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INDIA NEWSLETTER

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TAX AND REGULATORY UPDATES

CUSTOMS

Removal of mandatory warehousing requirements for EOUs, STPIs, EHTPs etc

- In line with the Government's objective of 'ease of doing business', It has been decided by the CBEC to dispense with the need to comply with warehousing provisions under Custom Laws by EOUs, STPIs, EHTPs, etc. units, with effect from 13th August, 2016.
- Notification No. 52/2003-Customs dated 31st March, 2003, is amended. As a consequence, these units shall stand delicensed as warehouses under Customs Act, 1962, with effect the above mentioned date.
- In view of the condition of warehousing having been dispensed with respect to the units, the warehoused goods register (warehousing bond register) shall not be required to be maintained w.e.f 13th August, 2016. However, in order to maintain records of receipts, storage, processing and removal of goods, imported by the units, as required under notification 52/2003-Cus dated 31st March, 2003 the Board has prescribed that the units shall maintain records of imported goods, in digital form, based upon data elements contained in Prescribed Form A.
- The digital records should be kept updated, accurate, complete and available at the unit at all times for verification by the proper officer, whenever required. A digital copy of Form A, containing transactions for the month, shall be provided to the proper officer, each month (by the 10th of month) in a CD or Pen drive, as convenient to the unit.
- This requirement of maintaining digital records, in the prescribed Form, is applicable from 13th August, 2016. Record of imported goods received on or after 13th August, 2016 shall be maintained as per the prescribed Form. The information regarding the stock of goods lying with the unit need to be integrated into the digital record as prescribed. However, data relating to goods already processed and/or cleared need not be updated in the digital records.
- In view of the warehousing procedures having been dispensed with for these units, the system of sending re-warehousing certificates to the customs station of import shall also stand dispensed.

[Circular No 35 /2016-Customs dated July 29, 2016]

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FOREIGN TRADE POLICY

Relief in Average Export obligation under EPCG scheme:

- Para 5.19 of the Hand Book of Procedures of Foreign Trade Policy (' FTP') 2015-20 permits re-fixation of Annual Average Export Obligation ('AEO'), in case the export in any sector/ product group decline by more than 5%. This entails that the sector/product group that witnessed such decline in 2015-16 as compared to 2014-15, would be entitled for such relief.
- In this context, the DGFT has issued Policy Circular listing the sectors eligible for this benefit. Based on this, eligible sectors would be entitled to get their AEO re-fixed.

[Policy Circular No 01/2015-2020 dated July 26, 2016]

Deduction of State/ Central Taxes collected from the customers while calculating foreign earnings for SFIS/SEIS Schemes:

- DGFT has clarified that for the purpose of benefits available under SFIS ('Served from India Scheme') & SEIS ('Services Exports from India Scheme'), service providers shall be entitled to duty credit equivalent of the foreign exchange earned by them.
- It is clarified that only foreign remittances that are earned as amounts in lieu of the services rendered by the service exporter would be counted for computation of entitlement under this scheme and the State/Central taxes payable by the customers to governments which are collected by service provider on behalf of government are not earnings and not to be considered.

[Trade Notice No 11/2015-2020 dated July 21, 2016].

CASE LAW HIGHLIGHTS

SERVICE TAX

Anchoring television shows, brand endorsement and fees from franchisee not liable to service tax, neither as 'Business Auxiliary Service' nor as 'Business Support Service'.

Former Indian cricket team Captain Mr. Sourav Ganguly received considerations for various activities like writing articles in magazines, anchoring television shows, brand endorsement and fees from IPL franchisee during the period May 2006 to June 2010 totalling to around Rs. 36.3 crores. SCN was issued amounting Rs. 1.5 crores demanding the service tax on the same.

Calcutta High Court quashed the SCN and held as follows:

- Writing articles for sports magazines cannot by any stretch of imagination be said to be amounting to rendering business auxiliary service, and observes that the articles were meant for information and even entertainment of the general public interested in sports.
- By anchoring a TV show, a celebrity or for that matter any other person does not render service with the object of enhancing any business or commercial interest and thus not liable to tax.
- The definition of 'brand promotion' was introduced in the law from July 1, 2010 and hence, brand endorsement was not liable to service tax before the amendment.
- Sourav Ganguly "was a purchased member of a team serving and performing under KKR and was not providing any service to KKR as an individual" and his services were not taxable as business support services and thus fees received from IPL franchisee was not liable to tax.

It is to be noted that this case relates to the pre-negative list regime.

SOURAV GANGULY Vs. UOI AND ORS [2016-TIOL-1283-HC-KOL-ST] [TS-259-HC-2016(CAL)-ST] - CALCUTTA HIGH COURT

CUSTOMS

Drawback on exported goods cannot be denied on ground that raw materials were imported under other export incentive schemes like DEPB or MLFPS.

The petitioner was in the business of manufacturing goods which were exported by the petitioner. For the purpose of the manufacturing activity, the petitioner had imported various inputs and raw materials. The petitioner imported various items such as polyethylene, adhesive epoxy, etc. by paying customs duty utilising Duty Entitlement Pass Book Scrip ("DEPB scrip" for short) which the petitioner had purchased from the market.

The appellant argued that there is no limitation on drawback being available when the customs duty is suffered through surrendering credit in the scheme, be it DPEB Scrip or MLFPS Scrip. In either case, it cannot be stated that the customs duty is not paid.
The department contended that the relevant notifications and the policy, do not permit drawback on imports made under DEPB and other similar export incentive schemes. In case of imports made under DEPB scheme, the customs duty is exempted. Goods therefore, not having suffered the customs duty, upon export of the final product, drawback would not be available.
After analysing various aspects, it was decided that an importer whether imports goods under DEPB scheme or pays customs duty on the imports on purchased DEPB Scrips credits, he essentially pays customs duty by adjustment of the credit in the passbook. It would therefore, be incorrect to state that the imports made in such fashion have not suffered the customs duty. Furthermore, neither section 75 nor the Rules of 1995, prohibits entitlement of drawback when the basic customs duty has been paid through DEPB Scrip.
Accordingly, the High Court allowed the Petitions and reversed the impugned orders.

RATNAMANI METALS AND TUBES LTD & 1Vs UNION OF INDIA THROUGH JOINT SECRETARY (REVISIONARY AUTHORITY) & 1 [2016-TIOL-1425-HC-AHM-CUS] - HIGH COURT OF GUJRAT AT AHMEDABAD

DIRECT TAX UPDATES

CIRCULARS/ NOTIFICATIONS/PRESS RELEASES

Negotiations for amendment to India - Cyprus tax treaty

The Press Release states that in-principle agreement has been reached on pending issues, including capital gains, in respect of India – Cyprus tax treaty. With respect to capital gains, the following provisional agreements will be placed for approval before cabinet, after which new treaty can be signed:

- Source based taxation is provided for capital gains on transfer of shares.
- Grandfathering clause will be provided to protect investments made prior to Apr 1,2017 i.e. capital gains in respect of such investments will be taxed in country of residence of taxpayer.

  Further, India will consider revoking the notification issued by Indian Government in 2013, wherein Cyprus was declared as notified jurisdictional area.

[Press Release dated July 1, 2016]

Deferral of Income Computation and Disclosure Standards (ICDS) by 1 year

Effective from April 1, 2015, new set of standards i.e. ICDS were issued by CBDT to be followed by taxpayers for computation of income under the head 'Profits and gains of business or profession' or 'Income from other sources'. The Expert Committee set up for examination of issues raised has recommended amendments to the ICDS and issuance of clarifications for stakeholders. Considering this alongwith necessary revisions to be carried out in tax audit report for compliance with ICDS provisions, the CBDT has deferred ICDS by 1 year and they shall now be applicable from April 1, 2016 i.e. fiscal year 2016-17.
[Press Release dated July 6, 2016]

Draft rules for determination of amount received by company to compute distributed income for tax on buy-back of shares

A company is liable to pay additional income tax @ 20% on distributed income in case of buy-back of unlisted shares under section 115QA of the IT Act. The distributed income is defined to mean consideration paid by the company on buy back of shares as reduced by the amount received on issue of such shares, to be determined as per Rules to be prescribed. In this regard, the CBDT has issued draft rules proposing the methodology for determination of amount received by the company under different circumstances:

Circumstance	Amount received by the Company
Shares issued on its subscription by any person	Paid up amount including premium actually received
Prior to buy-back, any sum returned out of amount received in respect of such share	Amount received in respect of such share minus sum returned
Shares issued by amalgamated company, under a scheme of amalgamation, in lieu of the share or shares of an amalgamating company	Amount received by amalgamating company determined as per Rules minus amount returned by amalgamating company before amalgamation.
Shares issued under a scheme of demerger	The amount received by demerged company in respect of original shares determined as per this Rule, in proportion of, net book value of assets transferred in demerger to net worth of demerged company immediately before such demerger
Share issued or allotted, without any consideration on the basis of existing shareholding in the company	Nil
Shares issued on conversion of bond or debenture, debenture-stock or deposit certificate	Amount received by the company in respect of the instrument so converted.
In any other case	Face value of the share

[Letter F.NO.370133/30/2016-TPL dated July 25, 2016]

No withholding tax on interest paid by IFSC Banking units

Section 197A of the IT Act provides for the circumstances where withholding of tax is not required. This inter-alia, includes interest paid by Offshore Banking units (OBUs) on deposits or borrowings from specified persons. The CBDT has now clarified that withholding is not required by IFSC Banking Units (IBUs) on interest paid on deposits or borrowing from non-residents or not ordinarily resident in India, as IBUs fulfil the necessary criteria for being considered OBU as defined in section 2(u) of the Special Economic Zones Act, 2005.
[Circular No.26/2016 dated July 7, 2016]

Paperless application process for tax registrations

A digital signature certificate based application process has been introduced for fast-tracking allotment of Permanent Account Number (PAN) and Tax Deduction Account Number (TAN). The Press Release states that PAN and TAN will be allotted within one day after completion of valid online application.
For individuals, a new Aadhaar e-signature based application process is introduced on the designated portals.
[Press Release dated July 22, 2016]

JUDICIAL DECISIONS

Transfer of trademarks by non-resident owner is not taxable in India, intangibles not covered under indirect transfer provisions

The Delhi High Court dealt with a case of taxpayer (Foster's Australia Limited), which permitted the Indian entity to use licensed trademarks under brand license agreement. The trademarks remained the absolute property of the taxpayer. Under India sale purchase agreement between taxpayer and SAB Miller A & A 2 and its nominee (purchaser), alongwith transfer of shares of foreign entity, the trademarks including those licensed to India were transferred.

The Delhi High Court held that income accruing to a non-resident taxpayer from transfer of right, title or interest in/to trademarks in brand intellectual property (IP) is not taxable in India.

While ruling so, the High Court noted that there is no specific provision with regards to intangible assets under the indirect transfer provisions, as is provided in case of shares deriving value substantially from assets located in India. The legislature, through a deeming fiction, could have provided for location of intangible capital asset, but Indian legislature has not done it. The well accepted principle of 'mobilia sequuntur personam' would have to be followed. The situs of owner of intangible asset would be the closest approximation of the situs of intangible asset, unless altered by local legislation. Since there is no such alternation in Indian context, the Court agreed with taxpayer that situs of trademarks and IP rights would not be in India, since owner was not located in India at the time of transaction.
[CUB PTY Limited WP[C] 6902/2008 (Delhi High Court)]

No disallowance for expenditure incurred on voluntary basis on Corporate Social Responsibility (CSR)

With effect from April 1, 2015, explanation 2 to section 37(1) of the IT Act disallows expenditure incurred on activities relating to CSR referred to in section 135 of the Companies Act. The Raipur bench of tax tribunal dealt with a case of taxpayer which incurred expenditure towards CSR on voluntary basis in fiscal year 2007-08. The tax tribunal held that explanation 2 does not have retrospective effect, since the provision in Companies Act itself came into existence in 2013 and amendment is not specifically stated to be retrospective. Further, disallowance is restricted to expenses incurred by taxpayer under a statutory obligation under section 135 of Companies Act, 2013 and it does not apply to expenditure incurred in discharge of CSR on voluntary basis. Accordingly, the expenditure was allowed as deduction under section 37(1) of the IT Act.
[Jindal Power Ltd 70 taxmann.com 389 (Raipur Tribunal)]

TRANSFER PRICING UPDATES

JUDICIAL UPDATES

Tax Tribunal rejects Foreign Associated Enterprise as tested Party

The Delhi Tax Tribunal rejected the taxpayer's methodology of selecting the Foreign Associated Enterprise (AE) as tested party since the same is not permitted within Indian Transfer Pricing (TP) regulations. The Tax Tribunal held that the profit realized by the Indian enterprise cannot be substituted with the profit realized by the foreign AE for the purpose of determining Arm's Length Price (ALP) of the international transaction. While analyzing the application of Transactional Net Margin Method (TNMM), the Tax Tribunal remarked that language of the Rule 10B(1)(e) clearly mentions that the it is the "net profit margin" of the enterprise (the Indian taxpayer) that is computed from the international transaction with associated enterprise and the same is compared with the comparable companies. The Tax Tribunal also held that the need for service cannot be determined by the revenue authorities and once the receipt of service is proved, the same cannot be questioned on the basis that the taxpayer did not realise any benefit from such services.

[GE Money Financial Services Pvt Ltd ITA NO. 440 (Del.) of 2014 (Delhi Tribunal)]

Tax Tribunal treats interest free loan as quasi capital and shareholder's activity, rejects the tax authorities re-characterization as loan transaction

The Delhi Tax Tribunal held that merely disclosing the transaction as interest free loan to its AE in Form 3CEB does not disentitle the taxpayer to claim that the transaction was, in substance, in the nature of quasi capital and shareholder activity. The Tax Tribunal noted that the interest free advance was converted into equity within 3 months and money was advanced as interest free loan just to ensure that the money is returned to taxpayer if the same is not utilized by the AE for the intended purpose.

[DLF Hotel Holdings Limited ITA NO. 6336 (Del.) of 2012 (Delhi Tribunal)]

Rejects tax authorities' selection of CUP and benchmarks royalty under entity level TNMM

The Delhi Tax Tribunal rejected the tax authorities' approach of benchmarking royalty payment separately by using the Comparable Uncontrolled Price (CUP) method. The Tax Tribunal held that when TNMM method is used at entity level, it covers royalty payment made to AEs, within its ambit relying on the decision of LG Electronics India Private Limited [TS-421-ITAT-2014(Del)-TP]. It was further held that it was not necessary to show that the expenses undertaken by the taxpayer resulted into profits in the current or subsequent years. The Tax Tribunal held that expenses incurred by the taxpayer should be "wholly and exclusively" for the purpose of business. The Tax Tribunal relied on the High Court judgement in case of EKL Appliances [TS-206-HC-2012(Del)-TP] and Cadbury India Limited [TS-122-ITAT-2013(Mum)-TP].

[Daksh Business Process Services Pvt Ltd ITA No. 2666 (Del.) of 2014 (Delhi Tribunal)]

Interest adjustment mandatory for inbound interest free loan

The Kolkata Special bench held that the AE of the Indian taxpayer advancing interest free loan to Indian taxpayer has to comply with Indian transfer pricing regulation. The Special Bench did not agree with the argument of the taxpayer that imputing arm's length interest in the hands of the foreign AE leads to erosion of tax base of India as per section 92(3) of the IT Act. ***The special bench categorically stated that Indian TP regulation, as it stands today, does not provide for a corresponding increase of deduction or claim of deduction in the hands of Indian AE as a result of imputation of income/increase of income in the hands of foreign AE.*** The Special bench held that there was no restriction on advancing interest free loans between group entities, however, if such transaction is an "international transaction", the income shall be computed based on the arm's length pricing.

[Instrumentarium Corporation Limited [ITA NO. 1548 and 1549 (Kolkata) OF 2009 (Kolkata Special Bench)]

OTHER TRANSFER PRICING REGULATORY UPDATES

Tolerance Band for fiscal year FY 2015-16 notified

The Central Board of Direct Taxes (CBDT) has notified that the variation between the arm's length price under section 92C(2) of the IT Act and the price at which the international transaction has actually taken place should not exceed 3% of the International Price of the transaction. Incase of wholesale trading, the tolerance band has been fixed as 1% of international price/specified domestic price. Further, the notification also defines wholesale trading and enumerates the situations wherein the taxpayer shall fall in the said criteria.
[CBDT Notification dated July 14, 2016]

THE CORPORATE LAW AMENDMENTS

1. The Ministry of Corporate Affairs ('MCA') vide their Notification dated 19th July, 2016 have notified the amendments in the Companies (Share Capital and Debentures) Rules, 2014. The noteworthy amendments are as follows:
   - Companies having a default in payment of dividend on preference shares/repayment of any term loan or interest payable are allowed to issue equity shares with differential voting rights upon expiry of 5 years from the end of financial year in which default is made good;
   - A start-up company is allowed to issue sweat equity shares up to 50% of its total paid-up capital, upto 5 years from date of incorporation or registration;
   - A start-up company is further allowed to issue Employee Stock option Plans ('ESOPs') upto 5 years from date of incorporation or registration to:
     (i) An employee who is promoter / person belonging to promoter group, or
     (ii) Director who either himself / through his relative / through anybody corporate holding more than 10% of outstanding equity shares;
   - Preference shares can now be issued as partly paid-up shares. Earlier, only fully paid preference shares were allowed to be issued;
   - Where the convertible securities are offered on preferential basis with an option to apply for and get equity shares allotted, the price of resultant shares shall be determined as follows:
     (iii) Either upfront at the time when offer of convertible securities is made or
     (iv) At any time, after 30 days and before 60 days when the holder of convertible security becomes entitled to apply for shares;
   - Companies are allowed to issue secured debentures by creation of charge on not only the properties/assets of the company but also its subsidiary or its holding company or its associate company; and
   - It is also clarified that where a Company intends to redeem its debentures prematurely, it may provide for transfer of such amount in Debenture Redemption Reserve as is necessary for debenture redemption even if it exceeds the limits as specified.

2. Vide a notification dated 21st July, 2016, MCA has issued National Company Law Tribunal ('NCLT') Rules, 2016 and National Company Law Appellate Tribunal ("NCLAT') Rules, 2016 that spell out the functioning of NCLT & NCLAT, prescribing the powers and functions of President, Registrar and Secretary, procedure relating to institution of proceedings, appeals/applications, etc.

3. MCA vide their Notification dated 27th July, 2016 have notified the amendments in the Company (Incorporation) Rules, 2014 and the Companies (Accounts) Amendment Rules, 2016. The noteworthy amendments are as follows:

   Companies (Incorporation) Rules, 2014

   - A person can be a nominee in a One Person Company ('OPC') and simultaneously be a member in another OPC.
   - If a subscriber to the Memorandum of Association already holds a Director Identification Number ('DIN') which is updated on MCA, then there is no requirement to attach the Proof of Identity in the incorporation form.
   - All companies having a website for conducting online business shall have to disclose their particulars on the home page of the website.
   - In case of shifting of registered office of a listed company, the requirement to send Notice to Securities Exchange Board of India ('SEBI') has been done away with.
   - With the issue of this notification, provisions pertaining to the conversion of Unlimited Liability Company into a Limited Liability Company by shares or guarantee have been included in the Company (Incorporation) Rules.

   Companies (Accounts) Amendment Rules, 2016

   - Exemption from preparation of Consolidated Financial Statements have been subjected to fulfilment of certain conditions
   - Amended rules empower 'body corporate' also to act as internal auditor.
   - Forms AOC-1 and AOC-4 have been substituted with revised forms.

Amendments by Securities Exchange Board of India ('SEBI')

SEBI, in consultation with the market participants, has now notified the provisions regarding Revised Formats for Financial Results and Implementation of Ind-AS by Listed Entities vide a circular dated 5th July, 2016. Highlights of this circular are as follows:

- The existing formats prescribed in SEBI Circular dated November 30, 2015 shall continue till the period ending 31st December, 2016, pursuant to which the applicable formats shall be the formats as prescribed in Schedule III to the Companies Act, 2013 (Not applicable to Banking/Insurance Companies);
- Until Companies (Indian Accounting Standards) Rules, 2015 ('Ind-AS Rules') become applicable, the listed entities shall adopt Companies (Accounting Standards) Rules, 2006 ('AS Rules') as prescribed by MCA;
- The Circular also prescribes the minimum information that shall be included in the Quarterly / Annual Segment Information published in compliance with the requirements as prescribed under Accounting Standard 17/ Indian Accounting Standard 108 of the AS Rules/ Ind-AS Rules, as applicable.

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