ACCOUNTING, REGULATORY & TAX NEWSLETTER

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Report of Implementation Group on IND AS to Insurance Sector in India- GAAP

IRDAI had constituted an Implementation Group (IG) to prepare the Indian insurance sector towards convergence with IND AS. IRDAI, on December 30, 2016, released 'Report of the Implementation Group on Indian Accounting Standards (IND AS) in insurance sector in India'.

The report includes the recommendations of the IG, which was constituted to examine the implications of implementing IND AS, address the implementation issues and facilitate the formulation of operational guidelines to converge with IND AS in the Indian insurance sector.

As per roadmap laid down by MCA, Scheduled Commercial Banks, Insurance companies and NBFCs shall comply with IND AS from April 1, 2018 onwards with one year comparatives.

The key recommendations of the IG are summarized under the Executive Summary section of the report. Some of the points covered therein include:

- Ind AS 40: Investment Property - life companies to revalue investment property at a minimum every 3 years and general insurance companies not to revalue investment property
- Ind AS 7: Cash Flow Statements – to be prepared as per the direct method
- Products where the death benefit cannot be less than 105% of the premiums paid are recommended to be considered to have the significant risk cover
- All the linked products (unit linked products and variable insurance products) and all the non-linked products (including variable insurance products classified as non-linked products) are recommended not to be unbundled
- In order to comply with the disclosure requirements an insurance company will need to determine the data available with it and then it will need to collate it suitably
- Cost may be mandated as the basis for the accounting for investments in subsidiaries, associates and joint ventures in the separate financial statements
- Trade date accounting may be prescribed as the uniform basis of initial recognition of securities by all insurers
- The IRDAI may consider permitting insurance companies to hedge their FVTOCI investments (debt and equity) to mitigate accounting and economic volatility
- Formats as defined shall be followed.

The IG also formulated Ind AS compliant formats for preparation of Financial Statements of insurers and summarizes the regulatory stipulations which need to be reviewed in light of the issues considered in the report. Specific Ind AS dealt with in the report includes:

- Chapter II: Ind AS 101: First-time Adoption of Indian Accounting Standards
- Chapter III: Ind AS 104: Insurance Contracts
- Chapter IV: Ind AS 109: Financial Instruments

ASSURANCE UPDATES

Manual on Concurrent Audit of Banks (2016 Edition)

The Internal Audit Standards Board (IASB) of ICAI has issued Manual on Concurrent Audit of Banks.

Reserve Bank of India had issued revised Concurrent Audit Guidelines in July, 2015 which focuses on effective controls, importance of checking high risk transactions and coverage of fraud prone areas. Keeping this in view and various other developments, the IASB has revised "Manual on Concurrent Audit of Banks" in January, 2017 which was earlier issued in 2012. The revised Manual includes updated checklist for Concurrent Audit, chapters on important areas like, Treasury, Forex and Core Banking Solutions. The Manual contains text of all important Master Circulars and Master Directions issued by the RBI, impacting concurrent audit, for ready reference. The contents of the Manual are broadly divided into following 3 Parts:

- Part I: Understanding the Banking Business and Its Legal Framework
- Part II: Domain of Concurrent Audit
- Part III: Concurrent Audit Checklist and Core Banking System

REGULATORY UPDATES

SECURITIES EXCHANGE BOARD OF INDIA (SEBI) AMENDMENTS

Introduction of new propositions to streamline the regulatory framework governing the schemes of arrangements

To safeguard the interest of shareholders in the listed companies entering in to the scheme of merger, SEBI has approved certain proposals. Key guidelines are as follows:

In case of merger of unlisted companies with listed companies:

- Unlisted company to provide material information as specified in the format for abridged prospectus.
- Pre-scheme public shareholders of listed company and qualified institutional buyers of unlisted company to hold atleast 25% of post Scheme shareholding.
- Merger of Unlisted company with listed entity only if listed company is on a stock exchange having nationwide trading terminals.

Other applicability

- Pricing formula applicable as prescribed under ICDR.
- Scheme approval through e-voting made compulsory for certain merger and demerger transactions.
- CS, CFO & Managing Director to certify compliance with Accounting Standards and the circular.

To make it compliant in line with Section 233 of the CoA, 2013, schemes involving merger of Wholly-Owned Subsidiary with Holding company need not be filed with SEBI but only with respective stock exchanges for disclosure purposes only.

Issue of Guidance Note on Board Evaluation

Since the concept of Board Evaluation is quite recent in India, SEBI has issued a Guidance Note on 'Board Evaluation' which covers all major aspects of Board Evaluation which would enable the listed companies to improve their evaluation process and maximum possible benefit can be derived.

Issue of guidelines for participation of Eligible Foreign Investors (EFIs) and Foreign Portfolio Investors (FPIs) in International Financial Services Centre (IFSC).

Guidelines have been issued for participation of EFIs and FPIs in IFSC. It lays down the regulatory framework for entry of FPIs and EFIs in the IFSC. These comprehensive guidelines are aimed to encourage their involvement in the functioning of the IFSC which would boost up the economy.

Amendment to SEBI (Foreign Portfolio Investors), 2014 Regulations

The permissibility to Foreign Portfolio Investors (**FPIs**) to include the shares is now made explicit to allow

the companies (listed or to be listed on a recognised stock exchange) through primary and secondary markets.

The restriction of transacting only through a registered broker has been relaxed for two more instances namely:-

- Transactions by Category I and II FPIs in specified corporate bonds.
- Transactions on electronic book provider platform of Recognised Stock exchanges.

Frequently Asked Questions (FAQs) on SEBI (Substantial Acquisition of Shares and Takeovers) (SAST) Regulations, 2011

SEBI has issued FAQs on the SEBI (SAST) Regulations to provide clarification related to steps to be followed, timelines, threshold limits, disclosure norms etc. Also, various terms have been explained in detail for removal of doubts.

Frequently Asked Questions on SEBI (Buyback of Securities) Regulations, 1998.

SEBI has also issued FAQs on matters related to buyback of securities which deals with matters like the manner in which buyback can take place, procedure, tender offer method, etc.

Amendment to SEBI (Alternative Investment Funds) Regulations.

SEBI, vide notification dated January 4, 2017 has brought about various positive reforms in regulations governing AIFs. These amendments are likely to encourage the use of AIFs as investment vehicles. The amendments include revision in the range for amount of investments, reduction of lock-in period to 1 year, etc. Also, maximum 200 angel investors can now participate in angel fund.

REGULATORY UPDATES

Disclosure and Compliance norms prescribed for REITs

SEBI, vide circular dated December 29, 2016 has prescribed multiple disclosure requirements and compliance by REITs whose units are listed. The annexures in the given circular lay down the prescribed financial and non-financial information which shall be disclosed by REITs to the respective stock exchanges.

Also, vide circular dated December 26, 2016, SEBI has prescribed detailed requirements of disclosure of financial information in offer documents by REITs.

These amendments have been made to increase the level of transparency.

The SEBI (Listing Obligations and Disclosure Requirements) (Third Amendment) Regulations, 2016

The amendment rules vide notification dated January 3, 2017, substituted the title of regulation 26 from 'Obligations with respect to directors and senior management' to 'Obligations with respect to employees including senior management, key managerial persons, directors and promoters'.

Restriction is placed on employees including key managerial personnel or director or promoter of a listed entity from entering into any agreement with any shareholder or any other third party with regard to compensation or profit sharing in connection with dealings in the securities of such listed entity subject to approval of directors as well as public shareholders by way of ordinary resolution, by inserting sub-regulation 6 to regulation 26.

The sub-regulation further inserts 4 proviso and an explanation to the above clause. The amendment rules shall come into force w.e.f. January 4, 2017

MINISTRY OF CORPORATE AFFAIRS ('MCA') AMENDMENTS

Exemption to Specified International Financial Services Centres ('IFSCs').

MCA, vide notification dated 4th January, 2017, has granted exemptions and relaxations from certain provisions of the Companies Act, 2013 to a non-listed public company as well as private company which is licensed to operate by the RBI or SEBI or IRDAI from the IFSC located in an approved multi services SEZ set-up under the SEZ Act, 2005.

Amendment to Companies (Incorporation) Rules, 2014

Vide notification dated January 25, 2017, it has now been mandated to include the Permanent Account Number (PAN) of the Company in the Certificate of Incorporation issued by the Registrar in Form INC-11.

For giving effect to the above amendment, corresponding changes have been made in the formats of Form INC-11 and INC-32.

Removal of Names of Companies from Register

MCA vide Notification dated December 26, 2016 notified Sections 248 to 252 of Companies Act, 2013 (the Act) and also notified Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 which shall be effective from December 27, 2016.

The said Sections 248 to 252 replaces the provisions of Section 560 of erstwhile Companies Act, 1956, to deal with the detailed procedure with respect to Removal of Names of Companies from Register of Companies, the effect on the company which is notified as dissolved and appeal to tribunal in relation to the same. Section also specifies the course of action taken by registrar of Companies in case a fraudulent application is made for removal of name.

Manner of removal of name of the Company from the Register of companies can be:

- By Registrar of Companies (ROC) suo-moto
- On application by Companies for removal of name (Form STK-2 which is yet to be developed)

FOREIGN EXCHANGE MANAGEMENT ACT ('FEMA') AMENDMENTS

Convertible note issued by Start up Company

A person resident outside India may purchase convertible note (as defined below) issued by an Indian startup company for an amount of INR 25 lacs (Rupees Twenty five lacs only) or more in a single tranche under the Automatic route or Government route(if foreign investment under the start up was under Government approval) if the startup company is engaged in the business which does not require government approval as per FDI policy. The remittance for such purchase shall be by debit to the NRE / FCNR (B) / Escrow account.

'convertible note' means an instrument issued by a startup company evidencing receipt of money initially as debt, which is repayable at the option of the holder, or which is convertible into such number of equity shares of such startup company, within a period not exceeding five years from the date of issue of the convertible note, upon occurrence of specified events as per the other terms and conditions agreed to and indicated in the instrument;

Investment by FDI/ FII/RFPI in Infrastructure companies

Vide a notification dated January 10, 2017, RBI amended regulations pertaining to foreign investment in 'Infrastructure Company in Securities Market'. Any non-resident shall be permitted to invest up to 49% under Automatic route irrespective of the investment being under FDI or investment by Foreign Institutional Investors ('FII') or Registered Foreign Portfolio investor ('RPFI'). Prior to the amendment, even though the ceiling was 49%, there was a cap limit for FDI limit @ 26% and for FII/RPFI @ 23% of paid up capital).

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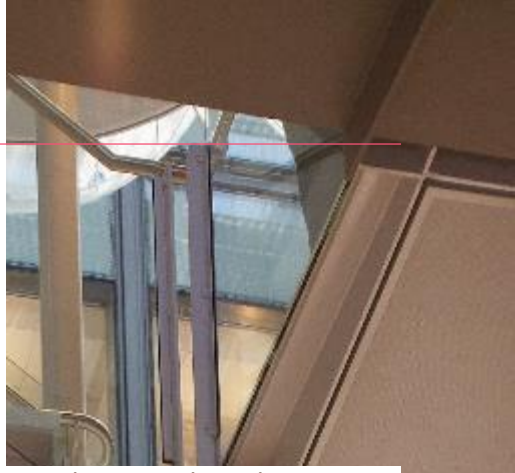

INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY OF INDIA (IRDAI)

Partial Modification of the provisions of Guidelines on Standardization in Health Insurance

IRDAI vide circular dated July 29, 2016 issued 'Guidelines on Standardization in Health Insurance' under the provisions of Section 34 (1) of Insurance Act, 1938 and under the powers vested with Regulation 2(i)(o) of IRDAI (Health Insurance) Regulations, 2016.

These guidelines deal with the following:

- defines the periodicity of the returns and reports to be submitted
- definition for 42 commonly used terms in health insurance policies under Chapter I of the guidelines
- nomenclature and procedures for 22 critical illnesses under Chapter II of the guidelines
- lays down the items for which optional cover may be offered by insurers under Chapter III of the guidelines
- sets standards and benchmarks for hospitals in the provider network under Chapter IV of the guidelines and
- provides the timelines of the Health Insurance Returns to be filed by all Insurers under Chapter V of the guidelines

IRDAI vide circular dated January 10, 2017 has amended Clause I in Chapter V of the guidelines to state that the yearly returns by health insurance companies shall be furnished within 90 days from close of the Financial Year which were required to be submitted within 60 days previously.

Formats for publishing Financial Results as required under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR Regulations)

IRDAI on January 30, 2017 has issued following formats for publishing financial results by Listed Insurance Companies to ensure compliance with the requirements of SEBI LODR Regulations. While SEBI has provided that the listed Insurance companies shall follow the format as prescribed by their regulator which is IRDAI and also the other requirements under LODR Regulations shall be continued to be complied with, It also specified that for the purpose of newspaper publishing, the Insurance Companies shall follow the SEBI Circular.

- The quarterly financial results - as per Annexure I
- Reporting of Segment wise Revenue, Results and Capital Employed along with the quarterly results - as per Annexure II
- Limited review reports by auditors - format prescribed in Annexure III
- In case of audited financial reports, the audit report shall be given by the auditors - format as per Annexure IV
- The financial results published in the newspapers in terms of Regulation 47(1)(b) of LODR Regulations, 2015 shall be - format prescribed in Annexure V

These formats (Annexure) are available along with the circular on IRDAI's website.

Report of IRDAI Committee on Risk Based Capital (RBC) Approach and Market Consistent Valuation of Liability (MCVL) of Indian Insurance Industry:

With an objective of examining the changes required in the method of valuation of liabilities and to value assets at marked to market / fair value, IRDAI had constituted a Committee on RBC Approach and MCVL, on June 10, 2016. In consultation with IRDAI and others, two Sub-committees- one each for Life Insurance and Non- Life (General Insurance and stand- alone Health Insurance) Insurance Business, including respective Reinsurance Business were formed.

The Questionnaire set by Working Group on Implementation of IND-AS, had three sections – Current Solvency Regulations, RBC framework and MCVL. The committee presented Part-I of Committee Report, covering review and recommendations on MCVL, assuming adoption of the IND AS for Insurance Industry in India by an early date. Besides an Introduction and Executive Summary, the Report consists of two sections- Life Insurance (IND AS 104) and General/Health Insurance (draft IFRS 4 2017).

TAX UPDATES
Direct Tax

CIRCULARS/ NOTIFICATIONS/PRESS RELEASES

Guiding Principles for determination of Place of Effective Management (PoEM) of a Company

With effect from fiscal year 2016-17, a foreign company is said to be resident in India if its PoEM in that year is in India. The Central Board of Direct Taxes (CBDT) has enumerated the guiding principles for determination of PoEM, after considering stakeholder comments on the draft guidelines circulated earlier in December 2015 (for summary, please refer BDO India Newsletter - December 2015). Some of the key principles incorporated in the final guidelines are summarised below:

- Guidance is provided on the terms 'income', 'value of assets', 'number of employees' and 'pay roll' for ascertaining whether a company is engaged in active business outside India.
- Interest income of company engaged in business of banking or public financial institution and regulated as such in country of incorporation will not be considered as passive income.
- Merely because board follows global policy of group in field of payroll, accounting, HR, supply chain functions, etc. that are not entity/(s) specific, would not constitute a case of board standing aside.
- To apply the test of active business outside India, data of accounting year ending during the relevant previous (fiscal) year and 2 prior accounting years is to be considered, in case tax year is different from previous year in the country of incorporation of company.
- If board has *de facto* delegated authority to make key management and commercial decisions for the company to promoters, strategic/legal/financial advisor etc. and only routinely ratifies the decisions made, the PoEM will ordinarily be place where such persons make those decisions.
- In case of circular resolution or round robin voting, factors such as frequency of such usage, type of decision made, location of parties involved in decisions etc. are to be considered. The determination of person having and exercising the authority to take decisions would be required.
- The shareholder decisions under Company Law are generally not relevant for determination of PoEM. However, whether shareholders' involvement turns into effective management (through formal arrangement or by actual conduct) has to be determined on case-to-case basis.
- Guidance has been provided on what constitutes operational and commercial decision. In case same person is responsible for both types of decisions, it is necessary to distinguish type of decision and then assess the location of where key management and commercial decisions are taken.
- The fact that foreign entity has a permanent establishment in India, would not, by itself, be conclusive evidence that the conditions for PoEM in India are satisfied.
- At the stage of initiation of proceedings for holding a company as resident in India based on PoEM, tax officer is required to seek prior approval of Principal Commissioner/Commissioner. Further, a finding of PoEM is to be given by tax officer after seeking prior approval of collegium of 3 members consisting of Principal Commissioner/Commissioners. The Collegium is required to provide an opportunity of being heard to the taxpayer before issuing directions.
  [Circular No. 6/2017 dated January 24, 2017]

Taxability of income from transfer of unlisted shares by Alternate Investment Funds (AIF)

The CBDT letter dated May 2, 2016 provided that income arising from transfer of unlisted shares would be considered as capital gains, except, inter-alia, in situation where transfer is made alongwith control and management of underlying business. On representation, the CBDT has considered that primarily, SEBI registered Category I & II AIFs invest in unlisted shares of ventures, more so new set ups or start-ups and therefore, some form of control and management of the underlying business may be required to be exercised by such AIFs to safeguard the interest of investors. Towards this, the CBDT has clarified that the exception referred above in letter of May 2016 would not be applicable to SEBI registered Category I and II AIFs. Accordingly, income from transfer of unlisted shares will be taxable as capital gains for such AIFs.
[CBDT letter dated January 24, 2017]

TAX UPDATES
Direct Tax

Clarifications on implementation of General Anti-avoidance Rule (GAAR)

The domestic anti-abuse GAAR provisions, effective from April 2017, are targeted at arrangements lacking commercial substance and whose main purpose is to obtain tax benefit. After considering comments of the Working Group to address queries regarding implementation of GAAR, the CBDT has issued certain clarifications. Some of the key clarifications are as below:

- GAAR and Specific Anti-Avoidance Rules (SAAR) can co-exist and are applicable, as may be necessary in facts and circumstances of the case, considering that SAAR may not address all situations of abuse.
- If a case of avoidance is sufficiently addressed by Limitation of Benefits clause of the tax treaty, GAAR shall not be invoked.
- GAAR will not restrain the right of taxpayer to select or choose method of implementing a transaction.
- GAAR will not apply if jurisdiction of foreign portfolio investor is based on non-tax commercial considerations and the main purpose of arrangement is not to obtain tax benefit. GAAR will not be invoked merely because entity is in a tax efficient jurisdiction.
- Income from transfer of investments made before April 1, 2017 is grandfathered under GAAR. Such grandfathering provisions will also cover:
  - investments in compulsorily convertible instruments before April 1, 2017 provided conversion terms are finalised at the time of issue of such instruments
  - Share split, consolidation of shares and bonus issue in respect of shares acquired prior to April 1, 2017 in the hands of the same investor
- GAAR provisions will not be invoked if arrangement is held as permissible by Authority for Advance Rulings and where Court has explicitly and adequately considered the tax implications while sanctioning an arrangement.
- Adequate safeguards are in place to ensure that GAAR is invoked only in deserving cases. The proposal to declare an arrangement as impermissible will undergo a two-stage vetting process – first at Principal Commissioner/Commissioner level and second at Approving Panel to be headed by High Court Judge
- On application of GAAR where a consequence is applied in the hands of one of the participants, corresponding adjustment in the hands of another participant will not be made.

[CBDT Circular 7/ 2017 dated January 27, 2017]

JUDICIAL UPDATES

Advances received by a beneficial shareholder, HUF from Company taxable as deemed dividend

Under section 2(22)(e) of the Income-tax Act, 1961 (the IT Act), advance or loan by a company to a beneficial shareholder or to a concern in which such shareholder is a member/partner/has substantial interest is treated as deemed dividend. The Supreme Court dealt with a case where HUF received certain advances from a company. The money towards shareholding was given by HUF but share certificates were issued in the name of Karta. The HUF was shown as registered and beneficial shareholder in annual returns of the company. The Supreme Court noted that HUF is the beneficial shareholder. It further observed that even if it is presumed that HUF is not a registered shareholder, once the payment is received by the HUF (covered within meaning of concern explanation to section) and shareholder (Karta) is a member of the HUF and he has substantial interest in the HUF, the payment made to the HUF shall constitute deemed dividend.

[Gopal And Sons (HUF) Civil Appeal No. 12274 of 2016 (Supreme Court)]

Doubly taxed 'income' and not 'gross-receipts' to be considered for computation of foreign tax credit

The Tax Tribunal dealt with a case of an Indian company taxpayer who claimed foreign tax credit (FTC) in respect of taxes withheld on gross receipts from foreign countries (Singapore and Indonesia). With respect to the manner of determining the quantum of doubly taxed income, the Tax Tribunal referred to both the tax treaties. It noted that though the tax treaty provides that FTC shall not exceed the part of the income tax as computed before deduction is given, "which is attributable as the case may be, to the income which may be taxed in that other State" but there is little guidance on how to compute such income. Accordingly, the Tax Tribunal interpreted that the expression used is 'income', which essentially implied 'income' embedded in the gross receipt, and not the 'gross receipt' itself. It referred to the OECD and UN Model Commentary to hold that it is the gross income derived from the source state less any allowable deductions (specific or proportional) connected with such income which is to be exempted. It is not the right approach to take into account the gross receipts.

In this present case, no expenses were allocable to majority of the receipts, given their peculiar nature. Accordingly, the order caveats that its decision cannot be

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the authority for the general proposition that only marginal or incremental costs incurred in respect of foreign income should be considered and the overheads cannot be allocated thereto. The allocation of proportional deductions can be justified in some situations, such as when business operations are somewhat evenly or even in a significant manner, spread over the residence and source jurisdiction, which is not the case of taxpayer where main business is carried out in India. The computation of taxpayer, without allocation of costs other than direct/incremental cost was accepted as reasonable on the argument that foreign receipts were only a passive income from isolated transactions in Singapore and Indonesia.

[Elitecore Technologies (P) Ltd. ITA No. 623 (Ahd) of 2015 (Ahmedabad Tribunal)]

TAX UPDATES
Transfer Pricing

JUDICIAL UPDATES

Tax Tribunal Rejects Internal TNMM Due To "Insignificant Sales" And Denies Working Capital And Capacity Utilisation Expenses

The Cochin Tax Tribunal upheld the contention of the Tax Authorities to reject internal Transactional Net Margin Method, as sales volume of Non Associated Enterprise (AE) vis-à-vis the AE sales was insignificant. The Tax Tribunal also rejected the taxpayer's claim for working capital adjustment, as adequate details of working capital adjustment was not mentioned in the transfer pricing study report.

Further, the Tax Tribunal held that sale of scrap was an operating income, as it was a direct bi-product of the manufacturing process undertaken by the taxpayer and should be reduced from the cost of raw material. Also, export entitlement was considered as operating in nature, as it was realization of export sales.

The Tax Tribunal rejected the taxpayer's claim for capacity utilization adjustment, as no adequate reasons for underutilization of the capacity was furnished by the taxpayer and held that capacity utilization adjustment is granted only in extraordinary situations like infancy, lockout of worker's unrest, power cut etc.

[FCI OEN Connectors Limited IT(TP)A No. 70 (COCH) Of 2016 (Cochin Tax Tribunal)]

No Ae Relationship Between Family Owned Entities As Conditions Of Section 92(a)(2) Of The It Act Not Fulfilled

The Ahmedabad Tax Tribunal held that in order to invoke transfer pricing provisions and deal with the determination of Arm's Length Price (ALP), it is essential that the international transaction in question must be between the AEs. The Tax Tribunal held that in order to constitute a relationship of an AE, the parameters laid down in both subsections (1) and (2) should be fulfilled and section 92A(1) and 92A(2) of the IT Act cannot be read independently while determining the relationship between the enterprises. The provisions of subsection (2) to section 92A supplements the definition of AE relationship given in subsection (1) by enlisting various situations under which two enterprises shall be deemed to be an AE. The Tax Tribunal further held that Section 92A(2) of the IT Act governs the operation of Section 92A(1) of the IT Act by controlling the definition of participation in management or capital or control by one of the enterprise in the other enterprise. If a form of participation in management, capital or control is not recognized by Section 92A(2) of the IT Act, even if it ends up in de facto or even de jure participation in management, capital or control by one of the enterprise in the other enterprise, it does not result in the related enterprises being treated as

'AE'. The Tax Tribunal relied on the judicial decisions of Orchid Pharma Ltd [TS-943-ITAT-2016(CHNY)-TP] and Page Industries Ltd [TS-382-ITAT-2016(Bang)-TP].

[Veer Gems ITA NO. 1514 (AHD) Of 2012 (Ahmedabad Tax Tribunal)]

Excluding Loss Making Comparables Without Examining Comparability Unjustified

The Mumbai High Court rejected the contention of the tax authorities to exclude loss making companies as Rule 10B(2) of the IT Rules does not require exclusion of a company, only because it had suffered a loss in a particular year. Further, the loss making companies was selected as comparables in the previous assessment cycle by the tax authorities itself as they reflected profits.

The High Court also held that depreciation and Duty entitlement Passbook (DEPB) expenses are operating and should be considered while computing the operating margins. Also, if a certain expense is taken as a deduction in the tested party margins, a similar treatment of those expenses should be given to the comparable companies also.

[Welspun Zucchi Textiles Limited ITA NO. 1286 (MUM) OF 2014 (Mumbai High Court)]

TAX UPDATES
Indirect Tax

STATUTORY UPDATES
SERVICE TAX

Rationalization of abatement for tour operator services

Notification No. 26/2012-ST has been amended to rationalise the abatement for the services provided by tour operators. It notifies that 60% of the amount charged for providing the service is taxable subject to the following conditions-

- CENVAT credit on inputs and capital goods used for providing the taxable service, shall not be taken under the provisions of the CENVAT Credit Rules, 2004.
- The bill issued shall indicate that it is inclusive of charges of accommodation and transportation required for such a tour and the amount charged in the bill is the gross amount charged for such a tour including the charges of accommodation and transportation required for such a tour.
  [Notification No. 04/2017 - Service Tax dated 12.01.2017]

Due date for payment of service tax for the month of December 2016 and January 2017 extended till 6th March 2017 for 'Online information and database access or retrieval services'

A proviso is inserted to the rule 6 of Service Tax Rules, 1994, namely:

"in case of online information and database access or retrieval services provided or agreed to be provided by any person located in a non-taxable territory and received by non-assesse online recipient, the service tax payable for the month of December, 2016 and January, 2017 shall be paid by 6th day of March, 2017"
[Notification No. 06/2017 - Service Tax dated 30.01.2017]

CASE LAW HIGHLIGHTS
SERVICE TAX

Retrospective restriction under Rule 6 of Service Tax Rules in case of payment to 'associated enterprises' made inapplicable

McDonalds India Pvt Ltd is a wholly owned subsidiary of McDonalds Corporation, USA and both companies qualify as 'associated enterprises'. McDonalds India provides management consultancy services to its USA corporation for undertaking franchise business in India and as a consideration it receives service fee and discharges appropriate Service Tax thereon.

Both adjudication proceedings and Commissioner (appeals) confirmed a demand on the basis of book entry made during FY 2006-07 and 2007-08 in terms of Explanation to Rule 6(1) of Service Tax Rules, 1994.

CESTAT held that Explanation inserted in Rule 6(1) of Service Tax Rules vide Notification No. 19/2008-ST is not applicable retrospectively and observed that in case of transactions between associated enterprises, effect of said amendment is that service tax is required to be paid immediately upon crediting / debiting of amount in books of accounts or receipt of payment, whichever is earlier.

In continuation, it was noted that legislative intent behind such insertion was explained by CBEC vide letter dated February 29, 2008, which was for plugging avoidance of tax on ground of non-realisation of money from associated enterprises. Also, by incorporating the Explanation in Rule 6, restriction prejudicial to interest of associated enterprises was imposed for first time and thus amendment will be considered as prospective in effect, otherwise the doctrine of 'fairness' would stand defeated.
[Mcdonalds India PVT LTD v. Commissioner Of Service Tax, Delhi - TS-571-CESTAT-2016-ST, Delhi CESTAT]

Renting of earthmoving equipments involves 'transfer of right to use' and hence taxable as 'deemed sale', not liable to service tax

Gimmco Ltd. was engaged in renting of earthmoving equipment (excavators, caterpillar etc.) and was not discharging service tax on the same. Revenue contended that the said activity would be taxable under 'Business Auxiliary Service' prior to 16th May, 2008 and under 'Supply of Tangible Goods for Use' post the said date.

CESTAT held that activity of renting of earthmoving equipment involves 'transfer of right to use' and hence taxable as "deemed sale" under MVAT Act r/w Article 366(29A) of Constitution from 16th May, 2008. CESTAT also noted that the responsibilities casted upon hirer clearly show that right of possession and effective control of equipment vested with hirer, since it was liable for any misuse / abuse, safe custody / security and to settle disputes with third parties in relation to use.

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CESTAT also referred to CBEC Circular No. MF (DR) 334/1/2008-TRU dated February 29, 2008 wherein it was clarified that "supply of tangible goods for use" leviable to VAT / sales tax as 'deemed sales' will not be covered under the scope of "Supply of Tangible Goods for Use" service. Relied on AP High Court ruling in case of G. S. Lamba which laid down essential requirements for transaction to constitute "transfer of right to use goods" and held that merely because restrictions were placed on lessee, it cannot be said that there was no right to use the equipment. As regards "Business Auxiliary Service" category prior to May 2008, CESTAT remanded matter to Adjudicating Authority for fresh consideration.

[Gimmco Ltd. V. Commissioner Of CE, Nagpur - Ts-552-CESTAT -2016-ST, Mumbai CESTAT]

CENTRAL EXCISE

Wrong availment of CENVAT credit – Recoverable under Rule 14 of CENVAT Credit Rules (even if the same is intimated to the Dept.)

Tata Toyo Radiators is engaged in the manufacture of radiators and was availing CENVAT credit on inputs, capital goods and input services. In September 2008, it availed CENVAT credit twice on the same set of documents and voluntarily reversed in the March 2009 and the fact was informed to the Range Superintendent. However, department alleged that the assessee has credit has been wrongly availed and is recoverable under Rule 14 of CENVAT Credit Rules, 2004.

CESTAT held that there is an interest liability on wrong availment of CENVAT credit under Rule 14 of CENVAT Credit Rules r/w Sections 11A & 11AB of Central Excise Act. Assessee contented that such wrong availment merely entailed an entry in CENVAT Credit Account, thereby not causing any loss to Revenue and since the same was reversed voluntarily, interest liability would not accrue. Also, assessee relied on Karnataka HC decision in Bill Forge Pvt Ltd.

CESTAT noted that as per Rule 14, where CENVAT credit is taken or utilized or refunded erroneously, same alongwith interest is recoverable from manufacturer / service provider and such recovery shall be effected in terms of Sections 11A & 11AB of Central Excise Act. Also, held that Bill Forge Pvt Ltd decision was held per incuriam by coordinate bench in case of Dr. Reddy's Laboratories Ltd. CESTAT followed Supreme Court ratio in case of Ind-Swift Laboratories Ltd.

[Tata Toyo Radiators Ltd. V. Commissioner Of Central Excise, Pune I - Ts-549- CESTAT -EXC, Mumbai CESTAT]

CUSTOMS

Notification denying All Industry Rate of drawback to EOU against exports inapplicable

Appeal was filed before Delhi CESTAT against adjudication order confirming demand of INR 2.92 crore against the appellant.

The appellant a 100% EOU engaged in the manufacture of readymade garments, article of apparel and clothing falling under chapter 61 and 62 of the Central Excise Tariff Act, 1985. They were manufacturing their final products out of the raw materials imported by them, free of duty. Such final goods were being cleared by them were exported by them under valid shipping bill without any claim of draw back. There was no dispute on export of the said goods.

Apart from that, the appellant was also procuring the duty paid inputs from indigenous manufacturer which were being used by them in the manufacture of their final product without the claim of any CENAVT credit. Such goods were exported by the appellant under green shipping bills under claim of All Industry Rate of drawback.

Subsequently, proceedings were initiated against the appellant by way of issuance of show cause notice to recover the said draw back amount already sanctioned to them and received by the appellant on the alleged ground that the appellant is a 100% EOU and as per notification No. 26/03-Cus (NT), as amended, an 100% EOU is debarred from claiming the benefit of notification.

After going through the rival submissions, CESTAT noted that the goods stand manufactured by the appellant himself. There is also no dispute that the materials used by them were of duty paid and the fact that appellant has not availed any credit of duty so paid is also admitted by the Revenue. Denial of drawback is on the sole ground that same would not be available to 100% EOU as against the express provisions of section 75 as also of the draw back Rules, the said stand of the Revenue cannot be appreciated and accepted.

Accordingly, CESTAT allowed the appeals, without adverting to other issues of revenue neutrality and limitation.

[Fancy Images & Others V. Commissioner Of Customs, New Delhi - TS-6- CESTAT -2017-cust, New Delhi CESTAT]

High Court noted that Notification stipulating limitation period for claiming SAD refund, not ultra vires

Under this petition, Hon'ble High Court rejected challenge to Notification No. 93/2008-Cus stipulating limitation

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period of 1 year for claiming refund of Special Additional Duty (SAD) from date of payment thereof.

Hon'ble High Court noted that only one condition cannot be declared ultra vires just because assessee desires to brush it aside and observed that assessee's contention that it had no control over market conditions since it would await installation orders in respect of ATMs supplied to SBI branches across the country, which took time, and hence, 1 year limitation could not commence unless goods were sold is not acceptable.

Hon'ble High Court observed that "The exemption being conditional, it is not permissible to pick and choose convenient conditions of the exemption Notification and leave out those which to parties like the petitioners, appear to be onerous and excessive"; There is no vested, much less absolute right, to seek refund and even a refund claim must be within framework of statute and admissible on terms thereof.

Further, it was observed that it is entirely for Central Government to take a decision w.r.t. exemption and conditions, and having exercised powers in terms of statutory provisions that must govern the whole field.

Hon'ble High Court holds that the condition imposing time bar or limitation to file refund, cannot be held as onerous, excessive and ultra vires Article 14 of Constitution. Accordingly, petition stands dismissed.

[CMS Info Systems Limited V. The Union Of India & Others - Ts-577-hc-2016(bom)-cust, Mumbai High Court]

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