CORPORATE UPDATE

12/2018

DIRECT TAX

INTERNATIONAL TAXATION

I. Tax treaty between India and Hong Kong enters into force

Notification No. 89/2018 dated December 21, 2018

The tax treaty between Hong Kong and India which was signed in March 2018 has now entered into force on November 30, 2018.

The treaty shall become effective from the financial year 2019-20 onwards. The treaty was notified by the Central Board of Direct Taxes (CBDT) on December 21, 2018.

Key highlights of this tax treaty is available in the March 2018 edition of our Corporate Update.

II. Protocol signed to amend India-China tax treaty

PIB Press Release dated November 26, 2018

India and China have signed a protocol on 26 November, 2018 to amend the tax treaty.

In terms of the Protocol, existing provisions relating to residency, exchange of information, dependent agent permanent establishment (PE), installation PE, etc. have been amended and new article relating to entitlement of benefits have been inserted, in line with the proposal of the Organisation for Economic Co-operation and Development ('OECD') in their Action Plan Reports under the Base Erosion & Profit shifting (BEPS) initiative.

The amended treaty shall enter into force after required procedures by both the countries have been completed. The same shall become effective in India from financial year beginning April 01 following the date on which the tax treaty enters into force.

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III. Mauritius Revenue Authority issues place of effective management guidelines

Statement of Practice (SP 17/18) of Mauritius Revenue Authority dated November 28, 2018

The Mauritius Revenue Authority (MRA) has amended its domestic tax residency provisions to incorporate place of effective management (POEM) concept in compliance with BEPS initiative.

A new section has been inserted which provides that a company incorporated in Mauritius shall be treated as non-resident if its POEM is situated outside Mauritius.

Furthermore, in determining the POEM, all the relevant facts and circumstances must be examined, such factors shall relate to the business activities of the company, including the use of information and communication technologies in the decision making process. The new section further lays down that generally, a company shall be deemed to have its POEM in Mauritius if:

(a) the strategic decisions relating to the company's core income generating activities are taken in, or from, Mauritius; and
(b) any one of the following conditions is met:
i. The majority of the Board of directors' meetings are held in Mauritius; or
ii. The executive management of the company is regularly exercised in Mauritius.

Resultantly, a company incorporated in Mauritius would now need to demonstrate that its POEM lies in Mauritius. In 2016, India-Mauritius tax treaty was amended to provide that capital gains from transfer of shares acquired on or after April 01, 2017 shall be taxable in India at 50% of the tax rate, subject to the provision of the Limitation of Benefit clause. Shares acquired on or after April 01, 2017 and sold on or after April 01, 2019 shall be liable to capital gain tax at normal rates.

However, it is pertinent to note that investment in shares acquired before April 01, 2017 have been grandfathered.

- Interest Earned on FDRs pledged for promoting business of group companies is Business income rather than income from other sources
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- Sponsorship fee' meeting the commercial expediency test irrespective of the benefit accrued to group companies is an allowable business expenditure

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- Review of the Policy on Foreign Direct Investment (FDI) in e-commerce.
- Foreign Exchange Management (Borrowing and Lending) Regulations, 2018

Also taxation of capital gains on transfer of capital assets other than shares of an Indian company remains the same. As such, availment of benefit under India-Mauritius tax treaty may be impacted by the introduction of POEM guidelines under the Mauritius domestic tax law.

IV. 'Grouting' work falls under 'construction' activity, no permanent establishment where threshold prescribed by treaty not met

ULO Systems LLC [TS-741-Tax Tribunal-2018(DEL)] dated December 26, 2018

Recently, the Tax Tribunal, Delhi bench, held that PE would not be triggered in the hands of UAE entity in India on account of grouting activities as the duration threshold of 9 months as prescribed under Article 5(2)(h) the Indo-UAE DTAA was not met.

On the facts of the case, the Assessee company, a UAE tax resident is engaged in providing grouting and precast solutions for subsea off-shore construction industry. The Assessee contended that grouting activities carried out by it fall within construction activity and no PE was constituted under Article 5(2)(h) of the tax treaty as number of days spent in India was less than 9 months.

However, the Revenue contended that Assessee had a fixed place PE in India under Article 5(1) relying on the decision in the case of Fugro Engineers B.V. (FEBV) wherein it was held that FEBV's case was not covered by Article 5(2)(i) of India-Netherlands tax treaty as it did not carry any installation or structural activity and consequently Article 5(1) would apply. The Revenue further contended that the Assessee had equipment PE in India as its equipment was in India for at least 264 days for execution of grouting work. The Revenue also contended that the Assessee indulged in on-going projects and it could not be said that the stay was less than 9 months.

The Tribunal held as under:

a) There was no bifurcation in respect of simple or complex construction work under Article 5(2)(h). Any further classification by the Revenue would amount to re-writing the treaty. Grouting activity would fall under 'construction activity'. Article 5(2)(h), being a specific provision, would prevail over the general provision of Article 5(1), as per well settled legal principle of *"generalia specialibus non deroganf".*
b) As the number of days stay in India as determined by the Revenue (264 days) is less than the time period mentioned in Article 5(2)(h) i.e. 9 months, no PE was constituted. Furthermore, aggregation of projects to compute duration threshold for PE purposes is not permitted under the Indo-UAE DTAA.
c) The establishment of PE in India ought to be examined with respect to each assessment year and there is no bar in carrying on the activities year after year.
d) The concept of 'Equipment PE' is nowhere mentioned in the India-UAE tax treaty.

In view thereof, the Tribunal concluded that the Assessee did not have a PE in India for the relevant year.

V. Disallowance of expenditure for non-deduction of tax at source not applicable under India-Mauritius tax treaty

Unocol Bharat Ltd. [TS-582-Tax Tribunal-2018(DEL)] dated October 05, 2018

In a recent decision, the Tax Tribunal, Delhi bench held that Article 7(3) of the India-Mauritius tax treaty does not cast any restriction on admissibility of expenses as per the domestic laws

of the Contracting State. As such, no disallowance could be made under Section 40(a)(i) of the Income-Tax Act on account of non-deduction of tax at source.

On the facts of the case, the Assessee is a tax resident of Mauritius and is engaged in identification of potential business opportunities in energy sector in India. During the relevant financial year, the Assessee pursued for contract of various projects in India and had PE in India. The Income-Tax Officer disallowed the employee cost, travel and entertainment expenses and operating contract expenses on two grounds, firstly due to non-furnishing of adequate details/ evidence in support of the expenses and secondly, under section 40(a)(i) on account of non-deduction of tax at source by the Assessee. On appeal, the Commissioner of Income Tax (Appeals) [CIT(A)] held that the expenditure was allowable as the same was incurred for the purpose of the business of PE. The CIT(A) also held that since no restriction has been provided in Article7(3) of India-Mauritius tax treaty for deductibility of expenses, no disallowance could be made under section 40(a)(i) of the Income-Tax Act.

On further appeal, the Tax Tribunal observed that the Assessee had furnished requisite details and as such the contention of the Income-Tax Officer that details were not given was not correct. With regard to disallowance under Section 40(a)(i), the Tribunal noted that there are tax treaties (such as India-US treaty, India-UAE treaty) which specifically provide that deduction of expenses which are incurred for the purpose of business of PE in a Contracting State would be subject to limitation of taxation laws of that State. The Tribunal observed that the phraseology used in India-Mauritius tax treaty under Article 7(3) is different and does not provide for any such restriction. The Tribunal, therefore concluded that if no restriction is provided in the treaty for application of domestic tax laws, then any limitation given under the Income-Tax Act cannot be imported into the treaty. Accordingly, the Tribunal held that no disallowance of expenses could be made under Section 40(a)(i) of the Income-Tax Act.

VI. Reimbursement made to Philippine company not having PE in India not taxable in absence of 'Fees for Technical Services' clause in the tax treaty

IBM India (P.) Ltd [100 taxmann.com 230] dated November 16, 2018

In the instant case, the Tribunal, Bangalore Bench held that salary cost reimbursements made by Indian company to Philippine company were not taxable in India as article relating to 'Fees For Technical Services' (FTS) is absent in India - Philippine tax treaty. The said reimbursements were monies received in the course of business and as Philippine company did not have PE in India, the business profits were not liable to tax in India.

On facts, the Assessee, IBM India (P) Ltd. is an Indian company engaged in the business of selling computers, software, besides rendering software development and IT services. During the relevant AY, the Assessee obtained services of expatriates employees of IBM Philippines for its business work and deducted tax at source (TDS) on salary paid to those employees by IBM Philippines under section 192. The Assessee reimbursed salary cost to IBM Philippines without deducting any taxes as payments remitted were on cost-to-cost basis. The Income-Tax Officer was of the view that Philippine company continued to be the employer of expatriates and therefore sum reimbursed were not salary but FTS taxable in India and therefore, the Assessee ought to have deducted TDS. The Income-Tax Officer consequently passed the order under section 201(1) of the Income-Tax Act. The CIT(A) confirmed the action of the Income-Tax Officer.

Before the Tribunal, the Assessee contended that in absence of FTS clause in the tax treaty, Article 7 (business profits) would be applicable as IBM Philippines provided services in normal course of its business and since IBM Philippines did not have PE in India, the receipts would not be chargeable to tax in India. The alternate contention of the Assessee was that even in case Article 7 was not applicable, the payments would fall under Article 23 (other income) and as such could not be taxed in the source country.

However, the Revenue contended that in absence of FTS clause in the tax treaty, the case would be covered by Article 24(1) (elimination of double taxation) of the tax treaty which provides that the domestic tax law shall apply except where provisions to the contrary are made in the tax treaty. As such, the Revenue contended that payments made by the Assessee would be governed by Section 9(1)(vii) of the Income-Tax Act, which lays down the provisions relating to FTS under the Indian tax law.

The Tribunal noted that Article 23, which is a residuary clause, would become redundant if one were to interpret Article 24(1) as conferring right to tax 'FTS' in accordance with domestic law of a contracting state.

The Tribunal referred to its earlier decision in assessee's own case wherein it was explained that Article 24(1) do not deal with characterization or taxability of income, which is dealt by Article 6-23 of the tax treaty. The Tribunal noted that the purpose of Article 24(1) is to provide that the manner of computation of doubly taxed income would be governed by the provisions of the domestic tax law, if the tax treaty does not specifically provide for the same. The Tribunal also stated that where receipts were in the course of business, the same constituted business income falling within Article 7 of the tax treaty and would not fall under Article 23(1).

In view thereof, the Tribunal held that monies received by IBM Philippines would not be chargeable to tax in India in absence of PE in India.

It may be noted that the Tribunal primarily decided on the premise that FTS clause was absent in the relevant tax treaty. The aspect whether any income element was involved in the transaction of salary cost reimbursements made on cost to cost basis was not specifically dealt with by the Tribunal.

VII. No tax deductible at source on reimbursement of salary costs of seconded employees

AT&T Communication Services (India) Pvt. Ltd. [TS-644-Tax Tribunal-2018(DEL)] dated October 31, 2018

Recently, in the case of AT&T Communication Services (India) Pvt. Ltd., the Tribunal Delhi Bench dealt with the issue of TDS on reimbursement of salary and related costs by the Assessee to its group company in US, AT&T World Personnel Services Inc. (AWPS).

AWPS was engaged in provision of manpower recruitment services and seconded certain employees to Assessee in India. The employees were released from obligations towards AWPS and solely worked under control, direction and supervision of Assessee. The Assessee reimbursed AWPS towards salary and other costs paid by AWPS to expatriates outside India

on behalf of Assessee. The Assessee deducted TDS under section 192 on salary paid to seconded employees and no tax was deducted on reimbursements made to AWPS.

The Tribunal noted that seconded employees were working as employees of Assessee company and their salary was subjected to TDS under section 192 and therefore section 195 was not applicable on reimbursements made by the Assessee to AWPS.

The Tribunal distinguished the decision of Delhi High Court in the case of Centrica India Offshore Pvt. Ltd. Vs. CIT (2014) 364 ITR 336 (Del.) and held that the said decision is not applicable.

The Tribunal observed that in the case of Centrica, the Indian company was established only to provide services to overseas entity to ensure that the services to be rendered to overseas entities by the Indian vendor were properly coordinated. However, in the given case, the seconded employees were not taking forward the business of AWPS in India and could not be said to be rendering services on behalf of AWPS, but were effectively working under the control and supervision of Assessee. Accordingly, the Tribunal held that, on facts, TDS was not applicable on reimbursements made by Assessee to AWPS.

In another decision in the case of DLF Projects Ltd. [TS-689- Tax Tribunal -2018(DEL)], the Tribunal Delhi Bench held that TDS is not applicable on the reimbursements of salary costs of seconded employees by Assessee to Cyprus based company, in respect of which, income element was absent. The Assessee had deducted TDS only on the portion of the invoice relating to 5% mark-up charged on reimbursements by Cyprus company. The Tribunal noted that the Cyprus company only supplied workforce and was not responsible for services performed by seconded employees and tax under Section 192 was deducted while making salary payments to seconded employees. Furthermore, the Tribunal concluded that reimbursement of salary costs could not be characterized as FTS in terms of Article 12 of India-Cyprus tax treaty, as service did not make available any technical knowledge, experience, skills, etc. In view thereof, the Tax Tribunal concluded that Tax was not required to be deducted in respect of reimbursements of salary cost of expatriates.

Ritu Theraja

Sr. Manager – Tax Advisory
Tel.: +91 11 47102272
therajaritu@mpco.in

TRANSFER PRICING

I. Supreme Court upholds the order of High Court - Corporate guarantee commission not comparable to Bank guarantee commission

Glenmark Pharamaceuticals Ltd. [TS-1268-SC-2018-TP]

In the case of Glenmark Pharmaceuticals Ltd., the Tax Tribunal, Mumbai Bench, while dealing with the Transfer Pricing ('TP') adjustment on corporate guarantee commission rejected Tax department's approach of taking commission rate for corporate guarantee at 3%, being the guarantee commission rates charged by the banks, holding that corporate guarantee commission are incomparable with the bank guarantee commission. Against such order of Tax Tribunal, the tax department filed an appeal before Hon'ble High Court of Bombay,

wherein considering the decision in the case of M/s. Everest Kento Cylinders Ltd. [TS-714-Tax Tribunal-2012(MUM)-TP] the appeal of tax department was dismissed and corporate guarantee fee charged by the Assessee at 0.53% and 0.47% was accepted.

Against such High Court order, tax department filed an appeal before Hon'ble Supreme Court, which upheld High Court order confirming the decision of Tax Tribunal that corporate guarantee commission is not comparable to bank guarantee commission.

II. Supreme Court dismissed SLP of tax department against application of RPT filter and exclusion of Wipro Ltd. as comparable due to its brand value

Oracle (OFSS) BPO Services Pvt. Ltd. [TS-1248-SC-2018-TP]

In the case of Oracle (OFSS) BPO Services Pvt. Ltd., the order of Tax Tribunal, Delhi Bench, resulted in deletion of Transfer Pricing ('TP') adjustments made by Dispute Resolution Panel. The Tax Tribunal in its order excluded some comparables applying Related Party Transaction ('RPT') filter of 25% and also excluded M/s. Wipro Ltd. holding the same to be not comparable due to its significant brand presence in the market. The Hon'ble High Court of Delhi, upheld the order of Tax Tribunal holding that the RPT filter is relevant and fits in with the overall scheme of a transfer pricing regulations. It also excluded M/s. Wipro Ltd. as a comparable holding that although two entities maybe in functionally similar, brand does play significant role in the price or cost determination.

Against such High Court order, tax department filed SLP before Hon'ble Supreme Court which was dismissed.

III. High Court allowed writ filed by assessee; Indirect shareholding not to be considered for the purpose of substantial Interest in section 40A(2)(b)

HDFC Bank Ltd. [TS-1299-HC-2018 (Bom)-TP]

In a recent ruling, High Court of Delhi allowed writ petition filed by the Assessee against the order of Income-Tax Officer treating certain transactions as Specified Domestic Transactions ('SDT') and referring the same to TPO, holding the parties with whom alleged SDT have been entered, to be beneficial owner of indirect shareholding in the Assessee and accordingly, held that the provision of section 40A(2)(b) would be applicable, as per which shareholding more than 20% constituted substantial interest.

On the facts of the case, the Assessee, HDFC Bank Ltd. is primarily engaged in the business of banking. During the year under consideration, it entered into certain SDT which were reported in its Form 3CEB. The Assessee, received a show cause notice with regard to non-reporting of following SDTs: a) Loans purchased from HDFC Ltd. and its subsidiaries, b) Services received from HBL Global Private Ltd. ('HBL Global'), and C) Interest paid to HDB Welfare Trust.

The Assessee made submissions before the Income-Tax Officer explaining why such transactions could not be termed as SDT. However, the Income-Tax Officer rejected the submission of the Assessee and reference to TPO was made to determine the ALP of such transactions.

Aggrieved by impugned order of Income-Tax Officer and reference made to TPO, the Assessee filed writ petition before High Court.

The Assessee purchased loan from HDFC Ltd. and its subsidiaries. HDFC Ltd. held 16.39% shares in the Assessee. In addition, HDFC Ltd. held shareholding in HDFC Investment Ltd. which in turn held 6.25% in the Assessee.

The Income-Tax Officer held such transactions to be SDT, since the consolidated shareholding of HDFC Ltd. (16.39% direct holding and 6.25% indirect holding)in Assessee crossed the threshold of owning 20% substantial interest in terms of section 40A(2)(b), the provision of said section would be applicable and in turn the transaction ought to have been reported in the transfer pricing certificate of the Assessee under section 92BA(i) as SDT.

The Assessee contended that HDFC Ltd. is the beneficial owner of only 16.39% and as such transaction did not take place with a person as contemplated under section 40(A)(2)(b) of the Income-Tax Act. It was contended that HDFC Ltd. cannot be held as beneficial owner of 6.25% shares held by HDFC Investment Ltd in the Assessee as there cannot be more than one beneficial owner of the shares. The Assessee highlighted that in this case the beneficial owner of such shares was only HDFC Investment Ltd., being the legal owner of the shares and relied on the decision of Bacha F. Guzdar Vs. CIT [(1955) 27 ITR 1] and Vodafone International Holdings BV Vs UOI [(2012) 6 SCC 613] to support its contention. Reference was also made to Guidance Note issued by the Institute of Chartered Accountants of India on report under section 92E, wherein for the purpose of section 40A(2)(b) only direct shareholding has to be considered.

Furthermore, the Assessee contended that for a transaction to fall within the meaning of SDT, the transaction has to be one which is not an international transaction and in which any expenditure in respect of which any payment has been made or is to be made by the assessee to a person referred to in section 40A(2)(b) of the Income-Tax Act. It was submitted that purchase of loan is purchase of asset and not an expenditure, hence not a SDT.

The High Court accepted the contentions of the Assessee and held that the law did not permit to club direct shareholding with indirect shareholding and such clubbing is contrary to provisions of Company Law, considering the judgments relied upon by the Assessee. Also, the said transaction was acquisition of asset and cannot be said to be in a nature of expenditure to be a SDT. Therefore, the transaction was held to be not a SDT.

Similarly, in respect of Services received from HBL Global and Interest paid to HDB Welfare Trust, the High Court held that the transactions do not fall within the meaning of a SDT.

Accordingly, the High Court allowed the wit of the Assessee.

IV. CBDT Notification dated December 26, 2018 in relation to CbC-R

In respect of furnishing CbC-R, section 286 of the Income-Tax Act prescribed a period of 12 months from end of the reporting accounting year. Such time period was also applicable where the Indian constituent entity was required to file CbC-R in the event where India does not have agreement for exchange of CbC-R or there has been a systemic failure of the other country in this regard.

The Finance Act, 2018 excluded the aforesaid circumstances from the applicability of 12 months period and the time limit for furnishing CbC-R under such circumstances was to be prescribed by the Central Board of Direct Taxes ('CBDT').

The CBDT vide notification dated December 18, 2018 carried out amendments to Income Tax Rules, 1962 and substituted sub-rule (4) of the Rule 10DB to provide that period of furnishing Country by Country Report ('CbC-R') by constituent entity referred in sub-section (4) of section 286 will be 12 months from the end of reporting accounting year. The constituent entity covered under sub-section (4) are constituent entities of international group resident in India, parent entity of which is resident of Country or Territory -

a) Where parent entity is not obliged to file CbC-R,
b) With which India does not have agreement for exchange of CbC-R, or
c) Where there has been a systemic failure of the Country or Territory and said failure has been intimated to such constituent entity.

The proviso to sub-rule (4), further provides that for the cases covered under (c) above, the period for submission of the report shall be 6 months from the end of the month in which said systemic failure has been intimated.

Further based on representation made on such notification with respect to time limits applicable for earlier accounting years, for example year ending on March 31, 2017 or December 31, 2017 for which the 12 months time has already lapsed as per the aforesaid amendment, CBDT has extended the period for furnishing of said report by the constituent entities covered in (a) and (b) above in respect of reporting accounting years ending upto February 28, 2018 to March 31, 2019.

Shweta Kapoor

Sr. Manager – Tax Advisory
Tel.: +91 11 47102253
shwetakapoor@mpco.in

DOMESTIC TAXATION

I. Department of Revenue is expected to penalise defaulted employers over delay in issuance of Form No. 16 and strict measures to be taken against them.

(Ramprakash Bishwanath Shroff vs. CIT (2018) 99 taxman.com 196 [Bombay])

In a recent petition filed by the assessee, being a senior citizen who suffered due to the delay in issuance of Form No. 16 by his employer, the Hon'ble High Court of Bombay at the pre-admission stage issued directions to Commissioner (TDS), Mumbai to file a comprehensive affidavit on the issue.

Hon'ble Court noticed that Ministry of Finance is expected to provide information of such defaulters so that employees would know in advance as to how they are expected to comply with law.

Also, Hon'ble Court expected from Department of Income-tax to impose penalty against such

defaulters and took other strict measures as contemplated by law.

Shashank Goel

Manager – Tax Advisory
Tel.: +91 11 47103314
shashank@mpco.in

II. Interest Earned on FDRs pledged for promoting business of group companies is Business income rather than income from other sources

Hightech Marine Services Private Limited v. The I.T.O. {TS-664-Tax Tribunal-2018(DEL)]

In a recent judgement, the Tax Tribunal, Delhi Bench has held that interest from the Fixed Deposits (FDRs) must be characterized as 'Business Income' and not as 'Income from Other Sources' as the same has direct nexus with the business activities of the Appellant. Further, the expenses claimed by the Appellant against such interest income are also allowable under Section 37 of the Income-tax Act.

M/s Hightech Marine Services Private Limited ('the Appellant') was established to undertake business of shipping, i.e., owing a ship/cruise and run it itself or let it on hire/charter basis or supply manpower etc. The return for AY 2013-14 was filed and interest income on FDRs were offered to tax as income from business and profession and certain expenses were also claimed against the said income.

During the assessment proceedings, the appellant explained that it had made investments in FDRs to obtain a Standby Letter of Credit ('SBLC') for an amount of Euro 10 million for its business activity. The Income-Tax Officer observed that SBLC was issued in favour of Vishal Cruise Pvt. Ltd., Mauritius ('VCPL') towards the purchase of cruise ship. The Income-Tax Officer further observed that the Ship purchased by Vishal was managed by Passat Kreuzfahrten GmbH ('Passat') in Germany. Both these were the group companies of the Appellant. The Income-Tax Officer observed that neither the ownership of cruise business nor its operation was handled by the Appellant at any stage and as such FDRs were being pledged for the business activities of the group concerns located and operating outside India. Therefore, the Income-Tax Officer held that the interest income should be treated as income from other sources and the expenses claimed should also be disallowed.

Before the Tax Tribunal, the Appellant contended that as its net worth was not adequate for doing the business, therefore, the appellant floated the aforementioned entities for acquiring shipping assets and operating in shipping business while the Appellant were supposed to oversee the maintenance and manpower requirement. The Appellant further contended that although the SBLC was used by the group companies in furtherance of business activity of the group, there was a direct nexus of the interest with the business of the appellant.

Based on the facts, the Tax Tribunal held that promoting the business of subsidiaries/group companies in itself is also a business activity and the expenditure had to be incurred for the purpose of business. The same need not be for the purpose of earning profit, to characterize the same as revenue in nature. As such, the expenses claimed were allowed.

Furthermore, The Tax Tribunal relying on the decision of Delhi High Court in Universal Precision Screws [2015] 94 CCH 0046 held that as the FDs have been used for the furtherance of the business activity, interest earned on FDs has a direct nexus with the business activities of the Assessee and hence taxable under the head PGBP.

III. 'Actual usage' based revenue recognition method for sale of prepaid cards is valid

Shyam Telelink Ltd. Vs. CIT [TS-704-HC-2018 (DEL)]

In a recent decision, the Hon'ble High Court of Delhi, while upholding with the decision of the Tax Tribunal, Delhi Bench, has accepted the method of recognition of income from sale of prepaid cards on the basis of actual usage. The High Court held that carry forward of, the outstanding unutilized amounts to the next year is correct and in line with the matching principles for revenue recognition as provided by the accounting standards.

M/s Shyam Telelink Ltd. ('the Assessee') was engaged in the business of providing basic telecom services and the customer base included both prepaid as well as postpaid subscribers. The receipts from the prepaid subscribers were recognized on the basis of actual usage on the basis of proportionate completion method of accounting. The unutilized amount was treated as an advance and was recognised as revenue only when the talk time was actually used or was exhausted upon expiry of the stipulated time in the subsequent years. The Income-Tax Officer took the view that the entire amount received from prepaid card sale must be recognised as an income in the year of purchase of card by the subscriber, and therefore should be taxed in such year only.

The Tax Tribunal, held that as long as the assessee is under the obligation to provide the services, the entire receipts cannot be recognised as an income. Aggrieved by the order, Revenue filed an appeal before the Hon'ble High Court.

Before the Hon'ble High Court, the Assessee contended that in line with the accounting standard on revenue recognition, it had followed proportionate completion method.

The High court while dealing with the issue in hand, placed reliance on the decision of Dinesh Kumar Goel [2011] 331 ITR 10 (Del), wherein, it was held that the advance tuition fee paid upfront at the time of admission was a debt due at the time of deposit as the services are yet to be rendered. In such decision, the advance receipts were treated in the nature of deposit or advance. Applying such principle, it was held that as the appropriation of the prepaid amount was contingent upon the Assessee performing its obligation and in case services are not delivered as promised, the assessee under the ordinary law of contract would be liable to refund the amounts. Hence, the High Court held that the method followed by the Assessee was correct.

Also, the High Court while relying on the decisions of the Supreme Court in JK Industries [2008] 297 ITR 176 and Woodward Governor [2009] 312 ITR 254 reiterated the significance of accounting standards.

IV. 'Sponsorship fee' meeting the commercial expediency test irrespective of the benefit accrued to group companies is an allowable business expenditure

GMR Projects Private Limited vs. ACIT [TS-665-Tax Tribunal-2018 (Bang)]

The Tax Tribunal, Bangalore Bench, in a recent decision, denied the deduction of advertisement expenditure paid on account of IPL sponsorship as the same did not fulfil the commercial expediency test.

GMR Projects Private Limited ('the Assessee') is a group company of GMR group and involved in in-house projects of GMR division. It became an associate sponsor along with other sponsors for the IPL Season 4 and therefore, contributed towards the sponsorship fee as per the agreement with GMR sports Pvt Limited. Under the agreement, a logo of GMR was to be positioned on the team jersey.

The Tax Tribunal reversing the order of CIT(A) observed that the name of assessee was not displayed on the outfits rather it was only a GMR group logo that was being displayed. It further observed that the Assessee was involved only in in-house project division of the GMR group and awarded contracts only by the group companies. The Tax Tribunal held that the Assessee failed to demonstrate as to how the expenditure resulted in getting more projects and therefore failed the benefit test. Therefore, the amount paid cannot be said to have been incurred for the purpose of business and profession and as such disallowed under section 37(1) of the Income-tax Act ('the Act').

PepsiCo India Holdings Private Limited [TS-691-Tax Tribunal-2018 (DEL)]

In another decision in the case of PepsiCo India Holdings Private Limited ('the Assessee'), the Tax Tribunal Delhi Bench allowed the advertisement expenditure in the nature of sponsorship fee paid to ICC Development (International) Limited ('ICC') for obtaining sponsorship rights in respect of various ICC cricketing events around the world under an agreement.

The Assessee in the present case was engaged in the manufacturing of soft drinks/juice based concentrates and other agro products. The Assessee was also engaged in supplying concentrates for aerated and non-aerated soft drinks to its deemed AEs as well as to franchisee bottlers in India.

The contention of the Assessee was that the Indian audience is a major viewer of cricket due to its mass popularity in India and therefore, the assessee has been consistently promoting its wide range of products using cricket as an advertising platform.

The Tax Tribunal observed that the commercial expediency of the expense was not in dispute in the present case and what is relevant is that the expense should have been incurred during the course of business and for the purpose of business. The fact that the other related parties are also getting benefitted from the said expense may be relevant for transfer pricing purposes but not while determining allowability under section 37(1) of the Income-Tax Act. Since the expenditure was ostensibly for the purpose of promotion of business, the Tribunal allowed the expenditure.

Conclusion: Based on the above two pronouncements, it is pertinent to note that benefit getting accrued to other group entities in relation to the advertisement expense being incurred by the Assessee is not relevant for determining the allowability under section 37 till

the time commercial expediency test is satisfied in the case of Assessee payer.

Ritu Gyamlani

Sr. Manager – Tax Advisory
Tel.: +91 11 47102274
ritu@mpco.in

FOREIGN EXCHANGE MANAGEMENT LAW

I. Review of the Policy on Foreign Direct Investment (FDI) in e-commerce

[Source: Press Note No. 2 (2018 Series) issued by DIPP, Ministry of Commerce & Industry, Government of India dated 26th December 2018]

The Government, with a view to provide clarity on FDI Policy on e-commerce, has replaced Paragraph 5.2.15.2 of the Consolidated FDI Policy, 2017 with a new Para, making certain clarifications/additions in the Sub-Para 5.2.15.2.4 containing "Other Conditions". This change shall be effective from 1st February, 2019.

This change is brought about with a view to curb the deep discounts that were offered by retailers having close association with the marketplace entities. The Government aims to ensure that the e-commerce entities maintain a level playing field and do not directly or indirectly influence the sale price of goods and services which may be to the detriment of the small retailers selling on these platforms or the traders running traditional brick and mortar stores. The Policy mandates that no seller can sell its products exclusively on any marketplace platform and that all vendors on the e-commerce platform are provided services in a "fair and non-discriminatory manner".

The clarifications/additions made are as given hereunder :

1. Earlier - Para 5.2.15.2.4 – clause iv) provided that E-commerce entity providing a market place will not exercise ownership or control over the inventory i.e. goods purported to be sold. Such an ownership or control over the inventory will render the business into inventory-based model.

   Now - An addition has been made here clarifying that the Inventory of a vendor will be deemed to be controlled by e-commerce marketplace entity if more than 25% of purchases of such vendor are from the marketplace entity or its group companies.

2. Earlier - Para 5.2.15.2.4 – clause v) provided that an e-commerce entity will not permit more than 25% of the sales value on financial year basis affected through its market place from one vendor or their group companies.

   Now - The above para has been replaced with para v) as given hereunder:
   " An entity having equity participation by e-commerce marketplace entity or its group companies, or having control in its inventory by e-commerce marketplace entity or its group companies, will not be permitted to sell its products on the platform run by such marketplace entity."

3. Earlier – Para 5.2.15.2.4- clause ix) provided e-commerce entities providing marketplace will not directly or indirectly influence the sale price of goods or services and shall maintain level playing field.

   Now - Here it has been added that the services should be provided by e-commerce or marketplace entity or other entities in which e-commerce marketplace entity has direct or indirect equity participation or common control, to vendors on the platform at arm's length and in a fair and non-discriminatory manner. Such services will include but not be limited to fulfilment, logistics, warehousing, advertisement/marketing, payments, financing etc. Cash back provided by group companies of marketplace entity to buyers shall be fair and non-discriminatory. For the purpose of this clause, provision of services to any vendor on such terms which are not made available to other vendors in similar circumstances will be deemed unfair and discriminatory.

4. Now - New clause added - Para 5.2.15.2.4- clause xi) – e-commerce entity will not mandate any seller to sell any product exclusively on its platform only

5. Now - New clause added - Para 5.2.15.2.4- clause xii) –e-commerce marketplace entity will be required to furnish a certificate along with a report of statutory auditor to Reserve Bank of India, confirming compliance of above guidelines, by 30th September of every year for the preceding financial year.

II. Foreign Exchange Management (Borrowing and Lending) Regulations, 2018

[Source: Reserve Bank of India Notification No. FEMA. 3 (R)/2018-RB dated December 17, 2018]

The Reserve Bank of India, vide its Notification No. FEMA. 3 (R)/2018-RB dated December 17, 2018 has issued the Foreign Exchange Management (Borrowing and Lending) Regulations, 2018 in supersession of Notification No. FEMA 3/2000-RB dated May 3, 2000 (Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000), as amended from time to time, Notification No. FEMA 4/20000-RB dated May 3, 2000 (Foreign Exchange Management (Borrowing and Lending in Rupees) Regulations, 2000), as amended from time to time and Regulation 21 of Notification No. FEMA 120/RB-2004 dated July 7, 2004 (Prohibition on issue of foreign security by a person resident in India) as amended from time to time.

The detailed Regulation is available on the following link:

https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11441&Mode=0

Ruchi Sanghi

Sr. Director – Tax Advisory Services
Tel.: +91 11 47103303
ruchi@mpco.in

For further information, please contact:

C.S. Mathur
Partner
Tel.: +91 11 47102200
csm@mpco.in

Vikas Vig
Partner
Tel.: +91 11 47103300
vvig@mpco.in

Surbhi Vig Anand
Partner
Tel.: +91 11 47102250
surbhivig@mpco.in

Main office	**MPC & Co. LLP**	**Associates**
New Delhi 1 A-D, Vandhna 11, Tolstoy Marg New Delhi-110 001	Delhi Pune Vadodara	Ahmedabad Bangalore Chennai Hyderabad Mumbai

www.mpco.in

IMPORTANT

DATES TO REMEMBER

Particulars	Date
Deposit of TDS for the month of January 2019	07.02.2019
Date of deposit of GST and filing of GSTR-3B for the month of January 2019	20.02.2019
Filing of GSTR I for the month of January 2019	11.02.2019

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