NEWS CRUNCH

April 01-15, 2018

WHAT'S INSIDE...

- Direct Tax
- International Tax
- Transfer Pricing
- GST

NANGIA & CO LLP
CHARTERED ACCOUNTANTS

NEWS CRUNCH

What's inside . . .

DIRECT TAX

1. Delhi Tribunal rules that domain registration fees charged by a non-resident entity is taxable as 'royalty' as per clause (vi) read clause (iii) of Explanation 2 to Section 9(1) because such rendering of services in connection with the use of an intangible property is similar to the trademark

Brief Facts of the Case:

- ❖ Godaddy.com LLC ('Assessee') is a limited liability company located in the USA. It is engaged in the business as accredited domain name registrar authorized by Internet Corporation for Assigned Names and Numbers ('ICANN').

- ❖ During the year under consideration, Assessee earned two different types of income, namely, income from web-hosting services and income from domain registration charges.

- ❖ While the Assessee offered its income from web-hosting charges as 'royalty', as it involved allowing use of space on its server to its clients

- While the Assessee offered its income from web-hosting charges as 'royalty', as it involved allowing use of space on its server to its clients

- However, Assessee claimed its income from "domain registration fees", which was essentially in nature of assistance to companies in registration of their websites with the ICANN, to be not taxable in India. The assessee claimed that such services were neither in nature of 'royalty' nor in nature of 'Fees for Technical Services', and thus could not be taxed in India in absence of any presence/ activities in India.

- However, the Assessing Officer ("AO") taxed income from 'domain registration services' as 'royalty' as per clause (vi) read clause (iii) of Explanation 2 to Section 9(1) of the Income Tax Act, 1961 ("The Act"), which was also confirmed by the DRP.

- Aggrieved, Assessee filed appeal before the Income Tax Appellate Tribunal ("ITAT" or "Tribunal").

Contentions of Assessee

- At the outset, the Assessee stated that it was governed under the Income Tax Act, 1961 ("The Act"), as being a tax transparent Limited Liability Company incorporated in the USA, it was not eligible to claim benefit under the provisions of India-USA tax treaty.

- The Assessee further contended that web hosting services and domain name registration services are independent services, and taxability of both the services have to be examined separately.

- The Assessee explained that domain name registration is the process of registering a domain name which identifies one or more IP address with a name that is easier to remember and use in URLs to identify particular web pages.

- The Assessee further stated it merely provided certain assistance in registration of website domain of its clients with the ICANN, which merely included services such as checking the availability of desired domain name, facilitating registration of the domain name of the users, assigning unique IP address for the domain name and maintaining a record of all the domain names and their IP addresses. The Assessee contended that the entire process of such assistance in domain name registration was automated process, without any human intervention and it did not involve granting of any right in the nature of copyright or trademark or any similar rights to give rise to income in nature of 'royalty'.

- The Assessee further contended that for providing domain registration service, none of the employees of the assessee visited India and all services are provided from outside India. The assessee doesn't have any fixed business presence in India in the form of any branch/liaison office and the business operations are undertaken from outside India.

- Hence, it was claimed that the income from 'domain registration fees' was not in the nature of 'royalty' or 'fees for technical services' and it could not be taxed in India, being not attributable to any activity carried out in India.

- The Assessee also placed reliance on decision of Hon'ble Delhi High Court in the case of Asia Satellite Telecommunications Co. Ltd. Vs. DIT-[2011] 197 Taxman 263 and of Authority for Advance Rulings in the case of Dell International Services (India) Pvt. Ltd.- [2008] 218 CTR 209.

Contentions of Revenue

- The Revenue argued that the transaction of domain name registration services and web hosting services are interconnected processes.

The revenue also stated that domain name is an intangible asset similar to trademark and services rendered by Assessee are integral and inextricably linked to domain name, which is similar to trademark.

- The Revenue contended that the assessee is rendering services in connection with such domain name registration and therefore, the charges received by the assessee clearly fall within the definition of royalty u/s 9(1)(vi) of the Act.

Hon'ble ITAT's Judgment

- While pronouncing its decision, Hon'ble ITAT relied on principles laid down under various case laws rendered in context of intellectual property rights disputes, including Supreme Court judgment in the case of Satyam Infoway Ltd. [2004] Supp (2) SCR 465 (SC), wherein it was held that internet domain names are subject to the legal norms applicable to other intellectual properties such as trademarks. Also the domain name is a valuable commercial right and it has all the characteristics of a trademark and accordingly, it was held that the domain names are subject to legal norms applicable to trademark.

- On the similar grounds, Hon'ble ITAT relied on Bombay High Court ruling in the case of Rediff Communications Ltd. –AIR 2000 Bombay 27, wherein it was held that domain names are of importance and can be a valuable corporate asset and such domain name is more than an internet address and is entitled to protection equal to a trademark.

- Further, ITAT discussed the Delhi High Court ruling in the case of Tata Sons Limited -90 (2001) DLT 659 (Delhi), wherein it was held that domain names are entitled to protection as a trademark because they are more than an address.

- Based on principles laid down in above-mentioned case laws, the ITAT held that "the rendering of services for is similar to trademark.

- Therefore, the charges received by the assessee for services rendered in respect of domain name is royalty within the meaning of Clause (vi) read with Clause (iii) of Explanation 2 to Section 9(1) of Income-tax Act".

- In view of the above, ITAT upheld the orders of the lower authorities and rejected Assessee's appeal.

NANGIA'S TAKE

- ***At the outset, this decision again highlights that principles laid down in context of commercial/ intellectual property disputes can also be used in deciding correct nature of a transaction and determining taxability of income from such transaction. Thus, while taking a position in complex tax issues, a Taxpayer must be mindful of principles laid down by various courts under other laws as well.***

- ***Further, this is one of very few decisions of the Tribunal, where issue of taxability of domain name registration charges has been discussed and decided by the Tribunal. In our view, positions taken by both Assessee and tax Authorities have reasonable basis to support their tax positions, and we can expect this dispute to travel to the Higher Courts, before a conclusive answer is arrived at in such issues.***

2. Authority for Advance Rulings rules that services rendered by an oil & gas service provider in the nature of seismic data acquisition, processing and interpretation though vessels/ equipment would constitute Fixed Place PE in India even for a duration of 113 days, in absence of a corresponding specific provision under India-UAE tax treaty for such services, rejects Taxpayer's contention for applying threshold provided for Service PE under the tax treaty, saying Service PE is not applicable for the kind of services rendered by Applicant.

Facts of the case

❖ SeaBird Exploration FZ LLC, UAE ('**the Applicant**') is a company incorporated under the laws of UAE, and is its tax resident. It is engaged in the business of rendering geophysical services to the oil and gas exploration industry which are aimed at increasing the exploration success of its oil and gas clients and maximizing their production.

❖ During the year under consideration, the applicant provided services to Oil and Natural Gas Corporation Ltd ('**ONGC**') for 4C-3D seismic data acquisition, processing and interpretation in the Mumbai High Field.

❖ Applicant sought ruling on following questions in respect of its tax liability in India:

i. Whether the services provided by the Applicant constitute Fees for Technical Services ('**FTS**') u/s 9(1)(vii) of the Income Tax Act, 1961 ('**the Act'**)?

ii. Whether the services provided by the Applicant constitute Royalty u/s 9(1)(vi) of the Act?

iii. Whether the Applicant can be considered as having a Permanent Establishment ('**PE**') in India in terms of Article 5 of the India-UAE Double Taxation Avoidance Agreement ('**DTAA**')?

iv. If income of the Applicant is taxable in India, whether the same can be computed in accordance with the provisions of Section 44BB of the Act?

Applicant's Submissions

❖ Applicant submitted that the income earned from the transaction is neither in the nature of FTS/ Royalty nor is the income taxable as business income as there is no PE of the Applicant in India.

❖ The Applicant used vessels for undertaking its operations in India and had a presence of 133 days in India in respect of ONGC's contract. Therefore, it submitted that it did not have a PE in India in terms of Article 5(2)(i) (Service PE) of the DTAA.

- It contended that the special provision has to be given preference and priority as against a general provision. Hence, the contract being a service contract, Article 5(2)(i) of the DTAA would apply, since the work was completed within 113 days, which was less than the threshold for creating a Service PE.

- The Applicant further relied upon the decision of Hon'ble Delhi High Court in the case of **National Petroleum Construction Company v. DIT [2016] 383 ITR 648** wherein it was held that, *"places of business as specified under sub-paras (h) and (i) of paragraph 2 of Article 5, cannot be construed as a PE of an enterprise unless they exist for a period of at least nine months."*

- Nevertheless, the Applicant submitted that without prejudice, its income from ONGC contract may be computed as per provisions of Section 44BB of the Act.

Revenue's Submissions

- Revenue agreed with Applicant's submission that the income earned by Applicant in respect of the activities carried out did not constitute FTS or Royalty in terms of the decision of Hon'ble Supreme Court in the case **ONGC v. CIT [2015] 376 ITR 306 (SC)**.

- Revenue further accepted that the activities of the Applicant fell within the purview of the term "in connection with" exploration of mineral oils, as stipulated u/s 44BB of the Act.

- In reference to Question No. (iii), the Revenue strongly contended that the Applicant has a "Fixed Place PE" within the meaning of Article 5(1) of the DTAA in the form of seismic vessels which were at the disposal of the Applicant. It further mentioned that Length of Period is not a criterion under Article 5(1) of the DTAA.

- Revenue was of the view that the movement of the vessel was an integrated one having commercial and geographical coherence. It took support of the judgment in case of **M/s Poompuhar Shipping Corp. Ltd. Vs. ITO(IT) [2014] 360 ITR 257 (Madras)** wherein, it was held that *"A movable place of business is thus treated as fixed place of business and most of the equipment is used at fixed points within a proximate area on a repetitive continuous basis for sufficient period of time as required by the business."* The Revenue also placed reliance on decision of Delhi Tribunal in case of **Fugro Engineers BV (ITA No. 269/DEL-2007) reported at [2008] 26 SOT 78 (Delhi)**, to contend that vessel of the Applicant constituted a Fixed Place PE in India.

<u>Advance Ruling pronounced by the Authority</u>

- Regarding Question (i) and (ii), the Authority agreed with the view of both, the Applicant and the Revenue that the income from the Activities under consideration does not constitute FTS or Royalty.

- Coming to Question (iii), the authority relied upon the decision of Hon'ble Supreme Court in the case of **Formula One World Championships Limited (2017) 80 taxman.com 347** to hold that the vessels used by the Applicant passed all 3 tests for constituting a PE as per Article 5(1) of the DTAA, namely, there is permanence of duration to the extent that is required by the business, and not meaning forever; there is a fixed place which are the vessels in the High Seas in a definite and composite geographical area, and from which its business of survey in connection with exploration is carried out; and lastly this place is at the disposal of the Applicant.

- The Authority referred to **Klaus Vogel's Commentary on Double Taxation Conventions, Third Edition (para 44, pg 294)** to conclude that whenever two States wanted clarity with regard to taxability of income arising from activities in connection with exploration of mineral oil, subject to a duration clause, they would incorporate a specific clause to that effect. And thus, since UAE DTAA has no such mention with regard to activities in connection with exploration or connected activities, it is clear that there is no specific provision in paragraph 2 of Article 5 of the India UAE DTAA, either mentioned or intended, that could cover the services carried out by the Applicant in connection with exploration of mineral oil. *Thus, the Authority held that there is no scope for getting into the debate of interplay between paras 1 and 2 of Article 5 of the India UAE DTAA, or to resolve any conflict therein, since the services rendered by the Applicant are not covered by any of the sub paras of para 2 of Article 5 or any other para.*

- It was therefore concluded that the Applicant has a fixed place PE in India, as per para 1 of Article 5, in the form of its vessels used in connection with the exploration of mineral oil/ natural resources under agreement with the ONGC.

- Lastly, regarding Question (iv), the Authority held that since the activities of the Applicant are in connection with exploration of mineral oils, the special provisions of section 44BB apply, and the income of the Applicant would be computed as laid out therein.

NANGIA'S TAKE

- ***In this ruling, the Hon'ble AAR has adopted a narrow interpretation of Service PE clause in a tax treaty and held that in case of Service PE, only those services will be covered, which are essentially personal services rendered through employees/ other personnel. In respect of services such as seismic data acquisition, processing and interpretation in the Mumbai High Field, which involve rendering of services through vessels/ various equipment mounted thereon and not merely personal services, the AAR has taken a view that for such activity, specific clauses involving oil & gas exploration services or installation/ structure used for exploration or extraction of natural resources could be applicable and not the Service PE clause.***

- ***The Ruling also puts emphasis that if a particular Treaty does not contain specific PE clause similar to activity being performed by a Taxpayer, then determination of PE may have to be governed by the general Paragraph 1 of Article 5 and therefore re-emphasizes the principle that, any determination of PE or taxability of any particular income would depend on specific provisions of relevant tax treaty instead of general perceptions/ provisions and taxpayers need to be careful about selecting their tax positions.***

INTERNATIONAL TAX UPDATES

3. India, Finland settle Nokia tax row

India and Finland have reached an accord on the tax dispute with Nokia under the Mutual Agreement Procedure (MAP), clearing the way for the sale of the company's Chennai plant, which has been idle for more than three years, officials said. This involves a payment of Rs 1,600 crore, a sum that was deposited with the government by Nokia in March.

The resolution covers disputes pertaining to Nokia India as well as Nokia Corp., said the officials.

Under MAP, settling a case with the other government essentially means closing all pending proceedings related to a tax matter. It is increasingly seen as the preferred mode for settling cross-border disputes.The resolution brings to an end one of the biggest tax disputes involving multinational companies. This, along with the Vodafone and Shell tax cases, had been identified with the aggressive stance of the tax department. "Resolution has been reached… Nokia has agreed to make provisional tax payment," a senior income tax department official told ET.

Source: https://economictimes.indiatimes.com/news/company/corporate-trends/india-finland-settle-nokia-tax-row/articleshow/63838851.cms

4. UK Revisits Proposed BEPS Changes To Its Double Tax Treaties

The UK tax agency, HM Revenue and Customs, on April 16, 2018, released proposed changes to the list of amendments it intends to make to its bilateral double tax avoidance agreements through the OECD's base erosion and profit shifting multilateral instrument.

The new document – Proposed changes to the provisional list of UK reservations and notifications under the MLI as made at signature – updates the UK's proposed policy set out when it first signed the MLI.

The BEPS MLI, developed through negotiations involving more than 100 countries and jurisdictions as part of the OECD's BEPS project, is intended to enable countries to incorporate BEPS-related amendments into their tax treaties without having to renegotiate bilateral treaties on a piecemeal basis. It is due to enter into force on July 1, 2018.

Source: https://www.tax-news.com/news/UK_Revisits_Proposed_BEPS_Changes_To_Its_Double_Tax_Treaties_76733.html

5. Looming Flipkart Tax Ruling on Discounts Creates 'Panic' in India

A pending tax court ruling could stymie foreign companies trying to enter or advance in the Indian marketplace by offering steep discounts on consumer goods—a common practice among e-commerce companies.

Flipkart India Pvt. Ltd., an India-based online retailer, is awaiting a decision from the Bangalore Income Tax Appellate Tribunal on whether losses incurred from discounting are taxable as a capital expenditure or deductible as a revenue expenditure.

The company is currently fighting the $16.8 million tax bill on the grounds that marketing expenses drive sales and should be deductible as a revenue expense.

Source: https://www.bna.com/looming-flipkart-tax-n57982091269/

6. German Industry Cautions Against EU Digital Tax

The Federal Association of German Industry (BDI) has said that proposals for a tax on digital companies will be detrimental to the European economy and exacerbate trade tensions between Europe and the United States.

In comments published on the association's website, BDI Chief Executive Joachim Lang called for an "internationally coordinated approach" to the taxation of the digital economy, rather than short-term unilateral solutions that will increase the tax burden on companies investing in digitization.

"Our companies are increasingly pursuing digital business models and are therefore also affected by the EU digital tax. As they digitize their products and processes, they face additional tax burdens. An EU digital tax is detrimental to the industry," Lang said.

"The proposal for an EU digital tax comes at an inopportune time because it exacerbates transatlantic tensions. The European Commission is risking to intensify the trade conflict with the US. The expense and income of the planned tax are disproportionate. Instead of short-term interim solutions at EU level, we believe that an internationally coordinated approach is necessary," Lang added.

Source: https://www.tax-news.com/news/German_Industry_Cautions_Against_EU_Digital_Tax____76728.html

TRANSFER PRICING

7. Delhi ITAT holds CBDT Instruction No. 3/2003, quashes TPO reference on international transaction <5 cr

Facts of the case

Calance Software Pvt. Ltd. ("the taxpayer") engaged in providing software development and manpower placing services. During the assessment year ("AY") 2006-07, the taxpayer provides software development service to its Associated Enterprises ("AE") amounting to Rs. 2.15 Crores and benchmarked the transaction using CUP method. Subsequently, the Assessing Officer("AO") made reference to the Transfer Pricing Officer ("TPO") for determining the arm's length price ("ALP") of the international transactions under section 92CA of the Income Tax Act, 1961. However, TPO determined the ALP of the international transaction by applying TNMM and held that no benefit of the amended proviso to section 92C(2) was available to the taxpayer since the difference between ALP and value of international transaction is more the 5% of the international transaction.

Thereon, the aggrieved taxpayer filed the objection before DRP against the draft AO order. The DRP upheld the TPO's findings in the instant case.

Being aggrieved by the DRP directions and final AO order, the taxpayer filed an appeal before Delhi Income Tax Appellate Tribunal ("ITAT"). The taxpayer filed an additional legal ground and submitted that the reference made to the TPO was bad in law as AO had not taken any approval from commissioner and the quantum of the international transaction was below Rs. 5 crores. For this purpose taxpayer placed reliance on CBDT instruction No. 3/2003, which provides that only cases where quantum of the international transaction was above Rs. 5 crores should be referred to the TPO. The taxpayer also relied upon the Instruction No. 3 of 2016 wherein it was categorically mentioned that all references made to TPO, which were not in consonance with the instruction of Board, should be withdrawn. Also, in support of its contention, the Taxpayer relied on jurisdictional HC ruling in **SPL's Siddhartha Ltd** and ITAT Special Bench ruling in **Aztec Software & Technology Services Ltd.**

Further, the taxpayer also submitted that the TPO has wrongly applied the TNMM method as it was a settled position of law that when internal CUP was available the no other method is preferred by placing reliance on OECD Guidelines and decision of ITAT in **Inter Garden** (Bangalore).
On the Other hand, Revenue submitted that the circular/ instruction was directive in nature and not mandatory and therefore, additional grounds should be dismissed.

Proceedings before ITAT

ITAT'S Ruling

ITAT accepted the taxpayer's contention that as per Instruction No. 3/2003 issued by the CBDT, the AO should have decided the issue of international transaction himself instead of referring the case to the

TPO as the quantum of the international transaction was below Rs. 5 crores.

ITAT noted that the Hon'ble Supreme Court in the case of UCO Bank held that the *'Circulars can be adverse to the IT Department but still are binding on the authorities of the Income Tax Departments but cannot be binding on the taxpayer if they are adverse to the taxpayer'*. ITAT further relied on the case of **Aztec Software & Technology Service Ltd** which reiterates that the CBDT directions are mandatory and binding on the AO and CIT.

ITAT also places reliance on the Jurisdictional HC in the case of ***SPL's Siddhartha Ltd.*** wherein it was held that the *"It is trite that when a statue requires, a thing to be done in a certain manner, it shall be done in that manner alone and the court would not expect its being done in some other manner".*

Thus, ITAT allowed additional ground in the favour of the taxpayer.

NANGIA'S TAKE

The verdict in the instant case reiterates that revenue department is bound to follow any circular / instructions that are mandatory and has binding force on the authorities of income tax department. Thus, the above judicial pronouncement by ITAT coupled with CBDT's new Instruction No 3/2016 which provides for risk based selection of cases for TP audits and restriction on the arbitrary powers used by the AO will certainly helps to streamline the TP audit process in India. As a result, this will curtail the number of cases being selected for scrutiny by the TPO and hence reducing mammoth TP assessments/ litigations.

Source: Calance Software Private Limited [TS- 196-ITAT-2018(DEL)-TP]

8. HC upheld ITAT's order, allowing overhead expense allocation by JV partners to taxpayer

Facts of the case

International Metro Civil Contractors ("the taxpayer"), a joint venture ("JV") of 5 parties, was formed for executing a contract for Delhi Metro Rail Corporation. During the Assessment Year ("AY") 2005-06, the Transfer Pricing Officer ("TPO") upon examination of the Agreement entered into between the taxpayer and the JV, noted that the agreement permitted the JV partners to allocate their head office expenses to the extent of 8.5% of turnover of the taxpayer, in their profit sharing ratio.

Further, in this regard, the TPO disallowed the allocation of the head office expenses by the JV partners on the ground that 85% of the job was sub-contracted on back to back basis and other direct expenses were debited in the books of the taxpayer. Thus, basis the same, the TPO made an upward addition in the income of the taxpayer.

Aggrieved by the same, the taxpayer filed an appeal before the Commissioner of Income Tax Appeals [CIT(A)].

The CIT(A) post inspecting the facts of the instant case, set aside the order of TPO by noting that the TPO had not furnished substantial findings on record to indicate that debiting of overhead expenses were excessive on the basis of comparables, i.e. no benchmarking of the expenses.

Aggrieved, the Revenue filed an appeal before the Income Tax Appellate Tribunal ("ITAT").

ITAT Ruling

ITAT opined that the issue pressed by the TPO is basically one of finding of facts and the TPO failed to show that the same are perverse in any manner. Further, the ITAT observed that the TPO was not correct in stating that the taxpayer has not furnished details in support of 8.5% allocation of overhead office expenses. In this relation, the ITAT placed reliance on the Certificate of Auditors of JV partners indicating its overhead charges and the Agreement entered into between the taxpayer and the JV partners wherein the said percentage was clearly mentioned.

In addition to the above, the ITAT also noted, basis the similar facts of the instant case, the TPO did not challenge the claim of overhead expenses in the earlier AYs. After considering these facts, ITAT confirmed deletion of adjustment.

Being aggrieved by the ITAT order, the Revenue filed an appeal before Bombay High Court ("HC").

The HC's Ruling

HC noted that the issue urged by the Revenue was essentially one of findings of the facts on which both the CIT(A) and the Tribunal had upheld the taxpayer's stand. HC also observed that the Revenue had failed to show that the finding of the fact was perverse in any manner.
Further, HC also noted that Tribunal had upheld the CIT(A)'s order on the fact for the subject AY, as there was no justification for enhancement the ALP by disallowing allocation of overhead expenses of the JV partners to the taxpayer.

Accordingly, the HC held that, "no substantial question of law arises for our consideration".

NANGIA'S TAKE

The verdict in the instant case highlights the fact that back-up documentation, including comprehensive agreement serves as a vigorous defense mechanism before the tax authorities. Further, it also reiterates that burden of proof shifts to the tax department if the taxpayer presents reasonable arguments and provides sufficient evidence that its transactions are at arm's length. Accordingly, in order to prove that taxpayer's transactions are not at arm's length, the AO/TPO will have to follow the statutory provisions to determine ALP including methodical and detailed benchmarking analysis in compliance with the guidelines provided for in the Act and the Rules.

Source: Pr. CIT vs. International Metro Civil Contractors [TS-175-HC-2018(BOM)-TP]

9. ITAT directs separate benchmarking for consultancy services and explains mechanism of capacity adjustment

Facts of the case

Daikin Airconditioning India Pvt. Ltd. ["the taxpayer"], a subsidiary of Daikin Japan, is engaged in the business of import and sale of all types of refrigeration equipments and accessories. During the Assessment Year ("AY") 2009-10, Transfer Pricing Office ("TPO") made an upward adjustment of INR 18.19 Cr. on account of Advertising, Marketing and promotion *("AMP")* expenses incurred by the taxpayer. Aggrieved by the same, taxpayer approached Dispute Resolution Panel ("DRP"), and post his directions, TPO reduced the adjustment to INR 5.58 Cr. During the AY 2009-10, the taxpayer capitalized the "consultancy fees" relating to setting up of manufacturing unit and aggregated the International transaction ("IT") of 'Payment of consultancy fee and training services' with the IT under manufacturing segment and benchmarked the same using Transactional Net Margin Method ("TNMM") as the most appropriate method ("MAM").

The TPO rejected the aggregation approach adopted by the taxpayer on the ground that taxpayer had not undertaken any manufacturing activity during the AY 2009-10 and benchmarked the aforesaid transaction by using Comparable Uncontrolled Method ("CUP") as the MAM and determined the ALP at NIL, post considering payment of consultancy charges as a separate transaction and thereby made a TP adjustment of INR 7.94 crore.

Further, the taxpayer claimed 'idle capacity adjustment' in the manufacturing segment. The TPO rejected the same on account of absence of any reliable data and lack of uniformity in computing the percentage of capacity utilization.

Aggrieved, the taxpayer filed an appeal before Delhi Income Tax Appellate Tribunal ("ITAT").

Proceedings before ITAT
ITAT's Ruling

❖ **Taxpayer's Plea with respect to AMP expenses**

The ITAT relied on the findings in the taxpayer's own case of AY 2006-07 to 2008-09, held that selling expenses should not be considered within the ambit of AMP expenses and restored the case back to the AO/TPO for taking fresh decision following earlier years.

❖ **Taxpayer's Plea on account of capitalizing consultancy fees**

ITAT rejects taxpayer's approach of aggregating the transaction of 'payment of consultancy fees' with manufacturing activity for AY 2009-10 and AY 2010-11 due to absence of close connection between the two transactions and further relying on the ruling in ***Gruner India Pvt. Ltd. [TS-202-ITAT-2016(DEL)-TP]*** *approved TPO's segregation.*

Additionally, the TPO's act of determining ALP at Nil on account of stating that no benefit was received by the taxpayer from these services is contrary to the ruling of ***Delhi High Court in Cushman & Wakefield India Pvt. Ltd***, thus remits matter to AO/TPO to follow directions in Cushman & Wakefield ruling after giving reasonable opportunity of being heard to taxpayer.

❖ **Taxpayers plea regarding acceptance of capacity adjustment in manufacturing segment**

Regarding Taxpayer's claim for grant of capacity under-utilization adjustment in manufacturing segment for AY 2010-11, ITAT explains step by step mechanism for computing capacity under-utilization adjustment.

Further, due to absence of financials of comparables, the computation of adjustment is remitted to AO/TPO with a direction that the adjustment should be computed with respect to "Installed Capacity" and not "Licensed Capacity".

NANGIA'S TAKE

The verdict in the instant case reiterates the fact that Aggregation of transactions or 'blended Transaction approach' is a wide-spread exercise for benchmarking the transactions when the transactions are closely interlinked. Further, Capacity under-utilization by enterprises is a factor affecting net profit margin because lower capacity utilization results in higher per unit costs, which, in turn, results in lower profits at a transactional or unit level. Accordingly, there is no doubt regarding the need for aforesaid adjustments, however the issue is about the reasonable accuracy in the mechanism for such adjustments; so long as a reasonable adjustment mechanism can be employed, objections to the adjustment by the tax authorities won't sustain.

Source: Daikin Airconditioning India Pvt. Ltd. *[TS-176-ITAT-2018(DEL)-TP]*

GST

10. No IGST on overseas trading absent importation of goods into India

Facts of the case

Applicant is in the business of trading in spices and spice products. Applicant has two modes of transactions. In the first kind, the applicant receives order from a customer in USA for the supply of spice products. Applicant will place a corresponding order to a supplier in China for supplying the goods ordered by the customer in USA. The supplier in China, based on the request of the applicant, ship the goods directly to the customer in USA. In other words, the goods do not come to India. The Chinese supplier issues invoice to the applicant, for which, payment will be made by the applicant in due course. Subsequently, the applicant will raise invoice on the customer in USA, and collect the proceeds.

PROVIDED AND ANALYSIS

- As per Section 2(10) of the Integrated Goods and Services Tax ('IGST') Act, "import of goods" means bringing goods into India from a place outside India;

- As per Section 7(2) of the IGST Act, supply of goods imported into the territory of India, till they cross the customs frontiers of India, shall be treated to be a supply of goods in the course of inter-state trade or commerce;

- As per Section 5(1) of the IGST Act, there shall be levied a tax called the IGST in all inter-state supplies of goods or services or both, except on the supply of alcoholic liquor for human consumption, on the value determined under Section 15 of the Central Goods and Services Tax Act, and at such rates, not exceeding forty percent, as may be notified by the Government on the recommendations of the Council and collected in such manner as may be prescribed and shall be paid by the taxable person;

- Provided that the integrated tax on goods imported into India shall be levied and collected in accordance with the provisions of Section 3 of the Customs Tariff Act, 1975, on the value determined under the said Act at the point when duties of customs are levied on the said goods under Section 12 of the Customs Act, 1962.

- The Customs Tariff Act, 1975 was amended by The Taxation Laws Amendment Act, 2017 by introducing sub-section (7) in Section 3 of the Customs Tariff Act, 1975 with effect from 01.07.2017 to enable collection of IGST on the goods imported.

- From a combined reading of the above provisions of the IGST Act, 2017, the Customs Tariff Act, 1975, and the Customs Act, 1962, it is evident that IGST on goods imported into India shall be levied and collected at the point when duties of customs are levied on the said goods under Section 12 of the Customs Act, 1962 i.e. on the date determined as per provisions of Section 15 of the Customs Act, 1962.

- When a question regarding the leviability of IGST on High Sea Sales of imported goods and point of collection thereof was raised before the Central Board of Excise and Customs [CBEC], the CBEC by *Circular No. 33/2017-Customs* dated 01.08.2017 had clarified that IGST on high sea sale(s) transactions of imported goods, whether one or multiple, shall be levied and collected only at the time of importation i.e. when the import declarations are filed before the Customs authorities for the customs clearance purposes for the first time. Further, value addition accruing in each such high sea sale shall form part of the value on which IGST is collected at the time of clearance.

- The clarification given by the CBEC in the above Circular regarding the leviability of IGST and the point of collection thereof in respect of high sea sales of imported goods is, mutatis mutandis, applicable in the case of the applicant.

RULING

The ruling delivered by Shri. Senthil Nathan S (Member, CGST) and Shri. N. Thulaseedharan Pillai (Member, SGST) ruled out that the goods are liable to IGST when they are imported into India and the IGST is payable at the time of importation of goods into India. The applicant is neither liable to GST on the sale of goods procured from China and directly supplied to USA nor on the sale of goods stored in the warehouse in Netherlands, after being procured from China, to customers, in and around Netherlands, as the goods are not imported into India at any point.

NANGIA'S TAKE

Presently, there is ambiguity regarding the taxability of the transactions wherein the assessee located in India purchases goods from an overseas vendor and goods are shipped directly from overseas vendor to overseas customer i.e. goods are supplied without entering into the territory of India. With the present Advance Ruling, applicant is neither liable to pay IGST on the sale of goods procured from overseas vendor, nor on sale of goods directly shipped to overseas customers without goods being imported into India at any point. It should be noted that an advance ruling pronounced by AAR shall be binding only on the applicant who has sought the advance ruling and on the concerned officer/jurisdictional officer in respect of the applicant. However, principles discussed in the said ruling may be referred in other cases as well.

-

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