MOHINDER PURI & CO.
CHARTERED ACCOUNTANTS

Corporate Update

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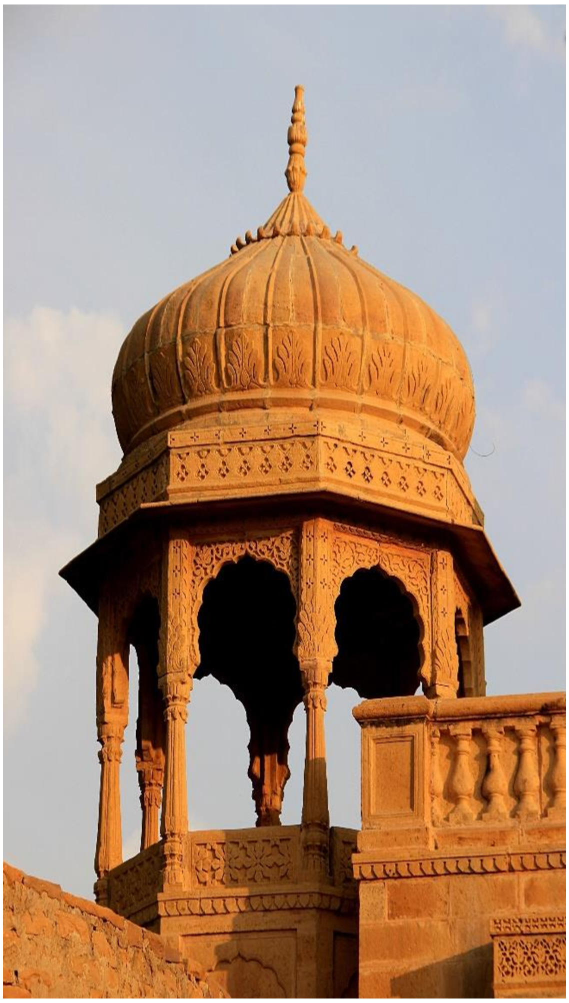

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FOREWORD

Dear Reader,

The Government of India's Annual Budget for the year 2023-24 was presented by the Finance Minister, Government of India, on February 01, 2023.

The Finance Minister in her budget speech has indicated that in the current Financial Year ending on March 31, 2023, economic growth is estimated at 7%, which is highest among all the major economies. The fiscal deficit is estimated at 6.4% of GDP, adhering to the Budget Estimate.

The fiscal deficit for 2023-2024 is estimated at 5.9% of GDP.

In the Budget speech, the Finance Minister focused on large capital expenditure, increase of 33%, to be incurred on various schemes covering Agriculture, Renewable Energy, Infrastructure sectors including Railway and Transport Infrastructure.

PAN will be used as Common Business Identifier for all digital systems of specified government agencies.

In respect of Direct tax, the budget mainly proposes to maintain continuity and stability in taxation.

There are no changes in the tax rates for corporates while in personal taxation, the government is keen to promote the new exemption-less taxation regime introduced in F.Y. 2020-21, for which progressive tax rates have been made more favourable.

There is a focus on simplifying and rationalizing tax provisions to reduce the compliance burden.

In the indirect taxes section, proposals have been introduced to provide reliefs/concessions in respect of customs duties levied on certain items with a view to reduce import costs, promote export competitiveness, to boost domestic manufacturing. These include Agricultural products, Minerals, IT and Electronics etc.

Increases in customs duties have been proposed on certain items in Automobiles, Chemicals, Gems and Jewellery sectors.

Amendments proposed in Goods and Services tax law ('GST') relate to input tax credit provisions, in timelines for filing of GST Return and changes to decriminalise provisions relating to prosecution for offences for certain defaults. No input tax credit is to be allowed on activities relating to expenditure on Corporate Social Responsibility.

While the above deals with broad Macroeconomic features of the Budget, the microeconomic details thereof will be published separately.

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DIRECT TAX

INTERNATIONAL TAXATION

Reimbursement of salary of seconded employees not liable for withholding tax

PCIT v Boeing India Pvt Ltd. [ITA 71/2022] dated October 11, 2022

On the controversial issue revolving around taxability of reimbursement of salaries of seconded employees, the High Court of Delhi has rendered an important decision. The High Court has held that where the host company has already withheld tax under Section 192 on salaries paid to seconded employees, the reimbursements of the salary costs to the home company is not liable to tax withholding.

On the facts of the case, Boeing India Pvt Ltd. ("BIPL") entered into an agreement with The Boeing Company ("TBC) for secondment of employees. For administrative convenience, payment of salaries in secondees' home country was firstly made by TBC- and then, BIPL reimbursed salary costs to TBC. The payment of salaries to seconded employees was made after withholding of tax under section 192 of the Act. The tax Officer, however, disallowed such payments on the premise that no tax was withheld thereon under section 195 of the Act, by relying on the decision of the Delhi High Court in the case of Centrica India Offshore Pvt. Ltd. vs. CIT (2014) 364 ITR 336 (Delhi).

Before the Tribunal, while referring to salary reimbursement agreement, the Tribunal observed that secondees were working for BIPL and were under the supervision, control, and management of BIPL as employees. Furthermore, TBC merely facilitated payment of salaries in the secondees' home country on behalf of BIPL.

The Tribunal came to a conclusion that BIPL was paying to its own employees. The Tribunal held that taxes were duly deducted under section 192 of the Act and therefore, provisions of section 195 of the Act were not applicable. Furthermore, as regards the applicability of the decision of Centrica India Offshore Ltd. (supra), the Tribunal distinguished this decision on the ground that in that case, the employees of overseas companies with requisite technical knowledge and skills were sent to newly formed Indian company and made available their experience and skills.

On revenue's appeal, the High Court concurred with the Tribunal that once the nature of payment is determined as salary and tax has been withheld under section 192 of the Act, the reimbursements thereof could not be subjected to withholding tax under Section 195 of the Act, as Section 195 is not applicable to salaries. Furthermore, the Hon'ble Court held that its earlier judgment in Centrica India Offshore Pvt. Ltd (supra) is inapplicable as the Tribunal came to a conclusion that the real employer of the seconded employees was BIPL and not the overseas entity, TBC.

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Advance Ruling binding on the Indian applicant and not on the foreign service provider (herein the assessee)

CIT (International Tax & Transfer Pricing) Vs. The Timken Company [TS-09-HC-2023(CAL)]

In a recent judgement the Hon'ble High Court of Calcutta held that the Advance Ruling obtained by Applicant in relation to deduction of TDS would be binding only on the Applicant and not on the service provider for taxability of transaction in latter's hands.

On the facts of the case, the assessee, the Timken Company, is a resident of USA and entered into an agreement with Timken India Limited (TIL), the Indian AE for providing services such as management services, management information services, information resources, system development etc. to the Indian AE. The Indian AE obtained Ruling from the Authority for Advance Ruling (AAR) in relation to deduction of TDS on payment for service provided by the assessee to the Indian AE. The AAR held that payment for such services was liable to TDS. The assessee, however, claimed such services to be not taxable under the Double Taxation Avoidance Agreement (DTAA) between India and US. In addition, certain actual bills raised by third parties for similar services provided by them to the Indian AE, were paid by the assessee in USA and were later reimbursed by TIL to the assessee in India. The Assessing Officer, however, held such services and reimbursement received for similar services to be taxable under Indo-US DTAA and made suitable additions to the taxable income of the assessee.

On appeal, the Commissioner of Income-tax (Appeals) [CIT(A)] and the ITAT deleted the aforesaid additions. Subsequently, the revenue filed an appeal before High Court.

The Hon'ble High Court based on the terms of the agreement held that the services provided by the assessee are Advisory services which do not involve transfer of technical plan or technical design. Therefore, since no technology is made available under the agreement and, therefore, the services are not taxable under Article 12(4) of the Indo-US DTAA. Moreover, in respect of reimbursement of third-party services the High Court took cognizance of the fact that the assessee has only recovered the cost of such services without any mark-up from the Indian AE which has also been accepted by the Transfer Pricing officer. In view of the same and since such services were also in the nature of Advisory services the same were also held to be not taxable under Article 12(4) of the Indo-US DTAA.

Regarding question raised by revenue whether the Ruling obtained by Indian AE was binding on the assessee, the High Court referred to the decision cited in the writ petition in some other matter of the assessee. It was decided in that writ petition that nothing more needs to be read in the Ruling than the answers to the questions rendered therein. Since the questions raised in Ruling pertain only to the Indian AE and its TDS obligation while making remittance to the foreign company, the opinion in regard to these questions is not binding on the foreign company. In view of the same, the Hon'ble High Court decided against the revenue and held that the Ruling obtained by Indian AE was not binding on the assessee a foreign company.

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Section 14A not applicable on dividend income earned from Oman Company even where no tax paid in India or Oman

IFFCO Ltd [TS-793-HC-2022(DEL)] dated October 13, 2022

Recently, the High Court of Delhi held that provisions of Section 14A (disallowance of expenditure incurred for earning exempt income) are not applicable to dividend income earned from Oman company even though no tax was paid on such income in Oman or in India in terms of Article 25 of India-Oman DTAA.

The assessee, an Indian company earned dividend income during the Assessment Year (AY) 2007-08 from its investment in OMIFCO-Oman. In the course of tax litigation, the Revenue contended that expenditure incurred by the assessee towards earning dividend income from OMIFCO-Oman was to be disallowed under Section 14A of the Act as no tax was paid on the said dividend in Oman and India, since no tax was leviable in Oman and further the tax sparing credit of notional tax on the dividend was allowed to the assessee under Article 25 of India-Oman DTAA. Thus, the Revenue was of the opinion that the assessee was effectively not paying any tax on the said income either in the source country or in India and that the said dividend income was exempted from tax for all purposes.

On appeal, the High Court of Delhi observed that since the dividend received by the assessee from OMIFCO, Oman was chargeable to tax in India under the head *"Income from other sources"* and formed part of the total income, the same was included in taxable income in the computation of income filed by the assessee. However, credit of tax has been allowed to the assessee from the total taxes in terms of Section 90(2) of the Income Tax Act read with Article 25 of the Indo-Oman DTAA. The High Court, thus, held that the provisions of Section 14A would not be attracted in this case.

In this regard, the High Court relied on the decision of CIT vs. M/s Kribhco [2012] 349 ITR 618 (Delhi) wherein it was held that the income on which the deduction is allowed forms a part of the total income, but are allowed as a reduction and reduced. The High Court, therefore, concluded that Section 14A of the Act would not be attracted in this case.

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Income from domain name registration is not taxable as Royalty in India

PDR Solutions FZC vs. DCIT [TS-1004-ITAT-2022 (Mum ITAT)]

Recently, the Mumbai Bench of Tax Tribunal has held that income received by the Appellant from domain name registration is not taxable as Royalty under Article 12(3) of India – UAE double taxation avoidance agreement (DTAA).

As per relevant provisions of Article 12(3) of DTAA, the term 'Royalty' has been defined to mean payment of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including *inter-alia* any trademark.

On facts, the Appellant is a tax-resident of UAE and is engaged in the business of web presence and sale of domain names to its global customers through its various B2B and B2C brands. Further, the Appellant is also engaged in the business of providing web hosting services wherein, server spaces are given on lease/ hire to the customers.

The Appellant filed its tax return for Assessment Year (AY) 2017-18 and AY 2018-19 which were selected for tax scrutiny proceedings by the tax officer. As an outcome of tax scrutiny proceedings for AY 2017-18, the tax officer made the following additions to the total income of the Appellant – (a) income from domain registration services of INR 274 million; (b) income from web hosting services of INR 30.5 million and (c) income from sponsorship services of INR 6.49 million. These amounts claimed as non-taxable were subjected to tax as Royalty and income from sponsorship services as business income.

On raising objections before Dispute Resolution Panel (DRP), the DRP upheld the additions of domain registration services and web-hosting services to the total income of the Appellant. However, as regards the addition of sponsorship income, the DRP directed the tax officer to pass a speaking order for constitution of permanent establishment (PE) of Appellant in India.

On appeal before the Tax Tribunal on the issue of taxability of income from domain registration services as Royalty under Article 12(3) of DTAA, the Tribunal held the following:

- In the instant case, the Appellant being a facilitator, merely checks for the availability of domain name in the registry and upon availability of the same, registers the domain name for the customer. Prior to registration of domain name for the customer, such domain name does not exist in the database maintained by the registry.
- The right in the domain name comes into existence in favour of the customer only upon registration and such right is only valid up to the period of registration. Thus, only upon registration the customer obtains an exclusive right over such domain name and the Appellant does not transfer any right in domain name to the customer.
- Apart from acting as an intermediary in the entire process of domain name registration, the Appellant does not have any other role to play. Thus, the Appellant does not have any right in the domain name registered in the name of customer much less any intellectual property right in the nature of ‘trademark’.
- The Tribunal factually distinguished decision of its coordinate bench in the case of Godaddy.com v. ACIT [(2018) (170 ITD 217 (Del ITAT)] as in the said case the Assessee had not claimed any benefit under the tax treaty. However, in the instant case, the Appellant being a tax resident of UAE holding a valid Tax Residency Certificate was eligible to the beneficial provisions of Article 12(3) of DTAA vis-à-vis the Income-tax Act, 1961.

The Tribunal held that as the Appellant did not have any right in the domain name, the income received from domain name registration was not taxable as Royalty under Article 12(3) of DTAA.

A second issue raised before the Tribunal pertained to taxability of income pertaining to web hosting services as Royalty under the Act as well as DTAA. The Tribunal observed that the definition of the term ‘Royalty’ is not as widely defined under Article 12(3) of DTAA compared to Section 9(1)(vi) of the Act. In the absence of grant of any control over equipment by the Appellant to its customers, the Tribunal held that income from web hosting services is not taxable as Royalty under Article 12(3) of DTAA.

The third issue raised before the Tribunal pertained to taxability of sponsorship income as business income by constitution of a PE of Appellant in India. The Tribunal observed that as per provisions of Section 144C(8) of the Act, DRP cannot set aside any proposed variation or issue any direction for fresh enquiry. Further, it was held that mere conduct of a two day conference does not constitute a fixed place PE and organizing such conferences was not the core business activity of the Appellant. Such conferences organized by the Appellant were merely preparatory or auxiliary activity in nature which were specifically excluded from the definition of PE under Article 5(3) of DTAA. Thus, the Tribunal held that in the absence of a PE of Appellant in India, the sponsorship income cannot be taxed as Business Income.

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DOMESTIC TAXATION

Issue of new show cause notice upon change of Assessing Officer does not mean dropping of the earlier show cause notice

In a recent decision in case of **DCIT v. Mastech Technologies Pvt. Ltd. (Now Avaids Technovators Pvt. Ltd.) [TS-901-SC-2022]**, the Supreme Court ("SC") has held that issue of new notice for reopening of assessment proceedings cannot be said to be dropping of the first notice by which the assessment was reopened.

In the instant case, the Assessing Officer ('AO') issued a notice to the assessee under section 148 of the Act for reassessing its income and also supplied the reasons for reopening the case. Subsequently, the AO was transferred and the new AO issued a fresh notice under section 148. Reasons for reopening of assessment were also provided. Thereafter, the new AO issued the notice under Section 142(1) for continuing the assessment proceeding and passed an assessment order under section 143(3) of the Act.

Aggrieved, the assessee filed a writ petition before the High Court challenging the re-opening of the assessment. The High Court set aside the reopening of assessment proceedings based on the following grounds:

a) By issuance of second notice, the first notice under section 148 was given up/dropped,

b) The second notice is considered to be the fresh notice and was barred by time limitation

c) No reasons were recorded when the second notice was reissued.

d) In the second notice, it was not specifically mentioned that the same is in continuation of the first notice.

On further appeal by the tax department, the Supreme Court observed that section 129 of the Income Tax Act permits to continue with the earlier proceedings in case of change of AO from the stage at which the proceedings were before the earlier AO. Therefore, the Supreme Court held that the judgment and order passed by the High Court for reopening of assessment is unsustainable. The Supreme Court further observed that the fresh notice was not at all required to be issued. As such, the subsequent issuance of the notice cannot be said to be dropping the earlier notice. Further, the High Court was not required to consider the reasons recorded for second notice as the reasons for reopening the assessment were already furnished by the AO. In view of this the Supreme Court quashed the order of the High Court.

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REGULATORY

REGULATORY COMPLIANCE

Foreign Investment in India - Rationalisation of reporting in Single Master Form (SMF) on FIRMS Portal

The Reserve Bank of India ("RBI") has issued a circular notifying the following changes being implemented with respect to the reporting of foreign investment in SMF on FIRMS portal:

(i) The forms submitted on the portal will be auto-acknowledged and the AD banks shall verify the same within five working days based on the uploaded documents, as specified.

(ii) In cases of delayed reporting, the AD banks shall either advise the Late Submission Fee (LSF) to the applicants, which will be computed by the system or advise for compounding of contravention, as the case may be.

Auto-acknowledgement of SMF in FIRMS and online calculation of LSF

The forms submitted in FIRMS Portal will now be processed as detailed below:

(i) All forms submitted with the requisite documents will be auto-acknowledged on the FIRMS portal with a time stamp and an auto-generated e-mail will be sent to the applicant.

(ii) The forms submitted within prescribed timelines, will be verified by the AD banks based on the uploaded mandatory documents and ensure that the same are in compliance with the extant guidelines.

(iii) The system would identify the delay in reporting, if any.

(iv) For forms filed with a delay less than or equal to three years, the AD banks will approve the same, subject to payment of LSF.

(v) The LSF will be computed by the system and an e-mail will be sent to the applicant and the concerned Regional Office (RO) of RBI specifying the amount and the timeline within which it is to be paid to the concerned RO of RBI.

(vi) Once the LSF amount is realised, the concerned RO will update the status in the FIRMS portal and the updated status will be communicated to the applicant through a system generated e-mail, which can also be viewed in the FIRMS portal.

(vii) The AD bank will approve the forms filed with a delay greater than three years, subject to compounding of contravention. The applicant may, thereafter, approach RBI with their application for compounding.

(viii) The remarks of the AD Bank for rejection of forms, if any, will be communicated to the applicant through a system generated e-mail and the same can also be viewed in the FIRMS portal.

For detailed guidelines, the FIRMS manual available at https://firms.rbi.org.in may be referred to.

[Source: A.P. (DIR Series) Circular No. 22 dated January 04, 2023 issued by Reserve Bank of India]

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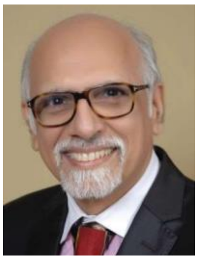

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