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SNK Newsletter

DIRECT TAXES

Judicial Pronouncements

E-Gain Communication Pvt. Ltd v. ITO 2008 TIOL-282-ITAT-PUNE

Determination of Arm's Length Price

The assessee, E-Gain Communication Pvt. Ltd is a wholly owned subsidiary of E-Gain Communication, USA. It is a captive company and provides software development services to its parent company. It is a 100% EOU and has been claiming Section 10A benefits. It has an agreement with its parent company which compensates it on cost plus 5 % markup. It used the TNMM as the most suitable method to determine the Arm's Length Price (ALP) for its transactions.

The Assessing Officer referred the question of computation of ALP to the Transfer Pricing Officer (TPO). The TPO compared the Net Cost Plus mark-up of 5.16 % earned with weighted average NCP of 16.12 percent earned by the set of 20 comparables chosen by the TPO and made an adjustment of Rs 1.08 Cr to the taxable income of the assessee. The CIT(A) upheld the AO's order.

While arguing before the Tribunal the counsel for the assessee said that the TPO committed an error in identifying the comparables without considering the sales turnover. Some of the companies selected had very high profit margin. AO also selected some of the companies having non-operative component of income in computing weighted average NCP of comparable companies.

Revenue argued that the margin in the industry in which the assessee functions is much higher than the one furnished by the assessee. Since the low margin claimed by the assessee was too low, it needed to be adjusted.

Having heard both the parties the Tribunal held that,

- While applying TNMM, necessary adjustments for differences on account of FAR analysis need to be made;

- If TNMM is used properly, it can be a highly reliable tool to make adjustments of differences;
- Similarities and dissimilarities of the transactions under comparison need to be examined to see differences of situations, circumstances and environment;
- Revenue was not justified in selecting oversized companies with high profit margins; and
- Depreciation should be worked out under the Companies Act and the assessee was correct in adjusting its NCP.

ACIT v. Pride Foramer France Sas 2008-TIOL-268-ITAT-DEL

Interest on Income Tax Refund and PE implication

As regards taxability of interest on income ax refund, the ITAT held that the assessee is not in a business of obtaining income-tax refunds and earning interest thereon. And, therefore, the interest is neither derived from nor attributable to the business activity of the assessee. It is merely fall out of the profits earned by the assessee and

is an appropriation of profit and when excess amount than what is due under the Act is appropriated, assessee get refund thereto, and when there is a delay in granting such refund, assessee is granted interest thereon which is taxable under the head Income from other sources. Therefore, also the interest earned by the assessee cannot be held to be related to activity of permanent establishment. Thus, cannot be related to article 12.5 of the DTAA with France. The Tribunal held that interest received by the assessee on delayed issue of refunds could be taxed only under article 12.2 of the DTAA with France.

ACIT v. Zimmer AG [2008-TIOL-259-ITAT-KOL]

Payment under Engineering know-how supply agreement - taxability

The assessee is a German company which is engaged in manufacture of plant and machineries capable of manufacturing of petrochemical products.

The assessee executed three separate agreements with M/s. SAPL, an Indian Company. Under the engineering know-how agreement the assessee had supplied technical know-how to an Indian company for a lump sum consideration of DM 7.2 Million which represented consideration for transfer of technical know-how, design and secret processes developed by the assessee.

The Revenue took the view that the amount received by the assessee from the Indian Company was, therefore, taxable in India as its royalty income under section 9(1)(vi) of the Income-tax Act, 1961. Even under Article 12(3) of the Double Taxation Avoidance Agreement between India and Germany the consideration of DM 7.2 million constituted royalty and, therefore, taxable in India being the country of source.

Having heard the parties the Tribunal observed that,

From cumulative reading of the Clauses and Articles of the Agreements; it appeared that the supply of engineering drawings and designs together with supply of plant and equipments; constituted one composite supply which enabled SAPL to erect, commission, set up, operate and maintain the plant for manufacture of bottle grade PET resins.

In our opinion, supply of engineering drawings and designs was integral part of supply of plant and equipment and it could not be viewed in isolation and, therefore, payment made by SAPL was not for acquiring mere right to use engineering documentation so as to constitute Royalty.

Thus the Tribunal held that the payments received by the assessee under Engineering Know-how Supply Agreement therefore was not royalty either under section 9(1)(vi) of the Act or Article 12 of Indo-German DTAA and upheld the order of CIT(A).

ACIT v. Goldmine Shares and Finance Pvt. Ltd. [2008-TIOL-220-ITAT-AHM-SB]

Set off of loss for s. 80IA deduction

Profit from eligible business for deduction u/s 80IA of Act has to be computed after deduction of notional brought forward losses and depreciation.

Shri M N Rajaraman v.. ACIT 2008-TIOL-293-ITAT-MAD

Penalty in search cases

If income is disclosed and return has been filed after raid, the same cannot be considered as voluntary and penalty is leviable.

Foster's Australia Ltd. In re AAR (2008) 217 CTR (AAR) 21

Transfer of intangible property - taxability

The Applicant is a non-resident company incorporated in Australia engaged in the business of brewing, processing, packaging, marketing, promoting and selling of beer products in Australia and abroad. The applicant entered into a brand licence (B.L.) Agreement with Foster's India Ltd. on 13th Oct., 1997, granting to Foster's India an exclusive licence to brew, packed, label, and sell Foster's lager beer and an exclusive right of user of the trade marks specified within the territory of India.

The applicant entered into a contract dated 4th Aug., 2006 in Australia for the transfer of shares and other intangible assets in the nature of intellectual property to SAB Miller, UK under an agreement styled as "India Sale and Purchase Agreement" (S&P Agreement).

Judicial pronouncements

As a sequel to this agreement, a deed of assignment dated 12th Sept., 2006 came to be executed between the applicant and SKOL Breweries Ltd. which is an Indian company nominated by SAB Miller, UK as the transferee in terms of the S&P Agreement.

The applicant submits that the B.L. Agreement was terminated in accordance with the S&P Agreement read with BL Agreement and pursuant thereto, the exclusive rights over trade marks, brand intellectual property and brewing intellectual property vested back with the applicant situated in Australia and sale thereof by way of agreement executed in Australia did not give rise to any income taxable in India as the situs of all such property was situated in Australia.

Applicant's contention that the intangible assets transferred by the applicant have no particular geographical location and that they have no situs apart man the domicile of the owner is not sustainable.

The intellectual property uprising of non-resident Foster's trade marks and brand IP can be said to be located in India where the business of Foster's India was being carried on in injunction with the applicant.

The Applicant's business presence in India manifested itself with the tie-up it had with

Foster's India which made use of the intellectual property rights granted by the applicant. Keeping this background in view, it is reasonable to hold that the marketing intangibles comprising the Foster's trade marks and brand which were in use for nearly a decade had their abode in India by the crucial date of transfer of the said capital assets.

In view of the same income is taxable in India.

Knowerx Education (India) (P) Ltd., In re AAR (2008) 217 CTR (AAR) 50

Fees for promoting professional exam - taxability

Double taxation relief—Agreement between India and USA—Permanent establishment—Applicant has entered into agreements with two US entities APICS and AST&L for promotion of professional examination/certification programmes of these entities—These entities will conduct examinations either through the applicant or through other entities in India—Income in the form of examination fees is to be received in India, by the applicant and remitted to non-resident entity abroad—Thus, the applicant receives income in India on behalf of the APICS and AST&L as their agent and same would be taxable under section 5(2)—Since both APICS and AST&L are corporations incorporated in USA, they are tax residents of USA, though these entities have been exempted from payment of tax under section 501(c)(6) of Internal Revenue Code and, therefore, the provisions of the DTAA are attracted—Applicant does not conclude any contract on behalf of APICS or AST&L—It does not in any way bind APICS or AST&L in the conduct of their examination programme in India—Applicant enjoys an independent status and carries on a variety of activities besides promoting examinations of APICS and AST&L—It is not wholly or substantially devoted to APICS and AST&L only—Thus, applicant cannot be deemed to be a PE of APICS and/or AST&L in India either in terms of para 4 or para 5 of art. 5— Therefore, payment of examination fees made to APICS and AST&L is not taxable in India in view of para 1 of article 7 and the applicant is not required to deduct tax at source from such payments.

Worley Parsons Services Pty. Ltd., In Re AAR 2008) 217 CTR (AAR) 65

Monitoring and supervision of project work - concept of making available

The assessee Australian company admittedly had a PE in India within the meaning of Article 5(k) of DTAA between India and Australia.

The assessee entered into an agreement with GAIL for monitoring and supervision of project work with a view to ensure its timely completion within the approved cost.

Receipts by assessee under this agreement with GAIL constituted business profits under Article 7(1) of the DTAA and not royalty under Article 12.3(g) as no technical knowledge, experience, skill or know-how is 'made available' to GAIL on account of rendering the services.

Income from such receipts are liable to be taxed as business profits in India in view of Article 7 of DTAA and only the profits attributable to the PE in India are liable to be taxed as per the provisions of IT Act.

Circulars / Notifications

Notification No. 70/2008-FTD, Dated 18-6-2008

DTAA with Botswana

An Agreement between the Government of the Republic of India and the Government of the Republic of Botswana for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income was signed in India on the 8th day of December, 2006.

Instruction No. 7/2008, dated 24-6-2008

Modification in DTAA with Denmark

In order to avoid the unintended hardship to the taxpayers, as well as for efficient management of collection of revenue, the Competent Authorities of India and Denmark have signed a Memorandum of Understanding (MOU) regarding suspension of collection of taxes during the pendency of Mutual Agreement procedure (MAP). The MOU is applicable in case of a taxpayer who

(i) is a resident of Denmark, or

(ii) an Indian resident entity in cases involving transfer pricing,

and in whose case MAP is invoked through the Danish Competent Authority and has been admitted by the Indian Competent Authority.

INDIRECT TAXES

Judicial pronouncements

Magus Construction Pvt. Ltd v. Union of India [2008-TIOL-321-HC-GUW-ST],

Service tax not applicable to builders

The petitioner-company constructs buildings and sells premises/flats in such buildings. During the course of development of such property and construction of buildings thereon and also after completion of such construction, the petitioner-company enters into flat purchase agreements with various premises/flat purchasers, where under the petitioner company allots and sells flat / premises, in such buildings, to the purchasers.

The said transaction is a transaction of sale of flats/premises and the consideration is payable to the petitioner-company in instalments as per the terms, which may be mutually agreed upon, though the terms of the agreement are, usually, co-related to the extent and the stage of the development of the constructional work. The agreement for sale of such flats is stamped as sale of flat/premises for the entire consideration. Before accepting money as advance payment or deposit out of the sale price, the petitioner-company enters into an agreement for sale, which is registered. The agreement contains various details and price including area of the flat, the price of the flat (the price of common areas and facilities being shown separately) and various other facilities concerning the flat, etc.

It was held that when a builder, promoter or developer undertakes construction activity for its own self, then, in such cases, in the absence of relationship of “service provider” and “service recipient, the question of providing taxable service to any person by any other person does not arise at all. In the present case too, the materials placed by the writ petitioners clearly show that the construction activities, which the petitioners have been undertaking, are in respect of the petitioners' own work and it is only the completed construction work, which is sold by the petitioner-company to the buyers, who may have made agreements for sale before the construction had actually started or during the progress of the construction activity or at the end or completion of the construction activity. Any advance, made by a prospective buyer, or deposit received by the petitioner-company, is against consideration of sale of the flat/ building to such prospective buyer and not for the purpose of obtaining service from the petitioner-company.

OTIS Elevator Co (India) Ltd. v CCE (CESTAT) (08/12/2006)

Classification of goods - demand of excise duty

Central Excise Tax Act, 1985 - Show Cause Notice issued proposing differential duty on the ground that the assessee has mis-classified their product manufactured by them namely parts of lifts and escalators classifiable under Chapter Sub-heading 8431 as lifts and escalators under Chapter Sub-heading 8428 though they were removing only parts of lifts and escalators – It was held that section Notes and Chapter Notes are relevant in respect of classification of any goods manufactured and in this case, the goods are parts made for use in or use with lifting machinery and equipments - The Chapter heading 8431 is sufficiently specific enough to cover the various items, components manufactured by them - The appellants' contention that if the items supplied by them are not treated as machinery, the tariff sub-heading 8428 will be rendered redundant is not correct as there are various items like Fork lifts, Kitchen lifts, mini elevators etc. which fall under this tariff-Commissioner's finding on classification and demand of duty cannot be faulted - Appeal dismissed.

Circulars / Notifications

Circular No. 08/2008-Customs

Pre-authenticated CT-3

Attention is invited to the Board's circular No. 84/2001-Cus dated 21.12.2001 for issuing pre-authenticated CT-3 form booklet by the jurisdictional Range officer for procuring raw material by EOUs except for those in textile and chemical sector. This circular was modified under the Board's circular No. 66/2002-Cus dated 08.10.2002 extending the facility of issuing CT-3 to EOUs in textile and chemical sector on case to case basis subject to the approval of Assistant/Deputy Commissioner of Customs or Central Excise in-charge.

Representations have been received that the existing procedure is causing difficulties to these two sectors. After examination, the Board has decided to extend the facility of issuing pre-authenticated CT-3 form booklets to EOUs in textile and chemical sector as well subject to certain additional safeguards as enumerated in the following paragraphs.

The request for issuing pre-authenticated CT-3 form booklet by EOUs in textile and chemical sectors will be submitted to the jurisdictional Asst./Dy. Commissioner of Customs / Central Excise. After examination of the request, the Asst./Dy. Commissioner of Customs /Central Excise may grant one-time yearly permission for issuing pre-authenticated CT-3 form booklet to such EOUs who have an unblemished track record as per following parameters:

(i) the unit has achieved Net Foreign Exchange/ export obligation wherever applicable;

(ii) the unit has not been issued a show cause notice or a demand confirmed, during the preceding 3 years, on grounds other than procedural violations, invoking penal provision and/or on account of fraud or collusion or any wilful mis-statement or suppression of facts or contravention of any of the provisions of the Customs Act, 1962, the Central Excise Act, 1944, the Finance Act, 1994 covering Service Tax, the Foreign Trade (Development & Regulation) Act, 1992, the Foreign Exchange Management Act,1999 or any allied Acts or the rules made thereunder.

Circular No. 874/12/2008-CX

Provisional attachment of property

Section 11DDA of the Central Excise Act, 1944 provides for provisional attachment of property for the purpose of protecting the interests of revenue during the pendency of any proceedings under Section 11A or Section 11D of the Act.

Guidelines are issued to maintain uniformity in its implementation by field formations as per the instructions of law ministry.

It is stated that the provisional attachment of property shall be resorted to only in a case where the duty or CENVAT Credit alleged to be involved in the above specified offences is more than Rs.25 lakhs (Rs. Twenty five lakhs). Other guidelines have also been incorporated.

Similar guidelines have issued for service tax and customs act.

The secret of success in life is for a man to be ready for his opportunity when it comes.

Notification No. 29/2008 - Service Tax, dated 26-6-2008

No service tax on supply of goods carriage

In exercise of the powers conferred by sub-section (1) of section 93 of the Finance Act, 1994 the Central Government, on being satisfied that it is necessary in the public interest so to do, hereby exempts the taxable service of supply of a goods carriage, without transferring right of possession and effective control of such goods carriage, referred to in sub-clause (zzzzj) of clause (105) of section 65 of the Finance Act, provided by any person to a goods transport agency for use by the said goods transport agency to provide any service, referred to in sub-clause (zzp) of clause (105) of section 65 of the Finance Act, to a customer in relation to transport of goods by road in the said goods carriage, from the whole of the service tax leviable thereon under section 66 of the Finance Act.

SEBI

Notification No. CAD-RO /GN/ 2008 /11/126538, dated 26-5-2008

Notification for intermediaries

Securities and Exchange Board of India (Intermediaries) Regulations, 2008 have been notified.

FOREIGN EXCHANGE MANAGEMENT ACT

A. P. (DIR SERIES) Circular No. 53, dated 27-6-2008

FDI by trust etc.

With a view to further liberalizing the policy on overseas investments, it has been decided, in consultation with the Government of India, to allow Registered Trusts and Societies engaged in manufacturing / educational sector to make investment in the same sector(s) in a Joint Venture or Wholly Owned Subsidiary outside India, with the prior approval of the Reserve Bank. Trusts / Societies satisfying the eligibility criteria as prescribed in the Annexure to the circular.

Due Dates of key compliances pertaining to the month of July -08:

5th July	*Payment of Service Tax & Excise duty for June*
6th July	*Payment of Excise duty paid electronically through internet banking*
7th July	*TDS/TCS Payment for June*
10th July	*Excise Return ER1 / ER2 /ER6*
15th July	*PF Contribution for June, Excise payment by SSI*
15th July	*TDS/TCS return of first quarter*
21st July	*ESIC Payment for June*
31st July	*Return of income for A.Y. 2008-09 for assessees whose accounts are not required to be audited.*