space to land owner
3. Share of profits from the projects
4. Fixed % on the consideration charged to buyers of units

There continue to be some doubts on valuation and timing issues. Similarly, the debate on land-related transactions such as taxability of development rights, land aggregation transactions, etc. are not yet addressed under the GST regime so far.

**Taxability in the hands of builder :**

**Model – 1 : Fixed monetary consideration to land owner :**

Developer enters into an agreement with the land owner for acquiring the development rights and constructing a property. The developer pays a fixed consideration for purchase of land. The sale of units by the developer before the completion certificate shall be subject to GST. The developer shall be liable to GST at 12% rate in case the composite consideration is charged from the buyers. However in case the developer charges separately for land & construction he shall also have an option to discharge GST at 18% only on the construction value.

**Model – 2 : Allotting free units out of constructed space to land owner :**

In this model free units are allotted to the land owner in lieu of land consideration. This is a barter transaction between the land owner and the developer where the land owner transfers the land and the developer transfers the part of constructed property to the landowner. The definition of supply under section 7(1) includes all forms of supply such as sale, transfer, barter, exchange, etc. Thus such supplies shall be continued to be taxed under GST regime also. However, under the present regime, service tax is levied on such free units but under VAT in most of the States the transactions are excluded as the definition of sale does not specifically cover the barter transactions.

The complication involved under such barter transactions would be the point of taxation & the valuation. As per section 13, the time of supply shall be the earliest of date of issue of invoice, date of payment or the provision of service if invoice not issued within prescribed time limit. In present case since the payment under barter transaction i.e. development rights are transferred on the very first day of the contract between developer and land owner, the time of supply shall be the date on which an agreement is executed between the landowner & the developer. Under service tax, the department had issued a clarification dated 20th Jan, 2016 on valuation of free units stating that the value of these units would be equal to the value of similar units charged by the builder/developer from the other category of service receivers which has been a subject matter of controversy.

However, under GST regime the value of such units shall be as per the Determination of Value of Supply Rules. As per Rule 1 where the supply of goods or services is for a consideration not wholly in money, the value shall be the open market value of such supply. The issues that remains is whether open market value of the units need to be seen or the services of a works contractor had a contractor been engaged by the land owner to construct on his land are required to be seen. According to the author it's the latter that is required to be assessed.

Further, if open market value is not available the value shall be the sum total of consideration in money if such amount is known at the time of supply. If value of consideration is not available, the value shall be the value of supply of services of like kind or quality. If all these fail one may have to go by the cost plus method and if that too is not possible then the residual method.

**Model – 3 : Share of profits from the projects**

In this model the developer and land owner share the profit from the development of project. Such cases may be treated by the department as an unincorporated JV which is subject to independent taxation. The said risk continues even under GST. Hence drafting of such contract continues to remain very critical.

**Model – 4 : Fixed % on the consideration charged to buyers of units**

In this model developer collects and remits a fixed percentage of consideration charged from the buyers of the units to the land owner towards the land. The authority to sell the units shall rest with the developer at his own responsibility. The consideration received from the sale proceeds before completion certificate shall be subject to GST, however the units sold after completion certificate shall be out of purview of GST. The developer shall have two options for valuation, either to pay GST at 18% on consideration excluding land value or to pay GST at 12% on consideration including land value.

**Taxability in the hands of land owner**

Under the development agreement, the land owner firstly transfers the development rights to the developer / builder for development and construction of new property. Such transactions are excluded from the purview of service tax under the present regime considering the same as transactions relating to immovable properties.

Under GST, as per para 5 of Schedule III of the Act, sale of land and sale of building are included under transactions which shall neither be considered as supply of services nor supply of goods. There is no mention of rights arising out of land in the said Schedule. And now with a very wide definition of services which includes anything other than goods, department may take a stand that even rights arising out of land like Transferable Development Rights (TDR) / Floor Space Index (FSI) would be taxable under GST. However in the views of the author such an extended view may not be possible so as to encapsulate all forms of immovable properties within the definition of service just because these rights have not been included in Schedule III. However this shall definitely create some controversy in industry for applicability of GST under such transactions.

Where the land owner receives the free units from the developer and he further sells these free units before the completion certificate, the same shall again be subject to GST with input credits of the taxes paid by the builder.

## 5. Redevelopment (including slum rehabilitation)

In case of redevelopment of constructed property the land owners i.e. the society or the members of the society enter into an agreement with the builder to redevelop the property owned by the society / the members of the society. The taxability of such transaction shall depend on a case to case basis.

Let us however take a basic case study to explain a possible scenario under GST :

A society consists of 3 buildings,

- Buildings A & B have around 100 offices sold out to the respective owners
- C which hosts 50 residential units on rent is owned by the society
- Additionally, there is a slum area consisting of around 30 units

**Redevelopment plan agreed by all the stakeholders with the builder**

- Builder shall demolish the existing property & develop 4 new buildings 'A', 'B', 'C' & 'D' & slum area
- Existing owners of buildings A, B & C & slum area shall get the additional 20% of constructed area than the present area
- Builder to pay rent & other compensation for temporary accommodation during the construction period.
- In addition, the builder shall pay some amount towards society's corpus fund.
- The additional units constructed by builder i.e. building D shall be sold by builder to new buyer at his own discretion.

Let us review the chain of events that would happen during redevelopment & check the tax impact of such events under the GST regime.

| Chain of Events | Taxability under GST | |
|---|---|---|
| | **In the Hands of Builder** | **In the Hands of Society / Building Owners** |
| Transfer of Development Rights by Land Owner & society to builder | Not Applicable | Considering that the transfer of land rights is out of the purview of definition of service, the same shall be out of GST |
| Registration for development, plan passing & permissions from local authority by builder | Such services received from local authority shall be covered under Reverse Charge & GST shall be payable under Reverse Charge by builder | Not Applicable |
| Payment towards Society's Corpus Fund | Not Applicable | It can be stated that the contributions / allowances received by the society / members constitute consideration for a single deliverable i.e. development rights and cannot be taken into account in isolated manner and hence shall remain non-taxable or shall adopt the same as the development rights |
| Rentals & other compensation paid to owners of Buildings & Society | Not Applicable | |
| Collections from the new owners (Before & After Completion Certificate) | Before Completion Certificate<br>Consideration received from the new owners before completion certificate shall be taxable as per para 5(b) of Schedule II | Not Applicable |

| Chain of Events | Taxability under GST | |
|---|---|---|
| | **In the Hands of Builder** | **In the Hands of Society / Building Owners** |
| | **After Completion Certificate:-**<br><br>Consideration received from the new owners after completion certificate shall not be taxable as per para 5(b) of Schedule II read with para 5 of Schedule III, as the same shall be considered as a sale of building. | |
| Transfer of units to existing building owners. | **Transfer of units to existing building owners:**<br><br>Units constructed by developer for the existing owners shall be subject to GST. The problem here shall be the time of supply & valuation. The time of supply shall be the date of agreement for transfer of rights by the owners & builder. The builder shall be liable to pay full GST on the units allotted to the existing owners. The valuation shall be done as already mentioned in Model 2 above. | Not Applicable |

## 6. Input Tax Credits

GST is expected to usher into a regime of free credit flows. Government has been making tall claims all across. However very silently the list of blocked credits under the act continues to deny a lot of credits which were hitherto unavailable in the earlier regime.

The word "Construction" for Input Tax Credit has been defined separately by way of explanation under section 17(5)(d) of the CGST Act and includes re-construction, renovation, additions or alterations or repairs, to the extent of capitalisation, to the said immovable property.

Section 17(5) of the Act provides exception where no credit would be available for:

'(c) Works contract services when supplied for construction of immovable property (other than plant and machinery) except where it is an input service for further supply of works contract service.

(d) Goods and services or both received by a taxable person for construction of an immovable property (other than plant and machinery) on his own account including when such goods or services or both are used in the course or furtherance of business.

These credit restrictions as per above exceptions would have significant impact in terms of the procurements of goods or services or works contract services for commercial/business purposes such as malls, business parks, warehouses, etc. meant for leasing or factories, plants, units for manufacturing and production, etc.

The moot issues that remain is whether the credits would be restricted towards goods and

services for the Developers who may be said to be constructing on their own account and also towards works contract services by not treating them as supplying the works contract services?

Relying on the past judgments of the Supreme Court where the Developers in broader terms were considered as doing Works Contracts and also by interpreting the word "own account" as meant only for the end consumer the availability of Input Tax credits do not seem to be an issue. Besides a rate of 12% would be very inflationary if not backed by Input Tax credits and thus denial of credits does not seem to be the intention of the Government by any stretch of imagination. However the Council could still have adopted a better language to remove any iota of doubt being raised by some of the experts.

The second issue that may be of concern to the developers is about reversal of proportionate Input Tax credits for properties booked after receipt of the Building Completion certificate. Where the immovable property constructed are sold after BU, they are not considered as a taxable supply under GST as per Schedule III. Section 17(3) of the Act specifically includes sale of such building as an exempt supply. Hence reversal may be required if the credits have been taken on the date of procurement of such inputs.

Another concern is that even in projects where all the units are sold before the Building Completion, would we still require reversal to the extent of the involvement of land. However in the views of the author since the value that is subjected to GST @ 12% is inclusive of land, the said portion of land should not be a subject matter for calculation of exempt supply. However issues may arise in cases where the builder enters into two separate agreements towards land and constructed portion. Assuming that the value of land is about 1/3rd of the total consideration payable by the customer, it may lead of input tax reversals to the extent of 33% on the common supplies.

## 7. Leasing of Properties

The current GST law states that:

(a) Any lease, tenancy, easement, licence to occupy land is a supply of services

(b) Any lease or letting out of the building including a commercial, industrial or residential complex for business or commerce, either wholly or partly is as supply of services.

The law is very clear as to treat these type of transaction as a supply of service. Unless otherwise exempted, long-term lease would have to be considered as service irrespective of the period involved as it is specifically covered under Schedule II. However residential leasing have been proposed to be exempted from the purview of GST as of now.

Further since the leasing properties are constructed with the intention of use on own account, the Input Tax Credits would get blocked thereby significantly increasing the cost of such properties. However credits would be available on expenses incurred towards Repairs to Building/Immovable property if the same have not been capitalised in the books of account.

## 8. Other collection and charges

As services have been defined to mean anything other than goods, real estate/construction will primarily be classified as service under Schedule II Entry number 5(b) & 6(b).

The GST Bill provides for concepts of composite supply and mixed supply:

Composite supply includes a supply consisting of two or more goods or services or a combination of goods or services which are naturally bundled and supplied in conjunction with each other in the ordinary course of business.

Mixed supply means two or more individual supplies of goods or services, or any

combination thereof, made in conjunction with each other by a taxable person for a single price where such supply does not constitute a composite supply.

Composite supply would be taxed at the rate applicable to principal supply while mixed supply would be taxed as supply attracting highest tax rate from the various components. Apart from the basic agreement value a developer normally collects a lot of other payments from the customer. Here is an illustrative list of some of these collections along with their taxability status under the current and the GST Regimes:

| Sr. No. | Types of Collection | Taxability under current regime | Taxability under GST regime |
|---|---|---|---|
| 1 | Subscription/Booking/Administration Fees | Taxed separately at Full rate under Service Tax | Taxable at full rate (Note 1 below) |
| 2 | Prime/Preferential charges for unit choice | Taxed as a bundle | Taxable as a composite supply (Note 1 below) |
| 3 | Floor wise extra charges | Taxed as a bundle | Taxable as a composite supply (Note 1 below) |
| 4 | Amnesty/Common infrastructure development charges whether IDC (internal) or EDC (external) like Road, Fire, Street Lights, Garden, Playground, Power back up etc. | Taxed as a bundle | Taxable as a composite supply (Note 1 below) |
| 5 | Club Membership | Taxed separately at Full rate under Service Tax | Taxable at full rate (Note 1 below) |
| 6 | Local Development authority fees | Non-taxable subject to Pure agent conditions | Not Taxable (Note 4 below) |
| 7 | Power, Sewerage & Water connection charges | Non-taxable subject to Pure agent conditions | Not Taxable (Notes 1 & 4 below) |
| 8 | Parking Space charges | Taxed as a bundle | Taxable as a composite supply (Note 1 below) |
| 9 | Annual Maintenance Deposit | Non-taxable as long as the same is non-refundable | Not Taxable (Note 4 below) |
| 10 | Taxes & Duties | Non-taxable | Taxable as a composite supply (Note 1 below) |
| 11 | Advocate/Legal Charges | Taxed separately at Full rate under Service Tax | Taxable as a composite supply (Note 1 below) |

| Sr. No. | Types of Collection | Taxability under current regime | Taxability under GST regime |
|---|---|---|---|
| 12 | Stamp duty & Registration charges | Non-taxable | Taxable as a composite supply (Note 1 below) |
| 13 | Modification charges | Taxed as a works contract as a separate contract | Taxable (Note 3 below) |
| 14 | Interest on delayed collection | Non-taxable (Rule 6 of ST (Det. of Value) Rules, 2006 | Taxable at full rate (Note 2 below) |
| 15 | Booking Cancellation charges | Taxed separately at Full rate under Service Tax | Taxable at a full rate (Note 1 below) |
| 16 | Miscellaneous & other charges, if any | Taxed separately at Full rate under Service Tax | Taxable at a full rate (Note 1 below) |

***Refer notes after Point No. 9 related to Maintenance of Housing Society.***

Further as far as cancellations are concerned no transitional provision has been prescribed for adjustment of tax refunded to customer on cancellation. However builder can go for refund claim u/s. 142(5) in respect of service tax refunded to customers on cancellation of flat post GST.

## 9. Maintenance of Housing Society

Lets look at the tax positions of various incomes earned by a Housing Society:

| Sr. No. | Types of Collection | Taxability under current regime | Taxability under GST regime |
|---|---|---|---|
| 1 | Membership / Subscription Fees | Taxed separately at Full rate under Service Tax subject to exemptions up to ` 5,000 per month | Taxable at full rate (Notes 1, 5 below) |
| 2 | Monthly Maintenance Deposit – Refundable | Non-taxable | Non-taxable |
| 3 | Transfer Fees – Non-refundable | Taxed separately at Full rate under Service Tax | Taxable at full rate (Note 1 below) |
| 4 | Renovation Maintenance / Construction Deposit – Refundable | Non-taxable | Non-taxable |
| 5 | Sinking fund or specific purpose fund – Refundable | Non-taxable | Non-taxable |
| 6 | Interest Income on FD from Bank | Taxed separately at Full rate under Service Tax if arising out of refundable deposits | Taxable at full rate if arising out of refundable deposits |

Notes:

1. GST will be calculated @12% as per declared schedule on total value of agreement i.e. including land value. All ancillary charges as long as considered as a part of the natural bundle would also be taxed at the same rate. However for some charges which cannot be considered as a natural bundle, it may be advisable to raise bill separately for the same taxing them at the regular rate of 18%.

   As per sub-section 2(a) of section 15 for valuation, any taxes, duties, cesses fees and charges levied under any law for the time being in force other than this Act, if charged separately by the supplier.

2. In terms of Section 15(2)(d), interest or late fee or penalty of delayed payment for any consideration/collection for any supply is liable to be included in the taxable value.

   Also, for the maintenance builder acts as an agent on behalf of the proposed society and such collections would be transferred to the society at the time of handover and are thus not liable to be taxed.

3. Modification in other than structural things during the construction of building, is difficult to be tracked. As long as stamp duty is paid on any such recoveries by considering it as a part of the agreement value, the same would be subjected at 12%. In other cases the same may be taxed at 18% considering the same to be a separate works contract.

4. Pure Agent conditions have been clearly defined under the Valuation rules.

5. As per draft released – Service Tax Exemptions to be continued in GST as decided by GST Council dated 19th May, 2017 – Entry No. 26(c),

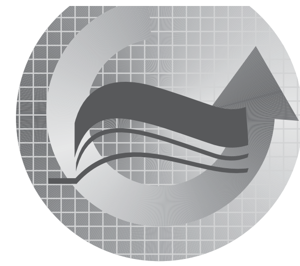
***"Service by an unincorporated body or a non-*** *profit entity registered under any law for the* ***time being in force, to its own members by way of reimbursement of charges or share of contribution – (a) as a trade union; (b) for the provision of carrying out any activity which is exempt from the levy of GST; or (c) up to*** *an amount of five thousand rupees per month* ***per member for sourcing of goods or services from a third person for the common use of its members in a housing society or a residential complex;"***

Thus we see that there are various implications to be faced by the real estate sector.

There are several issues where the language of the law may need more clarity from the Government. However it has been a tough journey for everyone and thus one may not expect a perfect law right from the day one.

When you are doing any work, do not think of anything beyond. Do it as worship, as the highest worship, and devote your whole life to it for the time being.

— ***Swami Vivekananda***



CA Amitabh Khemka

# Impact Study on Telecommunication

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

This article discusses some of the key aspects of telecommunication service from GST perspective.

## Location of the supplier for providing telecom services

India is a Union of States. For Goods and Services Tax ('GST'), the Union is of 29 States, two Union territorries (UT) with legislature and five UT without legislature. However, for telecom, the Union is of 22 telecom service areas – 19 telecom circles and three metro circles. The boundaries of 10 telecom circles coincide with that of the States; rest of the telecom service areas are consisting or more than one State and/or UT. Historically, telecom licences were granted for each telecom service area for providing access services (mobile/cellular services). Separate licence / authorisation is provided for fixed line services, national long distance services, international long distance services, internet services. Separate registration is required in respect of infrastructure services.

Under service tax regime, most of the telecom operators/telecom service providers are having centralised registration under service tax law. The question that emanates under GST is – should the registrations / area of operations / location of the supplier of services be based on the telecom services area (i.e., 22) or should it be based on the State/UT boundaries. Should separate registration be obtained for dfferent licences / authorisations or is the licensing regime irrelevant for registration under GST regime. For GST, shouldn't it be 'telecommunication services' alone, irrespective of nature of licence – access, long distance, internet – for determining the place from where services are rendered / location of the supplier of service / registration requirements.

Say for example, in a telecom circle – Bihar & Jharkhand – two States are involved. Say, the telecom operator has its office (fixed establishment) only at one place, in Bihar. Obviously it would have telecommunication network all over the telecom circle to provide telecom service. Assuming it does not have any place where it 'stores' goods in Jharkhand, can it be said that the telecom operator is providing telecom services from the "fixed establishment" in Bihar to the entire telecom circle – Bihar & Jharkhand. Seems "yes". The same fixed establishment would then be the 'location of the recipient of service' for the services received, (including spectrum, advertisements,

inter-opeator services) for that telecom circle. In which event, the transactions with customers (post-paid / distributors / enterprises) in Jharkhand would be inter-State supply, always. Mechanism can be instituted for transferring input tax credits that would be required to be taken in Jharkhand.

## Treatment of telecom vouchers

Under service tax regime, the telecom operator is required to pay service tax on the face value of the voucher and the distribution chain that distributes the telecom vouchers to the end-subscriber is exempt from service tax. Under GST law, "voucher" is defined to mean an instrument. Generally, an instrument would include a document and 'document' is defined in GST law to include 'electronic record' as defined under Information Technology Act, 2000 - which mean a data / record stored, received or sent in an electronic form. Telecom vouchers, both physical as well as electronic, in that case would be regarded as 'vouchers' as defined. The definition of 'voucher' as given in GST law is same as that issued / adopted by the Council of the European Union for treatment of vouchers for European Union VAT. The definition therein, was adopted to provide common solution for vouchers primarily for telecommunications, broadcasting and electronically supplied services.

Where the supply of services is pursuant to supply of vouchers by a supplier, then the time of supply of such service is the date of issue of voucher, where the supply of services is identifiable at that point, and in all other cases it would be the date of redemption of voucher. Just to clarify, the time of supply provisions determine time of supply of services and not the time of supply of voucher. Under the Council Directive issued by Council of the EU, for single-purpose voucher, VAT is required to be charged on each transfer, including on the issue, of such voucher and for multi-purpose vouchers, VAT is required to be charged when the services to which the voucher relates are supplied and any prior transfer of multi-purpose vouchers is not subject to VAT. Under the Indian GST law, the time of supply of service is only on the date of issue of voucher or date of redemption of voucher and not on each transfer of voucher or prior transfer of voucher.

The transaction value of supply of services would be equal to the money value of the services redeembable against the voucher.

Distribution chain of vouchers, should be regarded as 'intermediary', irrespective of the arrangement such distribution chain have with the telecom operators or with other persons / intermediaries within the distribution chain. 'Voucher' for that matter should be treated neither as 'goods' nor as 'services'. The distribution chain is 'intermediary' for the main service i.e., telecommunication services.

## Telecom towers – input tax credit

Under GST law, input tax credit (ITC) is available in respect of inputs and capital goods, i.e. goods. ITC is not available in respect of goods used / received for construction of immovable property; plant and machinery is carved-out from this exclusion. Plant and machinery is defined to exclude 'telecommunication towers'. Under the existing law, Bombay High Court has concluded that CENVAT credit cannot be availed in respect of telecom towers, such towers being 'immovable property' and hence not 'goods'. The High Court judgment has been appealed to the Apex Court; appeal has been admitted and no stay has been granted to the judgment of the High Court. Under GST law, the transition

provisions provide that the CENVAT credit shall not be allowed to be carried forward where the amount is not admissible as input tax credit under the GST law. In respect of capital goods, the credit should also be admissible as CENVAT credit under existing law.

Exclusion of telecom towers from the definition of plant and machinery should not make telecom towers, itself, ineligible for ITC *qua* the construction of immovable property. The term 'construction' for this purpose is specified as follows:

For the purposes of clauses (c) and (d), the expression "construction" includes reconstruction, renovation, additions or alterations or repairs, to the extent of capitalisation, to the said immovable property

It is appropriate that the telecom towers are finally held to be 'immovable' by the Apex Court, for the denial of ITC under GST law.

## Carry forward of CENVAT Credit on spectrum

CENVAT Credit of service tax paid in a financial year on the one-time charges payable for the service of assignment of the right to use any natural resource by the Government is required to be spread evenly over a period of three years. In case of further assignment in any financial year, the amount of balance CENVAT credit as does not exceed the service tax payable on the consideration charged for such further assignment, is to be allowed in the same financial year. A question does arises for the need of a transition provision in CGST law to carry forward the credit which was spread evenly and was not eligible to be allowed under existing law. One is looking for a transition provision similar to that provided in respect of capital goods where credit can be taken only for the amount not exceeding 50 per cent of duty paid, in the same financial year. It should be arguable that such provision is not required in case of natural resources (spectrum in case of telecom services), wherein the credit is not restricted from being taken; but such credit having been taken is required to be spread evenly over a specific period.

## Transactions between distinct persons

The Draft Valuation Rules provide that the value of taxable services provided, by such class of service providers as may be notified by the Government, between distinct persons as referred to in section 25, where input tax credit is available, shall be deemed to be Nil. Considering the numerous transactions between distinct persons within a telecom circle (multi-State/UT) or between different telecom service areas or between different licences / authorisations, it is expected that telecom services provided by telecom operators would be notified by the Government under these Rules. In the event, such services / service providers are not notified so, such numerous transactions would required to be identified, dissected, recorded and then all the compliances under GST law would be required to be undertaken. It is provided in the Draft Invoice Rules that an insurer or a banking company or a financial institution, including a non-banking financial company, or a telecom operator, or any other class of supplier of services as may be notified by the Government, making taxable supplies of services between distinct persons as specified in section 25, may issue the invoice before or at the time such supplier records the same in his books of account or before the expiry of the quarter during which the supply was made. A clarification/provision so as not to issue a Nil value invoice would be welcome.

## Transition provison required in Jammu & Kashmir

Under existing Jammu & Kashmir General Sales Tax law, telecom services attract sales tax. Telecom operators have challenged levy of such sales tax; they have also challenged levy of entry tax in the State of J&K. Government of J&K provided for exemption from entry tax to telecom operators provided they undertake to pay sales tax and the advance sales tax was paid when the goods entered into the State of J&K, calculation of which was basis the entry tax law. The Jammu and Kashmir GST law needs to provide for a transition provision to carry forward such advance sales tax paid. Awaiting the J&K GST law.

## Place of supply

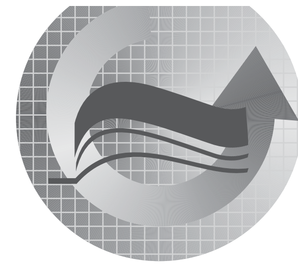
The place of supply for fixed telecommunication line, leased circuits and internet leased circuit is the location where the telecommunication line or leased circuit is installed for receipt of services. It is explained that - where the leased circuit is installed in more than one State or Union Territory and a consolidated amount is charged for supply of services relating to such circuit, the place of supply of such services shall be taken as being in each of the respective States or Union Territories in proportion to the value for services separately collected or determined in terms of the contract or agreement entered into in this regard or, in the absence of such contract or agreement, on such other basis as may be prescribed.

In the event of leased circuit being installed between India (say in one State) and outside India and the recipient is registered person in India or the recipient's address on record is in India, the installation being in one State in India, would attract GST for the full value of service.

The place of supply where mobile connection for telecommunication, internet service are provided on pre-payment basis through a voucher or any other means through a selling agent or a re-seller or a distributor of re-charge voucher, is the address of the selling agent or re-seller or distributor as per the record of the supplier at the time of supply. The intermediaries (selling agent / re-seller / distributor) should not determine the place of supply of their supply under this provision as they themselves are not providing the main supply of telecom service.

Do not hate anybody, because that hatred which comes out from you must, in the long run, come back to you. If you love, that love will come back to you, completing the circle.

— ***Swami Vivekananda***



Nikita R. Badheka, *Advocate & Notary*

# Impact Study on Oil Companies and Offshore Drilling Companies under GST

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

## GST – Impact on oil companies

1. The Goods and Services Tax provisions i.e. MGST (Maharashtra Goods and Services Tax Act) & CGST (Central Goods and Services Tax Act) defines "goods" to mean "every kind of movable property other than money and securities but includes actionable claim, growing crops, grass and things attached to of forming part of the land which are agreed to be severed before supply or under a contract of supply" (Section 2(52) of CGST Act and MGST Act). For the sake of brevity, in this article I would refer to provisions of MGST & IGST as applicable.

2. *Prima facie* therefore all types of movable property, tangible or intangible are covered within the scope of Section 2(52).

3. The GST Council and the Central Government have been repeatedly announcing that certain petroleum products namely: petroleum crude, high speed diesel, motors spirit (commonly known as petrol), natural gas and aviation turbine fuel (hereinafter collectively described as "these goods" or "petroleum products") would be out of the GST net. I would not go into the reason of keeping these goods out of the GST net presently, may be for a short-while. I have discussed the impact on the oil companies dealing in these products.

4. Section 9(2) of the MGST Act specifically states that the State Tax (MGST) and Central Tax (CGST) on supply of above specified petroleum products shall be levied with effect from such date as may be notified by the Government on the recommendation of the Council. Section 5(2) of IGST is worded in the same fashion. Therefore, presently, the intention is to defer the levy of GST on these products after the appointed date i.e. the Goods and Services Tax Act coming into force.

5. Under the MVAT Act, 2002, there were special notifications for the Oil Companies. Under Section 41(4), the State has power to exempt from levy of tax partly or fully on sale of motor spirits and petroleum products made by an oil company to another oil company. The oil companies for the purpose of MVAT Act notified were IOCL, BPCL, HPCL, IBP Limited, Kochi Refineries Limited, The Mangalore Refineries and Petrochemicals Limited, Tide Water Oil Company (India) Limited, ONGC, Chennai Petroleum Corporation Limited and Essar Oil Limited. Similarly, the motor spirit and other petroleum products are also notified which includes High Speed Diesel Oil, ATF

(duty paid), ATF (Bonded), Aviation Gasoline (duty paid), Aviation Gasoline (Bonded), Petrol, SKO, LPG, FO, LDO, Raw Naphtha or Naphtha and Low Sulphur Heavy Stock The sale of petroleum products and motor spirits as notified by any of the oil companies listed in the notification to any other oil company in the said list would be subject to 4% tax. The retail outlets selling motor spirits other than ATF and Aviation Gasoline were exempt from payment of tax. However, under GST regime, Petroleum Products would not be taxed till separately notified. The exclusion from GST is to limited products as detailed in para 3 above.

6. The Central Government has therefore introduced the Amendment to CST Act ***vide*** the Taxation Laws Amendment Act, 2017 – No.18 of 2017 dt. 4-5-2017. On introduction of GST Act, the applicability of CST Act would be restricted to a few products, now excluded from GST provision, namely, Petroleum Products, High Speed diesel, Motor Spirit (petrol), Natural Gas, Aviation Turbine Fuel and Alcoholic Liquor for Human Consumption. As per amendment, the meaning of 'goods' is restricted to only above specified goods. The definition of "Declared Goods' sec. 2(c) and section 14 and 15 will also be deleted. This amendment will come into force from the date to be notified. Thus, application of Central Sales Act, 1956 would be restricted only to the product specified hereinabove. Similar provisions or amendments are expected under the Excise and MVAT Act. There would not be a separate Act levying the tax on these products but the application of existing laws would be restricted to few products. The Constitution amendments are referred to hereafter.

7. The next immediate question can be whether oil companies dealing with the above specified products are required to get themselves registered/migrated under the provisions of GST Act. The oil companies are presently registered under the provisions of MVAT Act, Service tax and the Excise provisions. An interesting aspect about exclusion of oil companies from the GST regime is that, it is the products which would not be covered under the GST regime. Does that mean the services provided (if any), by these oil company would also be out of the GST purview. The answer is No. The supply as stated in Section 9(2) should be restricted to supply of goods only and not services. As per my information. normally oil companies do not provide any output services. Sections 9(1), 9(3), 9(4) etc. specifically refers to supply of goods or service or both, whereas Section 9(2) refers to supply of specific tangible goods. Therefore, migration process to the GST regime will have to be done by the oil company since they have many more inward and outward supply of goods and services .

8. The exclusion of these products from the GST regime is going to create multiple practical and administrative issues as such oil companies will have to comply with the provisions of the GST law as well as the existing law. ***Qua*** these sales and purchases of these goods they would be covered under the MVAT Act, Excise Act and for any other activity of service or of sale of goods other than the goods specified hereinabove, they will be complying with the GST Act.

9. Apart from the above specified products, the oil companies usually have huge purchases of goods like chemicals, stores, consumables, packing materials and above all capital goods. They also utilise the services and pay service tax on AMC contracts, design, project work, works contract, transportation, legal fees, Technical consultancy etc. If one of the petroleum companies in India is establishing a new project, there will be huge investment on capital goods under the GST regime. For the companies in SEZ unit, there would be some relief. However, the oil companies situated outside SEZ tend to lose mainly by way of ITC. Apart from this, oil companies sell scrap goods,

waste goods and residue products like sludge etc. On this outward supply they will be liable to pay the GST .

10. In terms of the MGST and CGST Acts, these goods would be non-taxable goods and supply of such goods would be non-taxable supply. Definition 2(47) defines 'exempt supply' to mean "supply of goods or services or both which attracts Nil rate of tax or which may be only exempt to tax under section 11 or under section 6 of IGST Act and includes non-taxable supply." Section 6 of the IGST Act and section 11 of the CGST / MGST Act refers to the power of the State or power of the Central Government to exempt generally either absolutely or subject to condition, the goods or services or both of specified description, on the recommendation of the Council.

11. Referring to the basic requirement of the ITC rule, there are many restrictions and prohibitions as regard the exempt supply. In terms of section 17(2) when the goods or services or both are partly used for effecting taxable supply and partly for effecting exempt supply under the Act, the amount of credit shall be restricted to so much of the Input Tax as is attributable to the taxable supplies including zero-rated supplies. The producers of petroleum products would not be able to claim ITC for the opening stock on the appointed day either of raw material or finished goods. However, the benefits under the MVAT Act would not be withdrawn. Input Tax Credit rule 7 prescribes the manner of determining the ITC in respect of inputs under section 17(2). This rule provides the method of apportioning the Input Tax Credit. The explanation to this rule 7(1)(i) states that for the purpose of this clause the aggregate value of exempt supply in total turnover shall exclude the amount of any duty or tax levied under Entry 84 of List-1 of the 7th Schedule of the Constitution. This entry as amended by Constitution 122nd Amendment reads as follows:

"84 – Duties of excise on the following goods manufactured or produced in India, namely:-

(a) Petroleum crude;

(b) High speed diesel;

(c) Motor spirit (commonly known as petrol);

(d) Natural gas;

(e) Aviation turbine fuel; and

(f) Tobacco and tobacco products"

12. This explanation also refers to Entries 51 and 54 of List-2. Entry 51 of List-2 refers to alcoholic liquor for human consumption and Entry 54 refers to tax on sale of petroleum crude, high speed diesel, motor spirit, natural gas, ATF and alcoholic liquor for human consumption but not including sale in the course of inter-State trade or commerce or sale in the course of international trade or commerce of such goods. Needless to add, prior to this amendment entry 54 referred to taxes on sale of purchase of goods other than newspapers, subject to the provision of Entry 92A of List-1. With the amendment now made, the power of the State to levy the tax is restricted to these limited products. As per this explanation the aggregate value of exempt supplies would be taken as net supplies (minus the tax) for the purpose of appropriation. The proviso to ITC rule 7(1)(m) states that if the amount of Input Tax relating to inputs or input services which has been used partly for purposes other than business and partly for effecting exempt supplies has been identified and segregated at the invoice level by the registered person, the same shall be included in T1 and T2 respectively and the remaining amount of credit on such input or input services shall be included in T4. T4 denotes the amount of ITC attributable to input and input services used exclusively or in relation to taxable supplies including zero-rated supplies. The amount of Input Tax attributable to

input and input services intended to be used exclusively for exempt supplies is denoted as T2. Therefore, the oil companies, though not registered, ***qua*** the petroleum products will have to ensure compliance with the invoice rules under the GST Act for claiming the rightful ITC for the goods other than exempt supplies.

13. The major blow to the oil companies would be in relation to the Input Tax Credit claim for the capital goods mainly plant and machinery. It would be a challenge for the authorities as well as for the oil companies to apportion the Input Tax Credit on capital goods. The phrase plant and machinery is defined by way of explanation to section 17 of the SGST Act. This definition excludes pipelines laid outside the factory premises. Whether this would mean pipelines laid outside the factory premises will not be eligible for Input Tax Credit. In my opinion, it would be possible to argue that the pipelines laid by the oil companies are for furtherance of business and should be eligible for Input Tax Credit. However, as per my experience, the pipelines are normally laid by a third company who provides the services of transporting the petroleum products. Therefore, since such companies would be providing services of transportation, they would not come within the restricted definition of supply of petroleum products. The services under the Reverse Charge Mechanism (RCM) approved by GST Council includes service provided by a goods transport agency in respect of transportation of goods by road. Therefore service of transportation of petroleum products by pipelines would not be covered by RCM. The buyer of petroleum products who uses this service would be paying the GST for the services provided.

14. It is no wonder that these oil companies have expressed their readiness to migrate to GST regime on 1st July onwards. Under the GST regime, once you have crossed the turnover liable for registration, or otherwise, it is beneficial to remain in the GST chain to get the benefit of ITC. The oil companies, even if they remain out of the GST chain ***qua*** specified products , would be facing the inquiry from the Excise Dept., Sales Tax Dept. as also from the GST dept.

15. **GST impact on Offshore Drilling Companies** : An immediate example of Offshore companies is ONGC. The Offshore drilling companies are normally situated beyond 12 Nautical miles from the shorelines, in the mid sea. The supply to these companies and supplies by these companies had led to multiple litigation. However it appears the Centre has learned some lesson and a probable solution is provided in Act itself. I am writing probable, as the disputes will still arise, as I shall point out.

16. Under the Constitution Article 1 defines India as follows

**Name and territory of the Union**

(1) India, that is Bharat, shall be a Union of States.

(2) The States and the territories thereof shall be as specified in the First Schedule.

(3) The territory of India shall comprise –

a) The territories of the States; b) the Union territories specified in the First Schedule; and 3) such other territories as may be acquired. Presently India comprises of 29 States and 7 Union Territories.

17. The word Import of goods and Import of services are separately defined under IGST Act. Sec. 2(10) ''import of goods" with its grammatical variations and cognate expressions, means bringing goods into India from a place outside India;

Sec. 2(11) ''import of services" means the supply of any service, where — (i) the supplier

of service is located outside India; (ii) the recipient of service is located in India; and (iii) the place of supply of service is in India;

2(56) of CGST Act – "India" means the territory of India as referred to in Article 1 of the Constitution, its territorial waters, seabed and sub-soil underlying such waters, Continental Shelf, Exclusive Economic Zone or any other maritime zone as referred to in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976, and the air space above its territory and territorial waters;

18. The instant distinction that one can make is that the import of goods is dependent on the geographical movement of goods, whereas in case of import of service it is the location of the supplier and the recipient that matters. One has to apply place of supply rules to find as to whether there is import of goods or not. In terms of place of supply provisions Sec. 7(4) supply of services imported into the territory of India shall be treated to be a supply of service in the course of interstate trade or commerce.

19. In terms of Sec. 7(5) the supply of goods or service or both, –

(a) When the supplier is located in India and the place of supply is outside India;

(b) To or by a special Economic Zone developer or a Special Economic Unit; or

(c) In the taxable territory, not being in intra-state supply and not covered elsewhere in this section,

Shall be treated to be supply of goods or service or both in the course interstate trade or commerce.

20. The next important definition is Sec. 2(4) of the IGST Act. The phrase "Customs Frontiers of India" means the limits of a customs areas as defined in Section 2 of the Customs Act.

21. Article 286 of the Constitution which is restricting the powers to levy the tax on Sale and Purchase of Goods is amended by 101st Amendment Act, 2016 which reads as follows

286(i) No law of a State shall impose, or authorise the imposition of, a tax on the supply of goods or of services or both, where such supply takes place

(a) Outside State or

(b) In the course of import of the goods or services or both into an export of the goods or services or both out of the territory of India.

22. Under Article 286(2), the Parliament is authorised by law to formulate principles for determining when a supply of goods or services or both in anyway mentioned in Article 286(1)

23. While discussing for the offshore companies we must know what is the territory of India, Exclusive Economic Zone, Continental Shelf, etc. The sovereignty of India extends to territory waters of India and to the sea bed and subsoil underlying, and the airspace over such waters. The limit of the territorial water is the line, every point of which is at a distance of 12 nautical miles from the nearest point of the appropriate baseline. All foreign ships (excluding war ships) enjoy the right of innocent passage through the territorial water. In terms of Article 297 of Constitution, all lands, minerals and other things of value underlying the ocean within the territorial waters or the Continental Shelves or the Exclusive Economic Zones of India shall vest in the Union. The Continental Shelf of India comprises the seabed and subsoil of the submarine areas that extend beyond the limit of its territorial waters throughout the natural prolongation of its land territory to the outer edge of continental margin or to a distance of 200 nautical miles from the baseline. The

Central Government has the power to declare the Continental Shelf and its superjacent waters to be designated area and make such provision as it may deem necessary with respect to exploration, exploitation and protection of the resources of the Continental Shelf within such designated area. The Central Government also has the power to make provision to make safety and protection of artificial island of shore terminals, installations and other structures and devices in such designated areas. The power to make provisions under the customs and other fiscal matters in relation to such designated areas is with Central Government.

24. The Exclusive Economic Zone of India (EEZ) is an area beyond and adjacent to the territorial waters and the limit of such zone is 200 nautical miles from the nearest point of appropriate baseline. Therefore the area up to a distance of 200 nautical miles is the Continental Shelf of India recognized as EEZ of India over which India has been given certain limited sovereign rights although such areas are not part of India. Therefore, although the sovereignty of India is not extended over Continental Shelf and EEZ, by a fiction created by the territorial waters, Continental Shelf, EEZ and other Maritime Act Zones, 1976, a fiction is created by which the EEZ and Continental Shelf are deemed to be a part of India for the purposes of such enactments which are extended to the areas by the Central Government by notification in Official Gazette. Whenever the legislature wanted, either under Income tax, Service tax laws or another Customs Act, the law to be extended to EEZ areas the notifications are issued accordingly. The detailed description can be found in ***CIT vs Ronald William Trikard and Others [215 ITR 638 (Mad.)]***.

25. In the case of ***Sun Industries (35 ELT 241 (SC))*** the Apex Court has an occasion to determine the meaning of taking out to a place outside India. The Apex Court held that taking out to a place outside India would also include a particular point or a portion of space occupied by or belonging to a thing under consideration. Therefore, in international trade the ship beyond the territorial waters of a country would be a place outside India. The Bombay High Court in case of ***Amership Management Pvt. Ltd. (86 ELT 15 (Bom.))*** following this verdict held that the oil rigs are considered to be vessels by the International community as all the oil rigs are required to carry International Load Line Certificate. The International Convention on Load Lines, 1966 to which India is a party provide for issue of this certificate to every ship which has been surveyed or marked in accordance with the present convention. International Maritime Organisation has also prescribed a code for the construction of equipment of mobile offshore drilling units. This unit is defined as a vessel capable of engaging in drilling operations for the exploration or for the exploitation of resources beneath the seabed such as liquid gas, hydrocarbon, sulphur or salt. The insurance policy for the oil rig is also issued on that basis. Therefore as per Chapter 89 of the Customs Act, 1962, oil rigs which are floating structures would be vessels. The oil rigs have flight platform but they are not engaged in carriage of goods or passengers but are meant for drilling operations in connection with offshore oil explorations. These are basically and essential drilling machines complete with accessories and auxiliary equipments required for drilling operations.

26. Accordingly, there were notifications issued under the Customs Act, Income-tax Act and under the Finance Act (Service Tax) to extend the law relating to levy of custom duty, income tax, service tax for the operations at the oil rigs or to and from the oil rigs. Unfortunately, the jurisdiction of Central Sales Tax Act, 1956 was not extended to the Continental Shelf and EEZ. The dispute therefore in case of Pure Helium (India) Pvt Ltd. was whether the supply of helium gas

to the oil rigs is export or whether it can be subjected to levy of Central Sales Tax. The lower authority treated ONGC rigs at Bombay High to be territory of India levied the tax under the Central Sales Tax Act and disallowed the export claim. (49 VST 14 (Bom.)). The pertinent observations are as follows :

27. The submission that Article 366(30) defines the expression Union Territory to mean any Union Territory specified in the First Schedule and to include any other territory comprised within the territory of India, but not specified in that Schedule is fallacious because it proceeds on the basis that the Continental Shelf and the Exclusive Economic Zone are comprised within the territory of India. The continental shelf and the exclusive economic zone do not constitute a part of the territory of India. As a matter of fact, it was in recognition of this position that Section 6(6) and Section 7(7) of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and Other Maritime Zones Act, 1976, empowered the Union Government to extend the provisions of any enactments in force in India to a designated area or to the Continental shelf or the exclusive Economic Zone and it was upon an enactment being extended that it would have effect as if the territory to which it is extended is a part of the territory of India. Upon being extended the enactment is to have effect as if the Continental Shelf or, as the case may be, the Exclusive Economic Zone to which it has been extended is a part of the territory of India. The words "as if" in Section 6(6) and Section 7(7) of the 1976 Act bring into existence a legal fiction. Under the legal fiction the enactment which is extended has to have effect as if the Continental Shelf or exclusive economic zone to which the enactment has been extended is part of the territory of India. The deeming fiction is for that purpose. A movement of goods from the State of Maharashtra to Bombay High does not constitute a movement from one State to another. Bombay High does not form part of any State in the Union of India.

28. Export of goods out of the territory of India envisages the movement of goods across the customs frontier. Once the customs frontier stands extended to a territory, there can be no export of goods to a territory which falls within the customs frontier. On January 14, 1987, (and with effect from January 15, 1987) the Union Government has extended the provisions of the Customs Act, 1962 to the designated areas of the Continental Shelf and Exclusive Economic Zone, the effect of which is to introduce the customs regime to such areas resulting in the levy and collection of customs duty on goods imported into those areas as if they are a part of the territory of India. A fiction created by legislation must be taken to its logical conclusion. Once the Union Government, acting as a delegate of a Legislature, has extended the provisions of the Customs Act, 1962 and of the Customs Tariff Act, 1975 to designated areas of the Continental Shelf or the Exclusive Economic Zone, with effect from January 15, 1987, it would be impossible to hold that a movement of goods from within the territory of India to that territory of the Continental Shelf or Exclusive Economic Zone constitutes an export of the goods out of the territory of India. The scheme of the Customs Act, 1962 has to be read together with other Acts such as the 1976 Act, which are ***pari materia***. Export for the purposes of Section 5(1) of the 1956 Act cannot have a meaning divorced from the applicability of the Customs Act, 1962 to a territory in pursuance of a notification issued in exercise of the powers conferred upon the Union Government in the 1976 Act.

29. In a later judgment, in the case Raj Shipping, relying on the fact that the delivery of goods at Nahava Sheva concludes the sale, the levy of tax on such transactions under the Local Act was confirmed.

30. Learning from this permanent litigations in relation to supply to, from the rigs the GST Act has opted to levy the tax under such

situation under the IGST Act. Section 9 of the IGST Act as a non obstinate clause and reads as follows:

Notwithstanding anything contained in this Act

(a) Where the location of the supplier is in the territorial waters, the location of such suppliers or

(b) Where the place of supply is in territorial waters, the place of supply, shall for the purpose of this Act be deemed to be in the coastal State or Union Territory where the nearest point of the appropriate baseline is located. For example, in case of oil rigs in Bombay High (to the extent geography I know) the IGST will be levied and collected by the State of Maharashtra.

31. The place of supply rules play a vital role for the supplies to offshore rigs. Take an example of a caterer providing services of preparation and supply of food on the rigs, the place of supply shall be the location at which the vessel is located in terms of Section 12(4)(b).

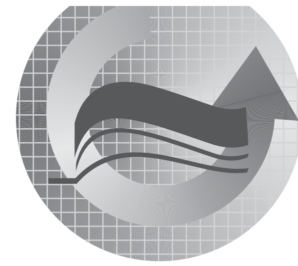
32. If the maintenance to machinery is provided at the rig what would be the place off supply. Can we apply Section 12(10) of the IGST Act which refers to supply of service on board, a conveyance, vessel, etc. to be the location of first scheduled point of departure of the conveyance for the journey. The answer is No. The rigs though may be recognized as vessel judicially, do not have a journey they are stationed at a place. It is for this reason that the statute has provided for an overriding provision in Section 9 to clear all the doubts. I must point out specifically that for the supply of goods or services or both to Special Economic Zone there is specific provision and therefore that should not be mixed with the supply of goods or service or both to and from rigs.

33. Once it is decided and concluded that Section 9 would apply in all the cases being overriding Section, there should not be any dispute that for all practical purposes one has to apply the provisions of IGST Act. The rest of the provisions like distinct persons, related persons would apply here. But, if ONGC makes supply from its rigs to its own factory in Maharashtra whether it would be treated as Sales in course of interstate trade. In my opinion such supplies would not be taxable as it shall be treated as transfer within the State. The companies holding rigs will have to disclose rigs as additional place of business. The next question can be whether ONGC rigs and ONGC head office at Mumbai can be declared as business vertical for the purpose of registration. I am giving a simple solution as intended by legislation. I am aware it is possible to argue. Rig is not a State, In my opinion we must look to the intent of legislation.

34. In terms of Section 2(18) of CGST and MGST Act, it is possible to disclose the ONGC rigs as business verticals and take a separate registration. However, keeping in mind the provisions of Schedule 1 (Clause 2), it would be treated as supply even if made without consideration. Therefore practically and ideally it is not advisable to treat the Bombay High rigs as business verticals. Separate registration for business vertical is an option which must be exercised with care.

35. In case where the oil recovered/drilled from Bombay High is transferred to Gujarat it would be treated as interstate supply and the relevant provisions will apply.

36. In my opinion therefore, the issues of territorial waters etc. is put at rest. The typical issues relating to interpretation of complex GST laws would however continue to give food for thought to our brains.



Mr. Rohan Shah, *Advocate* & Ms. Kriti Kalyani, *Advocate*

# Impact Study on Media and Entertainment Industry

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

## Introduction

The primary objective of the Goods and Services Tax ('GST') is to overhaul and revamp the existing structure of taxation within the federal setup, to create one simultaneous levy on goods and services imposed by the Centre and States. GST is a determined effort by the Government to move the taxation structure of the economy to a purely destination based-consumption tax, and avoid the cascading effect of taxes. This has been ensured by putting in place a system whereby the credit flows seamlessly through the supply chain. GST also seeks to resolve ongoing tussles between the Centre and State on issues of duality which currently result in double taxation.

The Media and Entertainment Industry ('M & E industry') is one of the classic examples of an industry that has been impacted by the federal structure of taxation in India. Some of the key challenges pertain to multiplicity of taxes, lack of delineation between subjects taxed by Centre and State, compliance costs in terms of both Central and State levies, and blockage of credits.

This article discusses the existing regime and its challenges, the impact of GST for various players in the M & E industry and the changes in taxation that the industry must prepare for. This article also assesses whether GST is an improvement over the current regime in terms of resolving key issues faced by this industry.

The article broadly discusses the following key concepts that are crucial to the M & E industry:

a) Levies subsumed in GST

b) Dual Taxation

c) Rate of tax

d) Registration

e) Place of supply

f) Liability to pay tax

g) Input Tax Credit

h) Anti-Profiteering

## Levies subsumed in GST

The prime reason for a cascading effect within the M & E industry is a multiplicity of taxes on the same transaction without full credit of taxes paid on the earlier leg of the supply chain. To take the most prevalent example, a distributor assigns theatrical rights to an exhibitor and charges Service Tax. However, the exhibitor is unable to claim credit of the Service Tax paid as he has to discharge Entertainment Tax on the movie ticket sales. Accordingly, in order to eliminate the cascading impact, the GST regime subsumes following taxes and duties, presently applicable to the M & E i ndustry:

| CENTRE | STATE |
|---|---|
| Central Excise duty<br>Service Tax<br>Central Sales Tax<br>Countervailing Duty (CVD)<br>Special Additional Duty (SAD) | State Value Added Tax<br>Entertainment Tax<br>Entry Tax |

Since GST subsumes all the aforesaid levies and is fully fungible, cascading effects *inter se* Central taxes and States taxes will be obviated.

A noteworthy remnant from the current regime is Entry No. 62 in List II of Seventh Schedule to the Constitution, which previously gave States the power to levy Entertainment Tax, but has been amended to read as follows:

> *"62. Taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council."*

While States will no longer be able to impose Entertainment Tax, a local levy may be imposed by a Panchayat/Municipality/ Regional Council or District Council, the administration of which will be entirely handled by such body.

## Dual taxation

Various pervasive issues of dual taxation abound in the M & E industry, and are elaborated below.

**Service Tax vs. VAT**

The M & E industry witnesses several transactions whereby intellectual property rights ('IPR') are transferred from one person to another. A transfer, by its nature and through a contract, may be permanent or temporary. An assignment of a copyright is governed by Sections 18 and 19 of the Copyright Act, 1957, which permit the assignment to be restricted in terms of time and territory. For instance, in the current regime, an agreement pertaining to the assignment of theatrical rights in a cinematograph film, entered into between a producer and a distributor, may attract Service tax, or VAT, depending on whether it is temporary or permanent, respectively, resulting in significant litigation.

In cases where the software was supplied to the end user in terms of End User Licence Agreement, the litigation from the VAT department and service tax department would ensue.

In the case of Direct to Home ('DTH') Operator service providers, a set top box is provided free of charge to enable supply of DTH services to their customers. The set top boxes continued to remain as assets in the books of account of the DTH service providers. The State VAT Departments have alleged this transaction to be a deemed sale of the set top box for which consideration was recovered in the form of installations charges and rent. Against this backdrop, VAT was sought to be levied. The DTH operators, however, did not treat this transaction as a deemed sale, but as an incidental part of the DTH services. This is again a typical case of blurred boundaries between the subject matters of State and Centre taxes.

**Service Tax vs. Entertainment Tax**

Another area where the same commercial transaction has borne the brunt of both Central and State levies is the activity of entertainment. Businesses like cinemas and amusement parks (for ticket prices above ` 500) have faced the levy of both Service Tax and Entertainment Tax with the justification that separate aspects of the same transaction are open to taxation by the respective authority. In case of cable television and DTH services, several State Governments sought to levy Entertainment Tax on the periodic subscription fee charged from the customers, even before their respective State Acts were suitably amended, on the basis that customers were being provided "admission to entertainment". Thereafter, the State Acts were amended to validate the levy. This was so even when a subscription fee was already being offered to tax under the Service Tax laws. However, writ challenges on the basis that the entire consideration collected from customers suffered two taxes, were negatived.

To bring more transactions within the tax net, the same commercial transactions have been subjected to State as well as Central levies simultaneously. Although justified by the "aspect theory", they did not afford the taxpayers benefit of cross utilisation of credit, leading to tax cascading and endless litigation.

However, with the advent of the concept of "supply" under GST with simultaneous powers to the State as well the Centre to impose tax, the aforesaid debates will now be put to rest. Both transfer of right in goods without transfer of title and temporary transfer or permitting the use or enjoyment of any intellectual property right have been deemed to be supply of services, taxed at the same rate under GST. This precludes any attempt to classify a transaction as either goods or service by both the taxpayer and the department. Grants of other rights, such as televisions rights and theatrical rights (not qualifying as IPR) will equally be treated as service.

Further, a given transaction of "admission to entertainment" in the form of cable, DTH etc., which previously also qualified as service, and therefore suffered both Service Tax and Entertainment Tax, will attract a singular levy of GST going forward.

## Rate of tax

The most anticipated piece of the puzzle was revealed a few days back when the GST Council announced the draft rates of tax for goods and services. The various rates of goods and services, as relevant to the M & E industry, are as under:

| PARTICULARS | CURRENT | GST |
|---|---|---|
| Selling of space for advertisement in print media | Exempt vide Section 66D(g) of Finance Act, 1994 | 5% with full ITC |
| Temporary transfer or permitting the use or enjoyment of any Intellectual Property (IP) to attract the same rate as in respect of permanent transfer of IP | Exempt under Entry no. 15 of Notification no. 25/2012 dated 20-6-2012 | 12% with full ITC |
| Services by way of admission or access to circus, Indian classical dance including folk dance, theatrical performance, drama (entry fee up to ` 250 per person is exempt) | Partially exempt under Entry no. 16 of Notification No. 25/2012 dated 20-6-2012 | 18% with full ITC |
| Services by way of admission to entertainment events or access to amusement facilities including exhibition of cinematograph films, theme parks, water parks, joy rides, merry-go rounds, go-carting, casinos, race-course, ballet, any sporting event such as IPL and the like; (entry fee up to ` 250 per person is exempt) | Partially exempt under Entry No. 47 of Notification No. 25/2012 dated 20-6-2012 | 28% with full ITC |
| Any transfer of right in goods or of undivided share in goods without the transfer of title thereof (supply of services) to attract the same GST rate and compensation cess as applicable on supply of similar goods which involves any transfer of title in goods (supply of goods). | Rate depending upon classification of goods and service | Same rate of GST and compensation cess as on supply of similar goods |
| All other services not specified elsewhere | – | 18% with full ITC |

Contrary to the industry's demands and expectations, GST has been placed in the slab of 28% for admission to entertainment events or access to amusement facilities including exhibition of cinematograph films, theme parks, water parks, etc.

It is interesting to note that intermediate services in the M & E industry are at relatively lower rates. However, the ultimate service is either at 18% or 28%, i.e. entry tickets to theme parks and sporting events like IPL or movie tickets find themselves in the higher band of tax rates.

Additionally, certain businesses in the entertainment industry, such as amusement parks enjoy exemption schemes under the State Entertainment tax laws under the current regime. However, the State Government's stand on the continuation of these assured benefits into the GST regime is unclear as of now. The tax policy could materially alter the financial projections based on which such projects found viability. It is essential that appropriate measures are adopted by the concerned State Government to grandfather the promised tax benefits, or at least compensate in some suitable manner for the loss incurred due to implementation of GST.

## Registration

The liability to get registered arises only in the State(s) from where supplies are made. It is therefore essential to identify the places from where supply is made. This determination is straightforward in case of tangible supplies. However, in case of services such as broadcasting, where the content may be uplinked from more than one station in different States, it may be challenging to keep track of the place from which a supply was made. This aspect would be crucial in case of news agencies, advertising companies, event organisers, performance troupes, as also those who hold conclaves, performances and other events in multiple States across the country.

The M & E industry, being predominantly service driven in nature, has also enjoyed the comfort of centralised registration under Service Tax. However, in the GST regime, the compliance cost would go up as registration would be required in each State from where a supply is made. Accounts and records would also have to be maintained at each location and multiple returns would have to be filed instead of the bi-annual Service Tax returns.

## Place of supply

The concept of place of supply has been defined by Parliament in order to determine whether a supply is intra-State, inter-state, an import into the territory of India or an export from the territory of India.

Service tax, being a tax levied by the Centre, and applicable to the whole of India (except J&K), did not require a determination of its place of provision within India. The need for place of provision in the current regime arose only in the context of an import or export of services. By contrast, the place of supply is essential under the GST to determine whether a transaction qualifies as intra-state or inter-state, and what taxes (CGST/SGST or IGST) would be leviable and in which State.

The default rule for place of supply of service (typically, the location of the recipient), would apply to the M & E industry except in case of certain special rules elaborated below. Various transactions, such as grant of IPR and other rights (such as theatrical rights and television rights) would fall under the default rule. Where the supplier is outside India and the recipient within India, such a grant of rights will typically be treated as an import of service; where the recipient is outside India and the supplier within India, such a grant of rights will typically be treated as an export of service.

Supply of services which are related to an immovable property, the place of supply of service would be the location where the immovable property is situated. For instance, Multiplexes availing the services of foreign architects to design the cinema halls, would be liable to discharge GST in all States where such

cinema halls are located under reverse charge mechanism.

In terms of the special rules, the place of supply of services provided by way of admission to a cultural, artistic, sporting, scientific, educational, entertainment event or amusement parks shall be the place where the event is actually held or where such park or other place is located. Events of all types are covered by this provision, including live performances, concerts, competitions, conferences etc. This provision is akin to that under the existing Service tax laws with respect to event-based services. These services are mostly B2C in nature and hence revenue would accrue to the State wherein these events are conducted. However, this poses a very intriguing problem as to whether services have been provided "from" such place where the event is held. In case the answer to this question is in the affirmative, the service providers such as cinema operators, amusement park operators etc. may have to obtain registration in each State where these services are provided from, subject to the threshold limits. This would entail huge compliance costs and wide exposure to scrutiny by officials of each State where registration is obtained.

However, the place of supply of services provided by way of organisation of cultural, artistic, etc. event, including supply of services in relation to a conference, fair, exhibition, celebration or similar events, or services ancillary to such organisation or assigning sponsorship to such events:

a. To a registered person, shall be the location of such person;

b. To a person other than registered person, shall be the place of event, or if the event is held outside India, shall be the place of the service recipient.

Event management services and sponsorship for events will fall under this rule. Further, where the event is held in more than one State or Union Territory, then place of supply of services shall be taken in each of the respective States or Union Territories in proportion to the value for the services separately in terms of the contract. This may prove difficult, unless suitable rules are provided for such pro-rating.

The place of supply for broadcasting services, cable and Direct to Home ('DTH') television services would be determined based on the location where the cable connection or dish antennae in installed for receipt of services. Direct to Home ('DTH').

In case of online entertainment services, such as digital streaming, downloading of music, online games etc., if these services are provided by a person located in a non-taxable territory and received by a B2C recipient in India, the supplier of services must appoint a representative in India to register and pay the GST. This position was recently introduced under the Service Tax and is being continued into the GST era.

## Liability to pay tax

Normally, the service provider is liable to pay service tax to the Government. However, in case of certain supplies of goods or services or both, the tax is to be paid on a reverse charge basis by the recipient or any other designated person. In terms of the drafts released by the GST Council, the following services in relation to the M & E industry have proposed to be covered under the reverse charge:

a) The temporary transfer of copyright relating to original literary, dramatic, musical, or artistic work – the liability for discharging the tax will fall upon the service recipient, i.e. the publisher, music company or producer.

b) Sponsorship service when provided to body corporate or partnership firm located in taxable territory – the liability to pay GST is on the service recipient.

Apart from the above, the GST law also provides for a "catch-all" reverse charge for any supplies made by an unregistered person to a registered person, whereby the registered person will need to discharge the GST under reverse charge. This may apply in the M & E industry where,

for instance, there are contracts with individual artists or freelancers who may not be GST-registered.

## Input Tax Credit

The GST law in India enables seamless flow of credit across States through a settlement mechanism between the Centre and the States, maintained by the GSTN. The M & E industry, owing to non-fungibility of Central and State taxes under the existing regime, faced some blockage of credit. For instance, no taxes (e.g. Service Tax discharged on the fees paid to artists and technicians) could be offset against output Entertainment Tax, and these inevitably became part of the cost of goods supplied. As another illustration, multiplex operators are unable to offset Service tax on inward supplies as they pay Entertainment Tax and VAT on a significant portion of their revenue.

In the GST regime, the various players in the industry would be eligible to avail Input Tax Credit, since their output will be leviable to GST. Due to the seamless flow of credit, the cost of goods and services is likely to be reduced over a period of time. The multiplexes will also be able to claim credit for the GST paid on a host of services used by them such as property rent, housekeeping and security.

Similarly, DTH operators who pay several duties including SAD on their set top box imports, which were not creditable today, will be able to claim the IGST paid on imports as Input Tax Credit under GST.

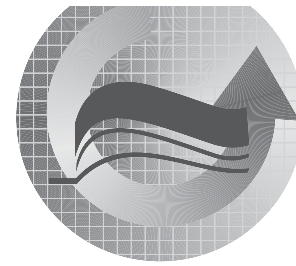
## Anti-profiteering measures

The ambitious anti-profiteering measure introduced in the GST law requires the taxpayer to pass on any benefits to consumers, which accrue due to a reduction in tax rate or increased benefit of input tax credit. This is to be carried out by factoring in these elements into the price of goods or services. The law also provides for the designation of an authority to regulate whether the industry passes on the benefit of GST to its consumers.

Once the anti-profiteering measures kicks into play, it may prove difficult for companies to explain increases in prices. A still more onerous task will be to separate the impact of reduction in rate of tax and benefit of enhanced input tax credit, from other market forces which include demand and supply forces, operating costs, higher input costs etc. Taxpayers would therefore require detailed cost records and variance analyses to justify any increases in price points under the GST regime, especially where such supplies are end-consumer facing. Key action point today is to analyse all the input taxes paid and identify which input taxes would be subsumed into GST and enter the credit chain. The benefits on account of enhanced input tax credit must be quantified for appropriate action when the detailed anti-profiteering laws are notified.

## Conclusion

GST may eliminate persistent disputes and the resultant scourge of double taxation under the current regime, resulting in a reduction in litigation, as several long contentious issues for the M & E industry are addressed by the GST provisions. Certain vexed issues under the existing laws, may, however, continue to persist into the GST. For instance, the position on the taxability of revenue share models between distributors and exhibitors and has not been specifically provided for under the GST, and remains unclear. Similarly, while all licensing of IPR (whether exclusive or non-exclusive) will be treated as service under GST, the issue of whether or not permanent assignment of IPR will constitute a supply of goods, remains open. Given that the M & E industry services consumers across all segments, it is important that sufficient attention it devoted to compliance with the anti-profiteering measure.



CA Jatin Christopher & CA S. Venkataramani

# Impact Study on IT Sector & IT enabled services

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

## 1. Preamble on IT-ITeS Sector

1. Information Technology sector secures a place of pride for India in the world and has carried forward India's industrial prowess into the 21st Century. GST as is hailed, has ushered a profound change in indirect tax reporting and compliance and in administrative transparency as well. One part of India's IT sector is the IT-enabled services (ITeS) community. This community exports services and it comprises not only of Captive Offices for multinational - technology and conventional businesses, but also home-grown pioneers and niche market operators. Domestic consumption is making strides but exports continue to be ahead. Ministry of Information Technology that now administers the policy and benefits of Software Technology Park scheme has done yeoman service since late 80's.

2. GST is a significant tax and game changing reform for the Indian economy and industry at large. From an origin based taxation system to a destination based one, businesses have to overcome the challenges to avail/gain the benefits that the GST regime proposes to extend. Importantly, the countenance of the transition involves many seen and unseen challenges having an impact on the cash-flow, profitability, revenues and policy framework which require businesses to devise a process to embrace GST from the appointed day.

3. Issues and challenges in a GST regime can be broadly classified into three parts – from the perspective of the Government, the Stakeholders and the common man.

- The Central and State Governments are grappling with the challenges of design aspects, rates of levy, drafting the law, rules, forms, notifications, constitutional framework, laws relating to Union Territories, date of introducing GST, education and training of their own staff and officers;
- The stakeholders are yet to come to terms with the complexity of several laws merging into one single legislation;
- The common man is buoyed to believe that there will be a "one nation one tax' regime and is not in the know of how the GST law is being implemented.

This article briefly provides an insight into the issues and challenges in GST on the IT and ITeS sectors.

## 2. Government support

It is important to note that IT and ITeS sectors have received considerable encouragement for the last 2 decades by way of Government Policies (both Centre & States) on the ground that they are net Forex earners and employment

creators. Several tax policies were put in place for the IT/ITeS sectors to make them export competitive.

## 3. Implementation Challenges

1. GST would be a single tax on goods and / or services and would be implemented on the principles of being a destination based consumption tax. These are significant deviations from the current scheme of taxation. Under the current scheme of taxation, there are multiple transaction taxes including but not limited to Customs duty / Special Additional Duty (SAD) / Countervailing duty (CVD), surcharges and cesses on import of goods, Central Excise on manufacture of goods, Service tax on provision of services, Value Added Tax (VAT) / Central Sales Tax (CST) on sale of goods, Local body levies such as Octroi / entry tax on causing entry of scheduled or notified goods in a local area for consumption, use or sale therein, luxury tax on providing luxury and lastly entertainment tax on amusement, taxes on lottery, betting and gambling etc. The new law must also take within its ambit the various exemptions granted to units either under the Excise or under the State Level VAT laws.

2. GST which would be a destination based consumption tax. tax would flow to the State where the goods and / or services are finally consumed. Accordingly, the challenges lie in implementation which involves ascertaining design changes, policy changes, procedural changes, process changes, impact on cash flows, compliance requirements etc. An attempt is made in this paper to explain a few challenges.

## 4. Procedural and policy changes

4.1 The process of implementation involves forming a committee of all the functional areas including but not limited to procurement, pricing manufacture, inventory, human resources, contracts, finance, tax, legal departments, logistics including supply chain, information technology, customers and vendors of goods and / or services, etc. This would enable various divisions of the business to understand the potential impact of GST which may consequentially require process / policy changes to optimise benefits of GST. This measure would largely depend on the nature of business, geographical area, volume of operations and the manufacturing cycle.

## 5. Impact on cash flows

5.1 To perceive the impact on cash flows, the real time transactional data for the previous year should be considered as the base. While the cash flows under the current tax laws could operate as a base, GST ought to be super imposed on the same to analyse and understand its impact. For instance, while stock transfers in a VAT regime does not envisage any tax outflows (other than input tax credit restrictions) it could well be subjected to IGST, envisaging huge tax outflows.

5.2 Each of the impact areas must be analysed and the tax cost should be determined for different situations (alternatives). The incremental administrative cost and outflow in terms of capital including the cost of process / policy changes should also be analysed and worked out. The simulation exercise and the cash flows impact would form the basis for decision making notwithstanding business compulsions.

5.3 Since, the decision is based on the transactions for previous years, there may be challenges to consider and one needs to analyse and understand the repercussions in relation to external factors viz., impact on allied laws, customer behaviour, competition, price fluctuations, market demands, etc., post the appointed date.

## 6. GST impact

a. GST impacts all businesses and every aspect of each of the business on a standalone basis and ITeS is no stranger to the effects of GST. Understanding the impact areas of GST can be overwhelming

and one efficient approach is to separate the impact areas based on the readiness of the issues to be addressed now and those that are best addressed near about the appointed date.

### b. Review of past cases

Litigation serves two purposes –

1) It questions the misapplication of law; and
2) It secures a binding precedent for the future.

Although every tax-payer believes in his innocence, misapplication of law is not always by tax administration. With the imminent introduction of a tax regime that completely alters the rule of law prevalent in current regime, it is important to review the pending cases whether the purposes that guided in pursuing these cases will be fulfilled at all. If not, withdrawing pending cases may score high on prudence. Cases contested on account of long-pending statutory forms could be one where admitting the inevitable displays prudence. Another case could be a demand of service tax on import of services relating to manpower supply from associate concerns outside India. Even with well-reasoned decisions of the Tribunal, there is no let-up in these cases. Angered by the frivolity of the case made out, they have been vehemently contested but still these have reached the Tribunal stage and are pending adjudication. While lower authorities appear to have a propensity to confirm high-stakes notices, sometimes Tribunals are too. Now, any adverse order, after appointed date, by the Tribunal (and client is or may be uncomfortable with a revision petition) the demand would have to be paid-up and without the benefit of credit of this tax paid due to lapse of time under section 140(1) of CGST Act. A decision may be taken about continuing the litigation but paying-up and claiming credit in the ST3 to be filed for Apr-Jun period may be an option.

### c. GST Registration

Not only should the ITeS enterprise obtain registration, but out of self-interest, immediately engage in discussions with suppliers – landlord of premises or caterer etc., – join in the migration process. ITeS enterprises do not always operate from a single location. Multi-locational delivery centers are common approach to de-risk any location-specific eventuality that could disrupt continuity of work and customer commitments. Registration, therefore, will be required of all those locations in different States. Once registered, several matters are to be attended relating to inter-branch activity – work-contribution identification, valuation and (internal) billing – are inescapable.

### d. Input Service Distributor (ISD)

ISD in service tax is not the same as in a GST regime. With the introduction of inter-branch supply of services in GST, ISD may need to be carefully considered/ evaluated whether it is available to ITeS enterprises to leverage.

### e. GST Strategy

GST by its very design is meant to bring prices down due to the removal of tax-cascading which is however, subject to several legal bottle-necks and restrictions & conditions. So, even without undertaking an exercise to extract newly-creditable taxes (such as excise credit to traders, etc.) contained in inventory, the price-lowering effect of GST is noticeable.

***Example: Invoice issued by a manufacturer***

**Current Tax Regime**

| INVOICE | |
|---|---|
| Name of Buyer: ABC (P) Ltd. | Invoice No. |
| Address: | Invoice date |
| **Description** | **Amount (Rs.)** |
| ANYTHING TAXABLE | 100,000 |
| **Sub-total** | **100,000** |
| Excise duty @ 12.5% | 12,500 |
| VAT @ 14% | 15,750 |
| **Sub-total** | **128,250** |

**GST Regime**

| INVOICE | |
|---|---|
| Name of Buyer: ABC (P) Ltd. | Invoice No. |
| Address: | Invoice date |
| **Description** | **Amount (Rs.)** |
| ANYTHING TAXABLE | 100,000 |
| **Sub-total** | **100,000** |
| CGST @ 9% | 9,000 |
| SGST @ 11% | 11,000 |
| **Sub-total** | **120,000** |

And if one were to investigate further, then the inevitable savings would also be that the excise duty paid on the inputs-in-stock must be recovered by the supplier (credit allowed u/s. 140(3)) and the revised cost be applied in the supply after appointed date.

***Example: Invoice issued by a distributor (receiving back-end incentive from manufacturer)***

**Current Tax Regime**

| INVOICE | |
|---|---|
| Name of Buyer: ABC (P) Ltd.<br>Address: | Invoice No.<br>Invoice date |
| Description | Amount (Rs.) |
| ANYTHING TAXABLE | 112,500 |
| Sub-total | 112,500 |
| Excise duty | — |
| VAT @ 14% | 15,750 |
| Sub-total | 128,250 |

**GST Regime**

| INVOICE | |
|---|---|
| Name of Buyer: ABC (P) Ltd.<br>Address: | Invoice No.<br>Invoice date |
| Description | Amount (Rs.) |
| ANYTHING TAXABLE | 100,000 |
| Sub-total | 100,000 |
| CGST @ 9% | 9,000 |
| SGST @ 11% | 11,000 |
| Total | 120,000 |

It is imperative that the ITeS enterprise notify all suppliers (traders) to ensure they take steps necessary to recover non-creditable taxes that are now made creditable by section 140(3) and then supply at reduced prices after appointed date. It is reasonable to expect that a supplier would be reluctant to make the efforts required to recover the taxes ***hidden in the costing*** only to pass it on to the enterprise. Not only is there ***prima facie*** reduction in purchase value of same goods and services, but there is a deeper level of reduction due to recoverability of hidden taxes.

Moving on the cost reduction to operational areas, GST will require transparency of activities on real-time basis. While taxable supplies have to be reported on the Common Portal, even dispatches other than supply have to be reported on Common Portal. GST does not support procrastination. It is well understood that outward supplies have to be reported by 10th and these have to be validated by 15th and any rectifications have to be addressed by 17th in order to file the monthly return by 20th.

***f. Service providers***

Surely, no one hopes to be able to keep these timelines by carrying out the verification from 11th and complete it by 15th. Using the services of an approved GST Suvidha Provider or an ASP (Authorised Service Provider who will also track down reconciliations) is (practically) inevitable. Those resisting this pressure to work with a GSP / ASP will come around after a few stressful days between 11th and 15th. But prudent-others will embrace the role of GSPs / ASPs recognising the efficiencies that will be derived by the convenience of mid-month validation-matching of inward supplies to escape the imminent stress of month-end exercise. If anyone is concerned about confidential information residing in the cloud-services of private GSPs / ASPs and is pessimistic about the controls placed by the Government before approving various GSPs / ASPs, in this day and age, all of us have already allowed intrusion into our private space by our extensive digital footprint in the internet by relentless use of social media. It is to be well borne in mind that these services would be at a cost and for all we know GST may be levied on procurement of such services as well.

***g. Book-keeping and audit***

In light of the understanding of the GST legal requirements, book-keeping will therefore need to be strengthened to accommodate the demands of GST. Tax administration will use business intelligence in the GSTN to query activities in the enterprise. State-wise accounts and GST-audit every year will require a major overhaul in the SOPs followed by the keepers-of-books. This one-time burden of upgrading accounting processes cannot be expected to be shouldered by big-budget ERP. ERP will only handle large volume of data but requires efficient process mapping. Unless the ERP is also GSP, enterprises will require an IT-bridge to connect seamlessly with GSTN (see FAQs on GSP on www.gstn.org). The illustration below provides (one possible sequence of) journal entries for inward-outward supplies in GST:

| Accounting | Inward Supplies | | | | Outward Supplies | | | |
|---|---|---|---|---|---|---|---|---|
| **Plain vanilla** | Purchase-Consumption | Dr | 100 | | Customer account | Dr | 236 | |
| | CGST Credit account | Dr | 9 | | Sales-Income-Revenue | Cr | | 200 |
| | SGST Credit account | Dr | 9 | | CGST payable account | Cr | | 18 |
| | Supplier account | Cr | | 118 | SGST payable account | Cr | | 18 |
| **With Control Accounts** *(Supplier debited for default, if any and balanced by Control accounts)* | Purchase-Consumption | Dr | 100 | | CGST Control account | Dr | 18 | |
| | CGST Credit account | Dr | 9 | | SGST Credit account | Dr | 18 | |
| | SGST Credit account | Dr | 9 | | Customer account | Dr | 236 | |
| | Supplier account | Dr | 18 | | Customer account | Cr | | 36 |
| | Supplier account | Cr | | 118 | Sales-Income-Revenue | Cr | | 200 |
| | CGST Control account | Cr | | 9 | CGST payable account | Cr | | 18 |
| | SGST Control account | Cr | | 9 | SGST payable account | Cr | | 18 |
| **Payment** *(Reverse any balance in Control accounts once post-supply conditions met)* | Supplier account | Dr | 118 | | Bank account | Dr | 236 | |
| | CGST Control account | Dr | 9 | | Customer account | Dr | 36 | |
| | SGST Control account | Dr | 9 | | CGST Control account | Cr | | 18 |
| | Bank account | Cr | | 118 | SGST Control account | Cr | | 18 |
| | Supplier account | Cr | | 18 | Customer account | Cr | | 236 |
| **Adjustment** *(Credit to defer or refund or utilize; carry forward only when no outward supply)* | CGST deferred/refundable | Dr | 9 | | CGST payable account | Dr | 18 | |
| | SGST deferred/refundable | Dr | 9 | | SGST payable account | Dr | 18 | |
| | CGST Credit account | Cr | | 9 | CGST Credit account | Cr | | 9 |
| | SGST Credit account | Cr | | 9 | SGST Credit account | Cr | | 9 |
| | | | | | GST Cash Deposit | Cr | | 18 |
| **GST-default** *(RCM by non-defaulting party)* | CGST Control account | Dr | 9 | | | | | |
| | SGST Control account | Dr | 9 | | | | | |
| | GST Cash Deposit | Cr | | 18 | | | | |

IGST accounts on same principle (not included in illustration above)

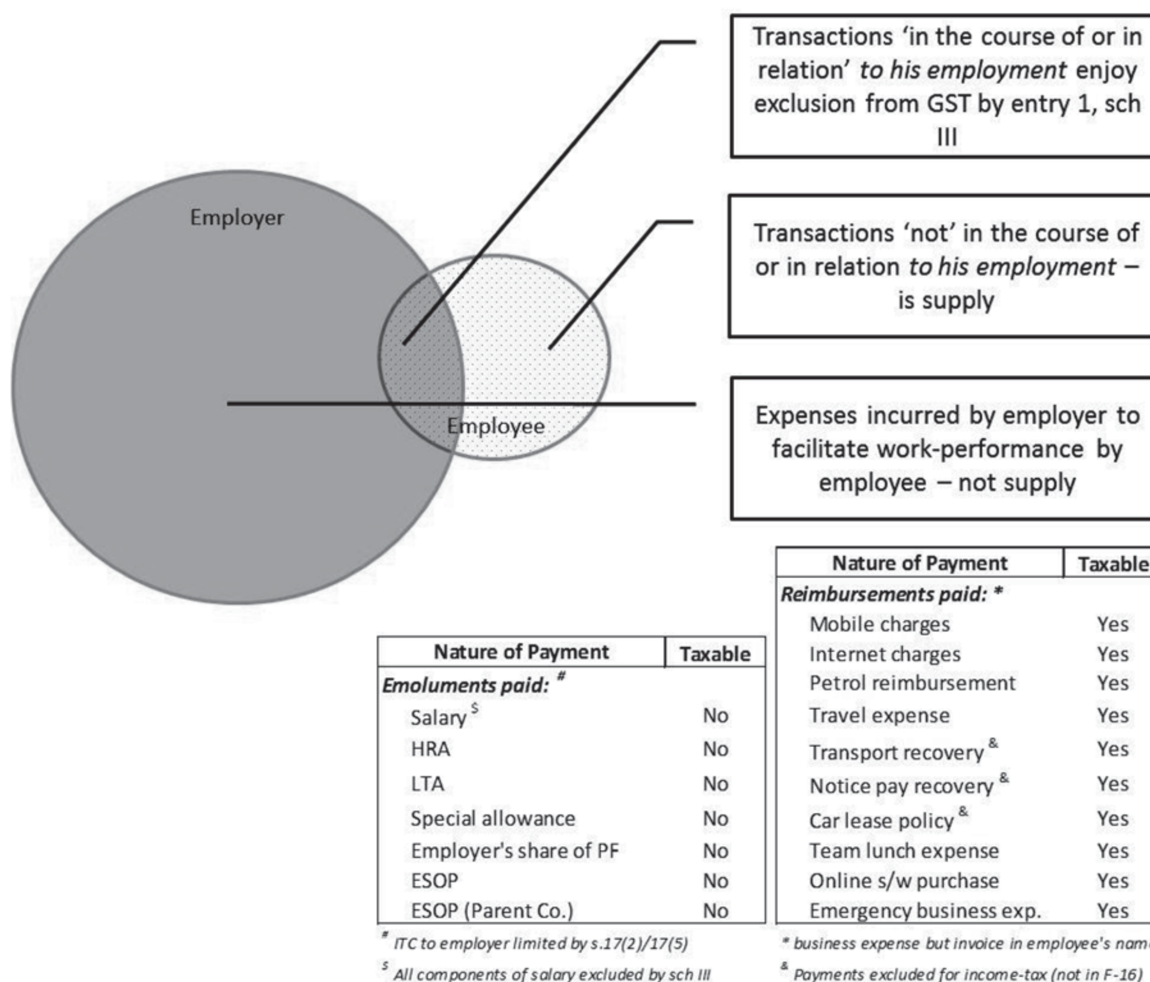
In case credit partly available, add non-creditable portion of tax paid to inventory and reduce from Control accounts without change in dues to supplier

In case of default in payment towards supply (value + GST), reversal of credit availed by Customer but GST on outward supply remains

Readers may add or modify the various control accounts to suite their requirements. But the need to review even journal entries in GST is inevitable. It is important to mention and understand that such tax credit accounts need to be maintained separately for each State / Union territory that the entity operates in.

### *h. Employer-employee transactions*

Shifting our focus to transactions between employer-employee, which is multi-dimensional in ITeS enterprises, it is visible that there are many monetary transactions between an employer and employee that is not accounted as 'salary and benefit' and duly subject to TDS u/s. 192 of Income-tax Act. Flow of emoluments pursuant to the employer-employee relations is excluded from GST by schedule III. But, there are admittedly several transactions that do not appear in Form 16 and not accounted as 'salary and benefits'. These are accounted as 'business expenses' of the employer but how can such payments (even if only actual reimbursement) enjoy the exclusion by schedule III. Entry 1, in schedule III is very specific – services of employee to employer 'in the course of or in relation' to his employment – and this exclusion should not be misunderstood as an immunity from GST for every transaction between them. Section 9(4) relating to reverse charge requires the registered person to pay tax on supplies from a supplier "who is not registered' (lawfully by threshold or non-business supply, or unlawfully by failing to register). Transactions that are not 'in the course of or in relation to' his employment, will attract section 9(4) making the employer liable to pay GST on reimbursement of mobile bill, team lunch, travel expenses, etc. where the actual supplier does not issue the invoice with the GSTIN of the employer.




| Nature of Payment | Taxable |
|---|---|
| ***Emoluments paid:*** # | |
| Salary $ | No |
| HRA | No |
| LTA | No |
| Special allowance | No |
| Employer's share of PF | No |
| ESOP | No |
| ESOP (Parent Co.) | No |

# *ITC to employer limited by s.17(2)/17(5)*
$ *All components of salary excluded by sch III*

| Nature of Payment | Taxable |
|---|---|
| ***Reimbursements paid:*** * | |
| Mobile charges | Yes |
| Internet charges | Yes |
| Petrol reimbursement | Yes |
| Travel expense | Yes |
| Transport recovery & | Yes |
| Notice pay recovery & | Yes |
| Car lease policy & | Yes |
| Team lunch expense | Yes |
| Online s/w purchase | Yes |
| Emergency business exp. | Yes |

* *business expense but invoice in employee's name*
& *Payments excluded for income-tax (not in F-16)*

Therefore, any payment made by the employer to employee that is not accounted as 'salary and wages' could potentially attract incidence of GST due to section 9(4) read with section 31(3)(f).

### *i. Last Returns*

The last returns to be filed under the current tax regime under the laws that stand subsumed into GST is crucial and it will have to be prepared with great care and diligence because the closing balance of credit will transition as GST credit. It is not uncommon for ITeS enterprises to have accumulated large amount of VAT/CENVAT credit and this credit balance is relatable to:

- Credit on doubtful input services which is availed-but-not-utilised to avoid inadvertent write-off of credits that may be held as allowable by a Court decision;
- Credit carried forward without properly complying with reversal of credit on account of Rule 6(3) and 6(8) of CENVAT Credit Rules where it is applicable;

- Credit refundable on account of export of services under Rule 5;
- Credit availed in inputs without reversal under partial rebating scheme under respective VAT laws;
- Similar credits would have to be considered even in respect of VAT laws.

Hence, it is time to sanitise closing balance of VAT-ST credit in the last returns to be filed before transition into GST. Refundable credits need not be carried forward but refund to be claimed under the current law even after appointed date needs to be. Section 143(3) permits refunds filed 'before, on or after' appointed date to be processed under repealed laws, respectively. Consequence of carrying forward some doubtful credits is that, it may be found to be a case of excess credit carried forward attracting liability to interest under section 50(3) of the GST laws. Such consequence would not be experienced if refund is claimed under the repealed laws.

***j. First Returns***

All the training and IT-tools that have been put in place in preparation of GST introduction, will come to be tested in the first returns. New transactions like inter-branch bill on internal transfer price and monitoring payment of tax by supplier in order to validly avail credit needs some learning. Expecting that the first returns will be smooth is only an overestimation of our abilities. It is a process of learning and those willing to learn will stabilise over the months following the introduction of GST.

## 7. Anti-profiteering in GST

Inquiry into margin earned by inaccurately presenting creditable taxes by deliberate devices to yield windfall gains at the expense of the customer is the objective of section 171 on anti-profiteering. Who is this authority? How will the authority make this determination? Will anti-profiteering factor in cost increase that coincides with the introduction of GST? These are the questions that beckon us to address. The power vested in this authority is scary and when scary provisions are found in the law, one of two things usually happen – high-handedness will surface only to be quelled by Court intervention or the erosion of trust that such high-handedness produces will leave this provision to gather dust by disuse. While this may have been the past, one must admit that GST is unlike anything we've seen in the past. So, why shouldn't the authority address anti-profiteering in a manner befitting the 21st Century legislation that GST promises to be? Let's hope it will.

While, claiming transition credit is almost a commercial necessity because customers would presume this would have been done and correct as per-GST PO values, let us revert to how this inquiry on anti-profiteering would be undertaken.

Following are the inevitable steps involved in anti-profiteering inquiry:

a. Profit determination – Based on the quantum of 'eligible duties and taxes' that would have been paid on inventory at each point in the supply chain, a reasonably accurate picture can be formed of the potential extent of profiteering that is possible in each product class, based on the number of intermediaries involved and the location of the person

b. Comparable prices pre-post GST – In order to make the allegation, there must be a ***prima facie*** case of profiteering. That is, the price charged after introduction of GST may remain same or increased in spite of the cost-reducing effect of GST. The extent of this effect may vary in each industry and nearly no industry can claim cost-neutral effect because of the large number of non-creditable taxes involved in each industry that is being subsumed into GST

c. Cost increase – Due introduction of GST increase in administrative effort is to be

determined so that the cost-reducing effect is not one-sided in the inquiry

d. <u>Injury determination</u> – With the above information, a fairly accurate 'injury model' can be constructed across each GST-rate matrix. Now, a thumb rule will emerge as to the 'target' price reduction due to GST which can be compared with the actual post-GST prices charged. Based on this calculation, proceedings to prosecute can be taken up. Perhaps a small tolerance could also be allowed for this deviation due to any non-standard factors

e. <u>Passing of orders</u> – After determination of extent of injury a non-perpetual order restoring the extent of profiteering carried out by the supplier must be notified in order to give effect to the findings in this inquiry

This may be one possible approach that a fair and equitable inquiry can involve. Now, the challenge shifts away from trade and towards tax administration. How will the anti-profiteering authority be able to undertake this kind of exercise and conclude the inquiry with a tangible finding against the supplier for profiteering. When all are so busy (the Government too) in trying to make sense of it all and get ready before July 2017, surely this 'fair and equitable' approach is what anti-profiteering will need to be to make us the nation that has this one-of-a-kind tax reform.

Based on the ambiguity in the definitions of Goods and Services defined under the CGST Act in clauses (52) and (102) of section 2, classification of software first requires a determination of whether software is goods or services.

Based on the SC decision in ***TCS vs. State of Andhra Pradesh 9137 STC 620), it would become goods provided it has the attributes thereof having regard to (a) its utility; (b) capable of being bought and sold; and (c) capable of being transmitted, transferred, delivered, stored and possessed.***

Accordingly, packaged software is certainly goods and when an article is classified as goods it does not also qualify as a service. Although currently the practice is to impose VAT 'and' ST on sale of software for the risk of demands by either department due to the expansive language used in the current law. GST addresses the mutual exclusivity of these two classifications without allowing room for any overlap. While there may be debate about customized software, the SC decision and the exclusivity of tax on goods and services in GST leaves no scope for GST to be applied twice – once as goods and once as services.

The tabulation provides brief of tax on various transactions involving software:

| Software Transaction | Taxes Applicable | Remarks |
|---|---|---|
| Import of packaged software (physical) | BCD + IGST | Physical import of goods requires to be assessed by Customs by section 5 of IGST Act |
| Import of packaged software (non-physical) | IGST | Non-physical import of software liable to payment of IGST on reverse charge basis by section 9(3) read with 7(1)(b) |
| Export of packaged software | Zero-rated | No IGST payable by section 16 of IGST Act |

| Software Transaction | Taxes Applicable | Remarks |
|---|---|---|
| Export of software services | Zero-rated | Same as above. Export of services conditions to be satisfied |
| Supply of packaged software (within India) | CGST-SGST or IGST | Taxable as goods; right-to-use is involved in all goods supplied |
| Supply of services of development of software | CGST-SGST or IGST | Taxable as services (entry 5(d), sch II) |
| Customisation of software already developed and supplied separately | CGST-SGST or IGST | Taxable as services (entry 5(d), sch II) |
| Installation of software already supplied | CGST-SGST or IGST | Taxable as services (entry 5(d), sch II) |
| Supply of manpower (for software development) | CGST-SGST or IGST | Taxable as services under section 7(1)(a) |
| Captive delivery centre in another State for software development project in different State | CGST-SGST or IGST | Inter-branch supply of services under 7(1)(c) read with Entry 3, sch I |

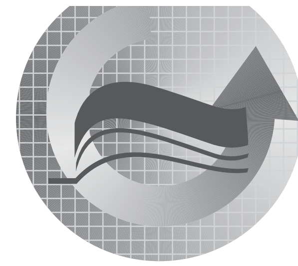
Finally, it merits to mention that entry 5 (c), 5 (d) and 5 (f) all appear to be applicable with respect to transactions involving software but it must be borne in mind that each entry has its own exclusive sphere of applicability and the existence of elements from each entry cannot draw the whole entry to cover a transaction. The substance of the supply must make up the pith of the entry for its applicability.

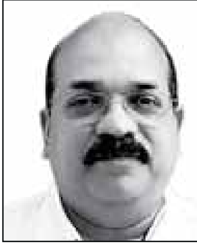
## 8. Conclusion

Let us hope that the collective wisdom that has brought us so close to herald this new tax regime will come to bear and we as professionals are able to support industry in making this transition into GST efficient. The challenges enumerated in this paper are indicative and not exhaustive. The challenges in a GST transition would depend on the nature of the industry. The process of transitioning into GST may involve certain other challenges based on the way the business is conducted. Initiating the process of implementation with an appropriate plan is the only solution to overcome all the challenges in a timely manner and in accordance with law.

We look forward to this game changing reform and how it takes shape on the appointed date. The Government is doing its best for a smooth transition and hoping for buoyant revenues. The stake holders, are rising up to the challenge and are most certainly looking forward to welcoming this game changing reform which will greatly reduce the multiplicity of taxes while optimising compliance costs and requirements. The common man is fairly certain that this change will usher in transparency while lowering the prices of goods and / or services.

Welcome GST !





K. Vaitheeswaran, *Advocate*

# Impact Study on Automobile Industry

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

The Goods and Services Tax Act, 2017 being one of the most significant tax reforms of the country is all set to roll out this July. The Central Government is racing against time to meet the deadline and is making all efforts for the smooth roll out of the Goods and Services Tax regime. More than half the States have passed their respective State GST Bills. The GST Council concluded its 14th meeting on 19th May at Sri Nagar and has indicated the rate of tax for both goods and services except for a very few items.

The GST can make or break businesses and a business which is not ready for change would find the road very difficult to travel. Unlike other GST countries which have a simple design and few rates of taxes, India has chosen to be different and is ushering in a complex regime with multiple rates of tax for both goods and services.

The automobile sector in India is subject to various types of duties and taxes such as Excise Duty, VAT, CST, Entry Tax, Infrastructure cess, Automobile cess, etc. and was looking at GST as a solution for a number of issues. Some of them have been addressed while fresh issues have also been created.

## Cascading Effect and GST

When a car is manufactured in a factory in India and sold within the State of manufacture, the VAT is calculated after adding the excise duty. Similarly where there is an inter-State sale, CST is payable on the price inclusive of excise duty. This cascading effect will be arrested in the GST regime since CGST and SGST would be calculated separately on the price for a local supply and IGST would be the only levy for an inter-State supply.

## Domestic Sourcing Patterns and GST

Most car manufacturers would identify suppliers/ vendors within the State in which their manufacturing facility is located since VAT qualifies for credit whereas CST does not qualify for credit and becomes a cost. This has increased the overall price since the local supplier fixes the price based on demand as well as his increased cost since most of the materials required for component manufacture are also purchased on CST basis. GST would give absolute freedom, both to the automobile manufacturers as well their vendors to procure items from any location since both local procurements and inter-State procurements qualify for credit. In other words, there would be better and optimum pricing in procurements.

## Import Segment and GST

There are two types of imports in the automobile segment. In the first segment, components are imported or vehicles are imported in CKD/ SKD condition and assembled in India. In the first segment the CVD and the SAD are significant cascaded taxes since CVD is calculated after adding BCD to value and SAD is calculated after adding value, BCD and CVD. Eventhough there is a cenvat credit of the CVD and SAD portion, the outflow is significant. In the GST regime, BCD will continue and will form part of cost as in the past but IGST would be the only levy in addition to the BCD and IGST would qualify for credit.

In the second segment, when cars are imported and sold as such within India, as a trader the CVD and SAD forms part of the cost since the trader discharges VAT and does not qualify for CENVAT credit of the CVD and SAD whereas in the GST regime, the trader would qualify for the IGST credit. This would bring down his cost significantly and there would be a consequential increase in trading operations.

## Job Work and GST

Job Work is the back-bone of the automobile industry. In the current system job workers are generally not liable to any indirect tax levy due to different exemption notifications. For example, where an automobile manufacturer engages a job worker for manufacture of components on job work basis, eventhough the activity amounts to manufacture, the job worker is not liable to pay excise duty when the automobile manufacturer follows Notification No.214/86. All that is required is declaration by the automobile manufacturer to the excise authorities of the job worker that the job worked materials would be used in the manufacture of final products on which duty would be payable. Where an activity amounts to manufacture service tax is not payable by virtue of Entry 30(i), Notification No.25/2012. Thus the job worker does not pay excise duty as well as service tax. All the materials required for job work would be provided by the automobile manufacturer and since there is no transfer of property in goods, the job worker is not liable to VAT. Where the job worker is engaged to carry out an activity which does not amount to manufacture, say processing or painting or heat treatment, even though there is a service, the job worker is not liable to service tax by virtue of Entry 30(ii), Notification No. 25/2012.

In the GST regime the biggest challenge for an automobile manufacturer is with reference to compliance by a job worker. The job worker becomes liable to GST and has to charge GST on the job work charges or labour charges; comply with the online filing requirements in order to facilitate proper availability of GST credits for the automobile manufacturer. Since most job workers do not have excise/ VAT/ service tax registration, they would not have migrated to GST and will have to seek fresh registrations after the law is notified. This would mean that there would be a time gap in procurements from job workers and hence automobile companies will have to plan and schedule their job work requirements accordingly.

In the GST regime, the provisions facilitate movement of goods from the automobile manufacturer to the job worker without GST as well as direct delivery to job work locations by vendors identified by the automobile manufacturer. To illustrate, a car manufacturer based in Pune can place a purchase order on a raw material vendor located in Delhi to supply the material directly to a job worker located in Thane. In terms of section 10(1)(b) of the IGST Act, 2017 the Delhi vendor would charge IGST on the automobile manufacturer provided the vendor understands and implements the GST law. The vendor will have to correctly reflect the GSTN number of the automobile manufacturer to facilitate credits for the manufacturer. The job worker will carry out the activity as specified in the work order and charge GST on the job work charges and raise invoices and comply with the GST law.

The following issues are likely to be faced by an automobile manufacturer:

(i) The definition of 'job work' refers to process or treatment undertaken on goods belonging to another registered person. The first issue is in the context of the status as a job worker when own materials are also used. The Supreme Court in the case of ***Prestige Engineering vs. CCE (1994) 73 ELT 497*** has held that addition of minor items by the job worker would not dilute the nature of activity of being job work. Job work when liable to excise duty is subject to a valuation mechanism under Rule 10A of the Central Excise Valuation Rules. In this context the Tribunal in the case of ***Audi Automobiles vs. CCE (2010) 249 ELT 124*** has held that where the principal manufacturer supplies the chassis and the job worker uses substantial other materials, the valuation would still be under Rule 10A which is the selling price of the manufacturer. In other words, the job worker status has not been denied.

(ii) The second issue would be the rate of tax that has to be applied on the materials used. Where the own materials are minor or insignificant, it would normally be captured in the negotiated rate for job work. Where the materials are significant, then the rate of tax question can arise if the job work rate is 18% (services) and the material rate is 12% or 28% (goods). If the transaction is considered as a composite supply of goods and services that are naturally bundled, it may be possible to consider service as the principal supply and apply the rate applicable for services. This would be beneficial if the rate for goods is 28% and counterproductive if the rate is 12%. The Industry would implement new business models based on the challenges on account of this including decisions for procurement of all materials by the automobile manufacturer.

(iii) The third issue would be where factory A is in one State manufacturing a component and the component is sent to factory B in the same State for carrying out a process and subsequently sent to factory C in the same State for assembling of the vehicle and all the factories belong to the manufacturer. Concepts such as intra-State stock transfers within the same registration not being taxed or treatment of own factory as a job worker would be different models that would be explored by the industry.

## Component Vendors and GST

At present, all the auto component parts used in the automobile industry are subject to MRP based valuation. The GST law does not have MRP based valuation and the vendor of the components would charge GST on the selling price subject to section 15 of the CGST Act, 2017. This would make the entire valuation system uniform and transparent. This also provides relief to the vendor who has a transaction value based system for OEM; MRP based system for dealers; Transaction value based system for items which qualify for exclusion under the Legal Meteorology Act. This also provides relief for eliminating locations such as duty paid godowns; first stage dealer locations; second stage dealer locations; CENVAT credit management where both manufacturing and trading is carried out by the vendor.

While the vendors for components would see significant ease of business on account of various changes referred to above, dealing with thousands of vendors will create its own problem for the automobile manufacturer, since the life line of GST which is the GST credit is linked with the vendor paying the tax; uploading correct date and filing the return. This might affect the cash flow of the vendors since automobile manufacturers would implement stringent requirements for vendor acceptance and would also explore scaling down and reducing the number of vendors.

## GST Rates

The current tax structure for a manufacturer who manufactures and sells automobiles in Tamil Nadu and the proposed GST structure for the same transaction is set out in the following table:

| Vehicle Category | Current Rates | | GST Rates | |
|---|---|---|---|---|
| | Excise Duty* | TNVAT | GST | Cess |
| Small cars under 4m | 12.5% | 14.5% | 28% | 1-3% |
| Length > 4m but engine capacity less than 1500cc | 24% | 14.5% | 28% | 15% |
| Length > 4m and engine capacity more than 1500cc | 27% | 14.5% | 28% | 15% |
| SUVs/MUVs (length > 4m, engine capacity >1500cc and Ground clearance > 170mm) | 30% | 14.5% | 28% | 15% |
| Two Wheelers | 12.5% | 14.5% | 28% | NA |
| Three Wheelers | 12.5% | 14.5% | 28% | NA |

*Further certain vehicles falling under Chapter Heading 8703 in the current regime attracts infrastructure cess of 4% and the cess is subsumed in GST.

## GST Compliance

GST is a tax based on supply. Every supplier is to be registered in every State from where he makes a supply. Hence compliance costs would increase. Further registration in each State would imply filing of returns, maintaining books of account, etc. An analysis of the draft rules indicates possibly 61 filings per State, taking into account outward supply filing, inward supply filing, monthly return, annual return, TDS Return and ISD return.

## Benefits for a manufacturer under GST

While the cost in compliance is bound to increase, the sector is likely to see certain advantages based on the following:

(i) Where the majority of the purchases are on CST basis, 2% which is the cost would now become IGST and qualify as a credit.

(ii) Manufacturers would review their depots and godowns and scale down the same since direct inter-State supply to the dealer will not have any credit issues as against the current system.

(iii) The CENVAT credit system has been linked with manufacture leading to litigation on what qualifies for credit. The definitions of inputs and input services linked with business would expand the pool of credit and has the potential to bring down costs.

(iv) The cascading effect of taxes would get eliminated and there would be cost savings on account of business review and leaner and efficient supply chain.

(v) The rates announced have been welcomed by the industry and many have stated that the rates are on expected lines.

## Working Capital Management – Impact of GST

The automobile industry will have to plan its working capital requirements on account of the following:

(i) Huge demands that can arise in completion of CST assessments for the past period by the State authorities specifically where the C Forms/ Form F/ Form H have not been collected.

(ii) CST purchases at 2% would move to a higher IGST rate of 12%/ 18%/ 28%, depending upon the commodity.

(iii) Items purchased from traders which would normally have only VAT would have CGST and SGST. Unless the prices have come down in the procurement, the CGST would be an additional outflow.

(iv) Higher cash outflow on account of increase in tax rate even though credit would be available.

(v) Higher cost of compliance on account of vendor management pertaining to input tax credit.

(vi) There would be taxes on advances even for goods which is not applicable in the current dispensation.

(vii) Higher cash outflow on account of transaction such as job work being subjected to tax.

## Automobile Dealers and GST

In so far as automobile dealers are concerned, the GST charged by the manufacturer will qualify for credit as against the current system where the credit is not available in respect of excise duty. IGST purchases would qualify for credit as against the current non-availability of credit on CST purchases. There would be an increase in direct billing from the manufacturing location as against billing from depots. Further a dealer would now see better credits since the GST paid on services would qualify as credit which can be set off against the GST payable on the supply of automobiles.

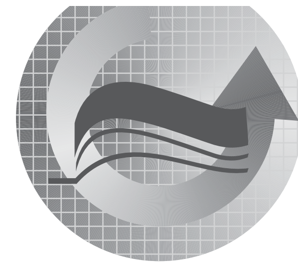
## Used Car Dealers and GST

The used car market has breathed a sigh of relief since a used car dealer cannot get an invoice from the owner of a car who sells the car nor the used car dealer expect the individual owner of a car to charge GST and comply with the GST requirements. The value addition would be very minor in the form of refurbishing and other services and ultimately the car would be sold with a small margin. Rule 5 of the Valuation Rules as approved by the Council indicates that the value of supply in respect of used goods would be the difference between the selling price and the purchase price and in case the value of supply is negative, it shall be ignored.

## GST and the Customer

The biggest relief from a customer perspective would be the subsuming of Entry Tax which was levied by the State on the entry of vehicles into the local area. Many States imposed entry tax even on imported cars on the premise that the goods enter the local area after they crossed the customs frontiers. The customer would also see marginal relief in the small car segment while the luxury cars segment may see some downward pricing.

> There is no help for you outside of yourself; you are the creator of the universe. Like the silkworm you have built a cocoon around yourself.... Burst your own cocoon and come out as the beautiful butterfly, as the free soul. Then alone you will see Truth.
>
> — *Swami Vivekananda*



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# Impact Study on Transport & Logistics sector

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

India set to implement Goods and Services Tax (GST) from 1st July, 2017. Transport and Logistics (T&L) sector is one of the largest service sectors in India and will be the great beneficiary of the introduction of GST in India. The cost of transportation and logistics is very high in India in comparison other countries. It is expected that the introduction of GST will bring consolidation, synergy, reduce transportation cost, transportation time, which will give a boost to this sector. Thus, GST is not a change in tax law but it's a game changer for this industry.

The introduction of GST requires an overhaul in various business functions including but not limited to, Information Technology software, marketing, warehousing, distribution, business process, etc.

The transport/logistics services are currently subject to service tax which is levied and collected by the Central Government. GST law levies Central Government GST (CGST) and State Government GST (SGST) on the supply of goods and services and thus, the services will be also subject to SGST. Thus, the service provider will be required to get registered under the GST law with the respective State Government.

Currently, the service provider is registered under the service tax under the centralised registration system and thus, are only required to file two service tax returns in a financial year. Under the GST law, since the service provider will be required to get registered with State Government, they will also be required to file returns and undertake other compliances under the SGST law.

## Location of Sevice Provider

Unlike other services, the transportation services involve multiple States for the supply of services to the customers. The Shipping/logistics companies either have their own offices or have a presence through their agents etc. in the various States to provides the services to customers and thus, they will require obtaining registration with the State authorities. The GST law also states that a person carrying out business through an agent in the State will be deemed to have an office in the State.

For better understating let's take an example of ocean transportation service, wherein a shipping line undertakes transportation of cargo from Delhi to Germany. The above transportation activities will have various underlying activities [i.e. ocean freight between two sea ports; terminal handling and inland transportation activities in India as well outside India] which will be performed by the service provider.

The transportation of cargo from Delhi [India] to Germany involves inland transportation of cargo from Delhi to Nhava Seva [Maharashtra], terminal handling services at JNPT [Maharashtra], ocean transportation

from Maharashtra [India] to the port located in Germany, terminal handling activities at overseas [Germany] port, transportation from Overseas [Germany] port to the location of the consignee in Germany.

To supply services, the shipping lines normally have offices in multiple States like Delhi, Maharashtra, etc., which undertakes respective activities as discussed above. Furthermore, the supplier of service may have a centralised office to process various documents, another office for processing invoicing and receipts, etc. Similarly, in above example only, shipper/consignor in India may have offices in multiple states from where RFP may be issued, consignment may be dispatched, payment may be processed, etc.

The GST law states that in case the service provider has a presence in more than one State, the most relevant office shall be the place of the service provider.

In such cases, it is practically difficult to determine most relevant office of the supplier and/or recipient of service for a particular transaction and accordingly, to determine as to from which State the invoice for services shall be raised.

Furthermore, in cases where there is a dispute over the place of supply of services, the taxpayer may get entangled in legal disputes. Currently, the GST legislation provides that if taxpayer wrongly pays, say CGST and SGST (on a belief that the transaction is intra-State), instead of IGST, then they will have to pay the correct taxes (i.e. IGST) again and claim a refund for wrongfully paid taxes. Ideally, instead of putting the onus on the taxpayer to determine whether the transaction is intra-State or inter-State, the GST law should provide for a simpler redressal mechanism.

In the entire chain of transactions, there are two critical documents which are issued by the respective offices (i.e. delivery order/Bill of Lading) which are the legal documents for the above activities.

Post-determination of the location of the service provider, the next biggest challenge is, to determine the nature of services [i.e. entire transportation services are one service in this example or there are multiple services involved in the transaction].

## Whether the services would be construed as composite/ mixed supply

The Central GST Act, 2017 defines the term 'composite supply' as the supply of two or more taxable supplies, which are naturally bundled and supplied in conjunction with each other in the ordinary course of business, one of which is a principal supply. A summary of the applicable rate is as follows:

| Services | Rate and conditions |
|---|---|
| Transport of goods in a vessel including services provided or agreed to be provided by a person located in non-taxable territory to a person located in non-taxable territory by way of transportation of goods by a vessel from a place outside India up to the customs station of clearance in India | 5% with ITC of input services |
| Transport of goods by rail | 5% with ITC of input services |
| Services of goods transport agency (GTA) in relation to transportation of goods [other than used household goods for personal use] | 5% No ITC |
| Transport of goods in containers by rail by any person other than Indian Railways | 12% With Full ITC |
| All other services not specified elsewhere | 18% With Full ITC |

The classification of services assumes significance importance since the transportation of goods by the vessel is subject to the lower rate of tax i.e. 5%, whereas the transportation of goods by rail by the container is subject to 12%, and other activities are subject to 18% rate of tax. Thus, the question arises for discussion is whether the entire transaction will be subject to 5% rate of tax applying the principle of composite supply, or whether the different activities will be subject to the different rate of tax.

The service provider issues one transport document (Bill of Lading/Airway Bill) for entire transaction chain, however, the lower rate of tax is only applicable to the transport of goods by vessel. Currently, the Shipping and Logistics Industry is of the view that the above services are not bundled/composite services and thus, the full rate is applied on the Terminal Handling Charges (THC), Inland Haulage Charges (IHC) and other charges.

The position of applying a lower rate of tax to the entire transaction is not immune from litigation and tax authority may demand tax at the higher rate of tax. From a commercial standpoint, the customer will get a tax credit of GST charged by the service provider and customer will be eligible to set off against his output tax liability. Thus, essentially, even if non-freight activities are subject to higher rate of tax, which is as of now as well, the customer will get full credit and may not be impacted.

## Export freight

The IGST Act provides that in the case of services supplied to registered person located in India, the place of supply of service shall be the location of such person in India. Accordingly, in above example of ocean transportation services supplied to the exporter in India exporting goods from India, who is registered under GST; the place of supply of service shall be India. Accordingly, applicable GST shall be levied on export ocean freight and other related activities, which will increase the cash flow to the exporter. The exporter will be required to claim a refund of GST from the respective Government.

In the case of air transportation, an exemption has been granted to inbound air transportation services, however, the outbound air transportation services are subject to the full rate of GST [18%]. The entire transportation Industry has been granted a lower rate of tax [5%], and only, export air transport is subject to this higher rate of tax. Although, the exporter will be eligible for a refund of GST, however, this will have a huge impact on the cash flow as well.

## Tax implication on freight in case of service provided to unregistered customer

The provision of IGST Act further provides that in the case of transportation services provided to the unregistered person, the place of supply of transportation services shall be pickup location. Accordingly, in the case of supply of transportation services to the unregistered customer by Shipping/logistics companies, the import freight may not attract GST as pick up location is outside India; whereas export freight will be taxable since pickup location is in India. The above does not fit well under the principal of the taxation which states that import of services shall be taxed whereas the export shall not be taxable.

## Tax implication on transport of goods by road services provided by GTA

The services provided by GTA is subject to reverse charge mechanism and accordingly, the recipient of services is made liable for payment of GST on the above transaction @5%. The above concessional rate of GST is subject to the condition that the tax credit is not availed. In addition to this, the goods transportation services provided by any person other than GTA has been exempted from GST.

It is worthwhile to note that unlike service tax, the GST law clearly states that exemption provided under the law is mandatory and the same is not optional.

## Services provided to overseas customer

The GST law provides different rules for determination of the place of supply for international and domestic customers. In the case of transport and logistics services provided to the international customer, various activities may be subject to GST due to the fact that these activities are categorised as performance based services (i.e. terminal handling charges). Thus, even though the services are provided to the overseas customer since the place of supply is in India, the above activities will be subject to GST. Furthermore, if the handling activities involve multiple CFS, then the respective tax liabilities will be determined accordingly.

## Services availed from overseas customer

The freight services availed by the logistics companies from their overseas offices or service provider located outside India will also be subject to reverse charge mechanism if the place of supply of services is in India.

For example, in the case of import ocean freight, the destination of cargo is in India, and thus, the above transaction will also be subject to GST under the reverse charge mechanism. In addition to this, the company is required to raise an invoice for the above transaction as well. The GST paid under the reverse charge mechanism will be eligible for a tax credit to the company.

## Container import and movement of container

Temporary import of container for ocean transportation service is exempt from customs duties at present. The fate of the above exemption under the GST regime is not clear since the Exemption Notification(s) for goods are yet to be issued by the GST Council.

The supply of goods and/or service between two distinct offices (i.e. two registered office of the same person in different States) is also subject to GST. Thus, the supply of services/ container by one office of the shipping line to another office will attract GST. In addition to this, the supply of container by a shipping line to its related logistics company will also be subject to GST.

This will cast an onerous task on the shipping line to track each movement of the container and pay applicable GST on the transaction. Furthermore, given the fact that there is various kind of container (20 ft., 40 ft.), Reefer etc., the determination of valuation of the container will also be a challenge.

The Valuation Rules provides a respite to this whole issue by specifying that in case, the recipient is eligible for full tax credit, then the valuation of goods will not be challenged by the tax authority.

## Input Service Distributor

The Input Service Distributor (ISD) mechanism states that a service provider can distribute the credit to other locations subject to the specified conditions.

In the example mentioned above, if Delhi Office raises invoice on the customer, Delhi Office will require paying GST on this transaction. However, the company will also avail port services from JNPT, transportation services from CONCOR etc, for transportation of container. Accordingly, the Mumbai Office will receive invoices from JNPT and CONCOR.

The GST law states that an ISD can distribute the tax credit received by it based on the invoices raised by the vendors to other offices in the specified ratio.

It shall be noted that GST law states that a separate return is required to be submitted for ISD and "ISD-GST ID" is required to be given to the vendor.

Thus, the company will require having a strict system to communicate the different GST ID for different activities to the vendor and accordingly, the vendor shall be instructed to raise invoice on the respective GST ID.

## Services provided by Head Office

The support services provided by the Head Office to the other offices in other States also falls under the definition of the term supply, and accordingly, the same transaction is also subject to GST. The company will require to identify, undertake valuation exercise and pay applicable GST on the above transaction. However, if the recipient State is eligible for a full credit of GST, then the valuation of services cannot be disputed.

## E-Way Bill

Given the fact that entire GST Eco-System tracks each and every invoice of respective buyer and seller, thus, practically, there is no need to have a separate mechanism for tracking the movement of goods.

The GST Council has specified that movement of goods of consignment value of more than INR 50,000/- will require E-Way Bill and accordingly, the supplier will require submitting the necessary information to GSTIN for generation of E-Way Bill.

The E-Way Bill has two parts i.e. the first parts contains invoice information; and the second part contains information for the Trucks, Transit Time, Driver etc. Thus, each movement of goods shall be accompanied with the Tax Invoice/ Delivery Challan and E-Way Bill. An option has been provided that the above document may also be carried in electronic format as well.

The Rules also states that in case the supplier has not generated E-Way Bill, it will be the responsibility of the transporter to generate the E-Way Bill.

In addition to this, any transporter transferring goods from one conveyance to another in the course of transit is required to generate a new E-Way Bill on the common portal in FORM GST INS-01 specifying therein the mode of transport.

In case of multiple consignments are intended to be transported in one conveyance, the transporter is required to indicate the serial number of E-Way Bills generated in respect of each such consignment electronically on the common portal and a consolidated E-Way Bill in FORM GST INS-02 is required to be generated by him on the common portal prior to the movement of goods:

The E-Way Bill generated by any party wherein the goods are either not being transported or are not being transported as per the details furnished in the E-Way Bill, then it is required to be cancelled electronically within 24 hours of generation of the same.

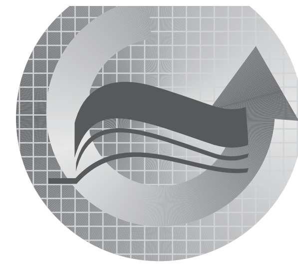
The E-Way Bill Rules also provides that E-Way Bill or the E-Way Bill number may be mapped to a Radio Frequency Identification Device (RFID) embedded onto the conveyance to ensure that smooth transportation of goods.

The above Rules will have huge cost and compliance burden on entire logistics industry since this entire process will involve lot of time and efforts.

## Change in logistics landscape

Currently, due to the existing tax benefits, the companies have established depot in multiple states. Under the GST regime, this situation will change since there will be no tax arbitrage by having depot in multiple States. This may lead to a paradigm shift, wherein the companies may start focusing on the consolidation of warehouses and have bigger warehouses, which will reduce the cost of logistics.

In summary, the GST will cast a lot of compliance burden on this industry, however, it will also provide much-needed boost to this industry in long run.



Jatin Harjai, Leader, J. Harjai & Associates

# Anti-Profiteering in GST – Necessity or Paradox

***"The article takes into account various provisions of GST Laws (including draft laws) as are available in public domain up to 31-5-2017."***

## A. Introduction & Need of Anti-Profiteering Law

We are going to witness biggest indirect tax reform in the history of independent India. However, global trends suggest implementation of Goods and Services Tax or Comprehensive VAT on Goods & Services lead to inflationary conditions in short to medium term economy. Our county being highly price sensitive market, necessarily requires to check whether implementation of new taxation regime should not lead to inflationary conditions or should have minimal impact on it.

Since GST Council has already declared different slab rates to be adopted in GST and all possible efforts has been put in place to ensure that mapping of Goods and Services be on the basis of existing effective industry rate. It is amply clear on the part of the Government, that it is not looking to have higher revenue from GST by charging higher rate of tax on any goods or services. However, effect of increase in tax base, reduced grey economy, and increased GDP will certainly add to the revenue kitty.

Now question arises, why increased inflation be there despite the fact that effective tax rate on all products will be more of less at par with existing rates. It is because the effective rate of tax at the consumer level gets changed immediately at the time of implementation, whereas industry takes time to pass on benefit(s) accrues to it to the consumer level because of many reasons such as unawareness about benefits available, lack of clarity on interpretational issues etc. At times it may be intentional in monopolistic market whereby industry wants to increase its profit by maintaining its selling price and pocketing whole of the benefits.

The same situation arised at the time of implementation of VAT in India. Many industries parked gains accrued to them on account of implementation of Value Added Taxation system and maintained prices till the time they were virtually certain about the gain. After implementation of VAT, Comptroller and Auditor General of India conducted a national study on 'Implementation of Value Added Tax in India' and released Study Report named 'Lessons for transition to Goods and Services Tax' in June, 2010. Relevant extracts from the report is as under:

*"Impact of VAT on prices*

***2.43 The white paper was sanguine that implementation of VAT will bring down the prices of goods due to rationalisation of tax rates and abolition of cascading tax effects in the legacy systems. But there was no system to monitor this impact and ensure that the benefits were indeed being passed on to the common man.***

*2.44 We selected a basket of goods and checked the records of 13 manufacturers in a State in three initial months of implementation of VAT, to check its impact on prices.* ***We found that manufacturer did not reduce the maximum retail prices (MRP) after introduction of VAT though there was substantial reduction of tax rates.*** *The benefit of ` 40 crore which should have been passed on to the consumer was consumed by the manufacturer and the dealers across the VAT chain. The dealers have undoubtedly enriched themselves at the cost of the common man."*

History, as observed by CAG, will repeat again if no legal deterrent is there. Let us understand this preposition with an illustration in case of a trader who purchased goods from a manufacturer:

**Cost Sheet in Existing Tax Regime**

| Description | Amount (INR) |
|---|---|
| Purchase Price of Goods (A) | 1,00,000 |
| Excise Duty on Inputs @ 12.50% (B) | 12,500 |
| Value Added Tax @ 5.50% | 6,188 |
| Total Purchase Price | 1,18,688 |
| Operational Exp. (Business Consumables & Services) (C) | 1,000 |
| Tax on Operational/ Indirect Exp. (D) | 150 |
| Total Cash Outflow | 1,19,838 |
| Sales Price for the dealer (E) | 1,25,000 |
| Output Tax (VAT @ 5.50%) | 6,875 |
| Total Cost to Consumer | 1,31,875 |
| Profit of Dealer (E–A–B– C–D) | 11,350 |
| Total tax whichGovt. has received (CG + SG) | 19,525 |

**Cost Sheet in GST Regime (If consumer prices doesn't change)**

| Description | Amount (INR) |
|---|---|
| Purchase Price of Goods (A) | 1,00,000 |
| GST | 18,000 |
| Total Purchase Price | 1,18,000 |
| Operational Exp. (Business Consumables & Services) (B) | 1,000 |
| Tax on Operational/Indirect Exp. | 180 |
| Total Cash Outflow | 1,19,180 |
| Sales Price for the dealer (C) | 1,25,000 |
| GST | 22,500 |
| Total Cost to Consumer | 1,47,500 |
| Profit of Dealer (C – A – B) | 24,000 |
| Total tax which Govt. has received (CG + SG) | 22,500 |

It is evident from above illustration, that if the prices of the products are not adjusted for the benefits accrued to the supplier, the consumers are going to pay higher price for goods and services and situation will lead to inflationary conditions. In the given case by implementation of GST the dealer is getting benefit of excise duty on goods and VAT/Service Tax on operational expenses, which it should ideally be pass to the consumer. In the illustration cited above (which is in line with study report of CAG), the dealer has not passed on any benefit to the consumer which results in increased cost to consumer and profits of the dealer increased to more than double. This is example of profiteering by dealer due to change in taxation regime and has to be regulated in new indirect tax regime.

## B. Legal provisions for Anti-Profiteering in CGST Act & Analysis thereof

Section 171 of the CGST Act;

*"1. Any reduction in rate of tax on any supply of goods or services or the benefit of input tax credit shall be passed on to the recipient by way of commensurate reduction in prices."*

*"2. The Central Government may, on recommendations of the Council, by notification, constitute an Authority, or empower an existing*

***Authority constituted under any law for the time being in force, to examine whether input tax credits availed by any registered person or the reduction in the tax rate have actually resulted in a commensurate reduction in the price of the goods or services or both supplied by him."***

***"3. The Authority referred to in sub-section (2) shall exercise such powers and discharge such functions as may be prescribed"***

In the first part Sec. 171(1) is casts responsibility to pass on benefit of GST to recipient for following two aspects:

***a. For any rate reduction in new tax regime***

As regards passing of benefit due to rate reduction, in case of exclusive tax supplies there should not be a big challenge, since reduction in tax rate will directly be evidenced by invoices and the recipient will get benefit of the rate reduction. However, in case where contract of supplies are for inclusive of taxes, this provision will cast responsibility on supplier to reduce the price due to reduction in rate of taxes. For example FMCG items which are normally sold on MRPs or some other fixed prices by retailers, if there is any reduction in rate of tax it has to pass on benefit to the ultimate recipient. Accordingly there shall be need to revise MRP or other prices fixed for such supplies.

***b. For any benefit of Input Tax Credit***

As regards passing of benefit due to better credit chain, it is going to affect almost all industries. In most places, be it service sector, manufacturing, trading or any specific industry, all are going to get advantage of better flow of Input Tax Credit. So the expectation of the provisions are commensurate reduction in prices of supplies. If we apply this principle in plain reading to the above illustration we can reframe it as under:

**Cost Sheet in GST Regime (If no one profiteer itself, on account of taxes)**

| Description | Amount (INR) |
|---|---|
| Purchase Price of Goods (A) | 1,00,000 |
| GST | 18,000 |
| Total Purchase Price | 1,18,000 |
| Operational Exp. (Business Consumables & Services) (B) | 1,000 |
| Tax on Operational/ Indirect Exp. | 180 |
| Total Cash Outflow | 1,19,180 |
| Sales Price [Cost (A+B) + plus existing margin] (C) | 1,12,350 |
| GST | 20,223 |
| Total Cost to Consumer | 1,32,573 |
| Profit of Dealer (C – A – B) | 11,350 |
| Total tax which Govt. has received (CG + SG) | 20,223 |

**Comparison of three scenarios:**

| Description | Existing Provisions | GST (Without adjusting prices) | GST (Without Profiteering) |
|---|---|---|---|
| Cost to Consumer | 1,31,875 | 1,47,500 | 1,32,573 |
| Profit of Dealer | 11,350 | 24,000 | 11,350 |
| Total Govt. Taxes | 19,525 | 22,500 | 20,223 |

After going through with comparison of three scenarios, it is evident that adequate reduction in prices is essential for success of biggest indirect tax reform of the country. Accordingly it is need of the hour that industry ***suo-motu*** reduce prices of goods and services. However if it doesn't do so, then legal provisions are there in place to cater such situations. Introduction of this measure is required to curb the practice of pocketing the tax benefit, rather than passing it on to the ultimate consumer by way of real reduction in the price of supplies. That is why, despite lot of agitation from industry after release of revised model law in November 2016, the Government maintained same provision in the CGST Bill too, which has already passed from both Houses of the Parliament, and has taken the shape of law of the land after signing from Hon'ble President of India.

As of now Sec. 171 it is an enabling provision only in the enactment, which is to be followed by Rules made by Central Government. No draft rules has been put in public domain by the Government to be discussed by the industry for implementation & preparation on this provision.

## C. International practices & Indian context

India is not the first country which is heading towards Comprehensive GST (VAT) with Anti-profiteering measure. Many countries like Canada, New Zealand, Australia and Malaysia etc. has witnessed such measure while adopting Goods and Services Tax regime. Broadly, as per overseas experience, the impact of Anti-profiteering law was troublesome for industry. Accordingly, India needs to learn from experiences of others while imposing anti profiteering measures in the Indian economy.

Recently, Malaysia had adopted Goods and Services Tax in 2015, whereby they brought Anti-Profiteering provisions for GST through their existing legislation called 'Price Control and Anti-Profiteering Act, 2011'. Amendment in the existing legislation was done through Amendment Act of 2014 whereby main operating provisions reads as under:

*"Sec. 15(1A) The mechanism to determine that profit* ***is unreasonably high referred to in sub-section (1) includes the Minister determining a certain period during which there shall be no increase in the net*** *profit margin of any goods or services."*

Further, Part II and Part III of Schedule to Price Control and Anti-Profiteering (Mechanism to Determine Unreasonably High Profit) (Net Profit Margin) Regulations, 2014 had prescribed mechanism to calculate net profit margin pre and post Goods and Services Tax regime respectively. After that both had to be compared in order to make sure that there is no increase in net profit margin post GST implementation.

In Australia too, the Anti-Profiteering measures were effected through amendment in existing legislation called "Australia Competition and Consumer Act, 2010". Whereby Sec. 44ZZT had been added to impose restriction as regard to Anti-Profiteering on class of Goods and Services.

Further, in India, The Competition Act, 2002 was enacted with following objectives as mentioned in section 18:

- Elimination of practices having adverse effect on competition
- Protection of interest of consumers
- Promotion and sustainability of competition
- Ensuring freedom of trade among participants in the Indian markets

Competition Commission of India (CCI) was duly constituted under the Competition Act to take due care of above mentioned objectives of the said enactment. Objectives of the CCI is more or less at par with objectives of proposed Anti-Profiteering law. Looking to the experience of handling similar nature of task, CCI may be entrusted as the competent authority under Section 171 of the CGST Act.

## D. Applicability of Anti-Profiteering provisions on credits held in stock as on Appointed Day

Sec. 140 of CGST Act provides carry forward of credit of eligible duties in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock, for certain classes of registered persons where such credit was not reflected in returns of respective law. By allowing carry forward of such credit to the registered person the Government has ensured that such stock, when supplied in GST regime, will not suffer double burden of taxes and relevant benefit are passed to the registered person. Now question arises whether this benefit of credit has to be passed on to consumer by way of reduction in price of supplies or not ?

As discussed above, Sec. 171 is clearly applicable in two circumstances only. Firstly being reduction in rate of tax, which is not the case. Secondly being benefit of Input Tax Credit. The definition of 'Input Tax Credit' as provided in Sec. 2(63) read with Sec. 2(62) means CGST, SGST, UTGST & IGST charged on any supply of goods or services. The credit of eligible taxes on stock carried forwarded in GST regime cannot be said to be tax charged in the GST enactment hence it seems Sec. 171 will not cover such kind of credit passed on into GST regime and accordingly need not be passed on to buyer.

It may be noted that in the Revised Model GST Law released in Nov 2016, there was a specific provision for passing on of such credit to the recipient, but the same is not there in CGST Act. It appears that Government has withdrawn this condition in the final law, looking to the demand of industry and computational challenges, difficulties arising in verification that whether such credit has been passed on to the recipient or not.

However, if the credit of tax paid in stock is claimed under proviso to Sec. 140(3) read with Rule 1(4) of Draft Transitional Rules (i.e. where registered person doesn't have the document evidencing payment of tax or duty), it is necessary to pass on benefit of such credit to recipient by way of reduction in prices.

## E. Issues & challenges

### 1. Computational mechanism

a. Practically it is very difficult to establish one to one correlation between ITC on inward supplies and tax payable on outward supplies. So ultimately it comes on margins or prices of supply. How the margins and prices are to be checked is a subjective matter. There may be various ways like:

- Profit on product in absolute terms.
- Profit percentage on cost of product.
- Profit percentage on sale price.

b. Further apart from benefits in terms of better credit chain, the business organisations are going to incur huge cost for implementation of GST majorly being installation of new IT systems, restructuring of operations, redesigning of SOPs, Compliances cost etc. Whether, the organisation can set off its gains in terms of better credit flow with its increased cost, before passing of the same to consumer. In other words, if rules prescribes for maintaining of margins, whether the same is to be maintained on Cost of Product Level, Gross Margin Level, Operational Profit Level or Net Profit Level.

Industry should represent before Government with its rational and demands. However, one thing which has to be ensured that rules should be detailed enough so that there will be no discretion available to any authority which leads to corrupt practices.

### 2. Determination of price

One fact needs to be noted that prices and margins are not solely dependent on taxes. Rather they are only a component of price like any other components. Price determination depends on many factors such as:

- Internal factors:
  - o Cost of raw material or other component
  - o Predetermined objectives (Higher profit or higher revenue)
  - o Image of the seller (Goodwill)
  - o Life cycle of the product (Initial level may be less priced or even free sample after that there may be increase in price)
  - o Credit period offered.
  - o Promotional activities (Heavy advertisement/promotional exp.)
- External factors:
  - o Competition
  - o Consumers (price sensitivity & purchasing power of buyer)
  - o Government Control
  - o Economic Condition (Recession)
  - o Supply chain (Longer the chain, higher would be the price)

Price determination of any product is most complex and continuous process, cycle of which depends on nature of product. If prices or margins are being freezed, on account of Anti-Profiteering Measures, then it may lead to disastrous situation in many industries. Further, at times there may be strategic pricing for some products which the companies doesn't want to share with anyone including tax authorities.

**3. Constitutional challenges**

a. Right to Free trade

Article 301 of our Constitution provides freedom of trade, commerce and intercourse throughout the territory of India. However, Article 302 authorises Parliament to impose reasonable restrictions. Anti-profiteering provisions or restriction on profits of trade of all goods or services may be treated as violation of fundamental right of freedom of trade, hence may be subject to judicial review.

b. Implication on State Tax/Assessees

It is pertinent to note that power to constitute authority u/s. 171 is with Central Government only. Article 302 also authorises Parliament to impose such restrictions, whereas there are stringent conditions for State legislatures to impose such kind of restrictions under Article 304.

In such a scenario implementation of Anti-profiteering measures in respect of

– State Tax (i.e. SGST) administered by any Govt. OR

– Registered Persons, under State Jurisdiction for all taxes may be subjected to judicial review.

## F. Conclusion

From consumer's point of view Anti-profiteering Provision is necessarily required to be there so as to ensure deserving benefit should pass on to them. At the same time, looking to the issues and challenges before industry and the efforts involved in reworking of cost sheet and re-fixing of prices, it is advisable that

a) A reasonable bandwidth for margin variation should be prescribed, say for example variation up to 10% of existing margins. If variation remains within such bandwidth, no registered person should face any penal consequences u/s. 171 of the CGST Act.

b) A threshold limit for turnover of taxable supplies may be prescribed, below which provision of sec. 171 shall not apply.

c) Further for above threshold limit, detailed rules, covering all aspects including computation mechanism, documents to be maintained etc, should be prescribed so that no discretionary power is left in hands of any authority which in turn can cause harassment of tax payer.

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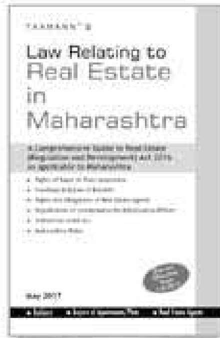

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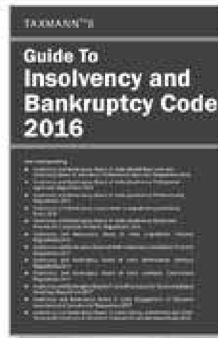

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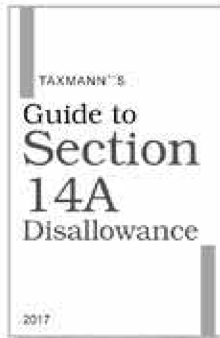

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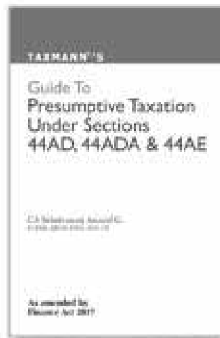

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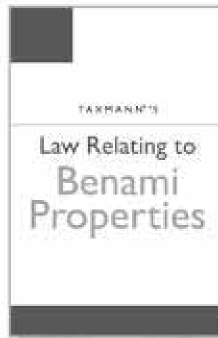

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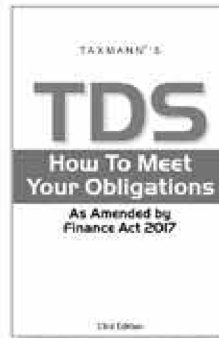

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# DIRECT TAXES
## Supreme Court

**Capital gains: An amount received from a wholly-owned subsidiary in consideration of transfer of shares of the WOS to a group of shareholders is not taxable as capital gains. The Department cannot subject a transaction under the Gift-tax Act and also levy tax under the Income-tax Act.**

*CIT vs. Annamalaiar Mills, Madurai [Civil Appeal No. 1864/2007, dated 28th March, 2017]*

(i) M/s Annamalaiar Textiles (P) Ltd. was the wholly owned subsidiary of M/s. Annamalaiar Mills (P) Ltd., which is the respondent herein. In the respondent company, there were two groups of shareholders; the majority shareholders called Group A was having 61.26 per cent shares whereas the minority shareholders called Group B were holding 38.74 per cent shares.

(ii) An agreement was entered into between the two groups on 24-6-1985 by which Group A came to hold all the shares in the holding company i.e. the respondent herein and Group B was given 100 per cent shares in the subsidiary company i.e. M/s. Annamalaiar Textiles (P) Ltd. However, M/s. Annamalaiar Textiles (P) Ltd. also paid a sum of ` 42.45 lakhs to the respondent company.

(iii) Proceedings under the Gift Tax Act were initiated in respect of payment of ` 42.45 lakhs received by the respondent company. The levy of gift tax was not the question under the present proceedings.

(iv) The Assessing Officer treated the amount of ` 42.45 lakhs paid by the M/s Annamalaiar Textiles (P) Ltd. to the respondent company as capital gains on the footing that since both the companies are now 100 per cent owned by Group A or Group B, as the case may be, payment of ` 42.45 lakhs was to offset valuation of the shares of M/s. Annamalaiar Textiles (P) Ltd.

(v) The Assessing Officer opined that the respondent company was liable to pay tax for capital gains which was upheld in the appeal before the Commissioner of Income Tax (Appeals). However, the Income Tax Appellate Tribunal, Madras, in appeal preferred by the respondent herein accepted the pleas

put forth by the respondent herein, set aside the assessment and restored the matter to the Income Tax Officer so that the assessee may approach the Central Board of Direct Taxes. The Income Tax Officer was further directed to finalise the assessment in accordance with the directions that may be given by the Central Board of Direct Taxes.

(vi) The matter was taken up before the High Court of Madras and the order of the Tribunal was upheld by the Madras High Court.

(vii) The sole question which arises for our consideration is as to whether the sum of ` 42.45 lakhs paid by M/s Annamalaiar Textiles (P) Ltd. to the respondent company is liable to any capital gains or not.

(viii) It is not in dispute that M/s Annamalaiar Textiles (P) Ltd. did not pay any amount to the shareholders who ultimately got the shares transferred in their names. The respondent was holding 100 per cent shares of M/s Annamalaiar Textiles (P) Ltd., before it was transferred to Group B. No payment was made to the shareholders belonging to Group B and, therefore, the question of there being any capital gains at the hands of the respondent herein does not arise.

(ix) Needless to mention that the transaction of payment of ` 42.45 lakhs had been subjected under the Gift-tax Act and the Department cannot claim both under the Gift-tax Act and also levy tax under the Income-tax Act.

**S.132 : It is but natural that concealed income found at the time of search and survey has to be distributed among all the family members who were carrying on business. It is also a reasonable conclusion that the income had been earned over a period of time and should be spread over various years**

***Commissioner of Income Tax, Salem vs. Rekha Bai***

*[Civil Appeal No. 1749 of 2007, dated 21st March, 2017]*

The Madras High Court held that:

(i) Less than 50% of the face value of the promotes should only be treated as the amounts advanced and consequently the undisclosed income of the assessee;

(ii) The concealed income has to be treated as belonging to various members of the assessee's family and dividing the same between them instead of taxing the entire amount in the assessee's hands;

(iii) The undisclosed income has to be spread over a period of five years.

On appeal by the department to the Supreme Court HELD dismissing the appeal:

The Department has failed to bring on record any material to the contrary except the seized documents which, in our considered opinion, could not absolve the Department or give any right to negate the view taken by the First Appellate Authority and the Tribunal. So far as the income divided among the family members of the assessee is concerned, we find that all of them were carrying on same business from the same premises. Therefore, it is but natural that if any concealed income has been found at the time of search and survey, it has to be distributed among all the family members who were carrying on business.

**Ss.132/158BC, 158BD : The fact that the search was invalid because the warrant was in the name of a dead person does not make the ss. 158BC/158BD proceedings invalid if the assessee participated in them. Information discovered in the search, if capable of generating the satisfaction for issuing a s. 158BD notice, cannot altogether become irrelevant because the search is invalid**

*Gunjan Girishbhai Mehta (Legal Heirs of Girishbhai K. Mehta) vs. Director of Investigation & Ors. [Special Leave Petition (Civil) No. 30282/2015, dated 21st March, 2017]*

(i) Notice u/s.132 of the Income-tax Act, 1961 was issued in the name of a dead person. The said notice was duly received by the present petitioner as the legal heir of the dead person. Notice of assessment u/s. 158BC of the Act was issued and in the assessment proceedings, where the income was declared to be 'nil', the present petitioner as the legal heir had participated. Thereafter, notice u/s. 158BD of the Act was issued to the present petitioner on the basis of information coming to light in the course of search. Aggrieved, the petitioner moved the High Court and on dismissal of the writ petition filed, the Special Leave Petition was instituted.

(ii) The point urged shortly put, was that if the original search warrant is invalid the consequential action u/s.158BD would also be invalid? Their Lordships did not agree. The issue of invalidity of the search warrant was not raised at any point of time prior to the notice u/s.158BD. In fact, the petitioner had participated in the proceedings of assessment initiated u/s. 158BC of the Act. The information discovered in the course of the search, if capable of generating the satisfaction for issuing a notice u/s. 158BD, cannot altogether become irrelevant for further action u/s.158BD of the Act.

(iii) The reliance placed on the decision of the High Court of Punjab and Haryana in *Commissioner of Income Tax, Karnal vs. Rakesh Kumar, Mukesh Kumar [(2009) 313 ITR 305 (P&H)]* against which Special Leave Petition [SLP(C) No... CC 3623/2009] has been dismissed by the Supreme Court and the decision of the Supreme Court in *Assistant Commissioner of Income Tax, Chennai vs. A.R. Enterprises [(2013) 350 ITR 489 (SC)]* were held to be entirely on different facts.

(iv) In Rakesh Kumar, Mukesh Kumar (supra) the challenge was to the proceedings of assessment u/s. 158BC of the Act on the basis of a search warrant issued in the name of a dead person. The issue in A. R. Enterprises (supra) has no similarity to the issue in the case of the petitioner namely, the validity of the proceedings u/s. 158BD of the Act.

**S.45/50(2) : If an undertaking is sold as a running business with all assets and liabilities for a slump price, no part of the consideration can be attributed to depreciable assets and assessed as a short term capital gains u/s. 50(2). If the undertaking is held for more than three years, it constitutes a "long term capital**

**asset" and the gains are assessable as a long-term capital gain**

***CIT, Ahmedabad vs. Equinox Solution Pvt. Ltd. [2017] 80 taxmann.com 277 (SC) [Civil Appeal No. 4399 of 2007, dated 18th April, 2017]***

The assessee claimed that as it had sold their entire running business in one go with its assets and liabilities at a slump price, the provisions of Section 50(2) of the Act could not be applied to such sale. It was claimed that it was not a case of sale of any individual or one block asset which may attract the provisions of Section 50(2) of the Act. It was also claimed that that since the undertaking itself is a capital asset owned by the assessee nearly for six years and being in the nature of long term capital asset and the same having been sold in one go as a running concern, it cannot be termed a "short term capital gain" so as to attract the provisions of Section 50(2) of the Act as was held by the Assessing Officer. This plea was upheld by the CIT (Appeals), the Tribunal and the High Court. Dismissing the appeal the Supreme Court held as under:

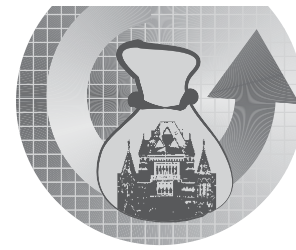
(i) In our considered opinion, the case of the respondent (assessee) does not fall within the four corners of Section 50(2) of the Act. Section 50(2) applies to a case where any block of assets are transferred by the assessee but where the entire running business with assets and liabilities is sold by the assessee in one go, such sale, in our view, cannot be considered as "short-term capital assets". In other words, the provisions of Section 50(2) of the Act would apply to a case where the assessee transfers one or more block of assets, which he was using in running of his business. Such is not the case here because in this case, the assessee sold the entire business as a running concern.

(ii) As rightly noticed by the CIT (Appeals) that the entire running business with all assets and liabilities having been sold in one go by the respondent-assessee, it was a slump sale of a "long-term capital asset". It was, therefore, required to be taxed accordingly.

(iii) Our view finds support with the law laid down by this Court in ***Commissioner of Income Tax, Gujarat vs. Artex Manufacturing Co. [1997(6) SCC 437 CIT].***

(iv) In ***Premier Automobiles Ltd. vs. Income Tax Officer & Anr., 264 ITR 193 (Bombay)*** also, the Division Bench of the Bombay High Court examined this question in detail on somewhat similar facts and has taken the same view. The larned Judge S.H. Kapadia – (as His Lordship then was as Judge of the Bombay High Court and later became CJI) speaking for the Bench aptly explained the legal position to which we concur as it correctly summarised the legal position applicable to such facts.

(v) Learned Counsel for the appellant (Revenue) was not able to cite any decision taking a contrary view nor was he able to point out any error in the decisions cited at the Bar by the assessee's counsel referred supra.



Ashok Patil & Priti Shukla, *Advocates*

# DIRECT TAXES
## High Court

### 1. Penalty – Validity

*S. Chandrashekhar vs. ACIT (2017) 293 CTR (Kar.) 409 A.Y.: 2006-07 SS: 271(1)(c) of IT Act*

Notice was issued to the assessee proposing levy of penalty u/s. 271(1)(C) of the Act. Contention of the assessee was that he had co-operated with the Department and there was no question of levy of penalty u/s. 271(1)(C) of the Act. Accordingly, he suspected that income of ` 22,74,000 were concealed by the assessee. He levied penalty u/s. 271 (1)(C) of IT Act. On appeal in CIT(A), CIT(A) dismissed appeal of assessee, relying on the Apex Court judgment in the case of *MAK DATA (P) Ltd. vs. CIT (2013) 263 CTR (SC)*. Tribunal confirmed order of CIT(A). On appeal in HC, HC reversed finding of lower authorities and held that notice issued in printed form mentioning "you have concealed the particulars of your income or furnished in accurate particulars of such income". Notice was thus not specific. Further, in the impugned notice, there was no clear indication about concealment of the particulars of income nor there was any clear indication of furnishing of inaccurate particulars of income on application of mind. In any case, there was no specific ground hence there could be breach of principles of natural justice and ultimately the order imposing penalty was non sustainable.

### 2. TDS u/s. 194H – Commission vis-a-vis Trade discount to Retailers

*CIT vs. United Breweries Ltd. (2017) 293 CTR (AP) 500*

Assessee was engaged in manufacture and sale of beer to AP Beverages Corporation Ltd. (APBCL). APBCL in turn sold beer to retail dealers. In order to boost its turnover, assessee launched incentives schemes for retailers under which retailers got discount on achieving certain sales target. For this purpose, assessee appointed del-credere agents through whom incentives were paid to retailers. As regards payment to del-credere agents, same was paid after deduction of TDS. However for non-deduction of TDS on incentives to retailers, AO treated assessee as in default u/s. 201(1) of IT Act. CIT(A) dismissed appeal of the assessee. Tribunal reversed finding of the CIT(A) and held that beer was sold by assessee to APBCL and APBCL had in turn, sold the beer, purchased by them from the assessee, to retail dealers and in absence of relationship of a principal and agent and also as there was no direct relationship between the assessee and the retailer, the discount offered by the assessee to the retailers was not commission and Section 194H was not attracted.

## 3. Penalty – Concealment – Applicability of Explanation 5

*Principal CIT vs. Neeraj Jindal (2107) 293 CTR (Del.) 298*

Assessee filed return after search was conducted and such revised return was accepted by the AO. The AO completed assessment u/s. 153A r.w.s.143(3) of the Act after accepting the declared income. In addition, he also initiated penalty proceedings u/s. 271(1) (C) of the Act on concealment of income. The CIT (A) and Tribunal both deleted penalty. On further appeal in HC. The Hon'ble HC dismissed appeal of the Revenue and held that Return filed u/s. 153A takes place of original return u/s. 139 and for purpose of levying penalty u/s. 271(1) (C), what has to be seen is whether there is any concealment in return filed by the assessee u/s. 153A, and not *vice versa* the original return u/s. 139 of IT Act. For Explanation 5 to apply, kit was necessary that there must be certain assets (such as money, bullion, etc.) found in the possession of the assessee during the search and that the assessee must claim that such assets have been acquired by him by utilising (wholly or in part) his income. Also such income must be in relation to a particular previous year that has either ended before the date of the search or is to end on or after the date of the search and such income is declared subsequently in the return of income filed after the search. Explanation 5 was not applicable for levy of penalty where no material was recovered during the search but cash of ` 5,26,530 was recovered during search on 11-1-2007 and assessee added ` 21,65,932 in the return filed u/s. 153A for A.Y. 2005-06 and 2006-07.

## 4. Applicability of Section 80P (4) – vis-à-vis deduction u/s. 80P (2)(i) of IT Act

*CIT vs. Nilgiris Co-operative Marketing Society Ltd. (2017) 293 CTR (Mad.) 367*

**Sections 80P (2)(a)(i) & 80P(4) of IT Act**

The question of law in HC was whether Tribunal was justified in holding that the assessee society engaged in selling of agricultural produce of the members are eligible for the benefit of s. 80(P) (2)(a)(i) of the IT Act in respect of the interest received from members? Dismissing Revenue's appeal in HC, Hon'ble HC held that as per the provisions of s.5(b) of the Banking Regulation Act, 1949, the crucial expression relevant for making one answer the description of banking is that it is capable of accepting money from the general public but not necessarily confined to its members. Any such activity carried on by anybody requires, apart from licensing, answering the regulatory domain prescribed under the 1949 Act. Even a co-operative bank which carries on banking activity requires to be regulated by the provisions of the 1949Act. Sec.80P (4) therefore is clearly attracted to such an institution, but not to credit society. Even while dealing with a co-operative bank, sub-section (4) has taken care to ensure that the primary agricultural credit societies and primary co-operative agricultural and rural development banks are kept out of the purview of the said provisions. Sub-section (4) of S.80P therefore, in its application is confined to co-operative banks only. In the instant case, the assessee being a co-operative credit society which in turn is providing for certain credit facilities to its, members alone but not to the general public at large and which also does not receive monies by way of deposit from the general public, it does not answer the description of a co-operative bank. Consequently, the main provision contained under sub-clause (i) of S.80P (a) gets attracted and consequently, the assessee is entitled to seek the deduction which has been provided for under s.80P of the Act.

Sameer Dalal & Jitendra Singh
*Advocates*

# DIGEST OF CASE LAWS
## Tribunal

**1. Cash credit – Bank deposit – Section 68 of the Income-tax Act, 1961 – Assessee not maintaining any account books – Bank statement could not be construed to be a books of account maintained by assessee – Merely on basis of information that assessee made a 'cash deposit' in her saving bank account no addition could be made as unexplained cash credit. A.Y.: 2006-07**

*Mehul v. Vyas vs. ITO – [ITA No. 727 / Mum./ 2013; Order dated 7-4-2017; Mumbai Bench]*

During the assessment proceedings, the Assessing Officer called upon the assessee to put forth an explanation as regards the nature and source of the cash deposit in the saving bank account. The A.O. rejected the explanation of the assessee and, treated the cash deposit as 'unexplained cash credit' and added the same to the income of the assessee by invoking the provisions of section 68 of the Act. The CIT(A) upheld the order of the A.O.

On appeal before the Tribunal, it was held that under section 68 of the Act an addition can only be made where any sum is found credited in the books of an assessee maintained for any previous year. Section 68 of Act pre-supposes a credit of an amount in the 'books of an assessee' maintained for the previous year. Thus, an addition made in respect of a cash deposit in the 'bank account' of an assessee, in the absence of the same found credited in the 'books of the assessee' maintained for the previous year, cannot be brought to tax by invoking the provisions of section 68 of the Act.

**2. Capital Gain – Deduction – Section 48 of the Income-tax Act, 1961 – Amount paid for getting illegal occupants evicted from land – Allowed as deduction while computing long-term capital gain arising on sale of land during the year. A.Y.: 2009-10**

*Smt. Anasuya Mekala vs. Dy. CIT [ITA No. 689 / Hyd / 2015; Order dated 26-4-2017; Hyderabad Bench]*

Assessee sold a piece of land, which was in the illegal occupation of certain people who were cultivating the land since long and refused to vacate the same in spite of the assessee selling the land. Thus, in order to hand over the peaceful possession of the property to the purchaser, the assessee paid

certain amounts to the occupants. Further, the assessee also paid some amount to the village elders, towards village development activity for getting the vacant possession of the land. It was a common practice that the village elders were settling such disputes and were paid some amounts towards village development activity. Both the above amounts were claimed as expenditure by the assessee while computing long term capital gain on sale of land, as all these expenditure were incurred for transfer of the property.

The claim of the assessee was disallowed by the Assessing Officer and confirmed by the CIT(A).

On appeal before the Tribunal, it was held that wherever the assessee was able to substantiate the genuineness of the payment by filing confirmation from the payees (the occupants of the land) the same ought to be allowed to the assessee as expenditure for the purpose of transfer of property. Further, as far as payment made to village elders the Tribunal allowed deduction of fifty per cent (50%) of the amount paid observing that it is was common practice that village elders intervene and settle the land disputes to safeguard the law and order and protect the peaceful atmosphere of the village.

**3. Charitable purpose – Registration – Section 2(15) read with Section 12AA of the Income-tax Act, 1961 – Assessee carrying on charitable activity of imparting education – Mere fact that it collected voluntary donations from some students at time of giving admission would not result in invoking provisions of Section 12AA(3) of the Act so as to cancel its registration. A.Y.:**

***Vignana Jyothi vs. DIT (E) [ITA Nos. 1751 / Hyd / 2014; Order dated 26-4-2017; Hyderabad Bench]***

The assessee was engaged in running educational institutions as part of its charitable activities. It was granted registration under Section 12A of the Act Subsequently, DIT(E) noted that assessee had collected capitation fee from students which was directly linked to admission of students in a college run by it Accordingly, he took a view that assessee was not carrying out activities as per charitable objects and he accordingly, passed an order under Section 12AA(3) cancelling registration of the assessee.

On appeal Tribunal set aside the order of the DIT (E) passed under Section 12AA(3) of the Act cancelling registration and restored the registration of the assessee as granted under Section 12A of the Act. The Tribunal held that, collection of donations by assessee was not capitation fee, while holding so, the Tribunal noted that, (a) assessee had filed letters from all concerned students wherein it was stated that donations were voluntary and no capitation fee was collected; (b) there was no allegation that funds collected by assessee were for any other purpose or that profits had been distributed to any person or persons.

The cheerful mind perseveres and the strong mind hews its way through a thousand difficulties.

*— Swami Vivekananda*

CA Tarunkumar Singhal & Sunil Moti Lala, *Advocate*

# INTERNATIONAL TAXATION
## Case Law Update

### A. SUPREME COURT

**1. Where the assessee had full dominion and control over the income earned out of racing events conducted at the Buddh International Circuit (fixed place in India), the said Circuit would constitute a fixed place PE under Article 5(1) of the India-UK Double Tax Avoidance Agreements and therefore payments received by it were subject to deduction of tax at source under section 195 of the Act to the extent of income attributable to such PE**

*Formula One World Championship Ltd. vs. CIT (IT) – TS-161-SC-2017*

1. Federation Internationale de I' Automobile ('FIA') is a non-profit organisation consisting of 213 member organisations which establishes the rules and regulations for conducting the Formula One World Championships ('Championships'). Formula One World Championship ('FOWC'), a company incorporated under the laws of the United Kingdom, had entered into an agreement with FIA and Formula One Asset Management Ltd ('FOAM') (i.e. an associate company of FOWC) by way of which it was licensed all the commercial rights in the Championships for a period of 100 years.

2. For the purpose of conducting a racing event viz. the Formula One Grand Prix in India, FOWC entered into a Race Promotion Contract dated September 13, 2011 with Japyee Sports International Ltd ('Jaypee') granting Jaypee the right to host, stage and promote the Formula One Grand Prix event at the Buddh International Circuit in India for a consideration of USD 40 million. The said Race Promotion Contract was effective for a period of 5 years. *Vide* a separate agreement, Jaypee had also agreed to give back the circuit rights i.e. media and title sponsorship to Beta Prema 2 and rights to sell paddock seats to Allsports who were both associated companies of FOWC. Subsequently, Beta Prema 2 had entered into an 'Title Sponsorship Agreement' with Bharti Airtel as per which Beta Prema 2 transferred title sponsorship rights to Bharti Airtel for a consideration of USD 8 million. FOAM was engaged to generate TV feed of the racing event.

3. At this juncture, FOWC and Jaypee filed an application before the Authority for Advance Ruling ('AAR') raising the following 2 questions:

i. Whether the consideration receivable by FOWC from Jaypee in terms of the Race Promotion Contract was royalty as defined in Article 13 of the India-UK Double Tax Avoidance Agreement ('DTAA').

ii. Whether FOWC had a Permanent Establishment in India in terms of Article 5 of the DTAA.

The AAR held that the consideration received by FOWC from Jaypee amounted to Royalty under the DTAA. With regard to the second question raised before it, the AAR held that FOWC did not have a PE in India. Further, it held that since the payment to FOWC was royalty, Jaypee was liable to deduct tax under section 195 of the Act.

4. Pursuant to the ruling of the AAR, FOWC and Jaypee filed writ petitions before the High Court contending that the payment of consideration did not amount to Royalty under Article 13 of the DTAA. The Revenue also filed a writ petition challenging the answer of the AAR on the issue of PE, contending that FOWC had a PE in India in terms of Article 5 of the DTAA.

5. The High Court reversed the order of the AAR on both the issues i.e. it held that the consideration paid to FOWC was not royalty under Article 13 of the DTAA and that FOWC had a PE in India and was thus liable to tax in India. Vis-à-vis the Constitution of PE in India the Court noted that FOWC and its employees had full access to the Buddh International Circuit, which was a fixed place in India, and that Japyee's capacity to act was extremely limited. It also noted that the access granted to FOWC was for a period of 6 weeks at a time during each season/each race and that the access was for a period of 5 years i.e. the duration of the Race Promotion Contract. Accordingly, it held that FOWC carried on business in India within the meaning of expression under Article 5(1) of the DTAA.

As regards royalty, the Court held that the amount received by FOWC was taxable as business income as the payment was a lump sum amount and not based on the extent of the IP rights used by Japyee.

6. Aggrieved, FOWC and Jaypee filed an appeal before the Hon'ble Supreme Court. The Revenue did not challenge the findings of the High Court vis-à-vis royalty and therefore that issue had achieved finality.

**Held**

1. The Apex Court examined the definition and scope of PE under the DTAA and relied extensively on the commentaries of Philip Baker and Klaus Vogel and noted that as per Article 5 of the DTAA, the PE had to be a fixed place of business through which business of an enterprise was wholly or partly carried on. It held that the Buddh International Circuit was a fixed place and since the races were conducted from the said circuit, it was a business activity.

2. Further, it examined whether the international circuit was put at the disposal of FOWC and whether it was a fixed place of business of FOWC. It refereed to the arrangements between FOWC and its affiliates (viz. FOAM, Beta Prema 2 and Allsports) and Jaypee and noted that all the agreements were to be read as whole to determine who was having real and dominant control over the event. It observed that the media and title sponsorship rights, the paddock rights and TV rights were all vested with the affiliates of FOWC. Further, it noted that commercial rights of the entire event in India was possessed by FOWC and that even the physical control of the circuit was with FOWC and its affiliates. Accordingly, it held that FOWC and its affiliates had full disposal over the Buddh International Circuit at which the event was held. It held that the race was physically conducted in India, which generated income in India and concluded that FOWC had made its earning in India through the said Circuit over which it had complete control during the period of the race. Further, the Apex Court acknowledging that FOWC was the commercial right holder of the event, held that the exploitation of these rights was only possible with the actual conduct of the races and the active participation of FOWC in the said races.

3. It dismissed the contention of assessees that the total duration for which limited access

was granted to FOWC was not sufficient duration to constitute the degree of permanence necessary to establish a fixed Place PE since the duration of the event was three days and the control, if any, would be for that period only. It noted the Revenue's contention that the Race Promotion Contract had been entered into for a period of 5 years and affirmed the finding of the High Court that during the full duration of the event, FOWC had full access to the Circuit and therefore number of days ***per se*** would not make any difference. Further, it held that mere construction of the track by Japyee was of no consequence while determining whether FOWC had disposal over the track.

4. Accordingly, it upheld the findings of the High Court and held that the tests laid down for constitution of a PE viz. stability, productivity and dependence were satisfied. It concluded that the Buddh International Circuit was the fixed place of business at the disposal of FOWC and that the taxable event i.e. earnings from the Grand Prix had taken place in India and therefore FOWC was liable to pay in India on such income earned by it. Accordingly, it held that Jaypee was bound to deduct tax at source under section 195 of the Act on the payments made by it to FOWC.

5. However, the Apex Court accepted the assessee's submission that only that portion of income of FOWC that was attributable to the said PE was to be treated as business income chargeable to tax in India and accordingly directed the AO to arrive at the profits attributable to the PE in India.

6. Accordingly, it dismissed the appeals filed by FOWC and Jaypee.

## B. HIGH COURT

### 2. The Court upheld Tribunal's order deleting TP addition on account of royalty payment for technical know-how and usage of brand made by assessee since the restriction of royalty payment was arbitrary and *ad hoc*

*CIT vs. Johnson & Johnson Ltd [TS-265-HC-2017(Bom.)-TP]*

**Facts**

1. The assessee, a subsidiary of Johnson & Johnson Inc. US (who held 75% of its shares, the balance 25% being held by DePuy Medical Pvt. Ltd., India) was engaged in the business of manufacturing, dealing, trading in various products. Its operations were divided in 3 segments: customer case, pharmaceuticals and medical products. During AY 2006-07, the assessee made a payment on account of technical know-how-royalty at the rate of 4% and Brand Royalty at the rate of 2%, net of taxes on net sales to its AE which was at ALP as determined by the assessee.

2. The TPO observed that there was no basis for payment of any royalty for use of trademarks/brand names as the products sold by the assessee had already acquired a reputation of quality before the conclusion of the royalty agreements. He also held that some of the products were introduced long ago and technology was fully adapted and therefore for such products, only updation of technology was required and the rate of royalty should have been lower on such products. Vis-à-vis the assessee's contention that since its royalty payment was approved by RBI, the same was at ALP, the TPO held that the RBI approval could not be considered as ALP benchmark. Further, he also observed that there was no need to pay royalty on traded products and it was to be considered only on manufactured products. TPO determined ALP of royalty for technical know-how @ 1% and brand and trademark royalty at @ 1% on all sales.

Further, TPO held that there was no provision in the agreement with the AE under which the assessee was required to bear taxes on such royalty. Accordingly, TPO made a disallowance of ` 41.26 crores (including disallowance of

tax and R&D cess and service tax borne by the assessee).

The TPO also disallowed a part of publicity and sales promotion expenses incurred by the assessee on ground that the AE should have borne such cost considering it received higher royalty due to higher sales

3. On reference, DRP confirmed the actions of TPO.

4. The Tribunal, the Tribunal relying on its earlier ruling in the assessee's own case for ***AY 2002-03 [TS-246-ITAT-2013 (Mum)-TP]***, deleted TP-addition for technical know-how and brand royalty paid to AE, holding that TPO was not authorised to make disallowance on ground of necessity, but could only examine quantum of expenditure. Further, it also observed that assessee's royalty rate was lower than average royalty rate for comparable technical / marketing know-how royalty approvals given by SIA/RBI. Vis-à-vis the disallowance of tax, R&D cess and service tax borne by the assessee, the Tribunal observed that the taxes were liability of the assessee under the terms of agreements and relying on its earlier ruling deleted the said disallowance.

With regard to the TPOs disallowance of a part of the publicity and sales promotion expenses, the Tribunal held that there was no merit in such disallowance as the TPO had not applied any method prescribed in arriving at his conclusion. The Tribunal also refused to the accept the Revenue's request for remitting the matter back to TPO to determine afresh in light of Special Bench ruling in ***LG Electronics [TS-11-ITAT-2013(DEL)-TP].***

5. Aggrieved, the Revenue filed an appeal before the Hon'ble High Court.

**Held**

1. The Court upheld the order of the Tribunal by relying on the co-ordinate bench ruling for AY 2002-03 wherein it was held that TPO's restriction of royalty payment to 1% without giving reasons or justification was arbitrary and ***ad hoc***, and that TPO had not carried out the exercise to determine the ALP by following one of the methods prescribed in Sec. 92C.

2. Vis-à-vis the TPOs disallowance of a part of the publicity and sales promotion expenses, the Court upheld the order of the Tribunal and held that the determination of the ALP had to be done only by following one of the methods prescribed under the Act and since the Revenue had not acted in accordance with the clear mandate of law, the Revenue's appeal did not give rise to any substantial question of law. Further, it upheld the Tribunal's refusal to remand the issue in light of the Special Bench decision in LG Electronics and held that no submissions had been made as to the reasons why the decision of the Special Bench in LG Electronics (supra) would be applicable in the present facts.

Note: Though the issue of disallowance of tax, R&D Cess and Service tax on royalty was taken up as a ground, the Court has not specifically commented or admitted the appeal on the impugned issue.

### 3. For the purpose of determining the ALP of services rendered by the assessee to its AE i.e., financial analysis of the borrowers, general market conditions and regulatory environment, the interest earned by the foreign AE could not be considered as the income of the assessee as the assessee had not contributed to the loan amount on which the foreign AEs had earned interest income

***DIT vs. Calyon Bank [TS-231-HC-2017(Bom.)-TP & TS-252-HC-2017 (Bom.)-TP]***

1. The assessee assisted its Head Office in foreign currency loan syndication by providing

financial analysis of the borrowers, general market conditions and regulatory environment.

2. During TP proceedings, the TPO held that 25% of the total amount comprising interest and fee received by the offshore branches of the bank should have been received by the assessee.

3. On appeal, CIT(A) reduced the adjustment from 25% to 20%. Aggrieved, the assessee preferred an appeal before the Tribunal.

4. The Tribunal, relying on a similar decision of the co-ordinate bench in the case of the assessee's group concern viz. ***Credit Lyonnais [TS-283-ITAT-2013(Mum.)-TP]*** for AY 2002-03, held that since the role of Indian entity in providing services was the core basis of taking the decision of granting loan for the overseas branches, income was attributable to Indian PE. Vis-à-vis the amount to be attributed to the Indian PE, it held that the interest income earned on the loan granted by the overseas branches could not be considered as income attributable as the assessee had not contributed to the impugned loan, which was done so by the foreign branches outside India. Accordingly, it directed the TPO to determine ALP by considering commission fees charged by foreign branches and held that the estimation made by the CIT(A) at the rate of 20% was just and proper.

5. Aggrieved, the Revenue filed an appeal before the Hon'ble High Court contending that the Tribunal had erred in holding that no interest income earned on the loan by AE could be taken into account and that the ALP of services was rightly determined by the TPO by considering 25% of interest income and fee charged by the foreign branches

**Held**

1. The Court noted the assessee's submission that Revenue had filed an appeal against Tribunal order in the case of ***Credit Lyonnais [TS-283-ITAT-2013(Mum.)-TP]*** for AY 2002-03 which was rejected by the Prothonotary and Senior Master of the Court on account of non-removal of office objection on 28th June, 2014, and subsequently the Revenue had not taken any steps to have the dismissed appeal restored and further that no appeal was filed by the Revenue against the order of the Tribunal in the case of Credit Lyonnais for AY 2003-04 as well.

2. In light of the above submission, the Court held that Revenue appeared to have accepted the Tribunal order in case of Credit Lyonnais since Revenue had not raised any question of law on this issue while filing appeal against Tribunal order for succeeding AY 2003-04.

3. Considering Revenue's stand in case of Credit Lyonnais which was followed in the impugned order in present case, the Court held that the proposed question did not give rise to any substantial question of law.

### 4. AMP – Expenses unilaterally incurred by assessee could not be construed as international transaction

***Honda Siel Power Product Ltd vs. DCIT [TS-182-HC-2017 (Del.) – TP]***

1. The assessee, was engaged in the business of manufacture and distribution/sale of portable gensets, general purpose engines and water pumping sets, processing of pressure Die Casting parts in India as well as outside India, including its overseas related parties.

2. Out of a total advertisement, marketing and sales promotion expenditure of ` 12.62 crore unilaterally incurred by the assessee, the TPO made an adjustment of ` 10.98 crores, applying the Bright Line Test, which was upheld by the DRP.

3. The assessee filed an appeal before the Tribunal wherein the Tribunal noted that co-ordinate bench in assessee's own case in AY 2008-09 had remitted similar addition made on account of AMP expenses to TPO for deciding as per Special Bench ruling in the case of the ***LG Electronics [TS-11-ITAT-2013(DEL)-TP].*** Further, it further noted that Special Bench ruling was

considered and overruled by Delhi High Court in the case of ***Sony Ericsson [TS-96-HC-2015 (Del.)-TP]*** and that the jurisdictional High Court, in assessee's own case in AY 2008-09 against co-ordinate bench order, had held that AMP expenses unilaterally incurred by assessee could not be construed as an international transaction. Accordingly, following the decision of Court in assessee's own case, the Tribunal deleted the adjustment for both years. [TS-238-ITAT-2016(Del.)-TP]

**Judgment**

1. The Court observed that the Tribunal had followed its own orders for previous years as well as High Court order in assessee's own case for previous year and thus upheld the order of the Tribunal and held that the question of law, therefore, did not arise.

## 5. The Court was *prima facie* satisfied with assessee's contention that the AO should have determined as to whether the transactions involved came within the ambit of the international transactions or not before making reference to the TPO and that the TPO did not have the jurisdiction to determine the existence of an international transaction.

*PriceWaterhouse and Anr – TS-284-HC-2017 (Cal) - TP*

**Facts**

1. The assessee had, ***vide*** writ petition filed before a single member bench, challenged the jurisdiction of the Transfer Pricing Officer (TPO) to entertain reference made by the AO for determination of arm's length price as the assessee claimed there was no international transaction between 2 AEs within the meaning of Chapter X of the Act.

2. The Court [TS-976-HC-2016(CAL)-TP] had upheld AO's reference to TPO in respect of alleged international transactions of the assessees for AY 2011-12, holding that Section 92CA(1) did not require the AO to first come to a definite finding that there was an 'international transaction' within the meaning of Section 92B before referring the matter to TPO, and a ***prima facie*** view would suffice. It further held that existence of international transaction was a factual issue which the TPO was equipped and competent to decide. It further held that the Writ Court was not a fact finding forum, and opined that, if the stand of the petitioner company was ***bona fide*** and indeed if no international transaction was involved, there was no reason why the Petitioner should shy away from the proceeding before the TPO and not urge and establish the same in the proceedings before the TPO.

3. Aggrieved, the assessee filed an appeal and challenged judgment of the single member bench before a division bench of the Hon'ble High Court, wherein the assessee contended that the AO should have determined as to whether the transactions involved came within the ambit of the international transactions or not before making reference to the TPO and that the TPO did not have the jurisdiction to determine the existence of an international transaction.

**Judgment**

1. The Court noted that the proceedings before the TPO had not yet commenced in terms of the directions contained in the judgment in view of pendency of this appeal at the request of the assessee.

2. It proposed to hear out the entire appeals and fixed hearing on 25-4-2017 and stayed the operation of the judgment of single judge order till 2-5-2017, stating that it was ***prima facie*** satisfied with assessee's case at this stage regarding the jurisdiction of the TPO.

## 6. The Court rejected the Revenue's recharacterisation of export commission as royalty and deleted the consequent

**disallowance u/s. 40(a)(i) for non-deduction of tax on the alleged royalty payment.**

*Hero Motocorp Limited [TS-180-HC-2017(Del.)]*

**Facts**

1. The assessee was engaged in the business of manufacture and sale of motorcycles using technology licensed by Honda Motor Co. Ltd., Japan ('HMCL') pursuant to a Technical Collaboration Contract ('TCC') [renamed as License and Technical Assistance Agreement ('LTAA')] with HMCL as per which the assessee was provided technical assistance to assessee to set up plant for manufacturing motorcycles. Under the LTAA, there was specific bar that prevented the assessee from using know-how to manufacture vehicles for export outside India. In 2004, a separate Export Agreement ('EA') was entered into between HMCL and the assessee which enabled the assessee to export specific models of two-wheelers to certain countries on payment of export commission @ 5% of the FOB value of such exports.

2. Firstly, the AO / TPO treated the ALP of the said transaction as nil and made a TP adjustment contending that such payment of commission was only benefitting the AE's units/ subsidiaries in the countries were products were exported and that it was unnecessary for the assessee.

Further, the AO noting that the LTAA restricted the use of know-how for exports, contended that the EA was an extension of the LTAA and re-characterised the commission payment under the EA as royalty/know-how payable under the LTAA. Accordingly, he held that tax ought to have been deducted at source and disallowed the payment of commission made under section 40(a)(i).

3. The DRP confirmed the order of the AO.

4. As regards the TP adjustment made by the AO / TPO, the Tribunal observed that the allegation of the AO that the assessee had not benefitted from such payment, was incorrect as the assessee had earned profits of ` 13.05 crores through exports. Accordingly, the TP adjustment made by the AO was deleted.

With regard to the AO's treatment of export commission as royalty, the Tribunal held that since the assessee had not been transferred or permitted to use any patent, invention, model, design or secret formula under the EA, the payment was not in the nature of royalty. Similarly, no managerial, technical or consultancy services had been rendered to the assessee under the agreement and therefore it was not in the nature of fee for technical services. Accordingly, the disallowance u/s. 40(a)(i) was deleted.

5. Aggrieved, the Revenue filed an appeal before the Court challenging the deletion of disallowance under Section 40(a)(i) on the ground that in the absence of a principal-agent relationship between HMCL and the assesssee, the payment of commission was nothing but a payment of royalty for the use of the know-how to manufacture vehicles for export which was liable for tax deduction at source. The Revenue also contested that no consideration / benefit accrued to the assessee by way of such payment. However, the deletion of TP adjustment by the Tribunal was not contested by the Revenue.

6. The assessee contended that EA was entered into two decades after it had entered into LTAA with HMCL and that it continued to pay separate royalty under the LTAA and therefore, the two agreements were separate. It further contended that it was only due to the payment of export commission that it was permitted to export the Hero Honda brand of vehicles and that the said payment led to the ceding of the territories by HMCL in favour of the assessee whereby the assessee was enabled to use the existing distribution network of HMCL to export its products.

**Judgment**

1. The Court held that EA which was entered into in June 2004 could not be said to be extension of LTAA as the technical know-how was being licensed to the assessee by HMCL since 1984 and accordingly, the two agreements were distinct and independent.

2. It further held that the payment of the export commission was not without consideration as it permitted the assessee to export specified two wheelers manufactured under the Hero Honda brand to the specified countries and the assessee did not have to pay for using the existing distribution and sales networks in those territories. Accordingly, there was no question of principal-agent relationship to justify payment of the export commission.

3. It further held that the attempt at recharacterising the transaction as one involving payment of royalty overlooked the fact that the payment under the LTAA was treated by the assessee itself as royalty. Further, it observed that the assessee had earned profits of ` 13.05 crores on account of exports and accordingly, was benefitted from the payment of export commission.

4. Accordingly, the Court upheld the Tribunal's order and held that the payment of export commission by the assessee to HMCL was not in the nature of payment of royalty or fee for technical services attracting disallowance under Section 40(a)(i) of the Act.

### 7. As there was no deliberate attempt by the assessee to conceal any income, the Court upheld the Tribunal's order wherein penalty under Section 271(1)(c) of the Act was deleted on the ground that the assessee had accepted the TP adjustment merely to buy peace of mind

*Gap International Sourcing India Ltd. [TS-323-HC-2017(Del.)-TP]*

**Facts**

1. The assessee, incorporated in India as a wholly owned subsidiary of GAP International Sourcing Inc, USA, operated as a procurement support service company whereby it facilitated sourcing of apparel merchandise from India for its AE. The assessee was remunerated at total operating costs plus a 15% mark-up thereon. The goods were sourced by the AE directly from the third party vendors in India and were not routed through the financial accounts of the assessee. The assessee, a low-risk service provider benchmarked its transactions with AEs by adopting TNMM as the most appropriate method.

2. The TPO accepted TNMM as the most appropriate method, however, re-characterised the assessee as a 'significant risk bearing' entity having intangibles as opposed to a low risk service provider. Accordingly, it determined ALP of assessee's transactions by determining commission at 5.22% (arithmetic mean of the comparables) on the value of goods procured by the foreign AE directly from third party vendors from India and made TP adjustment.

3. The addition made by the AO was confirmed by the DRP.

4. In the quantum proceedings, the Tribunal noting that it was entitled to a cost plus mark-up on total operating cost of Gap International Sourcing India Ltd. (and not the value of goods sourced by GAP US), rejected the assessee's recharacterisation as a significant risk bearing service provider and accepted the assessee's classification i.e. low risk service provider. However, the Tribunal did not accept assessee's mark-up of 15% and instead relying on the Delhi Tribunal's decision in the case of ***Li & Fung's [TS-583-ITAT-2011(Del.)-TP]*** substituted the mark-up of 32% (i.e. the maximum operating margin adopted in Li & Fung decision). The assessee conceded by accepting the mark-up of 32% consequent to the decision of the Tribunal where the final adjustment was restricted to only ` 6.92 crores as against addition of ` 255.97 crore made by the AO.

5. Thereafter, the AO levied penalty in terms of Explanation 7 of Section 271(1)(c), on the ground that the mark-up of 15% had not been accepted by the Tribunal and the enhanced mark-up had been conceded by the assessee and it could not be said that the computation of price charged or paid by the assessee in the international transaction was computed in good faith and with due diligence.

6. CIT(A) confirmed the order of the AO.

7. The Tribunal followed the decision of the Co-ordinate Bench in the assessee's own case for the earlier AY wherein similar penalty had been deleted on the ground that penalty could not be imposed merely because the addition was accepted by assessee. The Tribunal held that the assessee had made a choice to accept 2% of the addition (i.e. ` 6.92 crore vis-a-vis adjustment of ` 255.97 crore made by the TPO) made by AO and exercise of such choice in order to achieve peace of mind in the absence of *mala fide* intention, could not attract penalty u/s. 271(1)(c) for concealment or filing of inaccurate particulars. It further held that the TPO accepted TNMM as the most appropriate method and accepted PLI and comparables selected by the assessee. Further, the Tribunal in the quantum proceedings accepted assessee's claim that it was a limited risk bearing support service provider. Accordingly, it held that the TP study carried out by the assessee was in good faith and with due diligence adhering to the requirements of Section 92C.

8. Aggrieved, Revenue preferred appeal before the High Court.

**Judgment**

1. The Court noted that in the quantum appeal, the assessee had accepted the cost plus mark-up of 32% as suggested by the Tribunal based on the decision of Li & Fung (India) Private Limited to buy the peace of mind. Accordingly, it held that there was no deliberate attempt by the assessee to conceal any income or to underpay tax and upheld the Tribunal's decision deleting the penalty levied by AO.

## 8. Reimbursement of salary to seconded employees assisting the assessee in the business and in the area of consultancy, management etc. did not make available any technical know-how or consultancy and consequently was not fees for technical service under the India-UK DTAA.

*Marks & Spencer Reliance India Pvt. Ltd. [TS-178-HC-2017(Bom.)]*

**Facts**

1. The assessee, a joint venture between Marks and Spencer Plc, a UK entity (M&S) and Reliance Retail Ltd. (RRL) entered into an agreement with M&S whereby the assessee was provided personnel to carry out functions in the area of management, setting up of business, property selection and retail operation, product and merchandise selection and setting up merchandise team. For the said services, the assessee made a payment to M&S without deducting taxes at source u/s. 195 of the Act claiming the payments to be in the nature of mere reimbursement of salary to the seconded employees at cost without any mark-up/income element. However, the AO held that the sum was chargeable to tax as fees for technical services (FTS) under DTAA as the services i.e. management, selection of property, and retail operations were in the nature of business strategies and advisory and therefore, it was in the nature of FTS on which tax was to be deducted. Consequently, he passed order u/s. 201 treating the assessee as assessee in default.

2. CIT(A) ruled in favour of the assessee.

3. The Tribunal held that the impugned payment was not FTS as per Article 13(4) of India-UK DTAA since Marks and Spencer by providing employees to the assessee or assisting the assessee in the business and in the area of consultancy, management etc. did not make available any technical know-how or consultancy which was pre-condition for taxability under

Article 13(4). It further held that the payment made was a mere reimbursement of expenses at cost and therefore, in the absence of any profit element in the said transaction, TDS u/s. 195 was not deductible.

4. Aggrieved, Revenue appealed before Bombay HC.

**Judgment**

1. The Court upheld the order of Tribunal wherein the Tribunal concluded that the assessee's payment to Marks & Spencer PLC towards salary expenditure of employees providing assistance in area of management, setting up of business etc. amounted to deputation of employees of Marks and Spencer for the promotion of the business of the assessee. It held that since the said payment to the employees was already subjected to tax in India in the hands of the employees therefore there was no question of treating the assessee in default for non-deduction of tax at source.

## 9. Final assessment order passed without draft order is not a curable defect and would render the assessment proceedings invalid

*Turner International India Pvt. Ltd. [TS-400-HC-2017(DEL)-TP]*

**Facts**

1. The assessee, a wholly-owned subsidiary of Turner Broadcasting System Asia Pacific Inc. was engaged in the business of sub-distribution of distribution rights and sale of advertisement inventory on satellite delivered channels. For AYs 2007-08 and 2008-09, it had entered into international transactions involving Distribution Activity segment.

2. The AO made reference to the TPO, who passed separate orders for both the AYs after determination of the ALP. On the basis of the TPO orders, the AO passed draft assessment orders, which were objected to by the assessee before the DRP.

3. The DRP concurred with the TPO, the AO passed final assessment orders, which were appealed by the assessee before the Tribunal.

4. The Tribunal, observed that neither the assessee nor the TPO had taken into consideration appropriate comparables and therefore the ALP determination was not justifiable. Accordingly, it set aside DRP's order and remanded the matter to the AO for undertaking a transfer pricing study afresh.

5. Pursuant to the Tribunal's order, the TPO once again proposed upward adjustments for each of the AYs. Thereafter, the AO passed final assessment orders in respect of both AYs confirming the additions proposed by the TPO. The AO also issued notices of demand u/s. 156 and notices u/s. 271(1)(c) initiating penalty proceedings.

6. Aggrieved, the assessee filed a writ petition before Delhi HC challenging the final assessment orders and the consequent demand notices on the ground of non-compliance with mandatory provision contained in Section 144C(1) which requires the AO to first frame draft assessment order.

**Judgment**

1. The Court relied on the AP High Court ruling in the case of ***Zuari Cement Ltd. [TS-271-HC-2013(AP)-TP]*** (which was subsequently affirmed by SC [TS-270-SC-2013-TP]) and Madras High Court decision in the case of ***Vijay Television Pvt. Ltd. [TS-172-HC-2014(Mad.)-TP]*** wherein it was held that failure to pass a draft assessment order u/s. 144C (1) would render the final assessment order without jurisdiction, null and void and unenforceable and Madras High Court further held that the corrigendum passed by the AO treating earlier assessment order as draft order was also invalid.

2. It rejected Revenue's contention that the failure to adhere to the mandatory requirement of issuing a draft assessment order u/s. 144C(1) was a curable defect and that consequently, the matter should be remanded to AO to pass a draft assessment order.

3. It held that the failure by the AO to adhere to the mandatory requirement of Section 144C(1) of the Act (of first passing a draft assessment order) would result in invalidation of the final assessment order and the consequent demand notices and penalty proceedings. Accordingly, it set aside the demand notices issued by AO and the initiation of penalty proceedings.

## 10. Reimbursement of AMP expenditure would be part of operating profit while computing PLI

*Samsung Electronics India Information & Telecommunications Ltd [TS-324-HC-2017(Del.)-TP]*

**Facts**

1. The assessee had incurred advertising, promotion and marketing (AMP) expenditure which was partly reimbursed by its AE. In its books of account, it reduced the reimbursement from expenditure incurred and debited only the net expenditure to profit and loss account.

2. The TPO while computing AMP of the international transactions did not consider reimbursement as part of operating income while it treated AMP expenditure as part of operating expenses and accordingly, made TP adjustment.

3. On appeal, the CIT(A) upheld the assessee's claim of treating reimbursement as part of operating income and recomputed the assessee's margin after including reimbursement and accordingly, deleted the adjustment.

4. On appeal by the Revenue, Tribunal observed that the AO/TPO had equated reimbursement to the windfall gain or some adhoc payment. It followed its earlier order in case of Samsung India Electronics Pvt. Ltd. (which was merged with the assessee) and the same was affirmed by the Delhi High Court and held that the entire reimbursement received by assessee was to be treated as operating income.

5. Aggrieved, Revenue filed appeal before the Court.

**Judgment**

6. The High Court following its earlier decision, upheld the order of the Tribunal that the entire reimbursement received by assessee was to be treated as operating income.

## 11. Reimbursement of cost for idle infrastructure was to be excluded from operating margin computation since the reimbursement of costs was without any mark-up

*CPA Global Services Private Limited [TS-329-HC-2017(Del.)-TP]*

**Facts**

1. The assessee (CPA GSP), was wholly owned subsidiary of CPA Mauritius Limited (CPA Mauritius) which in turn was subsidiary of CPA Jersey. The assessee offered comprehensive range of legal support services to both its AEs as well as to independent third party customers and earned a margin of 36.08% on cost. Pursuant to the inter-company agreement with its AE, the assessee had received two kinds of reimbursement from its AE i) towards service which had mark-up and this was accounted for in working out the ALP; ii) reimbursement towards the cost on idle infrastructure which was without any mark-up. The assessee did not route this amount to its profit and loss account as it was a cost-cost reimbursement and did not include the same in its ALP computation.

2. While determining the ALP, the TPO included the cost of idle infrastructure in the operating costs (without including the reimbursement for such costs received from the AE as operating income) on the ground that the assessee had not produced any evidence in support of its claim that the expenditure towards maintenance of spare capacity was not to be included in the operating cost.

3. DRP held that all the costs should be included for ALP computation since the assessee had failed to give reasons for excluding the costs. However, it directed the AO to consider the

reimbursement of such costs for computing the margins.

4. Following the principles laid down by the Delhi Tribunal in ***Cheil Communications India P. Ltd. [TS-145-ITAT-2014(Del.)-TP]*** and Hyderabad Tribunal in ***Four Soft Limited [TS-104-ITAT-2014 (Hyd.)-TP]*** and after examining the relevant clauses of the agreement, the Tribunal held that the reimbursement costs of infrastructure were to be excluded as there was no mark-up on these reimbursements and they did not involve any functions to be performed so as to consider it for the profitability purposes. Accordingly, it directed AO/TPO to exclude such reimbursement costs while working out the operating costs.

5. Aggrieved, Revenue preferred an appeal before the Court. The Revenue contended that the Tribunal had overlooked the Delhi High Court's decision in the case of ***Cushman and Wakefield (India) (P.) Ltd. [TS-150-HC-2014 (Del.)-TP]*** wherein the Court had agreed with the Revenue under similar circumstances and had remanded the matter to the TPO for re-determination of the TP-adjustment. Further, the Revenue contended that the order of the Tribunal was perverse and bad in law since it failed to consider the reasons provided by the TPO/DRP in their orders for the inclusion of the costs.

**Judgment**

1. The Court observed that the Tribunal had examined the agreement and had arrived at a factual conclusion that reimbursement of the infrastructure costs of the assessee by the AE was without any mark-up and accordingly, was to be excluded.

2. The Court distinguished the facts of Cushman and Wakefield case since in that case the reimbursement was made by the Indian entity for costs incurred by the AE whereas in the present case it was *vice versa*. Further, in that case there was no categorisation of the reimbursement costs (as cost of infrastructure and cost of services). Accordingly, it held that each case was to be considered on the basis of peculiar facts as per the clauses of the agreement between the Indian entity and its AE.

3. Further, with regard to Revenue's contention that the Tribunal's order as 'perverse and bad in law' it held that this plea of the Revenue was a general plea as the Revenue had not pleaded with specificity as to in what manner there was perversity in the factual finding by the Tribunal and nor was any reference made to any particular document to support such plea. The Court observed that the Tribunal had examined the agreement between the assessee and its AE and had come to the conclusion that the reimbursement of the infrastructure cost had no mark-up.

4. Accordingly, in absence of any specific plea by the Revenue as to the perversity in the Tribunal's order, the Court dismissed the Revenue's appeal.

## 12. Payment made to University for training/collaborative research (used for recovery of oil) was in the nature of FTS since technical know-how was made available and since the assessee was not engaged in extraction/ production of mineral oil, provisions of section 44BB would not be applicable

***ONGC as representative assessee for M/s. University of Calgary, Alberta, Canada [TS-175-ITAT-2017(Del.)]***

**Facts**

1. The assessee had made payments to University of Calgary, Alberta, Canada ('University') pursuant to a contract for long term collaboration, participation, training, maintenance of air injection equipment which was used for increasing the recovery of oil. It filed its return of income showing nil income in its capacity as the representative assessee of the University on the ground that as per India-Canada DTAA, the sum payable to the University was not FTS as the University had not made available any know-how to the assessee while rendering the said services.

2. The AO treated the payment made as 'fees for technical services' u/s. 9(l)(vii) taxable on gross basis by applying Sec 115(A). The assessee contended that even if the said payment was taxable in India, the same should be taxed as per the provisions of Section 44BB as the payments were made for maintenance of the air injection equipment used for recovery of oil and since the services rendered was directly associated with extraction and production of mineral oil, the consideration paid would be excluded from the definition of fees for technical services. However, the AO held that the consideration paid was outside the purview of Sec 44BB.

3. CIT(A) dismissed assessee's appeal.

4. Aggrieved assessee filed an appeal before the Tribunal.

**Judgment**

1. The Tribunal observed that as per the scope of the agreement, the know-how possessed by the University was shared and 'made available' to the ONGC personnel as the agreement contemplated participation, training and collaborative research between the personnel of the University and the assessee. Accordingly, it held that the sum paid to University was FTS both under the Act and the DTAA.

2. Further, it observed that Section 44BB of the Act applies in case where consideration is for services relating to exploration activity which are not in the nature of technical services. If, the consideration was in the nature of fee for technical services, the provisions of either Section 44DA or Section 115A would be applicable. Accordingly, it held that the provisions of Section 44BB would not apply since the personnel of the University were not engaged in extraction or production of mineral oils. Therefore, it upheld the order of AO taxing the same as FTS.

## C. TRIBUNAL

### 13. Payment made for the purchase of shrink wrapped software would not amount to royalty

*National Stock Exchange of India Ltd. vs. DDIT (International Taxation) (2017) 50 CCH 0038 Mum. Trib.*

**Facts**

1. The assessee had procured a shrink wrapped software from Minitab Inc. USA under a non-exclusive and non-transferable licence together with the right to receive technical services, updates and maintenance of the software. The assessee had no right to use, copy, sell the software or to make more copies of it or to provide access to anyone other than its employees. The assessee did not deduct tax on the payment made on the ground that the assessee was allowed to use the software only for its own business without any liberty to transfer the said software or any rights therein and therefore, there was no transfer of any rights in the software purchased not amounting to 'Royalty' within the meaning of Article 12(3) of the India-US Tax Treaty.

2. The AO held that the assessee was getting licence to use software and since the software was an intellectual property which fell under the category of copyrights, patents, designs, trademarks, formula, process, commercial/ scientific knowledge and payment for the same amounted to royalty as per Section 9(1)(vi) as well as under Article 12(3) of the Indo-USA DTAA. Accordingly, it held that the assessee was required to deduct tax u/s. 195 and since, he failed to do so he issued notice u/s. 201(1) for treating the assessee as 'assessee-in-default'.

3. The CIT(A) upheld the order of the AO.

4. Aggrieved by the order of CIT(A), the assessee appealed before the Tribunal.

**Judgment**

1. The Tribunal following the decisions of Delhi High Court in the case of ***DIT vs Infrasoft Ltd. (264 CTR 329) (Del.)*** and various other Tribunals, held that the software sold by M/s. Minitab Inc USA to the assessee fell into the category of "copyrighted article" against acquisition of "copyright". Further, it held that the definition under the DTAA contemplated

use of copyright and was narrower than the definition under the Act. Accordingly, even if the payment was regarded as royalty as per explanation to Section 9(1)(vi), the DTAA would prevail over the Act.

2. Further, noting that there were contrary and possible views i.e., Delhi High Court decision in the case of Infrasoft in favour of the assessee and Karnataka High Court decision in the case of ***CIT vs. Samsung Electronics Co. Ltd. (2011) 345 ITR 494 (Kar. HC)*** against the assessee, it held that if two constructions are possible the one in favour of the assessee was to be adopted. Accordingly, following the Delhi High Court decision, it held that transfer/sale of software was not taxable as royalty and the assessee was not liable to deduct tax at source u/s. 195.

## 14. The Tribunal adopted LIBOR + 2% for benchmarking the interest on loan given to AEs, held that corporate guarantee given for the loan taken by the AE was not an international transaction and held sharing of profits between the assessee and its AE to be *bona fide*

***Dr. Reddy's Laboratories Limited [TS-331-ITAT-2017(Hyd.)-TP]***

**Facts**

1. The assessee engaged in the manufacture and sale of bulk drugs and other pharma products:

A) Had advanced loan to its AEs viz., Lacock Holdings Ltd. @ 5% p.a. and Falcon Mexico @ 9.56% p.a. In respect of loan given to Lacock Holdings Ltd., it adopted ALP of LIBOR + 2% and claimed the loan to be at ALP. In respect of interest on loan given to Falcon Mexico, the assessee adopted average lending rate prevalent in Mexico @ 8.3% and claimed it to be at ALP. Moreover, it claimed that the interest was at ALP since it was approved by RBI.

B) Had given corporate guarantee to its subsidiary and claimed that the same was not an international transaction since there was no expenditure or loss on account of the guarantee provided to the AE as a result of which it did not charge any fees.

C) Had developed a Drug for Glaxo Smithkline (GSK) USA's patented drug (Sumatripon) along with its AE (DRL, USA). It was agreed that since DRL USA had strong distribution network they would market the product of GSK (Sumatripon) in USA with support of DRL India pursuant to which the profits arising were to be split equally between DRL USA and DRL India. Further, the assessee entered into an agreement with DRL Switzerland whereby DRL Switzerland had undertaken the insurance for product liability and Shelf Stock Adjustment (SSA) risks. In return the assessee agreed to share 50% of its profits with DRL, Switzerland as a result of which DRL USA passed-on 50% of share of DRL India to DRL Switzerland (i.e. 25% of the transaction). Assessee offered only net profit arising out of / in marketing and distribution activities, received by it from DRL USA.

2.A) With respect to interest on loan to AE, the TPO contended that merely because interest was in accordance with RBI Regulations, it did not imply that the same was at ALP. In respect of interest charged to Lacock Holdings Ltd., since the loan was given in Euros, the TPO compared it with EURIBOR rate @ 4.37% and after adding suitable risk premium, adopted ALP of 6.5% as against 5% charged by the assessee. In respect of interest on loan given to Falcon Mexico, the TPO rejected assessee's adoption of average lending rate in Mexico @ 8.3% contending that the same was applicable for the customers having good credit rating whereas the assessee had low credit worthiness. Accordingly, it adopted prime lending rate in Mexico i.e. 12% as the ALP and made consequent adjustments.

B) With respect to corporate guarantee, the TPO determined ALP of the fee for corporate guarantee at 1.3% (based on the difference between recourse @ 0.7% and non-recourse rate 2%) of the loan. The assessee contended before the TPO that relying on the DRP's order in the earlier year, the guarantee commission should be restricted to 0.7%. However, TPO rejecting the assessee's contention, made TP adjustment.

C) With respect to profit sharing between the assessee and DRL Switzerland, the AO observed that, business arrangement between the assessee and the DRL, Switzerland was not reported properly in 3CEB report or in TP. documentation to show that the same was within arm's length range. He contended that the transaction between DRL, India and DRL, USA was an arrangement of shifting taxable profits (25%) from India to Switzerland. Accordingly, he disallowed the expenses claimed by the assessee.

3.A) With respect to interest on loans to AE, the DRP concurred with the view of the AO that the interest rates prevalent in the respective countries would be the current indicator and upheld the order of AO.

B) With respect to corporate guarantee, the DRP relying on its order for the earlier year, directed the AO to adopt 0.7% of the loan amount as ALP.

C) With respect to profit sharing between the assessee and DRL Switzerland, the DRP upheld the order of AO

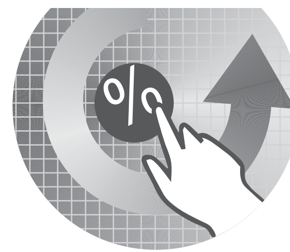
4. Aggrieved, the assessee appealed before the Tribunal.

**Judgment**

1.A) With respect to interest loan on to AE, the Tribunal relying on its decision in the assessee's own case for the earlier years accepted LIBOR + 2% for benchmarking interest transaction and thereby set aside the matter to AO directing him to adopt LIBOR rate applicable for the years under consideration + 200 basis points to arrive at the ALP.

B) With respect to corporate guarantee, the Tribunal, relying on the Delhi Tribunal's decision in the case of ***Bharti Airtel Limited [TS-76-ITAT-2014(Del.)-TP]*** and Mumbai Tribunal's decision in the case of ***Siro Clinpharm Pvt. Ltd. [TS-144-ITAT-2016(Mum.)-TP]***, held that even though explanation to Section 92B was stated to be clarificatory in nature, it was effective from the A.Y. 2013-14 and accordingly, it could not be applied retrospectively. Accordingly, it held that since the assessee had not incurred any costs in providing corporate guarantee it would not constitute international transaction within the meaning of Section 92B of the Act and deleted the TP adjustment. It further held that merely because in the earlier years the adjustment with respect to guarantee commission was accepted by the assessee, it could not be said that the assessee could not contest the same in the subsequent year.

C) With respect to profit sharing between the assessee and DRL Swiss, the Tribunal held that DRL SA (Switzerland) had undertaken product liability insurance and SSA risk to earn 25% share out of profits. It further noted that the assessee had entered into an agreement with DRL SA for sharing of profits from the point of being a business entity and held that the Revenue was not entitled to analyse the business decision from it's perspective. Accordingly, it held that the agreement between DRL India and DRL SA was not bogus and since the details of compensation received by were duly furnished in the TP report and it could not be said that there was shifting of profits.



CA. Hasmukh Kamdar

# INDIRECT TAXES

## Central Excise and Customs – Case Law Update

***Bar Association vs. Commissoner of C. Ex. & S.T., New Delhi. [2017 (349) E.L.T.477 (Tri. – LB) interim order dated 20-4-2017***

**Pre-deposit**

The issue in dispute in this case was whether an appellant has to pay 10% mandatory deposit over and above the mandatory deposit of 7.5% of duty liability/penalties, as the case may be, as provided under section 35F of the Central Excise Act, 1944. The dispute arose due to different orders of Tribunal, more specifically, Delhi Bench of the Tribunal in the case of ***Balaji Structural (India) Pvt. Ltd. vs. Commissioner of Central Excise Raipur***, held that deposit of 10% of the amount of duty and penalty as the case may be for preferring an appeal before the Tribunal against the Commissioner (Appeals) order is inclusive of 7.5% deposited at the time of preferring appeal before the first appellate authority from the adjudication order, while the Bench of the Tribunal in the case of ***Hindalco Industries Ltd. and Others [2017 (49) STR 590 (Tribunal)]*** and ***ASR Multimetals Pvt. Ltd. and Others [2017 (345) ELT 294 (Tribunal)]*** held that pre-deposit of 10% of the amount of duty and penalty as the case may be needs to be deposited over and above the amount mandated to be deposited before the first appellate authority.

On behalf of the revenue it was contended that the pre-deposit before the first appellate authority and second appellate authority are independent provisions. The plain reading of the provisions indicate that the appellant if he wants to prefer a second appeal has to deposit additional 10% of the amount of duty/penalty as the case may be over and above the amount of deposit made for preferring the appeal before the first appellate authority. Reliance was placed on the decision of the Tribunal in the case of ***ASR Multimetals Pvt. Ltd. and Others [2017 (345) ELT 294 (Tribunal)]*** and CBEC Circular No. 984/8/2014 dated 16-9-2014 for the same proposition.

None appeared for Bar Association but written submissions were made.

The Larger Bench quoted the following relevant provisions of the Central Excise Act, 1944:

Section 35F – Deposit of certain percentage of duty demanded or penalty imposed before filing Appeal –

The Tribunal or Commissioner (Appeals), as the case may be, shall not entertain any appeal –

(i) Under sub-section (1) of section 35, unless the appellant has deposited seven and half per cent of the duty, in the case where duty or duty and penalty are under dispute, or penalty where such penalty is under dispute, in pursuance of a decision or an order passed by an

officer of Central Excise lower in rank than Principal Commissioner of Central Excise or Commissioner of Central Excise.

(ii) Against the decision or order referred to in clause (a) of sub-section (1) of section 35B, unless the appellant has deposited seven and half per cent of the duty, in case where duty or duty and penalty are under dispute, or penalty where such penalty is under dispute, in pursuance of a decision or an order appealed against.

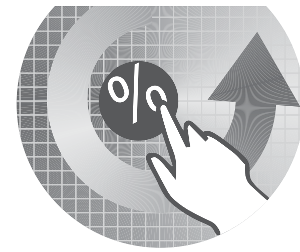
(iii) Against the decision or order referred to in clause (b) of sub-section (1) of section 35B, unless the appellant has deposited ten percent of the duty, in case where duty or duty and penalty are under dispute, or penalty where such penalty is under dispute, in pursuance of a decision or an order appealed against.

Provided that the amount required to be deposited under this section shall not exceed rupees ten crores.

The Larger Bench observed that the dispute is basically only on the point as to the pre-deposit mandated for preferring second appeal before the Tribunal. Revenue submitted that CBEC Circular dated 16-9-2014 indicates clear intention of the legislature. The Larger Bench further observed that paragraph 2.1 of the Circular only states that in the event of appeal of appellant against order of Commissioner (Appeals) before the Tribunal, 10% is to be paid on the amount of duty demanded or penalty imposed by the Commissioner (Appeals). In fact the clarification given by the Board does not indicate what is in the mind of the law makers while enacting the provisions of section 35F of the Central Excise Act, 1944. The Tribunal noted that the said provisions of pre-depositing an amount for preferring first appeal against the adjudication order needs to be done so, at the rate of 7.5% of the duty confirmed or penalty imposed as the case may be. This would mean that first appeal can be entertained only on deposit of such amount and on conclusion of the proceedings, he has option to go further in appeal before the first appellate authority or if the appeal is disposed of, the amount pre-deposited by him which is equivalent to 7.5% of the duty confirmed or penalty imposed as the case may be, needs to be refunded in accordance with law.

As regards the second appeal preferred against the first appellate authority's order, the quantum of pre-deposit has been set at 10% instead of 7.5% of the duty confirmed or penalty imposed. It was further observed that both the appellate proceedings i.e. before the first appellate authority and before the Tribunal, if it is to be treated as independent provisions than deposits as mandated needs to be made. In short, in order to prefer an appeal before the Tribunal, as assessee/appellant needs to deposit 10% of the amount of duty confirmed or the penalty imposed as the case may be irrespective of the amounts equivalent to 7.5% deposited by them for preferring an appeal to the first appellate authority. On reading the provisions of pre deposit under Central Excise Act, 1944 if an assessee wishes to exercise his statutory right of second appeal, then the said exercise of right, it needs to be considered as an independent right and proceeding subsequent to pre-deposit of the amount to exercise the first appeal needs to be considered as having come to closure. In that case the assessee may seek legal remedies available to him, as regards the mandatory pre-deposits made before the first appellate authority; it needs to be decided according to the law.

In view of the above discussion, the Larger Bench held that the decision of the Division Bench of the Tribunal in the case of ***ASR Multimetals Pvt. Ltd. and Others [2017 (345) ELT 294 (Tribunal)]*** is correct and the appellant is required to deposit separately 10% of the amount of duty confirmed/ penalty imposed, for preferring of appeal before the Tribunal against the order of Commissioner (Appeals).



Nikita Badheka, *Advocate & Notary*

# INDIRECT TAXES
## VAT Update

The Finance Minister of State of Maharashtra presented LA Bill No. XVIII of 2017 to amend certain provisions of the Maharashtra Value Added Tax (MVAT) Act and the other laws administered by the State of Maharashtra.

### A. Amendments to Profession Tax Act

**A.1** Section 3 of the Profession Tax Act (Short name) makes every person excluding firms (whether registered under the Indian Partnership Act, 1932, or not) and Hindu Undivided Family engaged actively or otherwise in any profession, trade callings or employment and falling under one or the other of the classes mentioned in the second column of Schedule I to be liable to pay the profession tax. In terms of the third proviso now amended, if a person who is liable to pay tax has remained unenrolled; then, his liability to pay tax under this section for the periods for which he has remained so unenrolled shall not exceed

i) Four years if the certificate of enrolment is granted after 1-4-2017

ii) Eight years in any other case from the end of the year immediately preceding the year in which the enrolment certificate is granted or the year in which the proceeding for enrolment is initiated against him, whichever is earlier.

**A.2** Section 4A is introduced to limit the liability of employer, who registers on or after 1-4-2017, to pay for four years from the end of the year immediately preceding the year in which the registration certificate is granted or the year in which the proceeding for Registration is initiated against him, whichever is earlier.

**A.3** A new section 4B is introduced under which the State Government is empowered to notify the class of persons who should deduct profession tax out of the amount of commission paid or payable to agent . The manner of making the payment by the Commission agent will be notified. The provisions relating to employer, employee will apply to such persons liable to deduct and pay.

**A.4** Section 9 of the Profession Tax Act relates to interest on unpaid taxes . Sub-section (2) is amended. An employer referred to in that sub-section shall be liable to pay simple interest at the rate prescribed on the amount of the tax payable for each month or part thereof after the last date by which he should have paid the tax.

### B. Amendment to Maharashtra Entry of Goods in Local Areas Rules, 2003

Rule 8(1) which restricted the time limit to assess the URD is deleted. Sub-rule 8(3) is substituted specifically from 1-4-2005. The

assessment of URD importer shall be made by the Assessing Authority in whose jurisdiction the specified goods are found or detected to have been consumed, used or sold.

### C.1 Amendment to Assessment & Appeal Provisions: Sections 23 & 26 of MVAT Act

Drastic amendments are made in appeal and assessment provisions. In an appeal against ex parte order the Appellate Authority is now empowered to set aside the ex parte order and remand the matter to the Assessing Authority. Such remand order should be passed within 9 months of the commencement of this Act for the appeals which are already filed on the commencement date. For the appeals which are filed after this Act coming into force, the Appellate Authority may remand the matter within six months from the date of filing the appeal. The Assessing Authority shall pass a fresh assessment under section 23(6) within 18 months in case of remand by the First Appellate Authority and within 36 months if the remand is by any other authority. The period of limitation starts from the date of communication of the order to the concerned authority.

### C.2 Cancellation of Order powers withdrawn

Simultaneously Section 23(11) which allowed cancellation of order by the Assessing Authority will no longer be applicable to the assessment orders passed after commencement of the present Act.

### C.3 Stay – Mandatory Part Payment

The grant of stay was a separate proceeding till date once the appeal is filed. The dealer could continue the matter on merit without grant of stay. In the present Bill Section 23 Sub-section 6A is introduced wherein it is made mandatory to file the appeal with the proof of payment of 10% of the disputed tax. However, with the liability in the order is on account of non-production of declaration then in terms of 23(6) already existing in the statute book, the dealer will have to pay full tax for the declarations which are not received till passing of the order. If the appeal is against the separate order imposing penalty, the Appellate Authority can direct the deposit of amount, not exceeding 10% of the amount of penalty disputed by the appellant. The 10% payment of the disputed tax has the upper cap of ` 15 crores. Therefore, if the disputed tax is more than ` 150 crores, say for example, ` 200 crores, the maximum 10% amount payable is ` 15 crore only.

### C.4 Second Appeal – Mandatory payment

Section 23 Sub-section 6B is inserted for making similar amendment for a Second Appeal to be filed before the Tribunal with the only difference that the 10% payable would be of balance amount of disputed tax. On the amount being paid as stated in sub-section 6A and 6B the stay shall be granted to the appellant. Consequential amendments are made to section 40 of the MVAT Act.

**C.5** Time limit for filing appeal before the High Court is extended to 180 days from the date of communication of the order of the Tribunal.

### C.6 Amendment to Interest Provision

Under newly inserted section 30(5), the State Government is empowered to issue notifications to remit the whole or part of the interest in respect of any period, payable by the prescribed class of registered dealers, who are not able to pay the tax due to technical problem of automated system of Department or who have obtained the registration late.

### C.7 State to have first charge for recovery

In terms of the newly inserted section 37(2), the first charge of the State as mentioned in 37(1) shall be deemed to have created on completion of the 30 days of service of the demand notice issued by the Commissioner.

### C.8 Interest on Delayed Refund

Sub-Section 1A is inserted into section 53. This beneficial provision reduces the time for grant of interest if the refund due after the

commencement of this Act, is delayed beyond 60 days.

**C.9 Amendment to section 8(3C)**

An amendment was made to this section in 2012. This sub-section empowers the State Government to exempt fully from payment of tax, the transfer of property in goods involved in processing the textiles described in First Schedule of the Additional Duties of Excise (Goods of Special Importance) Act, 1957. The words (as it stood immediately before 8th April, 2011) are substituted by inserting a new clause a-1 to the effect that the notification that 2012 amendment shall be deemed to come into force from 8th April, 2011.

One more amendment is made to section 8(3D). This sub-section empowers the State to exempt by way of notification, the transfer of property in goods involved in sizing and wrapping of yarn either retrospectively or prospectively. The notification is discussed hereafter

## D. Amendment to Schedule Entries

| Schedule Entry No. | Description | New Rate of Tax |
|---|---|---|
| **Sr. No. 1 Schedule A-64 New Entry** | Sale, during the period from the 1st April, 2005 to 31st March, 2016, of processed, semi-processed, semi-cooked, ready-mix, ready-to-eat, shelled sweet corn, whether or not sold<br>(a) In a frozen state, or Treasury.<br>(b) In a sealed container, or<br>(c) Under a brand name,<br>except when served for consumption<br>Condition:<br>(1) Tax should not have been collected from the customer.<br>(2) Tax should not have been paid into Government Treasury | **NIL** |
| **Sr. No. 2 Schedule A-8A** | **Card Swipe machines for merchant transactions** | **NIL** |
| **Sr. No. 3 Schedule A-9A** | (a) Paddy, rice, wheat and pulses in whole grain, split or broken form; (b) The flour of wheat & rice including atta, maida, rawa and suji whether sold singly or in mixed form; (c) The flour of pulses including besan when sold singly and not mixed with flour of other pulses or cereals, sold during the period from 1st May, 2006 to the date immediately preceding the date on which GST law shall come into force | **NIL** |
| **Sr. No. 5 Schedule A-25A Newly inserted** | Gas or electric fired human body incinerator | **NIL** |
| **Sr. No. 6 Schedule A-25B** | Geomemberine use for farm pond of thickness of not less than 500 mircons having BIS specification | **NIL** |

| Schedule Entry No. | Description | New Rate of Tax |
|---|---|---|
| **Sr. No. 7 Schedule A-33A** | Milk testing kit for detecting milk adulteration | **NIL** |
| **Sr. No. 8 Schedule A-44A New entry** | Soil testing kit for determination of soil nutrients | **NIL** |
| **Sr. No. 9 Schedule A-51(ix)** | Amsul | **NIL** |
| **Sr. No. 10 Schedule A-51, 59** | All the goods described in this entry shall continue to be exempt from 1-4-2017 to the date immediately preceding the date on which GST law shall come into force | **NIL** |
| **Sr. No. 11 Schedule C – 108** | All the goods described in this entry shall continue to be exempt from 1-4-2017 to the date immediately preceding the date on which GST law shall come into force | |
| **Sr. No. 12 Schedule D** | Amendment is made in the heading. Schedule D as list of goods for which rate of tax is up to 60% | |
| **Sr. No. 13 Schedule D-11A New entry** | Aviation, turbine fuel (duty paid) sold within the State of Maharashtra during the period starting on 1st April, 2017 to 31st March, 2027 for flights under regional connectivity scheme as communicated by Airport Authority of India, subject to the conditions to be notified in the Official Gazette. | **1%** |
| **Sr. No. 14 Schedule D-6** | Aviation, turbine fuel (duty paid) other than those covered by Schedule C-8 and Entries 11 and 11A of this Schedule | **25%** |
| **Sr. No. 15 Notification relating to liquor under section 41(5)** | The Notification relating to liquor covered by D1, 2 & 3 dated 30th April, 2011 is modified. The exemption in Schedule 1 of this notification refer to a formula as<br>MRP x 30/130 in respect of sales mentioned in column 3<br>This formula is now substituted by MRP x 35/135 with effect from 1st April, 2017.<br>Some further amendments are expected to this notification. However, the same is not uploaded | |

## E. Amendment to CST act

The taxation laws Amendment Act, 2017 – No. 18 of 2017 dt. 4-5-2017

On introduction of GST Act, the applicability of CST Act would be restricted to a few products, namely:

Petroleum products, High Speed Diesel, Motor Spirit (petrol), Natural Gas, Aviation Turbine Fuel and Alcoholic Liquor for Human Consumption.

Accordingly CST Act is amended to restrict the meaning of goods to only above specified goods.

The definition of Declared Goods sec 2(c) and sections 14 and 15 will also be deleted

**This amendment will come in to force from the date to be notified.**

**F.1 Amendment to Schedule entry D-10 – 21st April, 2017 and 17th May, 2017**

This entry is twice amended.The entry reads as follows up to 16th May 2017 :

Any other kind of Motor Spirit

(a) When delivered,

(i) To a retail trader for trading from place of business situated within the geographical limits of the Municipal Corporations of the Brihan Mumbai, Thane, Navi Mumbai and within such other areas for such period as may be notified by the State Government in the Official Gazette;

**Rate amended from 22nd April, 2017 to 16th May, 2017 – 26% + Nine rupees per litre**

(ii) To a person other than the retail trader having place of business situated within the geographical limits of the Municipal Corporations of the Brihan Mumbai, Thane, Navi Mumbai and within such other areas for such period as may be notified by the State Government in the Official Gazette;

**Rate amended 26% + Nine rupees per litre from 22-4-2017 to 16th May, 2017**

(b) When delivered in circumstances other than those mentioned in clause (a) above.

**Rate amended from 22-4-2017 to 16-5-2017 – 25% + Nine rupees per litre**

**After 17-4-2017 – entry merged as follows.**

**D-10 w.e f. 17th May, 2017**

Any other kind of Motor Spirit

(a) When delivered,

(i) To a retail trader for trading from place of business situated within the geographical limits of the Municipal Corporations of the Brihan Mumbai, Thane, Navi Mumbai and within such other areas for such period as may be notified by the State Government in the Official Gazette;

**Rate amended w.e.f. 17-5-2017 – 26% + Eleven rupees per litre**

And

ii) To a person other than the retail trader having place of business situated within the geographical limits of the Municipal Corporations of the Brihan Mumbai, Thane, Navi Mumbai and within such other areas for such period as may be notified by the State Government in the Official Gazette;

**Rate amended w.e.f. 17-5-2017 – 26% + Eleven rupees per litre**

**F.2 Amendment regarding sizing and wrapping of yarn**

Please refer to C-9 above wherein I have referred to amendment to section **8(3D)**. This sub-section empowers the State to exempt by way of notification, the transfer of property in goods involved in sizing and wrapping of yarn either retrospectively or prospectively. Accordingly a notification is issued on 19th April, 2017, modifying the notification dt. 29th April, 2016. The said Order is made effective from 1-4-2005. The conditions added to the earlier order are as follows:

a) No exemption if the tax is recovered from the Customer

b) The tax is recovered or paid in part, the exemption will be restricted to the extent not recovered.

c) If the tax in full or part is recovered ,but not deposited in Govt. Treasury, the same ought to have been deposited within one month from 17th April, 2017

d) If tax is paid, setoff will be granted to the extent deposited with Government.

**F.3 Notification regarding remission in interest on account of delayed application for registration**

In furtherance to power granted u/s. 30(5), a Notification No. VAT 1517/C R 43 (c)/ Taxation-1 19th April, 2017 is issued the Notification provides remission of 75% of Interest subject to following conditions

a) Application for registration is made between 18th March, 2017 and 30th June 2017

b) Compute the tax liability for URD period as if he is RD.

c) Pay the full tax and file returns for such period on or before 31st July, 2017

d) Make application to concerned J C (VAT –ADM-Nodal Division in the forms specified on or before 31st July, 2017

e) Compute the interest under section 30(1) for each period and make payment of 25% on or before 31st July, 2017.

Kindly refer to Ciruclar 38T of 2016 dt. 30th December, 2016. This circular gives details of the dealers who qualify for grant of ADM relief under MVAT Act, CST Act and Maharashtra Tax on Luxuries Act.

**G.1 Circular by the Commissioner for GST Registration**

Trade Circular No. 5T of 2017, dated 27-2-2017, Trade Circular No. 6T of 2017 dated 4-3-2017, Trade Circular No. 9T of 2017 dated 9-3-2017 and Trade Circular No. 12T of 2017 dated 25-4-2017, 17T of 2017 dt. 30-5-2017

All the above Circulars refer to distribution of GST Provisional ID and access to the token of Phase-1, Phase-2, Phase-3 & Phase-4. The last Circular i:e. 12T refers to Phase-4 and the types of dealers covered by Phase-4. The dealers not covered by Phase-4 are the dealers newly registered after 31-3-2017, dealers already registered for Service Tax or Central Excise Registration No. although registered under MVAT the Mahavikas database on PAN is either blank or invalid PAN. If there are dealers who have not been able to register in the above 4 Phases should contact the JC-Mahavikas. The latest Circular No. 17T opens up for the Phase 5 dealers .Dealers whose PAN amendment is carried out up to 12-5-2017 are not included in this phase. The dealers whose name do not appear in Phase 5 and are registered under Excise or Custom are directed to contact help desk.

For the information of members the portal is reopened from 1st June, 2017 and will remain open up to 15th June only.

**G.2 Trade Circular 8T of 2017 dated 16-3-2017**

This refers to facility to view draft return before submitting the same. There is some modification in the process which is explained in this Circular. The process of preparation of return in excel and converting into txt file remains the same. The dealers are required to upload txt extension file. A draft return will get prepared. The dealer will receive the SMS and e-mail in excel template which shall mention that the draft of the return uploaded is ready for submission. The dealers are requested to check SPAM folder for the mails so delivered. If the dealer is satisfied with the return uploaded he may choose to file the draft return. If he chooses to modify the draft return then he should again upload modified return in

txt extension file. For the addition tax payable on account of modification the dealer should make the payment for taxes for a return period and mention the same in amount already paid in the return. A video demo of this process is available on the Mahavat Website. As regards goods return claim under the CST Act all the deductions on account of rate difference and discount, if the turnover of sale or purchase is less than goods return, such goods return could not be shown in CST return. The Commissioner has directed by this Circular to enter such difference in the manner enterable in the MVAT return. (In the new template i:e. "Latest Return Template Version 3.0.000 for VAT/CST" it is possible now.)

**G.3 Trade Circular 9T of 2017 dt. 1st April, 2017 r/w Circular 14T of 2017 dt. 26th April, 2017 & 16T of 2017 dt. 17th May**

Circular 9T refers to exemption for payment of Late Fee u/s 20(6). In the last circular 34T of 2016 the dates for filing Monthly returns for April to Sept., 16 was mentioned. Circular 8T of 2017 stated that no late fees would be charged if the tax dues are paid before the due date. On representation from Trade & Tax Consultants Association the due dates were extended.In the latest Circular 16T by virtue of the powers u/s. 20(6) the whole of the late fees payable by any dealer who files returns for the periods of any month or quarter for 2016-17 shall stand exempted if such returns are filed on or before 15th June, 2017. It is further clarified that no further extension will be allowed to file the returns for the above periods. The return filing process is explained in detail in this Circular.

**G.4 Trade Circular 10T of 2017 dt. 6th April, 2017**

This Circular explains the amendment made to the liquor provision and amendment to Schedules A, C & D. The effective date of each of the amendment is stated in this Circular.

These details are already discussed in the previous paragraphs and therefore not repeated herein.

**G.5 Trade Circular 11T of 2017 dt. 15th April, 2017**

This Circular explains various amendment made to the MVAT & Allied Law, The Legislature having received the accent on 15th April, 2017 the circular is issued to explain the amendment. Few of the important things now clarified are as follows:-

a. The curtailed period of tax liability of 4 years to the persons unrolled under the Profession Tax Act would be admissible to the persons who have obtained enrolment after 1st April, 2017. (For the dealers enrolled between 1-4-2016 and 30-9-2016 the concession was already granted in the previous year). Similarly the employers who have obtained registration after 1st April, 2017 would only get the benefit of restricted liability of 4 years.

b. As regards to amendment to the appeal provisions the Commissioner has clarified that even if the appeal is pending before Tribunal against part payment order arising out of ex-parte order, then such assessment orders be set aside and remanded back in terms of section 23(7) and the appeal before Tribunal be withdrawn.

c. As regards mandatory part payment of10% it is clarified that the amended provisions would apply to appeals filed against the order passed on or after 15th April, 2017. It is clarified that the provision will not apply to the appeals pending before First Appellate Authority or the Tribunal. The Tribunal and the First Appellate Authority would not have discretion to fix the part payment for admission of appeal. The provision regarding mandatory 10% part payment would apply to the appeals passed under CST Act, excluding the liability on account of missing declaration.

d. As regards liability on account of missing declaration it is clarified that if the liability

arose despite furnishing the declaration as the same are disallowed as defective the dealer will not be required to pay 100% of disputed tax.

### G.6 Trade Circular 13T of 2017 dt. 26th April, 2017

In furtherance to amendment made to Profession Tax Act three notifications are issued under the Profession Tax Act. In terms of the first notification the benefit of exemption of whole of late fees would be available to employer who files return for payment of tax for any period up to 31st March, 2017 on or before 30th September, 2017. The second notification specifies that the provisions of filing of return, payment of tax, assessment, recovery, appeal etc. in relation to the employer and employee shall ***mutatis-mutandis*** apply to the insurer liable to deduct the profession tax and the agents from whom such tax has to be deducted.

The third notification under Profession Tax Act gives the modified interest rate w.e.f. 1st May, 2017

| Sr. No. | Period liable for interest | Rate of interest |
|---|---|---|
| 1 | Delay up to one month | One and quarter per cent of amount of such unpaid tax, for the month or for part thereof. |
| 2 | Delay up to three months | (1) ***Delay up to one month*** – One and quarter per cent of the amount of such unpaid tax, for the month or for part thereof<br>(2) ***Delay beyond one month up to three month*** – One and half per cent of the amount of such unpaid tax, for each month or part thereof. |
| 3 | Delay more than three months | (1) ***Delay up to one month*** – One and quarter per cent of the amount of such unpaid tax, for the month or for part thereof<br>(2) ***Delay beyond one month up to three month*** – One and half per cent of the amount of such unpaid tax, for each month or part thereof.<br>(3) ***Delay more than three months*** – Two per cent of the amount of such unpaid tax, for each month or part thereof. |

An example is given in the Circular to demonstrate the amendment.

### G.7 Trade Circular 15T of 2017 dated 26th April, 2017

Pursuant to the powers given to the State Government to issue notification to provide remission of interest a notification is published on 19th April, 2017. Details already explained herein above in F-3 under the Notification Heading. The procedures are explained in this Circular along with the application form.

### G-8 Important Internal Circular regarding ITC Match-Mis-Match

Internal Circular 11A of 2017 dt. 3rd May, 2017 refers to guidelines regarding cross checking of ITC. The benefit of Circular 1A of 2013 is extended to all the periods up to 2015-16. It is further clarified that –

a. Unmatch ITC means ITC not matched due to one of the TIN not being uploaded in either J1 or J2. Whereas Mis-Match ITC is due to difference in amount of transaction disclosed. Out of the total purchase on which ITC is claimed ITC on

purchase from non-genuine dealer, RC cancelled dealers and return non-filers will be disallowed after due verification and from the remaining suppliers the Top 10 suppliers or the suppliers covering 50% of ITC (whichever is more) should be considered.

To the extent unmatch ITC in top 10 or 50% suppliers, the same can be allowed only after supplementary J1 or J2.

b. Mis-match in ITC from top 10 suppliers or suppliers covering 50% of ITC (Whichever is more). Such ITC can be verified through confirmation of ledgers along with copy of returns, acknowledgment for the month of March for the financial year in dispute or acknowledgment of 704 filed for the said financial year duly signed and stamped by the dealer.

It is further clarified that the ledger confirmation will not be asked if the claim of ITC is below ` 5,000/- per supplier per year.

**G.9 Amendment to Composition Scheme for Builders and Developers**

In this circular in para 6 the Commissioner has explained the liability of Builders under GST. Considering the construction contracts which will continue after GST coming into force, the CST has opined that supply that takes place after commencement of SGST Act would be liable to pay GST irrespective of the fact that the Developer has discharged the liability on the value stated in the registered agreement. The CST has relying on sec 142(11)(C) opined that such dealers would be able to take benefit of Tax paid under MVAT Act.

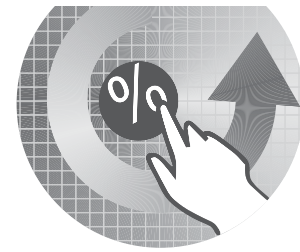
Notification of 1% rate of tax is amended for the agreements which are not registered on or before 31st May, 2017. In terms of this amendment the Developer who desires to opt for the revised composition scheme is required to pay 1% of the amount received (as advance or otherwise) towards booking of the aforesaid property. In terms of the new amendment, the link between payment of tax and registration is done away with. For the agreements which are not registered on or before 31st May, 2017 the Developer is required to pay 1% of the amount received as advance or otherwise in respect of flats. The tax so computed should be paid on or before 30th June, 2017. The Developer should disclose turnover of sale for the month of June.

For the agreements to sale whether registered or not after 1st June, 2017, the Developer to pay 1% of the amount received as advance in respect of flats. The Developer should pay the tax so computed before 21st day after succeeding month in which the payment is received. The Developer should disclose the turnover of sale in the return for the said month.

Therefore, the Developer who opts for composition on or after 1st June, 2017 till the date of commencement of SGST would be liable to pay 1% tax in respect of the amount received from the prospective buyer towards booking of flat.

As a corollary to the above amendment, a new section 3B is added to section 42. After the commencement of GST the Developer would get the credit of the tax paid under MVAT Act to the extent of supply made on or after commencement of SGST Act.

As a result of this amendment the Developer who has paid tax under the old composition scheme of 2010 and if the supplies are continued on or after commencement of SGST Act, then the Developer has to mandatorily determine 1% tax of the amount received as advance or otherwise, immediately before the date of commencement of SGST Act. The Developer shall deduct 1% tax so calculated from the composition amount paid under the old scheme and if the tax paid under the earlier composition is more than 1% tax amount calculated as per new scheme, then the Developer would be eligible to take the credit into the electronic credit ledger under SGST Act.



CA Rajkamal Shah & CA Naresh Sheth

# INDIRECT TAXES

## Service Tax – Statute Update

### I. Service Tax on Transportation of goods by a vessel from a place outside India up to the custom station of clearance in India

Pursuant to withdrawal of exemption for services provided by a person located in non-taxable territory to a person located in non-taxable territory by way of transportation of goods by a vessel from a place outside India up to the custom station of clearance of India effective from 22nd January, 2017, the Government has issued Notification no. 13/2017-ST, 14/2017-ST, 15/2017-ST and 10/2017-CE (NT) all dated 13th April, 2017. The effect of these notifications have been summarised in the circular dated 13-4-2017 as under:

1. Person liable to pay tax – The importer of goods as defined in the Customs Act, 1962 (w.e.f. 23-4-2017)

2. Alternate mechanism to pay service tax (w.e.f. 22-1-2017)– Option to pay an amount calculated @1.4% of CIF value of the imported goods + 0.05% of Swachh Bharat Cess + 0.05% Krishi Kalyan Cess totalling to 1.5% of the CIF value (as determined u/s. 14 of The Customs Act, 1962 and rules made thereunder) – no conditional exemption of payment of tax of 30% value shall be allowed for non availment of CENVAT credit as provided Notification No. 26/2012-ST.

3. Point of taxation – The date of bill of lading of the goods in the vessel at the port of export (no service tax is payable if B/L is dated prior to 22-1-2017).

4. The importer shall be allowed to avail CENVAT credit on the basis of challan or payment of service tax (w.e.f. 23-4-2017).

> All the powers in the universe are already ours.
>
> — ***Swami Vivekananda***

Janak C. Pandya, *Company Secretary*

# CORPORATE LAWS
# Company Law Update

## Case Law No. 1

*[2017] 202 Comp Cas 179 (Guj.)*
*[In the Gujarat High Court]*
*Ajay Surendra Patel vs. Deputy Commissioner of Income Tax*

**Section 179 of the Income-tax Act is itself a statutory creation of piercing of corporate veil and can be invoked to lift corporate veil to crack the corporate shell even in case of a public limited company. Thus, in a situation where exigency arises, in absence of any statutory provisions, the court is entitled to lift the corporate veil.**

**Brief case**

The petitioner has filed the present petition for challenging the legality, validity and propriety of an order under Section 179 of the Income-tax Act, 1961 ("ITA"). The facts are as follows:

1. The petitioner had joined as a director of Hirak Biotech Ltd. ("Company").
2. He had also subscribed to the shares of the Company and was holding about 98% of the total share capital of the Company.
3. A show cause notice was served upon him under Section 179 of the ITA as a director for non-payment of dues payable by the Company.
4. The petitioner had earlier filed a petition before this Hon'ble High Court for quashing the said show-cause notice.
5. The Hon'ble High Court partly allowed the petition and directed the Income Tax Authority ("Authority") to follow the due process of law and giving the petitioner an opportunity to reply.
6. After observing the statutory provisions, the Authority issued a fresh show cause notice to the petitioner giving all particulars and details and stated as to why steps should not be taken under Section 179 of the ITA.
7. Various correspondences were exchanged between the petitioner and the Authority, including the last reply sent from petitioner's tax consultant stating that there is no liability of the petitioner for the affairs of the Company.
8. The Authority passed an order by lifting the corporate veil of a company and held all the three directors, including the petitioner, as defaulters under Section 179 of the Act.
9. The petitioner invoked the extraordinary jurisdiction of the court against the said order of the Authority.

On behalf of the petitioner, the following submissions were made:

1. Company is a public limited company and hence invocation of Section 179 of the ITA is impermissible and without the authority of law. None of the conditions which are required to be established for invoking Section 179 were made against the petitioner.
2. The petitioner had not participated in the operation of the Company and had not signed any tax returns. He only held 98% of the total share capital of the Company.
3. He had resigned long back as a director of the Company.
4. The Petitioner was not guilty of any misuse of power nor he had grossly neglected or committed any breach of duty in any manner as alleged by the Authority.
5. Authority had materials on records which indicated that another director was dealing with the Company's operations.
6. Vicarious liability cannot be inferred when the petitioner never participated as a director. Unless a fraud is practised to benefit the petitioner, lifting or piercing of corporate veil cannot be permitted.
7. The facts of the judgment in ***Pravinbhai M. Kheni vs. Asst. CIT*** as referred for lifting of corporate veil is incorrect. It was submitted that in that case, the demand was for ` 150 crores and that the court had found that the Company was structurally incorporated as a public company but was akin to a private company so to skip the provisions of Section 179 of the ITA. However, the said judgment cannot be applied as a straitjacket formula for current case.

From the Authority's side, following submissions were made:

1. The Company was formed with a view to provide accommodation entries in the form of bogus share capital and share premium.
2. The Petitioner had joined the Company for very limited period. During this period, he had acquired 98.33% of the share capital.
3. The maximum cash flow had come into Company's bank accounts during the tenure of the petitioner. This smacks a clear doubt about the version which has been projected by the petitioner.
4. Even though the Company was formed as a public limited company, the characteristics of its affairs are found to be akin to a private limited company.
5. When a person holds majority shares of a company, then it is deemed that such person participated in the affairs of the Company. In this case, the petitioner provided full support to another director and thus it appears to be a serious dereliction of duty on his part as a majority shareholder.
6. The Authority also provided the assets position of the Company and stated that after taking action under Section 226(3) of the ITA, the balances of various assets becomes zero. Further, during this period, the properties in question were sold. There was a huge demand of other financial institutions also.
7. The total demand, including penalty from regular assessment, was ` 240.08 lakhs, which is further subject to interest under Section 220(2) of the ITA. When such huge demand for relevant period has remained unpaid when the petitioner was a director, he is equally responsible for the ultimate outcome of the Company.
8. It is the petitioner who has brought the affidavit of another director, who has

taken the responsibilities on himself just to accommodate the petitioner and therefore close nexus ***inter se*** between them cannot be encouraged.

**Judgment and reasoning**

The court opined that there appears to be no infirmity in the order and dismissed the petition with a view that same is devoid of merits. The points considered by the court are as follows:

1. Though the Company is a public limited company, the directors appeared to have acted in a detrimental way which falls within the purview of Section 179 of the ITA. There were several instances of defaults in financial transactions with other banks too.

2. Based on the facts, the Company had obtained the commencement certificate only after the petitioner joined as an additional director. The Company has started the business only after the petitioner acquired majority share capital and joined as a director. The huge demand from the Authority is for the year when the petitioner was the director.

3. The court analysed Section 166 of the Companies Act with respect to the position of a director. It was noted that a director has a fiduciary relationship with the company and he cannot plead ignorance completely about the affairs of the Company. The court has also referred the Supreme Court judgment in the case of ***N. Narayanan vs. Adjudicating Officer, SEBI [2013] 178 Comp Cas 390 (SC); AIR 2013 SC 3191*** has held that …" failure of a corporate governance on the part of directors if they failed to exercise due care and diligence and thereby allowing fabrication of figures and false disclosures, they would be liable for such omissions and commissions.". The judgment in the case of *Official Liquidator, Supreme Bank Ltd. vs. P.A.Tendolkar [1973] 43 Comp Cas 382* ***(SC); [1973] 1 SCC 602*** was also referred. In the said judgment, it was held that a director may be shown to be placed closely and personally associated with the management of the Company that he will be deemed to be liable for fraud in the conduct of the Company even though no specific act of dishonesty is provided against him personally.

4. On lifting of the corporate veil, the court referred the judgment of ***Aron Salomon vs.*** *A. Salomon and Co. Ltd. [1897] AC 22 (HL).* The judgment of the Supreme Court in the case of ***Juggilal Kamalpat vs. CIT [1970] 75 ITR 186 (SC)*** was also referred. In the said judgment, it was held that the court can lift the corporate veil if the same is used for tax evasion or to circumvent the tax obligations. A similar kind of judgment in the case of *CIT vs. Sri Meenakshi Mills Ltd.,* ***[1967] 63 ITR 609 (SC)*** was also mentioned.

5. The concept of lifting corporate veil to crack the corporate shell can be restored even in the case of a public limited company. The judgment in the case of ***Pravinbhai M. Kheni vs. Asst CIT [2013] 353 ITR 585 (Guj.)*** was referred. Section 179 of the ITA was made applicable for recovery of tax dues as the said section is itself a statutory creation of piercing of corporate veil.

6. The judgment of the Division Bench of the Delhi High Court in the case of ***India Waste*** *Energy Development Ltd. vs. Government of NCT of Delhi [2003] 114 Comp Cas 82 (Delhi)* was also referred. In the said judgment, the court held that even in situation where exigency arises, in absence of any statutory provisions also, the court is entitled to lift the corporate veil.

CA Mayur Nayak, CA Natwar Thakrar &
CA Pankaj Bhuta

# OTHER LAWS
## FEMA Update and Analysis

In this article, we have discussed proposed and recent amendments to FEMA:

### 1. Draft Regulations under Foreign Exchange Management Act, 1999 for Cross Border Mergers

Section 234 of the Companies Act, 2013 provides for mergers and amalgamations between Indian companies and foreign companies. Recently, Ministry of Corporate Affairs has issued Companies (Compromises, Arrangements and Amalgamation) Amendment Rules, 2017 on April 13, 2017 to operationalise this section.

In order to address the issues that may arise when an Indian company and a foreign company enter into Scheme of merger, demerger, amalgamation, or rearrangement, Reserve Bank of India on 26th April, 2016 placed on its website the draft guidelines for cross-border merger, demerger, amalgamation and arrangement between Indian companies and foreign companies pursuant to the Rules notified by MCA as mentioned above.

These Regulations stipulate conditions that should be adhered to by the companies involved in the Scheme. The Regulations shall be named Foreign Exchange Management (Cross-Border Merger) Regulations.

Members of public, including the stakeholders and experts in the area, were requested to offer their views and comments on the proposed Regulations latest by May 9, 2017.

The salient features of the draft guidelines are as follows:

#### A. Inbound Merger – Merger or amalgamation of a Foreign Company with an Indian Company

In case of cross border mergers where the resultant company is an Indian company,

a. Any issue or transfer of security by the resultant company to a person resident outside India shall be in accordance with the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000.

b. Any borrowing or impending borrowing of the foreign company from overseas sources which becomes the borrowing of the resultant company or any borrowing from overseas sources entering into the books of resultant company arising shall conform to the External Commercial Borrowing norms or Trade Credit norms or other foreign borrowing norms, as

laid down under Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 or Foreign Exchange Management (Guarantee) Regulations, 2000, as applicable.

c. The resultant company may acquire and hold any asset outside India which an Indian company is permitted to acquire under the provisions of the Act, rules or regulations framed thereunder. Such assets can be transferred in any manner for undertaking a transaction permissible under the Act or rules or regulations framed thereunder.

d. Where the asset or security is not permitted to be acquired or held by the resultant company under the Act, rules or regulations, the resultant company shall sell such asset or security within a period of 180 days from the date of sanction of the Scheme of cross border merger and the sale proceeds shall be repatriated to India immediately through banking channels.

**B. Outbound merger – Merger or Amalgamation of an Indian Company with a Foreign Company**

In case of cross-border mergers where the resultant company is a foreign company,

a. A person resident in India may acquire or hold securities of the resultant company in accordance with the Foreign Exchange Management (Transfer or issue of Foreign Security) Regulations, 2000 or the provisions of the Liberalised Remittance Scheme, as applicable.

b. The resultant company shall be liable to repay outstanding borrowings or impending borrowings as per the Scheme sanctioned by the National Company Law Tribunal in terms of the Companies (Compromises, Arrangement or Amalgamation) Rules, 2016.

c. The resultant company may acquire and hold any asset in India which a foreign company is permitted to acquire under the provisions of the Act, rules or regulations framed thereunder. Such assets can be transferred in any manner for undertaking a transaction permissible under the Act or rules or regulations framed thereunder.

d. Where the asset or security is not permitted to be acquired or held by the resultant company under the Act, rules or regulations, the resultant company shall sell such asset or security within a period of 180 days from the date of sanction of the Scheme of cross-border merger and the sale proceeds shall be repatriated outside India immediately through banking channels.

**C. Valuation of companies involved in cross-border merger**

The valuation of the Indian company and the foreign company for the purpose of cross-border merger shall be done as per internationally accepted pricing methodology for valuation of shares on arm's length basis which should be duly certified by a Chartered Accountant/public accountant/ merchant banker authorized to do so in either jurisdiction.

**D. Reporting**

The transactions arising due to cross-border mergers are proposed to be reported to RBI as required under FEMA.

Further, the Indian company and the foreign company involved in the cross-border merger shall be required to furnish reports as the Reserve Bank may prescribe.

Also, deemed approval shall be given by the Reserve Bank as required under Rule 25A of

the Companies (Compromises, Arrangement and Amalgamations) Rules, 2016, for any transaction undertaken in accordance with the above draft FEMA Regulations.

*Draft Notification No. FEMA/2017 RB dated April 2017)*

***(Comments: The provisions under Section 234 of the Companies Act, 2013 allowing cross-border mergers was ineffective in absence of corresponding regulatory approvals under FEMA and hence the proposed relaxation has long been awaited and has in fact become necessary in light of various amendments in domestic tax laws (POEM, GAAR, etc.) and international tax laws (CbCR & BEPS Action Plan). This amendment will allow the trade and industry to restructure their cross-border operations. Heavy penalties may be imposed if the resultant company does not adhere to time limit of 180 days for unwinding positions (Loans, Assets, etc.) which are not in accordance with FEMA.)***

## 2. Cabinet approval for phasing out Foreign Investment Promotion Board

The Union Cabinet chaired by the Prime Minister Shri Narendra Modi has given its approval to the phasing out of Foreign Investment Promotion Board (FIPB). The proposal entails abolishing the FIPB and allowing administrative Ministries/ Departments to process applications for FDI requiring Government approval.

Henceforth, the work relating to processing of applications for FDI and approval of the Government thereon under the extant FDI Policy and FEMA, shall now be handled by the concerned Ministries/Departments in consultation with the Department of Industrial Policy & Promotion (DIPP), Ministry of Commerce, which will also issue the Standard Operating Procedure (SOP) for processing of applications and decision of the Government under the extant FDI policy.

*(Press Release dated 24th May, 2017 by Press Information Bureau, Government of India)*

***(Comments: This is a welcome move. Foreign Investors will find India more attractive destination and this will result in more inflow of FDI. The move will provide ease of doing business and will help in promoting the principle of Maximum Governance and Minimum Government.)***

## 3. FAQ on Overseas Direct Investment

RBI Update on FAQs on April 12, 2017 on overseas Direct Investment.

*Refer https://www.rbi.org.in/Scripts/FAQView.aspx?Id=120*

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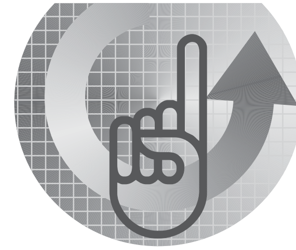

Ajay R. Singh, *Advocate*

# BEST OF THE REST

## 1. Passport to foreign national – Child born in India to British Citizens enjoying status of overseas citizens – Not entitled to issuance of passport: Passport Act section 20 & Citizenship Act Sections 7A & 7B

The Petitioner is a two-month old baby, born to parents, who are overseas citizens of India cardholders, represented by her guardian and mother. Petitioner is aggrieved by the stand of the 2nd respondent in not receiving her application for a passport enabling her to go abroad along with her mother, a permanent resident in United Kingdom.

The parents of the petitioner were Indian citizens and their marriage was solemnised in the year 2006 as per the rites prevailing in Hindu Nair community. Parents of the petitioner were holding Indian passport till 2010. In the year 2008, mother of the petitioner. became a British citizen, and in the year 2013, father of the petitioner became a British citizen. Therefore, parents of the petitioner have secured British Passport. Parents of the petitioner, by virtue of the provisions of Indian Citizenship Act, 1955, are registered as overseas citizens of India. As per Section 7B of the Act, an overseas citizen of India cardholder is entitled to all those rights and privileges other than those coming under sub-section (2) of Section 7B of the Act. The mother of the petitioner is working as a Nurse in Al-Ain hospital, Abu Dhabi and has to return for duty by 15th of September, 2016 and she wants to take the petitioner along with her for which a valid passport and other travel documents issued by the 1st respondent is necessary. It is the further contention of the petitioner, as per Section 20 of the Passport Act, the competent authority can issue the passport or travel documents to a person who is not a citizen of India.

The question to be considered is whether a child born in India to British citizens, enjoying status of overseas citizens, is entitled to secure a passport under the Passports Act, 1967.

The Hon'ble High Court observed that the father and mother of the petitioner were Indian citizens. However, both of them renounced Indian citizenship and acquired British citizenship in 2013 and 2008 respectively. The parents of the petitioner are cardholders of overseas citizens of India issued under Section 7A of the Act. However overseas citizens of India are provided with only limited rights enumerated above, as per Section 7A of the Act. Therefore, over and above the rights conferred to the overseas cardholders, no other right can be demanded by the parents of the petitioner. In that view of the matter, merely because parents of the petitioner were Indian citizens by origin, who have secured citizenship of United Kingdom, have no liberty to seek issuance of passport merely because they hold card of overseas citizens of India.

According to the learned counsel for the petitioner, Section 20 is an enabling circumstance for the petitioner to apply for a passport in order to have a way out to get over the present situation. However, Section 20 is qualified with a very important factor namely, public interest which differs from situation to situation. It may be a situation where extradition is done by the Government of India. It may be a situation where political asylum is provided by the Government of India to a non-national. It may be a situation where a non-national is deported in the best interest and security of the country, but it can never be said, the child born in India to foreign citizens of Indian origin is entitled in 'public interest', for an Indian passport. Therefore, the said ground raised by the learned counsel for the petitioner cannot also be sustained.

The Hon'ble Court observed that securing of passport is not a vested right not even to a citizen of India but it can only be secured on the basis of the provisions contained under the Passports Act, 1967. Moreover, Section 20 of the Passports Act deals with issuance of a passport to a foreign national. When there is a specific provision under the relevant statute to deal with a situation, it cannot be said that, in the absence of prohibition contained under Section 7B(2) of the Citizenship Act, 1955, petitioner is entitled as of right to obtain a passport.

However, the Court observed that the petitioner is entitled to seek appropriate reliefs before the Government of India, which may be in a position to extend necessary assistance to the petitioner on the basis of any treaty, agreement etc. etc. It is also observed that, the Ministry of External Affairs may explore the possibility of making a provision to tackle such a situation, exercising the power conferred on it under the Passports Act, 1967, or the Citizenship Act, 1955 and the rules thereunder, enabling to secure a travel document for a short duration.

***Seana Shanth vs. Union of India: Air 2017 Kerala 17.***

## 2. Judgment – Has to be pronounced in open Court, signed and dated : Cr. P.C. Sec. 353

Though CrPC does not define the term “judgment”, yet it has clearly laid down how the judgment is to be pronounced. The provisions clearly spell out that it is imperative on the part of the learned trial judge to pronounce the judgment in open court by delivering the whole of the judgment or by reading out the operative part of the judgment and explaining the substance of the judgment in a language which is understood by the accused or his pleader. Non-availability of judgment, needless to say, can never be a judgment because there is no declaration by way of pronouncement in the open court that the accused has been convicted or acquitted. A judgment, as has been always understood, is the expression of an opinion after due consideration of the facts which deserve to be determined. Without pronouncement of a judgment in the open court, signed and dated, it is difficult to treat it as a judgment of conviction. Practice of announcing result of case by stating “reasons to follow” is deprecated. In present case, judgment was not available on record and hence, declaration of result cannot tantamount to a judgment as prescribed in CrPC. That leads to inevitable conclusion that trial in both cases has to be treated to be pending.

***Ajay Singh and Anr and etc. vs. State of Chhattisgarh and Anr. AIR 2017 Supreme Court 310.***

## 3. Family Settlement – Whether compulsorily registrable: Registration Act, 1908 Sec. 17(1)(b)

Appellant-plaintiff had filed the suit for declaration to the effect that he is owner in possession of 50% share of house/plot.

The plaintiff-appellant and defendant-respondent were the real brothers having no other brother. The defendant joined the Army

in young age and plaintiff helped his father as well as was cultivating the agricultural land. In the year 1968, defendant approached the plaintiff with an idea that they should purchase some property outside their native village and proposed to buy house in a modern city like Delhi or Chandigarh. Defendant represented that both of them shall be joint owner of the plot and house purchased and constructed by the money of the plaintiff. The plaintiff believed and trusted his elder brother blindly and gave him ` 48,000/- in cash out of his income and funds earned from agriculture on the promise that defendant shall buy the plot in Chandigarh in the joint names of the plaintiff and defendant showing both of them as owner to the extent of 50%. Later on, he came to know that defendant has purchased/got allotted a two canal plot out of the said money. Thereafter, they decided that they will put their entire transaction in writing, so that there may not be any dispute in future and both the brothers would keep their share to the extent of 50% each. Ultimately, a family settlement regarding the aforesaid plot/house in question was executed between the parties in the presence of the witnesses on 10-11-1970, which was executed by defendant out of his free will since he felt morally bound and obliged as all the money for buying as well as for raising construction thereupon was raised by the plaintiff.

Thereafter, the plaintiff has been reminding the defendant off and on with respect to the entry in the record of the Estate Office, Chandigarh regarding 50% ownership in his favour, but each time the defendant had been putting of the matter on the excuse. Then, the plaintiff immediately demanded from the defendant regarding the change in the records as per the terms and conditions of the family settlement, but of no avail. Hence the suit.

The legal position is that where the document is containing terms and recitals of a family settlement made under the document and the beneficiary thereof had no pre-existing rights and the rights in the property are being created, declared and assigned for the first time by the documents itself in present or in future in any immovable property worth more than ` 100/-, the said family settlement will require compulsory registration. It is the duty of the Court to examine the family settlement to arrive at the conclusion as to whether the said document is just a memorandum of the family settlement which has already taken place or the document itself creates right. If it is found that it was just a memorandum of partition/ family settlement, which has already taken place between the parties and said memorandum has only been reduced into writing later on, that will not require registration. But, at the same time, as already mentioned in the document itself in present or in future creates a right, title or interest in the property for the first time, it shall be compulsorily registrable.

The court observed that the document shows that the right in the property has been created for the first time in favour of the plaintiff through the family settlement, the plot in question was allotted to defendant from the defence quota being an Army Officer. It was not established that the plaintiff has paid or contributed any amount for the purchase of the said plot, so he was not having any pre-existing rights in the said plot. So, the family settlement was compulsorily registrable, but the same is an unregistered document, hence the same is inadmissible in evidence and will not convey any right, title or interest in the suit property in favour of the plaintiff. Thus, he cannot claim himself to be the owner in possession of the plot in dispute to the extent of 50% share by the dint of the family settlement.

*Hargursharan Singh vs. Lt. Col. Hargobind Singh. AIR 2017 Punjab And Haryan*

## 4. Year – Term can mean calendar year or financial year, but would not mean 365 days. General Clauses Act – S. 3(66)

The Chief Engineer, Public Health (Urban), Odisha, Bhubaneswar – opposite party No.2 floated a tender, inviting applications from the intending bidders to participate in the national competitive bidding through e-procurement for distribution system in connection with water supply. The petitioner having satisfied all the eligibility criteria, submitted his application through e-procurement pursuant to such advertisement. Along with the petitioner, opposite party No.4 had also participated, but, he, having failed to satisfy the eligibility criteria. Subsequently, on the representation of opposite party No.4, his tender was considered and he was selected for execution of the work in question. Being aggrieved by such conduct of the authorities, the petitioner has approached this Court by filing the present writ petition.

Petitioner specifically urged before this Court that opposite party No.4 submitted his tender paper without satisfying the eligibility criteria, as required under sub-clause (i) of Clause (6) of the brochure. Though the intending bidders were required to have commissioned similar nature of work valuing not less than ` 90.33 lakhs in any one year within the last five years, on erroneous furnishing of information by opposite party No.4, even if he was initially qualified in the technical bid, subsequently, by virtue of the representation filed by opposite party No.4, his case was taken into consideration and was selected for the work in question by relaxing the terms and conditions of the tender call notice, which amounts to *mala fide* exercise of power by the authority.

The Court submitted that it is undisputed that the petitioner, vis-à-vis opposite parties No.4 and 5, participated in the said bid. Opposite party No.4, having not satisfied the requirement under sub-Clause (i) of Clause-6 of the tender call notice, i.e., experience of commissioning the similar nature of work valuing not less than ` 90.33 lakhs (30% of the estimated cost) in any one year during the last 5 (five) years, was totally disqualified by the Technical Committee from participating in the technical bid.

Opposite party No.4 was not eligible to participate in the bid, as he had not commissioned the work of similar type valuing not less than ` 90.33 lakhs (30% of the estimated cost) in any one year during the last 5 (five) years. Once the bid submitted by opposite party No.4 was rejected, having not submitted in conformity of sub-Clause (i) of Clause 6 of the tender document, subsequently, on submission of representation dated 19-2-2016, the Tender Committee considered the same in its 3rd sitting held on 22-2-2016 wherein it was unanimously decided that since there was an anomaly on the concept of "one year" in Clause 6(i) of the Detailed Tender Call Notice, the stipulation of "complete one year" would be considered as any of the following:

***"(i) One Calendar year (1st January to 31st December)***

*(ii) One financial year*

***(iii ) One year (365 days)"***

Therefore, in order to broaden the scope of competition, opposite parties No.4 and 5 along with the petitioner were declared qualified, for opening of their respective financial bids on the next day

In ***Raman Dayaram Shetty v. International Airport Authority of India, (1979) 3 SCC 489***, the Apex Court held that the words used in a document are not superfluous or redundant but must be given some meaning and weightage:

The meaning of "one year" in absence of any specific clarification thereof, the provisions contained in sub-section-66 of Section 3 of General Clauses Act, 1897 would be taken into consideration, which reads as follows;

***"Year" shall mean a year reckoned according to the British calendar"***

Considering the definition of the 'year' as mentioned above, one year preceding five years under sub-Clause (i) of Clause (6) has to be construed that a year reckoned according to the British calendar, meaning thereby it should be from first January of a year ended

with 31st December of the same year. Any subsequent clarification to this one year as 365 days or the financial year has no meaning at all, rather the same cannot be clubbed together to determine the eligibility of opposite party No.4 to participate in the technical bid.

The "one year" has to be construed as a calendar year, regardless whether it be a leap year or otherwise. The word 'year' has been considered in different context on the basis of the provisions contained under respective Acts. Meaning thereby a 'year' can be calendar year or a 'year' can be a financial year, but nowhere it has been stated that it should be 365 days. In absence of any specific clarification given in detailed tender call notice, issued by opposite party No.2, the year can be construed as a financial year in view of definition of sub-Section 66 of Section 3 of the General Clauses Act, 1897.

By giving relaxation to sub-Clause (i) of Clause (6) at the midst of the tender process, many other similarly situated persons have been debarred from participating in the tender process, as they found themselves ineligible to offer their bid when it was invited. If such subsequent relaxation is allowed to stand and benefit of such relaxation is extended to opposite party No.4 only, it would amount to unequal treatment in favour of opposite party No.4, which is unconstitutional and impermissible in law.

***Prafulla Kumar Pradhan vs. State of Odisha and Others AIR 2017 Odisha 19.***

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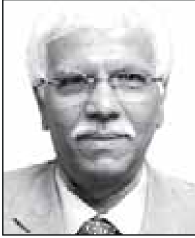

Kishor Vanjara, *Tax Consultant*

# TAX ARTICLES FOR YOUR REFERENCE

Articles published in Taxman, Current Tax Report (CTR), The Tax Referencer (TTR), Income Tax Report (ITR), ITR's Tribunal Tax Reports (ITR (Tribunal), The Bombay Chartered Accountant Journal (BCAJ), The Chamber's Journal (CJ), The Chartered Accountant Journal (CAJ), All India Federation of Tax Practitioners Journal (AIFTPJ), Company Case, Times of India and Economic Times for the period April to May, 2017 has been arranged and indexed topic-wise.

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Everything is easy when you are busy. But nothing is easy when you are lazy.

— ***Swami Vivekananda***

You have to grow from the inside out. None can teach you, none can make you spiritual. There is no other teacher but your own soul.

— ***Swami Vivekananda***

CA Hinesh R. Doshi, CA Haresh P. Kenia
*Hon. Jt. Secretaries*

# The Chamber News

Important events and happenings that took place between 8th May, 2017 and 8th June, 2017 are being reported as under.

## I. Admission of New Members

1) The following new members were admitted in the Managing Council Meeting held on 1st June, 2017.

**Life Membership**

| | | | |
|---|---|---|---|
| 1 | Mr. Meghnani Pravin Suresh | B.Com | Mumbai |
| 2 | Mr. Wadhwani Haresh Indru | B.Com | Mumbai |
| 3 | Mr. Patil Pandurang Hari | ITP | Kolhapur |
| 4 | Mr. Shah Dhiraj Ashok | Advocate | Kolhapur |
| 5 | Mr. Gawande Nitin Ratnakar | Advocate | Mumbai |
| 6 | Mr. C.K. Partha Sarathy | CA | Bengaluru |
| 7 | Mr. Jajoo Vinod Hiralal | CA | Nashik |
| 8 | Ms. Maru Hetal Deepak | CA | Mumbai |
| 9 | Mrs. Khajanchi Heena Chirag | CA | Mumbai |
| 10 | Mr. Jain Ajit Kumar J | CA | Mumbai |
| 11 | Mr. Bhandari Hemanth Hastimalji | CA | Chennai |
| 12 | Mr. Singh Mukesh Awadhesh Singh | CA | Mumbai |
| 13 | Mr. Hemani Bandish Jayesh | CA | Mumbai |
| 14 | Mr. Oza Janam Bharat | CA | Mumbai |

**Ordinary Membership**

| | | | |
|---|---|---|---|
| 1 | Mr. Gor Ashwin Vinod | ITP | Mumbai |
| 2 | Mr. Gilda Harilal Maneklal | CA | Mumbai |
| 3 | Mrs. Rustogi Shikha Aseem | CA | Mumbai |
| 4 | Mrs. Vora Bhakti Kush | CA | Mumbai |
| 5 | Mr. Madnani Akshay Ashok | CA | Mumbai |
| 6 | Mr. Nangia Jayant Ruplal | CA | Mumbai |

| | | | |
|---|---|---|---|
| 7 | Ms. Shah Ruchira Manish | Advocate | Mumbai |
| 8 | Mr. Chawla Divesh Raju | Advocate | Mumbai |
| 9 | Mr. Chaudhary Vaibhav | CA | Delhi |
| 10 | Mr. Goda Bhaumik | CA | Mumbai |
| 11 | Mr. Vora Viral Dilip | ICSI | Mumbai |
| 12 | Mr. Jain Kumarpal Mahendrakumar | CA | Mysore |
| 13 | Mr. Kumar Abhay | CA | Mumbai |
| 14 | Ms. Ajmera Shweta Girish | CA | Mumbai |
| 15 | Mr. Bogi Bikash Lakhi | CA | Mumbai |
| 16 | Mrs. Shettigar Chitrakshi Paresh | CA | Mumbai |
| 17 | Mr. Sinha Vinay Bhupendra | Advocate | Mumbai |
| 18 | Mr. Jain Arvind Ratanchand | ITP | Mumbai |
| 19 | Mr. Talwar Mandeep Singh Udham Singh | CA | Mumbai |
| 20 | Mr. Shah Ashish Ashwin Kumar | CA | Mumbai |
| 21 | Mr. Parekh Mihir Kirit | CA | Mumbai |
| 22 | Mr. Gupta Sumit Shashikant | Inter CA | Mumbai |
| 23 | Mrs. Sardesai Sheetal Suraj | CA | Mumbai |
| 24 | Mrs. More Neeta Anant | ITP | Mumbai |
| 25 | Mr. Bijur Narayan Macha | Advocate | Mumbai |
| 26 | Mr. Vaishnav Suresh Bherudas | CA | Mumbai |
| 27 | Mr. Varaiya Atul Venilal | ITP | Bijapur |
| 28 | Mr. Shah Tejpal Dharamchand | CA | Mumbai |
| 29 | Mr. Sumaria Jenti Jethalal | CA | Mumbai |

**Student Membership**

| | | | |
|---|---|---|---|
| 1 | Mr. Prajapati Nayan Babu | CA Final | Mumbai |
| 2 | Mr. Doshi Pranav Dimple | F.Y. B.Com | Mumbai |
| 3 | Mr. Beria Abhishek S. | CA | Mumbai |
| 4 | Mr. Shah Dwijesh H. | CA Final | Mumbai |

**Associate Membership**

| | | |
|---|---|---|
| 1 | Tata Steel Ltd. | Mumbai |

## II. Past Programmes

### 1. STUDENT & IT CONNECT COMMITTEE

A) Half Day Seminar on "DATA Crunching & Reporting with Pivot Tables" was held on 26th May, 2017. The Seminar was addressed by CA Nikunj Shah.

B) Study Course titled "Articles Orientation Programme" for Students was held on 2nd & 3rd June, 2017.

## III. Future Programmes

### 1. DIRECT TAXES COMMITTEE

A) Full Day Workshop on "Income Computation & Disclosure Standards (ICDS) covering: Issues, Case Studies, Implementation and Reporting Requirement" will be held on 17th June, 2017 at Mysore Association Auditorium, Matunga.

B) Webinar on "Revision Proceedings u/s. 263 and 364 of the I.T.Act, 1961 " will be held on 27th June, 2017 and will be addressed Mr Paras S. Savla, Advocate.

C) Half Day Workshop on General Anti Avoidance Rules (GAAR) will be held on 1st July, 2017 at M. C. Ghia Hall, Fort, Mumbai.

### 2. DELHI CHAPTER

Full Day Workshop on "Income Computation & Disclosure Standard (ICDS)" will be held on 10th June, 2017 at Indian International Centre, New Delhi

### 3. INTERNATIONAL TAXATION COMMITTEE

A) The "11th Residential Conference on International Taxation, 2017" will be held on 22nd June, 2017 to 25th June, 2017 at The Hotel Taj, Nashik.

B) The International Taxation Committee has announced the commencement of a webinar series once in a month on " International Taxation" to be hosted by Dr. Amar Mehta and other top professionals in the field of International Taxation.

### 4. STUDENT & IT CONNECT COMMITTEE

Half Day Seminar on "GST Compliance- Information Technology Perspective" will be held on 19-6-2017 at Babubhai Chinoy Hall, IMC, Mumbai.

### 5. 90TH YEAR CELEBRATION COMMITTEE

To commemorate the Journey of 90 Glorious Years of the CTC, the 90th Year Celebration Committee has organised a Grand Musical Evening along with fellowship dinner for the CTC members, their teammates, family and friends at Shree Vile Parle Gujarati Mandal, Vile Pare (E), Mumbai from 6.00 p.m. to 10.30 p.m.

### 6. NOTICE OF ANNUAL GENERAL MEETING

The Ninetieth Annual General Meeting of The Chamber of Tax Consultants will be held at Garware Club House, Wankhede Stadium, D Road, Churchgate, Mumbai- 400 020 on Tuesday, 4th July, 2017 at 4.30 p.m.

### 7. RENEWAL OF MEMBERSHIP FEES 2017-18:

The Renewal Fees for Annual Membership, Study Group, Study Circle and other Subscription for the financial year 2017-18 was due for payment on 30th April, 2017. The Renewal notices has been sent separately which contains entire information of members as per CTC Data Base. In case any changes of information of members shown in form, kindly provide updated information along with the form. Members are requested to visit www.ctconline.org for online payment of the Renewal Fees.

# NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the Ninetieth Annual General Meeting of THE CHAMBER OF TAX CONSULTANTS will be held at Garware Club House, Wankhede Stadium, D Road, Churchgate, Mumbai- 400 020 on Tuesday, 4th July, 2017 at 4.30 p.m. to transact the following business:

1. To consider the Annual Report of the Managing Council for the year 2016-17.
2. To consider and adopt the audited accounts for the year ended 31st March, 2017.
3. To appoint auditors for the year 2017-18 and fix their honorarium.
4. To announce results of the election of President and Fourteen Members of the Managing Council.
5. To felicitate members.
6. To transact any other business with permission of the Chair.

For and on behalf of the Managing Council of
The Chamber of Tax Consultants

Sd/-

**Hinesh R. Doshi**
**Haresh P. Kenia**
*Hon. Jt. Secretaries*

Place : Mumbai
Dated : 20th April, 2017

**Office:**

3, Rewa Chambers,
31, New Marine Lines,
Mumbai – 400 020.

***Notes:***

1. As per the decision taken at 86th Annual General Meeting, Annual Report would be circulated in electronic form. It shall also be available on the Chamber's website after 19th June, 2017. Any member desiring physical copy can send written request and get it collected from Chamber's office after 19th June, 2017. Alternatively such members can also send written request for sending it by post or courier.
2. If there is no quorum by 4.30 p.m. the meeting will be adjourned for half an hour and the members present at such adjourned meeting shall form the quorum.
3. The members are requested to send their queries, in writing, if any, on the Statements of Accounts and Annual Report for the year 2016-17 to the Hon. Jt. Secretaries at least four days before the day of the Annual General Meeting.

## INTERNATIONAL TAXATION COMMITTEE

**FEMA Study Circle meeting on Capital & Current Account Transactions (including bank accounts) and FEMA provisions relating to immovable property in & outside India held on 3rd May, 2017 at CTC Conference Room**

CA Natwar Thakrar addressing the members

## DIRECT TAXES COMMITTEE

**Webinar on Amendments to Sections 115BBE and 271AAC of Income-tax Act, 1961 held on 9th May, 2017**

CA Mahendra Sanghvi addressing the members

**Webinar on Reassessment Proceedings under Income-tax Act, 1961 held on 23rd May, 2017**

CA Ketan Vajani addressing the members

## STUDY CIRCLE & STUDY GROUP COMMITTEE

**Study Circle Meeting on Overview of Prohibition of Benami Property Transaction Act, 1988 held on 11th May, 2017 at SNDT Conference Room**

CA Jagdish Punjabi addressing the members

**Study Group Meeting on Recent Judgments under Direct Taxes held on 12th May, 2017 at SNDT Conference Room**

CA Sanjay Parikh addressing the members

## MEMBERSHIP & PUBLIC RELATIONS COMMITTEE

**Full Day Seminar on GST & Cash Transaction and Related Penalties under Income-tax Act, 1961 Jointly with TCA, Income Tax Bar Association of Kolhapur and STPAM held on 27th May, 2017 at Rotary Sunrise Community Hall, Kolhapur**

Mr. R. R. Doshi – Advocate (President of Income Tax Bar Association, Kolhapur) inaugurating the Seminar by lighting the lamp. Seen from L to R – CA Hemant Parab (Chairman of Membership & PR Committee), Shri Raj Shah, Joint Secretary of GSTPAM, CA Devendra Jain (Speaker), Mr. Dhiraj Shah – Advocate (Chief Coordinator and committee member of Membership & PR Committee)

CA Hemant Parab (Chairman of Membership & PR Committee) delivering opening remarks. Seen from L to R – S/Shri Mr. Dhiraj Shah (Advocate) Chief Co-ordinator, Mr. R. R. Doshi – Advocate (President of Income Tax Bar Association, Kolhapur)

CA Devendra Jain (Speaker) addressing the participants

**Self Awareness Series held on 7th June 2017 at CTC Conference Room**

Dr. Ravin Thatte (Speaker) addressing the participants

## STUDENT & IT CONNECT COMMITTEE

**Half Day Seminar on Data Crunching & Reporting with Pivot Tables held on 26th May, 2017 at Jai Hind College, Mumbai**

CA Parimal Parikh (Chairman) giving opening remarks and welcoming the Speaker. Seen from L to R – CA Bhavik Shah, CA Dinesh Tejwani, CA Nikunj Shah (Speaker) and CA Ankit Sanghvi

CA Nikunj Shah (Speaker) addressing the participants

**Article Orientation Programme (Only for Students) held on 2nd & 3rd June, 2017 at Mithibai Hall, Mithibai College, Mumbai.**

CA Hitesh R. Shah (President) giving opening remarks. Seen from L to R – CA Parimal Parikh (Chairman), CA Abhay Arolkar (Speaker) and CA Bhavik Shah

CA Abhay Arolkar (Speaker) addressing the students

CA Amit Purohit (Co-Chairman) welcoming the speaker

CA Heneel Patel (Speaker) addressing the students

**The Chamber of Tax Consultants had initiated Project of reconstruction of Shree Shadnan Shishuniketan Primary School in Chopada District Rudraprayag, Uttarakhand as part of its Uttarakhand Relief project**

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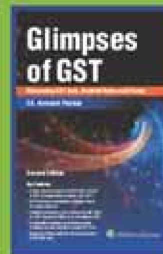


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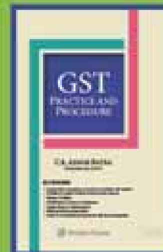


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