Tax News

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INCOME TAX

Reminder For April '11

Action Due	Due Date
TDS for March 2011 (*) see note	**30-04-11**
PF for the month of Mar 2011	15-04-11
ESI for the month of Mar 2011	21-04-11
Issue of Form no.16/16A as the case may be	30-04-11

(*) Inadvertently, the due date was mentioned as 07-04-2011 in the Tax News Briefings circulated on April 4. Apologies for the error.

SERVICE TAX

Action Due	Due Date
Service tax return for 2nd half (Oct-Mar)	25-04-2011

INCOME TAX

Vital Notifications / Changes

No circular to be reported in this edition.

Supreme Court / High Court Judgments

Income deemed to accrue or arise in India (India UK Treaty): It was held by the Court that consideration paid by the assessee for transfer of drawings, designs, etc., by an English company, to the assessee, outside India, did not constitute royalty under Article 13 of the DTAA.

Since the definition of royalty in DTAA has a limited scope, the remittances in this case could not be construed as royalties, but could only constitute business profits of the assessee. Consequently, tax at source could not have been deducted against these remittances. In the absence of having a permanent establishment in India, the business profits could also not be taxed in India. *D.C.M. Limited vs. CIT, (2011) 10 taxmann.com 124 (Delhi).*

TDS in case of payment to head office abroad by an Indian Branch: Assessee, a Netherlands based banking company, was having its principal Branch in India. In course of its banking activities, the branch in India remitted substantial funds to its head office as payment of interest. The assessee claimed that for purpose of computation of expenditure, branch and head office were to be taken as separate entities, but for purpose of TDS on interest payment, it was to be taken as one entity and no deduction of tax was to be made.

It was held that by virtue of article 5 read with article 7 of DTAA, permanent establishment and head office were to be taken as separate entities for all purposes, and therefore, neither can permanent establishment nor branch or head office, be treated as one entity for TDS purpose u/s 195(1). It was also held that in order to attract section 195(1), remittance of interest must result in an income which is chargeable under the Act. Since, by virtue of DTAA between India and Netherlands, assessee's head office was not liable to pay any tax under the Act, so there was no obligation on part of assessee's Indian branch to deduct tax while making interest remittance to its head office or to any other foreign branch. *ABN Amro Bank, N.V. v. CIT, [2011] 10 taxmann.com 89 (Cal.)*

Tribunal Judgments

Business disallowance not applicable for salary paid outside India: Since the salary paid to non-residents for services rendered in Netherland, is not chargeable to tax in India, provisions of section 40(*a*)(*iii*) will not be applicable. Accordingly, disallowance under section 40(*a*)(*iii*) cannot be made in respect of salary paid to non-residents for the services rendered abroad. *Mother Dairy Fruits & Veg. (P.) Ltd (2011) 10 taxmann.com 131 (Delhi - ITAT).*

Deduction of tax from fees for technical services: It was held that nature of payment made by assessee to the New Zealand based company was for liaisioning and coordinating to ensure

that blood samples collected by the assessee were properly received at US, and reports were received in time and as per terms fixed by the US Embassy. These services could not be termed as managerial, technical or consultancy service, so the payment did not fall within the term 'fee for technical services', under section 195 of the Income-tax Act. *MRO (India) (P.) Ltd. [2011] 10 taxmann.com 123 (Delhi - ITAT)*

Deductibility of expenditure incurred on scientific research: Where assessee incurred expenditure on building, plant and machinery, and claimed deduction of 100 % on such expenditure u/s 35(1)(iv), there was no justification for denial of claim by referring to the provisions of section 35(2AB). *Shree Pacetronics Ltd. - [2011] 10 taxmann.com 118 (Indore - ITAT)*

Double Taxation Relief, where no agreement exists: An assessee is entitled to tax credits in respect of taxes paid in USA & Canada as envisaged by section 91, even though the assessee is covered by the scope of India US and India Canada Tax Treaties. The fact that a taxpayer is entitled to make a particular claim, in accordance with a tax treaty provisions, does not disentitle him to make the claim in accordance with the provisions of the Act. The provisions of section 91 are to be treated as general in application and these provisions can yield to the treaty provisions only to the extent the provisions of the treaty are beneficial to the assessee. *[2011] 10 taxmann.com 87 (Mum. - ITAT)*.

Section 10A: It was held that there should be parity between export turnover and total turnover and therefore the leased line charges, which were attributable for export of software and excluded from the export turnover, should also be excluded from the total turnover. Also, where the assessee had obtained approval from RBI for the unrealised amount within the stipulated period, that was realised subsequently, the amount cannot be excluded while computing the deduction u/s 10A. *M/S Cepha Imaging (P) Ltd vs ITO Bangalore, 2011-TIOL-140-ITAT-BANG.*

Sale of a going concern: The Tribunal held that a business undertaking as a going concern includes all variety of elements, both tangible and intangible. It includes rights, assets, contingent or definite, corporeal and incorporeal, and all interest in advantage, present or future. It also includes the management, executive employees and anything which goes as part of organization including the potential of the organization to grow. A going concern is essentially a functioning living organism and it would not be possible to conceptualize the cost of acquisition of such a going concern as well as its date of acquisition. If the cost of acquisition and/or the date of acquisition of the asset cannot be determined, then it cannot be brought within the purview of section 45 for levy and computation of capital gains. Hence in this case consideration realized by the assessee would be outside the purview of capital gains under sec. 45, and so no capital gains tax can be levied. *2011-TIOL-197-ITAT-MUM.*

Transfer Pricing: The assessee, a courier company, paid a substantial sum to its holding company in Netherlands towards the reimbursement of transport cost of consignments. The Transfer Pricing Officer & Commissioner of Income Tax (A) adopted the TNMM method, and claimed that as the operating profit /operating income of the comparables was higher than that earned by the assessee, an adjustment had to be made. It was also claimed that the assessee was not entitled to rely on the data of prior years, while computing ALP for FY 2001-02. On appeal to the Tribunal, it was held that:

a) For computing ALP, the assessee should use the relevant data available at the time of filing of the return. The argument that at the time of doing the Transfer Pricing study the relevant data for FY 2001-02 was not available is not acceptable. If the relevant data was available by the time the return was filed, it should have been used. Further, prior year data was relevant only if the assessee was able to prove that the pricing pattern of the assessee for the relevant FY had been influenced by the market conditions/product life cycle of the prior years (which was not true for the courier business).

b) For arriving at the net margin of operating income, only operating income and

operating expenses for the relevant business activity of the assessee are to be taken into consideration. Other income, such as dividend income, profit on sale of assets, donations etc. which are included in the operating incomes of other comparable companies should be excluded. Working capital adjustments also have to be considered while arriving at the operating net margins. Non-operating income & expenditure should be excluded while comparing.

c) The assessee is entitled to a standard deduction of 5% as provided under proviso to sec. 92C (2) before making adjustments of the transfer price. *Schefenacker TNT India Pvt. Ltd. V. ACIT (ITAT Bang).*

Taxability of amount received on transfer of IPRs : This case highlights that (1) consideration received for transfer of Intellectual Property (business secrets, process documents etc.), can be considered as long term capital gain, provided it can be established that this IP had been accumulated over a long period of time. (2) Valuation report prepared prior to entering into a business transfer agreement, can be considered as sufficient evidence to establish the amount of non-compete fee included in the total consideration, even if such amount is not explicitly mentioned in the business transfer agreement. (3) Non-compete fee is a capital receipt and hence non-taxable. *M/s DINESH PLATECHEM LTD.*

SERVICE TAX

Vital Notification / Changes

No circular to be reported in this edition.

SC/HC Judgments

Statutory Apellate remedy vs Writ petition: When interpretation of a clause is in doubt, and not its constitutional validity, petitioners should invoke statutory appellate remedy before the Tribunal and not the writ jurisdiction of this Court. Resorting to writ proceedings is disapproved, unless violation of a statutory enactment is involved, or there is complete lack of inherent jurisdiction, or the authorities seem to have acted in a malafide manner with ulterior motives. *[2011] 10 taxmann.com 56 (DELHI)*.

Principal laid down by the Court for stay or waiver of pre deposit: It was held by the Court that the following principles are to be kept in mind by the Tribunal while considering the applications for stay or waiver of pre-deposit under Section 35F of the Act:

1) The applications for stay should not be disposed of in a routine manner unmindful of the consequences flowing from the order requiring the assessee to deposit full or part of the demand;

2) Three aspects to be focused while dealing with the applications for dispensing of pre-deposit are: (a) prima facie case, (b) balance of convenience, and (c) irreparable loss;

3) Interim orders ought not to be granted merely because a prima facie case has been shown;

4) The balance of convenience must be clearly in favour of making of an interim order and there should not be the slightest indication of a likelihood of prejudice to the interest of public revenue;

5) While dealing with the applications twin requirements of consideration i.e., consideration of undue hardship, and imposition of conditions to safeguard the interests of revenue have to be kept in view;

6) When the Tribunal decides to grant full or partial stay, it has to impose such conditions as may be necessary to safeguard the interests of the revenue. This is an imperative requirement; and

7) An appellate Tribunal, being a creature of the statute, cannot ignore the statutory guidance while exercising general powers or expressly conferred incidental powers. The High Court held that the stay order in the present case, when tested in the background of the above principles, did not suffer from any error. *2011-TIOL-173-HC-AP-ST in Service Tax.*

CESTAT Judgments

Taxability of letting out of vacant land: It was held that letting out vacant land is not covered under 'Renting of Immovable Property Service'. Also, operation and maintenance of a mud plant is not covered under 'Maintenance & Repair Service'. *2011-TIOL-381-CESTAT- BANG.*

Taxability of Banking and Other Financial Services: The assessee was engaged in the manufacture of motor vehicle parts, steel parts, steel forgings, etc. It availed Cenvat credit on service tax paid on payment made to M/s P L Advisory Services Pvt. Ltd. for advisory and financial services in connection with the private placement of its preferential equity shares. It was held by the Tribunal that the services received by the assessee in respect of its private placement of preferential shares for raising the capital is an activity related to the business and hence, eligible for Cenvat credit as per the definition of input service given in the Cenvat Credit Rules, 2004. Merely because the invoice has been raised on the head office, the credit cannot be denied to the factory of the assessee in the present case. *2011-TIOL-402-CESTAT-MUM in Service Tax.*

Exporting goods through the merchant exporter: The assessee was engaged in manufacture of DOC (Soya Extraction Meal) and it was being exported through merchant exporter. During the course of export, the merchant exporter availed certain taxable services. There was an agreement between the assessee and the merchant-exporter which inter alia provided for payment of service tax by the assessee in respect of the above services availed by the merchant-exporter.

Subsequent to such export, the assessee filed refund claims for refund of service tax paid on the specified services used for export of the goods by the merchant exporter under Notification no. 41/2007-Service Tax dated 6.10.2007. The same were rejected by the original adjudicating authority on the ground that the refund claims were filed by the manufacturer and not by the merchant exporter.

It was held by the Tribunal that the service was to be received by an exporter and was to be used for export of goods. The said Notification allowed the exporter, whether manufacturer or merchant exporter, to claim the refund of the service tax paid on the services availed for exporting the goods. No other person can claim the refund of the service tax paid on the services availed by the exporter for exporting the goods. Hence, relying on the decision laid down by the High Court of H.P. in the case of Indian Overseas Corporation, Tribunal also gave the view that the exemption Notification no. 41/2007 is available only to the exporter not to the manufacturer. *2011-TIOL-362-CESTAT-MUM in Service Tax.*

Taxability of consumption of service in India: Assessee, a US company, entered into an agreement with IOCL, Vadodara for designing, constructing, operating, maintaining, repairing, re-constructing of unit for the commercial practice of Fluidized Catalytic Cracking (FCC). The said agreement had 3 parts i.e. Licence Agreement, Engineering Agreement, Guarantee Agreement.

In terms of Licence Agreement, certain technical know-how and patent rights relating to RFCC unit and EDV technology were licenced to IOCL. The technical information and patents were solely meant to be used by IOCL for the purpose of designing, constructing, operating, maintaining and repairing and re-constructing a RFCC / FGS units at Gujarat Refinery using the EDV technology. In lieu, assessee was paid royalty as detailed in the agreement.

In terms of Engineering Agreement, the assessee provided certain engineering design, specifications and related services pertaining to RFCCU and EDV technology. Under this agreement, the assessee was to prepare, process, design and provide basic engineering designs and deliver copies of the same to IOCL, which were to be used by them and their engineering contractors for the purpose of preparation of detailed designs and perform detailed engineering, procurement, construction, operation, maintenance and re-construction of the unit.

The Tribunal found that it was the case where designs, technical know-how etc which were admittedly prepared by the assessee in Boston, stood transferred by them to IOCL. The Commissioner, in his order, had specifically observed that the services rendered by the assessee in USA had been consumed in India. In that case, it could be concluded that the services were not rendered in India. The consumption of service in India was not a taxable event. The taxable event had not occurred in India, inasmuch as the activity of development of technology,

technical information & know-how, transfer of design, drawing etc had taken place in USA. The consumption of such services in India, when admittedly no such service was provided by the assessee in India, cannot be held to be a taxable event. *2011-TIOL-330-CESTAT-MUM in Service Tax.*

Mandap Keeper's Services: A 'members club' is not covered by Finance Act, 1994, for imposition of service tax, for letting the use of its space as "mandap" to its members. If the club space is allowed to be occupied by any member or his family members or by his guest, for a function, by constructing a mandap", the club cannot be called as "mandap keeper" because the club is allowing its own member to do so, who is, by virtue of his position, a principal of the club. *[2011] 9 taxmann.com 313 (GUJ.)*

Cenvat Credit - The contention of the revenue that refund of Cenvat credit should have been taken in the same months in which export has taken place was not correct because there will be a time lag between the date of availment of credit of service tax paid on inputs service and the claim for refund of the same. Also, the Board has prescribed a time limit of one year for filing refund claim and the refund is to be filed on quarterly basis. - [2011] 9 taxmann.com 320 (Bang. - CESTAT)

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