NEWS CRUNCH

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NANGIA & CO LLP
CHARTERED ACCOUNTANTS

What's inside . . .

1. No service PE by considering only solar days of services rendered in India

- Bangalore Income Tax Appellate Tribunal ("ITAT") in the case of a company resident of Saudi Arabia ("the Assessee"), dealt with the issue of taxability of income for rendering services in India, under the India-Saudi Arabia Double Taxation Avoidance Agreement ("DTAA").

Placing reliance on the Mumbai ITAT's decision in Clifford Chance v. DCIT[1], the ITAT ruled that for the purpose of computation of threshold for service permanent establishment ("Service PE"), solar days need to be considered, not man days.

Background

The Assessee received income from an Indian company by rendering certain services through four engineers sent to India. The engineers spent more than 360 man days individually, but their collective stay in India was 90 days only. The Indian company paid the Assessee for services provided by the engineers in India. While filing the return of income in India, the Assessee claimed that income from services to the Indian company were in the nature of FTS and, in the absence of a provision on FTS under the DTAA, such income is not taxable in India.

[1] 76 TTJ 725

Reliance was placed on the Madras High Court ruling in the case of Bangkok Glass Industry Co. Ltd. v. ACIT[2] in this regard. Furthermore, by placing reliance on the Mumbai ITAT's decision in the case of Clifford Chance (supra), it was contended that only solar days should be considered for the purpose of determining the existence of a service PE. Accordingly, as the presence of engineers in India was less than 182 solar days, no service PE was created.

On the other hand, the Tax Authority was of the view that the Assessee's income was taxable in India as "royalty" under the Income-tax Act ("the Act"), as well as the DTAA. Furthermore, a Service PE is created when aggregate man days (360) of stay of the engineers in India are considered. Reliance was also placed on a recent ruling of the Bangalore ITAT (supra) to contend that the physical presence of the employee is not essential, as services can be rendered through various virtual modes. Aggrieved, the Assessee filed an appeal before the ITAT.

Ruling of ITAT

In the present case, as the presence of the Assessee's engineers in India was for less than 182 days (i.e., only 90 solar days), there was no service PE created under the DTAA. The ITAT observed that the Assessee did not render any other service in virtual mode and all the services were rendered by the engineers who were physically present in India. To that extent, a previous decision of the Bangalore ITAT[3] on the constitution of a service PE for services rendered virtually, as well as physically, was distinguished on facts. Furthermore, it was held that in the absence of the "Fees for Technical Services" (FTS) Article in the DTAA, income shall be covered under the "Other Income" Article, such that it is taxable only in Saudi Arabia. ITAT rejected the contention of virtual PE application in the absence of services rendered virtually.

[2] 2015 (4) TMI 503
[3] TS-256-ITAT-2017(BANG)

NANGIA 'S TAKE

- ***This ruling reiterates the accepted principle that for the purpose of calculation of threshold for constitution of a service PE, solar days, and not man days, should be considered.***

- ***However, an interesting aspect is that in the absence of the FTS Article under the DTAA, while the ITAT has ruled that the "Other Income" Article shall be applicable, assessees may have to evaluate their facts to invoke decisions in the cases of ACIT v. Paradigm Geophysical Pty Ltd.[4] and Tekniskil (Sendirian) Berhard v. CIT[5], wherein the view had been expressed that FTS is general business income and that, in the absence of a specific FTS Article, the same should be covered within the purview of "business profits" and taxable only if attributable to PE in the source country. In the present case, no taxation was triggered in India under the "Other Income" Article of the DTAA, which allocates exclusive taxation rights to the country of residence, but the conclusion may be different it the "Other income" Article grants taxation rights to the source country.***

[4]ITR(T) 178
[5]222 ITR 551

2. Contract receipts of a JV result in diversion of income to JV members; receipt not an income of the JV

- In a recent decision of the Jammu and Kashmir (J&K) High Court ("HC") in the case of Soma TRG Joint Venture[6] ("the Assessee"). The HC, in this case, was concerned with the issue of whether the contract revenue received by a joint venture (JV) accrues as income in its hands or whether it results in diversion of income at source from the JV to the JV members.

Background

- An Indian company ("A Co."), wanted to bid for a tender floated by the Indian Railways for construction of tunnels. However, the Indian Company did not satisfy the conditions which were laid out by the Indian Railways in the tender notice. Another Indian company ("B Co."), had the necessary experience which would make it eligible to bid for the tenders floated by the Indian Railways. Thus, both (JV members) entered into a JV agreement to set up a JV with the intention of filing a joint bid for the tender floated by the Indian Railways.

- As per the JV agreement, B Co. would act as the lead party of the JV. Furthermore, both A Co. and B. Co. would jointly exercise the authority to incur liabilities on behalf of the JV. As per the terms of the existing JV agreement, the JV members entered into a new JV agreement, neither B Co. nor the JV was required to do any work in relation to the contract.

[6]TS-405-HC-2017(J&K)

Owing to the limited role of B Co., the JV members agreed to share the contract revenue in the ratio of 97:3.

In the relevant financial year (FY), the contract revenue was allocated by the JV to A Co. and B Co. in the ratio of 97:3 and the JV filed a return of income in the status of AOP and declared nil income for the relevant FY by contending that the income from the contract was diverted to the JV members at source and there was no accrual of income in its hands. The JV members offered the contract revenue to tax in the agreed ratio. However, the Tax Authority treated the contract revenue as income of the JV. Furthermore, the Tax Authority considered the payment made by the JV to JV members as payment towards sub-contracting charges. Since the JV had failed to withhold taxes on the same, the Tax Authority disallowed the payment made to the JV members under the disallowance provisions.

Aggrieved by the orders of the appellate authorities, the Assessee appealed before the HC.

Ruling of the HC

❖ ***On diversion of income at source***

The terms of the JV agreement indicate that the JV was formed only for the purpose of submission of the tender bid and once the contract was awarded, work was executed by the JV member. The JV has not performed any work or activity in relation to the contract. The amount received by the JV is, thus, not an income accruing to it. The primary test for determining whether there has been a diversion of income is to determine whether the income gets diverted before it accrues to the taxpayer or whether it is applied by the taxpayer after it accrues to it.

Though the definition of income is very wide, in the facts of the case, income from the contract is diverted at source itself before it accrues to the JV. Hence, it cannot be regarded as income of the JV.

❖ ***Applicability of the disallowance provisions***

The HC referred to the Supreme Court (SC) ruling in the case of R.B. Jodha Mal Kuthiala[7] in support of the proposition that a provision which is inserted in the Act to rectify an unintended consequence and to make the provision workable, is to be treated as having retrospective application. Basis this, the HC held that the amendment to the disallowance provisions is curative and is retrospective.

In the present case, the JV members have paid the taxes on the income received. The case is protected by the amended disallowance provisions. Alternatively, the disallowance provisions will apply only to an amount which remains unpaid at the end of the relevant FY and will not apply to an amount which is already paid during the FY. In the present case, there is no amount payable to the JV members at the end of the relevant FY and, hence, there can be no disallowance in the hands of the JV.

NANGIA'S TAKE

There has been an ongoing litigation on the issue of whether, in a case where there is internal overriding understanding between members, the principles of diversion of income by overriding title apply to the AOP.

[7](1971) 82 ITR 570(SC)

Furthermore, whether such principles can be drawn by the AOP to contend that income received from the contract is diverted at source in favor of the members which executed the contract and, hence, such receipt should not constitute income in its hands.

The judicial precedents on this aspect indicate that the primary test for determining whether there has been a diversion of income is to determine whether the income gets diverted before it accrues to the assessee or whether it is applied by the assessee after it accrues to it.

To that extent, this HC ruling does provide some guidance to assessees on the circumstances in which a consortium may claim that the amount received by it is diverted in favor of its members.

3. Aadhaar based e-sign facility for Provident Fund Portal

- The Employees' Provident Fund Organisation (EPFO) issued a circular introducing Aadhaar-based e-sign facility for employers to authenticate various documents on the Provident Fund portal on 06 October 2017. Earlier, the authentication was done through Digital Signature Certificate ("DSC").

Specific software installations and settings are required to use the DSC on the Provident Fund portal. Many employers had reported to the EPFO that they were facing difficulties in authenticating the documents using the DSC. Considering the above, the EPFO has now introduced Aadhaar-based e-sign facility in addition to DSC for authentication of documents. Once the authorized signatory is registered for e-sign, the documents can be authenticated by using the one-time pin ("OTP") sent on the mobile registered with Aadhaar of the authorized signatory.

- The employers whose DSC is already registered can activate their Aadhaar base e-sign by providing Aadhaar of the authorized signatory, name, designation, gender and date of birth on the Provident Fund portal. An OTP will be sent to the mobile number registered with Aadhaar of the authorized signatory. On submission of the OTP, Aadhaar-based e-sign will be registered.

- The employers whose DSC is not registered can activate the Aadhaar based e-sign by providing Aadhaar of the authorized signatory, name, designation, gender and date of birth on the Provident Fund portal.

An OTP will be sent to the mobile number registered with Aadhaar of the authorized signatory. On submission of the OTP, a request letter will be generated to be sent to the EPFO. The signed request letter will need to be submitted to the relevant regional EPFO office for approval. Upon approval, the Aadhaar-based e-sign will be registered. As per the circular, regional EPFO offices have been advised to approve the Aadhaar-based e-sign registration requests immediately.

NANGIA'S TAKE

The EPFO has also issued a User Manual for registering the authorized signatory for Aadhaar-based e-sign. The EPFO has launched many initiatives to make its services completely digital. This new Aadhaar based e-sign facility will help the employers who were facing difficulties in authenticating the documents using DSC on the Provident Fund portal.

REGULATORY UPDATES

4. Reserve Bank of India issues Master Directions for regulating Peer to Peer Lending Platforms in India

- In April 2016, the Reserve Bank of India (RBI) issued a consultation paper on Peer to Peer (P2P) Lending, providing an overview of business models that are operational both domestically and internationally, and assessing the need to regulate such business models operating in India, considering the impact that it can have on the traditional banking channels and the non-banking financial company (NBFC) sector.

After a year-long wait, on 24 August 2017, with the approval of the Central Government, the RBI notified non-banking institutions carrying on the business of a peer to peer lending platform to be NBFCs.

Pursuant to this notification, on 4 October 2017, the RBI issued Master Directions[9] providing the framework for registration and operation of NBFCs that carry on/propose to carry on the business of a P2P lending platform. These Master Directions shall come into force with immediate effect.

[9]DNBR (PD) 090/ 03.10.124/ 2017-18 dated 4 October 2017

Background

- With the advent of online industry, Peer to Peer (P2P) lending has emerged as a growing market over the years, globally and in India, and has the potential to bring changes in the traditional lending landscape.

- P2P lending platforms are basically online platforms that act as an intermediary to match lenders with borrowers in order to provide unsecured loans.

- Considering the significance of and the risks associated with the online industry and the impact which it can have on the traditional banking channels/ Non-banking Financial Companies (NBFCs), the Reserve Bank of India (RBI) considered it necessary to have an explicit framework in place to regulate the P2P lending platforms in India.

- With this intention, the RBI issued a consultation paper on P2P lending in April 2016, providing an overview of various business models that are operational both domestically and internationally and assessing an urge to regulate such business models.

- In order to regulate the P2P lending platforms, the Department of Non-Banking Regulation of the RBI, after receiving approval from the Government of India, on 24 August 2017, notified a company who undertakes 'the business of a peer to peer lending platform' to be designated as an NBFC.

- Pursuant to this notification, on 4 October 2017, RBI has issued Master Directions providing the frame-work for the registration and operation of NBFC-P2P Lending Platform (NBFC-P2P).

Salient Provisions of the Master Directions

Key definitions

'P2P lending platform' has been defined to mean an intermediary providing the services of loan facilitation via online medium or otherwise, to the participants.

'Participant' is defined to mean a person who has entered into an arrangement with an NBFC-P2P to lend on it or to avail of loan facilitation services provided by NBFC-P2P.

Eligibility criteria

- Only companies which have sought prior approval from RBI to be NBFC-P2P can undertake business of P2P Lending Platform.

- Existing companies undertaking the business of P2P lending platform shall apply for registration as NBFC-P2P within three months from the issuance of the Master Directions.

- Every company seeking registration with the RBI shall have net owned funds of not less than INR 20 million or such higher amount as RBI may specify.

Scope of activities

NBFC-P2Ps shall –

- act as an intermediary providing an online marketplace or platform to the participants involved in P2P lending;

- not raise deposits as defined by or under Section 45I(bb) of the Reserve Bank of India Act, 1934 (RBI Act) or the Companies Act, 2013;
- not lend on its own;
- not provide or arrange any credit enhancement or credit guarantee;
- not facilitate or permit any secured lending linked to its platform;
- not hold, on its own balance sheet, funds received from lenders for lending, or funds received from borrowers for servicing loans;
- not cross sell any product except for loan specific insurance products;
- not permit international flow of funds;
- ensure adherence to legal requirements applicable to the participants as prescribed under relevant laws.
- store and process all data relating to its activities and participants on hardware located within India.

Also, NBFC P2Ps shall –

- undertake due diligence of participants;
- undertake credit assessment and risk profiling of borrowers;
- require explicit consent of the participant to access its credit information;
- undertake documentation of loan agreements and other related documents;
- provide assistance in disbursement and repayment of loans and render services for recovery of loans originated on the platform.

NANGIA'S TAKE

Regulating the P2P business model would certainly build confidence amongst various stakeholders and also bring in competitiveness in the market vis-à-vis traditional lending channels. Having said that, certain aspects of the Master Directions do require further clarifications and certain relaxations by the RBI to ensure growth in this industry.

5. Japan, Denmark sign new tax treaty

- The governments of Japan and Denmark on October 11 signed new tax treaty, Japan's Ministry of Finance has announced. The new treaty, signed in Tokyo, would amend the countries' 1968 tax treaty, revising the taxation of business profits, and reducing the taxation of investment income. Under the treaty, dividends paid by subsidiaries are exempt from withholding tax in some cases, and the tax rate is 15 percent in other cases. Cross-border payments of interest and royalties are exempt from tax.

- The treaty also introduces a "principal purposes" test to prevent tax treaty abuse, and provides for arbitration of tax treaty disputes. The agreement also provides for assistance in the collection of tax claims. Further steps must be taken by each country before the new agreement enters into force.

Source: https://mnetax.com/japan-denmark-sign-new-tax-treaty-24016

6. Hong Kong Gazettes Key Tax Info Exchange Law

- Hong Kong's Inland Revenue has gazetted a law to become party to the Multilateral Convention on Mutual Administrative Assistance in Tax Matters. It will also align the Inland Revenue Ordinance (IRO) with the Common Reporting Standard (CRS), the OECD's new information exchange standard providing for automatic information exchange.

- The IRO was amended in June 2016 and further amended in June 2017 to mandate financial institutions to collect account information of tax residents from 75 jurisdictions so that this information can be exchange automatically under the CRS. Participation in the Convention will facilitate these exchanges, exchanges of country-by-country reports, and the spontaneous exchange of information on tax rulings.

Source:https://www.tax-news.com/news/Hong_Kong_Gazettes_Key_Tax_Info_Exchange_Law___75457.html

7. Dutch government rolls out carpet for business with tax cuts

- The incoming Dutch government rolled out the red carpet for big business on Tuesday, firming up plans to lower the corporate tax rate to 21 percent and scrap a 15 percent tax on dividends.

- As part of the biggest tax overhaul in years, it also introduced a tax on royalties in a bid to counter a reputation for abetting tax avoidance by housing shell companies that act as a conduit for money destined for tax havens.

- He said Britain's decision to leave the European Union gave the Netherlands a chance to attract firms based in Britain but seeking a European headquarters

Source: https://www.reuters.com/article/netherlands-government-tax/update-2-dutch-government-rolls-out-carpet-for-business-with-tax-cuts-idUSL8N1ML3EN

8. Wall Street set to resume rally on tax reform hopes

- U.S. stocks looked set to resume their recent rally on rising optimism over President Donald Trump's proposed tax overhaul. Hopes of tax reforms brightened after the Republican-controlled U.S. House of Representatives on Thursday approved a fiscal 2018 spending blueprint to help them advance an eventual tax bill.

- Two of the biggest banks - JPMorgan Chase and Citi - kick off the quarterly results season proper on Thursday.

- Earnings are expected to have increased 4.9 percent in the third quarter, according to Thomson Reuters data, down from double-digit growth in the first two quarters of this year.

- Weak jobs numbers halted an eight-day winning streak for the S&P 500 on Friday, but the Nasdaq ended up for a ninth straight day. Chalking up employment losses last month to the temporary hit of a severe hurricane season and reiterating expectations that inflation will strengthen, Federal Reserve policymakers on Friday signaled they still expected U.S. interest-rates to rise gradually.

Source: http://www.business-standard.com/article/reuters/wall-street-set-to-resume-rally-on-tax-reform-hopes-117100900878_1.html

TRANSFER PRICING

9. Miscellaneous Application before ITAT not 'alternate remedy' to High Court appeal: The HC Refuses delay condonation

Facts of the case

Agnity Technologies Pvt Ltd ("the taxpayer") is a wholly owned subsidiary of Agnity Inc., USA and is engaged in providing software development services/information technology services to its overseas associated enterprises ("AEs"). During the assessment year under review, the taxpayer entered into international transactions with its AEs in the nature of IT services which were benchmarked using Transactional Net Margin Method ("TNMM"). Both the taxpayer and Revenue filed cross appeals before the Delhi Income Tax Appellate Tribunal ("ITAT") seeking exclusion/inclusion of certain companies from the list of comparables. ITAT decided in favor of Revenue and retained the set of final comparable companies as proposed. Aggrieved with the decision, the taxpayer filed an appeal before Delhi High Court ("HC") with a delay of 439 days.

Proceedings before HC

Taxpayer's plea

Before the HC, the taxpayer submitted that the delay in filing appeal was caused because an alternate remedy by way of Miscellaneous Application was being pursued before the ITAT in order to exclude a particular company from the list of final comparables. The taxpayer contended that the ITAT, in other cases had been consistent in excluding this company from the final set of comparables. The taxpayer held that the period during which it pursued the alternate remedy before the ITAT should be excluded and cited Sec 14 of the Limitation Act 1963 relying upon the Supreme Court ("SC") ruling in ***M.P. Steel Corporation v. Commissioner of Central Excise***.

The HC's Ruling

The HC rejected the taxpayer's plea that an application filed before the ITAT under section 254(2) of the Act was an alternate course of action to the filing of an appeal under section 260A of the Act. The HC remarked that *"An application under Section 254(2) of the Act is for rectifying 'mistakes apparent from the record' which is much narrower in scope than an appeal under Section 260A of the Act where an order of the ITAT can be challenged on substantial questions of law."*

It also clarified that the time period for filing an appeal under Section 260A of the Act does not get suspended on account of the pendency of an application before the ITAT under Section 254(2) of the Act."

The HC reaffirmed that the question of invoking Sec 14 of Limitations Act would not arise and therefore, the decision relied upon is not applicable to the facts of this case. Thus, the HC held that the taxpayer did not provide substantial reason for the extraordinary delay in filing the appeal and accordingly, dismissed the taxpayer's request and appeal for condonation of delay.

NANGIA'S TAKE

The HC with its judgment has clarified that there must be substantial reason for not filing of appeal in the stipulated time period. It clarified that the time period under section 260A of the Act does not get suspended on account of filing a miscellaneous application before the ITAT under section 254(2) of the Act.

Source: Agnity Technologies Pvt Ltd [TS-729-HC-2017(DEL)-TP]

10. Guidelines for claiming IGST refund on exports and other procedural requirements

❖ CBEC vide Instruction No. 15/2017-Customs dated 09 October, 2017 has issued detailed guidelines for claiming IGST refund on exports. Summary of the guidelines are provided below:

1. REFUND PROCESSING FOR JULY 2017 EXPORTS

- The GST council has recommended that IGST refund for exports made in July 2017 should start by 10 October 2017 instead of 10 November 2017 being the due date of filing of GSTR-3 for the month of July 2017.
- The refund for the month of August would be cleared from 18 October 2017 and refunds for subsequent months would be handled expeditiously.

2. PRE-CONDITIONS FOR IGST REFUND

- The Shipping bill filed by an exporter shall be deemed to be an application for refund of integrated tax paid on the goods exported.
- Filing of correct EGM (Export General Manifest) is must for considering shipping bill or bill of export as a refund claim.
- The applicant has furnished a valid return in GSTR -3 or GSTR 3B.

3. BANK ACCOUNT DETAILS

- As per rule 96 of CGST rules 2017, the refund is to be credited in the bank account as mentioned at the time GST registration.
- In case, bank account details available with the Customs department do not match with bank details provided for GST registration, refund would be credited in the bank account available with the Customs department to ensure smooth processing of refund.
- Further, as the payments are being routed through PFMS portal, bank account details need to be verified and validated by PFMS.
- The status of validation of bank account with PFMS is available in ICES.

4. GSTR-1 TABLE 6A FOR AUGUST, 2017 (Separate Utility)

- Due date of furnishing GSTR-1 for August, 2017 has not been notified yet. Hence, a separate utility for filing details in table 6A (export details) of GSTR-1 would be available on the GST portal specifically for ease of completion of procedural requirement of refund application.

5. POWER TO WITHHOLD REFUND

- The proper officer will withhold the refund on request made by the Jurisdictional Commissioner of Central tax, State tax, or Union territory tax and copy of intimation for withholding of refund has to be transmitted on the common portal to the applicant.

NANGIA'S TAKE:

- ***While considering the various inference for claiming refund under GST due to procedural intricacies, CBEC is taking initiative to fasten the process of refunds. This would result reduction in working capital requirements.***

- ***These guidelines would ensure a smooth processing of refund of IGST paid on export of goods. Further, it would provide immediate relief to the export sector and enhance export competitiveness of India. In view of such steps taken by the council, the current situation of the depressed exporters would get much awaited relief and will change GST on a positive note.***

OUR OFFICES

NOIDA
Nangia Tower, A - 109, Sector 136, Noida
Ph: +91-120-2598000, Fax: +91-120-2598010

DELHI
B-27, Soami Nagar, New Delhi-110017, India

MUMBAI
11th Floor, B Wing, Peninsula Business Park,
Ganpatrao Kadam Marg,
Lower Parel, Mumbai–400 013, India

DEHRADUN
First Floor, "IDA", 46 E. C. Road
Dehradun – 248001

SINGAPORE
24 Raffles Place, #25-04A
Clifford Centre
Singapore- 048621

www.nangia.com
nangia@nangia.com