



India Tax Konnect

April 2017

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Editorial



Recently, the Rajya Sabha passed four supplementary legislations which will enable the government to rollout the landmark Goods and Services Tax (GST) Bill. GST regime is expected to create a semblance of a common market where all goods and services irrespective of where it's transacted will have a common treatment and a common rate.

Central Board of Excise and Customs (CBEC) issued eight GST rules like Composition Rules, Valuation Rules, Transition Rules, Input Tax Credit (ITC) Rules, Revised Invoice Rules, Revised Payment Rules, Revised Refund Rules and Revised Registration Rules. The government has sought comments from industry and stakeholders on 4 set of rules i.e. Composition, Transition, Valuation and ITC Rules.

The Finance Bill, 2017 received president's assent and it has become an act. The latest amendments inter alia provide that

Aadhar should be quoted for filing income-tax returns as well as to obtain PAN, capping the limit of cash transaction to INR2 lakh from the earlier INR3 lakh and provisions relating to limitation on interest deduction have been linked to the incurrence of expenditure by way of interest or of a similar nature of expenditure, to exclude asset or capital asset mentioned therein, which is held by way of investment, directly or indirectly, in a Foreign Institutional Investor (FII).

To improve the ease of doing business for newly incorporated companies, the Central Board of Direct Taxes (CBDT) has tied up with Ministry of Corporate Affairs (MCA) to issue Permanent Account Number (PAN) and Tax Deduction Account Number (TAN) in 1 day. The applicant companies shall submit a common application form SPICe (INC 32) on MCA portal and once the data of incorporation is sent to CBDT by MCA, the PAN and TAN will be issued immediately without any further intervention of the applicant. The certificate of incorporation of newly incorporated companies includes the PAN in addition to the Corporate Identity Number (CIN). TAN will also be allotted simultaneously and communicated to the company.

The Special Bench of the Hyderabad Tribunal in the case of Nagarjuna Fertilizers and Chemicals Ltd. held that the provisions of Section 206AA of the Act will not have an overriding effect on the provisions of tax treaty to the extent they are beneficial to the taxpayer.

We at KPMG in India, would like to keep you informed of the developments on the tax and regulatory front and its implications on the way you do business in India. We would be delighted to receive your suggestions on ways to make this Konnect more relevant.



Buy back of shares

Background

In common parlance, buy back of shares can be considered as the process by which a company buys back its shares from its shareholder. Earlier, a company could buy back its shares from the shareholders only with a prior sanction of the court. Subsequently, the promulgation of the Companies (Amendment) Ordinance, 1998 has introduced Section 77A in the Companies Act, 1956 (Companies Act) that allows a company to purchase its shares subject to certain conditions.¹ Consequently, the Finance Act, 1999 amended the provisions of Section 2(22) and Section 46A of the Act, whereby the income arising to a shareholder on buy back of shares is to be treated as income from capital gains and not dividend income.

In some of the cases, the tax department re-characterised the purchase consideration for buy-back of shares (undertaken prior to 1 June 2013) as dividends. The Authority for Advance Rulings (the AAR) in the case of A Ltd.² (the applicant) dealt with a case where a Mauritian shareholder of an Indian company accepted the offer of buy-back of shares given by the Indian company. The AAR held that this buy-back scheme was a 'colourable device' for avoiding payment of Dividend Distribution Tax (DDT), which is otherwise payable on the distribution of the dividend under Section 115-O. Accordingly, the consideration received by the shareholder is taxable in India as dividend, which is liable for deduction of tax under Section 195.

On the other hand, AAR in the case of Armstrong World Industries Mauritius Multiconsult Ltd.³ held that the proposed buy-back of shares by an Indian company from a Mauritian company is not a tax avoidance scheme and it is not liable to capital gains tax in India under Article 13(4) of the India-Mauritius tax treaty.

The Memorandum to the Finance Bill, 2013 stated that unlisted companies, have been resorting to the buyback of shares instead of payment of dividends. These companies avoid the payment of tax by way of DDT, particularly where the capital gains arising to the shareholders are either not chargeable to tax or are taxable at a lower rate. In order to curb such practice, Chapter XII-DA was introduced in the Act, to provide that the consideration paid by the company for purchase of its unlisted shares, which is in excess of the sum received by the company at the time of issue of such shares (distributed income) will be charged to tax. The company would be liable to pay additional income-tax at 20 per cent of the distributed income paid to the shareholder. The additional income-tax payable by the company shall be the final tax on similar lines as DDT. The income arising to the shareholders in respect of such buy-back would be exempt if the company is liable to pay such additional income-tax.

The taxpayers were aggrieved since the rate of DDT was 15 per cent under Section 115-O of the Act, whereas, the levy of additional tax on distributed income is at the higher rate of 20 per cent. Further, the reduction of issue price from the consideration paid for computation of distributed income may not be appropriate as it would lead to double taxation under certain situations for e.g. if a shareholder has acquired shares through secondary transaction by paying cost, which is higher than the issue price received by the company, the total tax paid by the shareholder and the company, will be more than the tax on the total income in the hands of all shareholders. These provisions did not provide for the manner to determine amount received by the company on the issue of shares at the time of corporate actions such as bonus, share split, share consolidation, merger of company, etc.

In order to provide clarity and remove ambiguity on the above issues, the Finance Act, 2016 amended the provisions relating to buy-back of shares. The Memorandum to the Finance Bill, 2016 explained stated that lack of clarity in the manner of determination of consideration received by the company would lead to avoidable disputes. Also, such ambiguity presents a tax arbitrage opportunity to scale-up the consideration, particularly under a tax neutral business reorganisation followed by buy-back of shares.

Accordingly, Section 115QA was amended to provide that the provisions of this Section apply to any buy-back of unlisted share undertaken by the company in accordance with the Companies Act, and not necessarily restricted to Section 77A of the Companies Act, 1956. Further, for computing distributed income, the amount received by the Company in respect of the shares being bought back shall be determined in the prescribed manner.

Buy-back of shares rules

In view of the above amendment, the Central Board of Direct Taxes (CBDT) issued draft rules⁴ to prescribe the methodology for determination of the amount received by the companies under different circumstances in which the shares have been issued. The CBDT had invited comments and suggestions from various stakeholders on the draft rules.

Pursuant to comments received from the stakeholders, CBDT notified final rules⁵ for buy-back of shares. The rules came into effect from 1 June 2016. These rules prescribed the manner of determining the amount received by a company in respect of the share issued by it, being the subject matter of buy-back referred to in the Section 115QA, as follows:

1. This amendment was introduced with effect from 1999

2. A Ltd. [2012] 20 taxmann.com 52 (AAR)

3. Armstrong World Industries Mauritius Multiconsult Ltd. [2012] 210 Taxman 303 (AAR)

4. F No 370133/30/2016-TPL, dated 25 July 2016

5. Rule 40BB vide Notification No. 94/2016, dated 17 October 2016

- In the case of share issued by a company to any person by way of subscription, the amount including premium, actually received by the company.
- If the company, prior to the buy-back of the share, returned any sum out of the amount received in respect of such share, the amount as reduced by the sum so returned shall be the amount received by the company. However, if the company has paid the additional income tax under Section 115-O on the sum so returned, then such sum shall not be reduced.
- Where the shares are issued under an ESOP or as sweat equity shares, the fair market value of the share to the extent it is credited to the share capital and share premium account.
- In case of the shares issued under a scheme of amalgamation, in lieu of the shares of an amalgamating company, the amount received by the amalgamating company in respect of such shares.
- In case of the shares issued by a resulting company under a scheme of demerger, the amount which bears to the amount received by the demerged company in respect of the original shares determined in accordance with this rule, the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before such demerger.
- The amount received by the demerged company in respect of the original shares in the demerged company shall be deemed to have been reduced by the amount as so arrived under sub-rule (6) i.e. for the shares issued by a resulting company.
- With regards to the share issued as part of the consideration for the acquisition of any asset or settlement of any liability, the amount shall be determined in accordance with the prescribed formula. Similarly, in the case of shares issued on conversion of a firm into the company or succession of sole proprietary concern by the company, the amount shall be determined in accordance with the prescribed formula.
- Where the share has been issued without any consideration, on the basis of existing shareholding in the company, the consideration in respect of such share shall be deemed to be 'Nil'.
- Where the shares have been issued on conversion of preference shares or bond or debenture, debenture-stock or deposit certificate in any form or warrants or any other security issued by the company, the amount received by the company in respect of such instrument as so converted.
- Where the shares are held in dematerialised form, the amount received for the issue of the share determined in accordance with this rule on the basis of the first-in-first-out method.
- In any other case, the face value of the share.

Thus, the final rules on the buy-back of shares have provided the manner of determination of the amount in various circumstances including shares being issued under tax-neutral reorganisations and in different tranches.

Summing up

The provisions relating to buy-back of shares were introduced in the Act as an anti-tax avoidance measure. The Memorandum to the Finance Bill 2013, explained that unlisted companies bought back shares instead of payment of dividend. With this objective in mind, the rate of additional-tax on buy-back of shares should have been 15 per cent in line with the rate of DDT. Under Section 115-O, while computing DDT, the recipient holding company is allowed credit for dividends received, whereas similar provisions do not exist for buy-back of shares. Aligning both the tax rates and the conditions for taxability, would provide relief and bring confidence in the minds of investors. In the case of a foreign investor, the buy-back of shares is taxable as distribution tax, but it may still be liable to capital gain tax in the foreign jurisdiction. Since the additional tax is payable by the Indian company, the foreign investor is unable to take the credit of such tax, which leads to double taxation.

Overall, the final rules are in line with the government's efforts to bring in an environment of simplified tax regime and at the same time providing clarity to the taxpayers. The final rules have resolved many issues, which were not addressed in the draft rules for instance, issues pertaining to the issue of shares under ESOP or Sweat Equity shares, for the acquisition of an asset or settlement of the liability, on succession or conversion of a firm or proprietary concern by the company, conversion of preference shares, shares held in dematerialised form, etc. However, there are some aspects, which have not been addressed in the final rules for instance, a shareholder cannot take benefit of indexation on the cost of acquisition since the company has to pay tax on such distributed income without considering indexation. Further guidance may be needed to deal with the practical issues in the implementation of the rules.





Decisions

Consideration received by the foreign company for its e-platform for facilitating purchase and sale of products is not taxable in India

The taxpayer is resident of Switzerland and is engaged in the business of operating websites, which provide online platform for facilitating purchase and sale of products worldwide. During the years under consideration the taxpayer has operated in its India specific websites, viz., www.ebay.in and www.b2motors.ebay.in and they provided online platform for facilitating purchase and sale of goods and services to users based in India. Further the taxpayer has entered into marketing support agreements with two of its subsidiary companies, viz., M/s. e-Bay India Private Limited and M/s. e-Bay Motors Private Limited. These websites were operated from servers located outside India. The modus operandi of its operation was that it signs agreement with the Indian customers, who wish to list their products and services on their websites. For listing the products at prominent places, the taxpayer charged a listing fee. Besides the above, as and when transaction of sale was successfully completed, transaction fee was also charged by the taxpayer from the seller. No fee is charged from the buyers of the products/ services. The agreement for purchase and sale of goods is entered directly between the buyer and seller of the products/ services, i.e. the taxpayer never acquired any right or property in the goods sold.

The AO took the view that the taxpayer has business connection in India in terms of Section 9(1)(i) of the Act and accordingly took the view that the revenue generated by the taxpayer has accrued in India. The said revenue falls in the category of Fee for Technical Services (FTS) within the meaning of Section 9(1)(vii) of the Act and accordingly assessed the revenue generated by the taxpayer from listing as well as service charges earned on completion of transaction as FTS in all the three years under consideration.

The Tribunal relied on its earlier decision in the taxpayer's case where it was observed that:

- It is necessary to analyse whether the revenue received by the taxpayer is consideration for rendering managerial or technical or consultancy services.
- The term 'managerial services' refers to managing certain affairs, a quid pro quo for which will be described as FTS. The taxpayer becomes entitled to the user fee when there is a successful completion of sale between the buyer and seller through its website. The taxpayer's websites are analogous to a market place where the buyers and sellers assemble to transact. By providing a platform for doing business, the taxpayer can, by no standard, be considered as having rendered any managerial services either to the buyer or to the seller, for which it received fee from the seller.

- The products along with necessary details are displayed on its websites. Neither the buyer nor the seller is required to avail any technical service from the assessee so as to enter into transaction.
- There is no question of considering the fees received by the taxpayer as a consideration for rendering any 'consultancy services'. There is no point at which the taxpayer renders any consultancy, either to the buyer or to the seller, as regards the goods to be purchased or sold. It is neither open nor possible for the buyers to consult the taxpayer before making any decision as regards the product to be purchased by them.
- Accordingly, the fee received by the assessee from the sellers cannot be considered as a consideration for rendering managerial, technical or consultancy service within the meaning of Explanation 2 to Section 9(1)(vii) of the Act. The revenue was in the nature of business profits.
- With respect to Permanent Establishment (PE), it was held that the two subsidiary of taxpayer in India do not satisfy the conditions of Article 5 of the India-Switzerland tax treaty. Therefore, taxpayer did not have PE in India.

Relying on the above decision the Tribunal in the instant case held that the revenue earned by the taxpayer was not FTS in nature. Further the taxpayer was not having any PE in India.

DDIT v. E-BAY International AG (ITA No.699/Mum/2013) – TII

Even in the absence of a PAN, lower tax rate prescribed under the tax treaty will apply

The taxpayer made certain payments in the nature of FTS to non-residents. In view of tax treaties, tax at the lower rate as prescribed in the relevant Articles of the tax treaties was deducted by the taxpayer even in case of payees, who did not furnish a valid Permanent Account Number (PAN). While processing the Tax Deducted at Source (TDS) returns filed by the taxpayer, the taxpayer was held to be liable to deduct tax at source at a higher rate of 20 per cent in such cases for want of PAN of the concerned non-resident payees as per the provisions of Section 206AA of the Act. The Commissioner of Income-tax (Appeals) [CIT(A)] rejected the taxpayer's case and observed that Section 206AA inserted in the Act with effect from 1 April 2010 was an overriding provision and there was no escape for the taxpayer except to quote the deductee's PAN or to deduct tax at source at 20 per cent. It was held that a PAN was required to be quoted for making declaration under Section 197A of the Act for claiming exemption from TDS to be valid. It was also held that Section 206AA starting with non-obstante clause overrides all other sections including Section 90(2), Section 115A and Section 139A of the Act.

Keeping in view the conflicting decisions of the Bangalore Tribunal in the case of Bosch Limited⁶ and the Pune Tribunal in the case of Serum Institute of India Limited⁷, a reference was made to constitute a Special Bench to decide the issue and resolve the controversy.

The Special Bench of the Tribunal observed that Section 206AA of the Act falls in Chapter XVII –B dealing with tax deduction at source, it follows that the treaty provisions which override even the charging provision of the domestic law by virtue of Section 90(2) of the Act would also override the machinery provisions of Section 206AA of the Act irrespective of non-obstante clause contained therein and the same is required to be restricted to that extent and read down to give effect to the relevant provisions of tax treaties, which are overriding being beneficial to the taxpayer.

To apply the non-obstante provisions under Section 206AA of the Act, Section 90 of the Act should have

Specifically provided to give an overriding effect of Section 206AA of the Act over Section 90(2) of the Act, which clearly shows the intention of the Legislature is not to give overriding effect of Section 206AA of the Act over the provisions of the relevant tax treaty. Further, it was also observed that the Finance Act, 2013 introduced Section 90(2A) to have an overriding effect of Section 95 [General Anti-Avoidance Rules (GAAR)] even if these provisions are not beneficial to the taxpayer.

In view of above, the Special Bench of the Tribunal held that the provisions of Section 206AA of the Act will not have an overriding effect on the provisions of the tax treaty. The provisions of tax treaty to the extent they are beneficial to the taxpayer will override Section 206AA of the Act by virtue of Section 90(2) of the Act.

Nagarjuna Fertilizers and Chemicals Limited v. ACIT (ITA No. 1187/H/2014, AY 2011-2012) (SB)

Notifications/Circulars/Press Releases

CBDT circular on POEM

On 24 January 2017, CBDT (vide Circular no.6/2017) issued guiding principles for determining Place of Effective Management (POEM) of a company. Simultaneously, CBDT also issued a press release stating that POEM guidelines shall not apply to a company having turnover or gross receipts of INR50 crore or less in a financial year.

The CBDT recently issued a Circular no. 8/2017 clarifying that the existing provisions of Section 6(3)(ii) of the Act, shall not apply to a company having turnover or gross receipts of INR50 crore or less in a financial year.

CBDT Circular No. 06/2017, dated 24 January 2017

Government notifies protocol to the India-Israel tax treaty

India has entered into a tax treaty with Israel on 29 January 1996. On 14 October 2015, the Protocol amending the India-Israel tax treaty was signed. The government vide notification no. 10/2017 has notified the Protocol amending the existing tax treaty. Key features of the protocol are summarised as follows:

- The Protocol introduces Limitation of Benefits (LOB) Article which provides that tax treaty benefit will not be available to a resident of a contracting state or with respect to any transaction undertaken by such resident, if the main purpose or one of the main purposes of the creation or existence of such resident or of the transaction undertaken by it, was to obtain benefits of this tax treaty that would not otherwise be available. The LOB Article permits application of domestic GAAR dealing with prevention of tax evasion or tax avoidance. It also introduces 'beneficial ownership' test for availing tax treaty benefits.
- The Protocol removes tax credit available under Article 24 (Elimination of Double Taxation) which provides for 15 per cent tax credit on dividend and 10 per cent tax credit on interest income.
- The existing Most Favoured Nation (MFN) clauses dealing with royalties, FTS, interest, dividend and tax rate of PE have been omitted.
- The Capital Gains Article amended to provide that gains derived by a resident of a contracting state from the alienation of: a) shares, deriving more than 50 per cent of their value directly or indirectly from immovable property situated in the other state (at the time of alienation or at any time during the twelve preceding months) or b) an interest in a partnership, trust or other entity, deriving more than 50 per cent of its value directly or indirectly from immovable property situated in that other state (at the time of alienation or at any time during the twelve preceding months); may be taxed in that other State.
- The Protocol provides for internationally accepted standards for effective exchange of information on tax matters including information held by the bank.
- In India, the Protocol comes into effect from 1 April 2017 i.e. fiscal year beginning on or after the first day of April next following the date on which the said Protocol enters into force.⁸

Notification No. 10/2017 F. No. 500/14/2004-FTD-II

6. BOSCH Ltd. v ITO [2013] 115 TTJ 354 (Bang)

7. DDT v. Serum Institute of India Limited [2015] 68 SOT 254 (Pune)

8. The Protocol has entered into force on 19 December 2016



Decisions

Retainership payments to independent professionals constitute 'salaries' and hence withholding of tax under Section 192 of the Act is applicable

The taxpayer was engaged in the business of film production. During the Financial Year (FY) 2004-05, the taxpayer paid remuneration to various persons pursuant to the service contract agreement. In terms of the agreement, the compensation paid to the persons was termed as 'retainership fee' and the taxpayer deducted tax under Section 194J of the Act on these payments on the ground that these persons were independent professionals and amount paid to them was in the nature of 'fee'. The AO observed that there existed employer-employee relationship between the taxpayer and these persons and hence the taxpayer was required to deduct tax under Section 192 of the Act. Accordingly, the AO worked out the amount of INR3 lakh for shortfall in deducting tax under Section 192 of the Act. The CIT(A) upheld the order of the AO.

Tribunal's ruling

Withholding of tax under Section 192 of the Act

The Tribunal observed that independent professionals are engaged in specific assignments/jobs whereas employees are assigned with the duties which are not feasible to be defined in specific terms in advance. On a perusal of the service contract, the case was different. There was no variation clause or escalation clause indicating that remuneration shall be increased or decreased depending upon the quantum of work. The Tribunal observed that certain perks have been provided to the persons as are generally provided in the case of an employee. These perks also indicated that persons were engaged on full time basis and that is why the taxpayer was pleased to provide these facilities. The persons were required to attend office on daily basis to perform the duties as may be assigned from time to time by the taxpayer, and were also provided with leaves of around 30 days in a year. These types of terms are kept in the case of employees only and not in the case of independent professionals. The 'termination of employment' clause, shows that this contract was drafted keeping in view the relationship of employer-employee. Thus, there existed an employer-employee relationship between persons and the taxpayer. Accordingly, the taxpayer was liable to deduct tax under Section 192 of the Act since remuneration paid to them constituted salary.

Red Chillies Entertainment Pvt. Ltd. v. ACIT (ITA No.6655/Mum/2014) – Taxsutra.com

Tax payable under voluntary disclosure scheme is a different from normal tax and hence benefit of TDS paid under the Act cannot be availed to adjust the tax payable under the voluntary disclosure scheme

The taxpayer was incorporated in the year 1991. During the relevant AYs⁹, the taxpayer had not filed its return of income in spite of having income by way of rent and interest chargeable to

tax. Therefore, on promulgation of the Scheme of 1997 Act, the taxpayer made a declaration of its undisclosed income in the prescribed form on 31 December 1997. In terms of the Scheme of 1997 Act, the taxpayer opted to pay the tax within three months of the filing of the declaration along with interest as provided thereon. The taxpayer claimed that the rent/interest income had already suffered tax under the Act in the form of TDS and therefore, the TDS being also a payment of tax, should be given credit so as to determine the tax payable on the declared undisclosed income under the Scheme of 1997 Act. The AO rejected the taxpayer's request that credit for TDS should be given.

High Court ruling

It has been observed that if the charge is different, then the tax paid under the Scheme of 1997 is not tax under the Act. Consequently, TDS under the Act is not the tax payable under the Scheme of 1997 Act. Therefore, it cannot be taken into account to determine the tax payable under the Scheme. The Scheme is a part of the Finance Act, 1997 and it is self-contained. The Scheme of 1997 Act is a different and distinct statute from the Act. Therefore, even though the tax which is payable under the Scheme of 1997 Act, is a tax on income, it is not a charge to tax under Section 4 of the 1961 Act, but an income tax charged to tax under Section 64 of the Scheme of 1997 Act.

The person is qualified to avail of the voluntary disclosure scheme only if the person voluntarily discloses undisclosed income on which tax has not been paid for any AY. It has no nexus/connection to bring income of the previous year which a person is liable to tax, is obliged to disclose as under Section 4 of the 1961 Act. Therefore, the benefit of TDS under the Act cannot be availed to adjust the tax payable under the Voluntary Disclosure of Income and Wealth Tax, 1976. The tax payable under the Scheme of 1997 Act is indeed a 'different animal' from the tax payable under the 1961 Act. Therefore, the tax deducted at source and/or any other mode of payment of tax under the 1961 Act cannot be used to discharge the obligation to pay tax under the Scheme of 1997 Act on the disclosure of undisclosed income.

Earnest Business Services Pvt. Ltd v. CIT (Writ Petition No. 616 of 1998) – Taxsutra.com

Disallowance under Section 14A is applicable on the expenditure on strategic investments

During AYs 2011-12 and 2012-13, AO made disallowance under Section 14A of the Act. The taxpayer claimed that since investment was made in subsidiary/associate companies being held for the purpose of its business, disallowance under Section 14A of the Act cannot be made. Rejecting the taxpayer's stand, AO invoked Rule 8D(iii) of

9. 1995-96, 1996-97 and 1997-98

the Rules and made disallowance for indirect expenditure. The CIT(A) upheld the disallowance made by the AO.

The Tribunal observed that Section 14A of the Act mandates disallowance of any expenditure in relation to income not forming part of the total income, and does not concern itself with the character of such income. In the present case, dividend income, though bearing the character of business income, would fall under Chapter III of the Act since it satisfies the qualifying condition of Section 14A of the Act. Accordingly, the holding of the asset/property under reference either as an investment or as stock-in-trade becomes inconsequential or irrelevant. The disallowance being independent of the head or the nature of the income arising there-from, and the only thing relevant is if it is tax-exempt. Investments forming part of the taxpayer's stock-in-trade does not preclude application of Section 14A of the Act, investments made for business.

With respect to indirect expenditure disallowance as per Rule 8D(iii) of the Rules, the Tribunal rejected the taxpayer's stand that no expenditure was incurred for strategic investments. The considerations for making investment in an associate/subsidiary company may be different from that which obtain for an 'outside' company. In fact, laying down the policies, and undertaking activities with the stated object of pursuing the policies, is the task of the top management of a company, entailing expenditure, which generally percolates down to its lower echelons as well.

Voltech Engineers P. Ltd. v. DCIT (ITA. Nos.1801 & 1765/Mds/2016) – Taxsutra.com

Since carbon credits are neither being sold or transferred in the year under consideration, the same cannot be considered as income for the purpose of tax

The taxpayer is engaged in the business of manufacturing of transmission line towers and steel structures, commissioning of transmission line tower and supply of transmission and distribution line material. During AY2009-10, the AO brought to tax carbon credit on the ground that the amount was receivable. On appeal, CIT(A) reversed AO's order. The Tribunal confirmed CIT(A)'s order holding that since sale of carbon credits/Certified Emission Reductions (CERs) was not transferred/sold in subject AY, the same was not taxable.

The High Court observed that the issue whether the amount could be said to be accrued and/or would be required to be included in the income of the taxpayer and in which year is no more res integra. The High Court referred to the Supreme Court's decision in the case of CIT v. Excel Industries Limited [2013] 358 ITR 295 (SC). Applying the 'accrual' principles laid down by Supreme Court in aforesaid case, the High Court held that the carbon receipts were neither sold nor transferred in favour of foreign companies in the year under consideration, the same cannot be included as receipt/income in the year under consideration.

Pr. CIT v. Kalpataru Power Transmission Ltd (Tax Appeal No. 141 of 2017) – Taxsutra.com

Notifications/Circulars/Press Releases

CBDT issues a standard operating procedure for assessing officers while verifying cash transactions relating to demonetisation

In the recent past, litigation in service related matters including disciplinary matters have seen an inordinate increase. The number of Court cases including appeals in High Courts and Supreme Court are rising steadily. Many of these cases are lost in Court as either the tax department is unable to project the facts involved before the court properly and/or because there is an inordinate delay in filing of appeal or the Government's response. The CBDT is deeply concerned about the delay and quality of representations, including briefs given to the departmental counsels.

Recently, the CBDT has issued an instruction providing a Standard Operating Procedure (SOP) for effective, efficient and time bound handling of the cases of service litigation. The CBDT instructed that all the field authorities should meticulously observe the prescribed guidelines within stipulated time limits as mentioned in the SOP.

CBDT Instruction No.3, dated 21 February 2017

CBDT issues notification on disclosure of information in accordance with Section 138(1) of the Act

On 23 May 2003, CBDT issued a notification no. 137 under Section 138(2) of the Act. The Notification prohibited providing information/record/document to any person or authority by the income tax authorities. However, two exceptions were mentioned where the information can be made available. The first exception pertained to providing information by DGIT (Systems) in respect of records or data related to PAN, tax deduction account number and computerisation of income-tax records of taxpayers. The second exception was related to disclosure of information in accordance with notifications issued under Section 138 of the Act from time to time.

The said notification was issued under Section 138(2), which starts with a non-obstante clause, the implication appeared to be that the information could be provided only to the authorities/persons which are so notified under Section 138(1) (a)(ii) of the Act by the central government while disclosure of information under Section(s) 138(1)(a)(i) and Section 138(1)(b) of the Act was prohibited. Therefore, an apprehension was raised by some of the stakeholders that the said notification puts restriction on the powers of the authorities mentioned in sub-sections (1)(a)(i) and (1)(b) of Section 138 of the Act, thereby, making these provisions virtually redundant.

Therefore, in order to remove any ambiguity in interpretation of the said notification, central government, with retrospective date (23 May 2003), has decided to clarify that clause (ii) of the proviso in the Notification No. 137 would mean the disclosure of any information in accordance with the provisions of Section 138(1) from time to time.

CBDT Notification No. 12/2017, dated 21 February 2017

Transfer pricing



Decisions

Penalty for concealment of income is to be deleted even though adjustment made by TPO is accepted by the taxpayer

- The taxpayer, a subsidiary of Mitsui Chemicals Inc., engaged in the manufacturing business. During the year under consideration, the Transfer Pricing Officer (TPO) held that the taxpayer did not avail any services for which payment was made to Associated Enterprises (AEs) and that no benefit was shown to have been received from AEs. The TPO held that it was a case of duplication of services and determined the Arm's Length Price (ALP) of the three international transactions of availing of specified business and consultancy services, engineering support services and management support services at 'Nil' applying the Comparable Uncontrolled Price (CUP) method.
- The AO, rejected the taxpayer's claim that the Transactional Net Margin Method (TNMM) was applicable and instead imposed CUP method under Section 92CA of the Act.
- Against the assessment order, the taxpayer did not file an appeal. However, AO initiated penalty proceedings premised upon the understanding that an adverse order under Section 92C attracted the 7th Explanation to Section 271(1)(c) of the Act. The AO opined that the explanation offered by the taxpayer was not satisfactory and did not display good faith which was a prerequisite under the 7th Explanation of section 271(1)(c).

High Court's ruling

- Tribunal's order has elaborately dealt with the rationale of rejecting AO's imposition of penalty. The view taken by the Tribunal does not in any manner deviate against the Explanation of Section 271(1)(c).
- Rejected tax department's contention that the taxpayer failed to disclose the benefits and advantages they had derived from the services and that its failure resulted not only in rejection of TNMM but also reduction of losses, which warranted the application of Explanation 7 of Section 271(1)(c).
- Considering that the taxpayer's claim was in respect of a new line of business of manufacturing, introduced for the first time in the given year, its failure per se could not have triggered the automatic presumptive application of Explanation of Section 271(1)(c) as perceived by the revenue authorities.
- The application of the exception has to be based upon the facts of each case and no generalisation can be made.

Delhi High Court in the case of Pr. CIT vs Mitsui Prime Advanced Composites India Pvt. Ltd. (ITA 913/2016, CM APPL.46519/2016)

Sales to two customers which constitutes more than 20 per cent of total sales of the taxpayer shall constitute 'dominant influence'; AE relationship upheld

- The taxpayer, subsidiary of Hospira Pte, Singapore, is incorporated by acquiring the generic injectable pharmaceuticals business of M/s. Orchid Chemicals & Pharmaceuticals Ltd (Orchid India) as a going concern on slump sale basis. The agreements entered into by Orchid India and various Distribution Partners (DPs) were inherited by the taxpayer termed as legacy agreements. The business model of the taxpayer with its DPs is on profit sharing basis.
- The TPO proposed adjustment on account of deficiency in pricing of supplies to Hospira Group; Profit shared on sale on the pharma products with its AEs and interest paid by the AE on the Inter Corporate Convertible Debentures (ICCD) issued by the taxpayer to its AE.
- While proposing these adjustments, the TPO concluded that Apotex Corp and Apotex Inc. Signet (DPs) as AEs, by relying on the settlement commission order of Orchid India for Assessment Years (AYs) 2006-07 to 2010-11.

Tribunal's ruling

- The Tribunal relied on the ruling of Orchid Pharma Limited for interpreting section 92A(2)(i) of the Act, from which it is understood that 92A(2)(i) envisages a dominant influence, which automatically leads to a de facto control over the enterprise.
- The Tribunal held that as per Sec 92A(2)(i) influence implies dominant influence where 'a person who purchased more than 1/5th of the total sales of the taxpayer would have a distinctly dominant influence on the pricing and can exercise a de facto control'.
- More than 20 per cent of the taxpayer's sales are to Apotex entities, which creates a dominant influence on the taxpayer by Apotex entities. The Tribunal held that Apotex entities are considered as AEs of the taxpayer.
- With regard to the profit share of 60:40 determined by the lower authorities relying on the settlement commission order of Orchid India, the Tribunal held as follows:
 - The lower authorities erred in determination of the profit share by merely relying on the settlement commission order without analysing the facts and circumstances of the taxpayer.
 - Further, Rule 10B(d) of the Income-tax Rules, 1962 (the Rules) is not properly applied by the lower authorities

10. Orchid Pharma Limited vs DCIT (ITA No. 771/Mds/2016 - AY 2011-12)

while determining the profit share between the taxpayer and DPs.

- Thus, the Tribunal set aside the orders of lower authorities in relation to determination of profit share, deficiency in pricing of supplies to Hospira Group and interest paid on ICCDs and accordingly, remanded the same back to the AO/TPO for fresh consideration.

Chennai Tribunal in the case of Hospira Healthcare India Private Limited vs DCIT (ITA No. 821/Mds/2016 - AY 2011-12)

Notifications/Circulars/Press Releases

Rollback provision applicable for bilateral APAs between India and Korea

The tax treaty between India and Korea was revised with effect from 12 September 2016, to incorporate para 2 in

Article 9, which provides recourse to the taxpayers to apply for Mutual Agreement Procedure in transfer pricing disputes as well as for bilateral Advance Pricing Agreements (APAs).

In respect of Article 9(2) of the revised tax treaty between India-Korea, CBDT clarified that bilateral APA applications under India-Korea tax treaty can be filed along with request for rollback in prescribed form for APA period beginning FY 2017-18, which shall be processed in accordance with provisions of Section 92CC(9A) of the Act and the applicable rules. Further, the inclusion of rollback provision in such bilateral APAs would be subject to applicable regulations in Korea.

CBDT press release dated 17 March 2017





Service tax - Decisions

Provision of security guards by State Board to industries is not 'statutory function' and liable to Service tax

In the instant case, the Mumbai Tribunal dealt with the issue whether the activity of providing security guards by a State Welfare Board (which was a statutory body established under a State enactment) to industries would constitute 'statutory function' and therefore not be liable to Service tax.

The Mumbai Tribunal observed that the expenses and salaries of the Board were not charged to the Consolidated Fund of India or paid by the state government. Therefore, the said activity does not qualify as 'sovereign/statutory function' and accordingly, the charges collected by the Board would be liable to Service tax.

Security Guards for greater Bombay and Thane District v. Commissioner of Central Excise, Thane II, TS-593-CESTAT-2016(Mum)-ST-SGB

Notifications/Circulars/Press Releases

No Service tax on services of Common Effluent Treatment Plant and admission to museum

The central government has directed that Service tax is not required to be paid on services provided by operator of Common Effluent Treatment Plant and services by way of admission to a museum for the period 1 July 2012 to 31 March 2015.

Notification No. 8/2017- Service Tax dated 20 February 2017 and Notification No. 9/2017- Service Tax dated 28 February 2017

Service tax exemption only on specified services rendered to pre-school/ higher secondary schools

The scope of Service tax exemption on specified services provided to educational institutions (such as transportation of students, catering, security, services relating to admission or conduct of examination, etc.) has been amended to provide that such exemption would be available only if the services are provided to institutions providing pre-school and upto higher secondary education or equivalent.

Notification No. 10/2017- Service Tax dated 8 March 2017

Central Excise - Decisions

CENVAT credit cannot be rejected on the ground that invoices are in the name of head office

In the present case, the Show Cause Notice was issued alleging that CENVAT credit is not eligible in cases, where the invoices was issued in the name of the head office of the company.

The taxpayer submitted that, the goods were used in the manufacture by the unit and accordingly eligible for the

credit. However, Revenue raised doubts on use of goods in manufacture activity and receipt of such goods in the factory.

In this background, the Madras Tribunal observed that, mere exhibition of the name of the taxpayer's Head Office address on the invoice shall not disentitle from availment of CENVAT credit. It may be appreciated that the basic rule of allowance of CENVAT credit is that input should have been received in the factory and used in the manufacture. The said aspect is not being questioned in the present appeal and therefore, taxpayer is entitled to CENVAT credit of the goods in question.

Shobikaa Impex Pvt Ltd vs CCE (2017-TIOL-829-CESTAT-MAD)

Eligibility of CENVAT credit on inputs when value was shown as written off in their books of account

The taxpayer has availed CENVAT credit for the inputs, the value of which has been written off, under the category of 'Other income', in their books of accounts. A demand notice was issued alleging that since the value of the inputs has been written off, accordingly, in view of the CBEC's Circular dated 22 February 1995, the credit on the said inputs was recoverable with penalty.

On adjudication, the demand was confirmed with equal amount of penalty. Aggrieved by the said order, the taxpayer filed the appeal before the learned Commissioner (Appeals), who in turn, rejected their appeal. Hence, the present appeal was filed before the Ahmedabad Tribunal.

The taxpayer submitted that the value of the inputs was written off in their books of accounts for the sole reason that the said amount was not intended to be paid to the supplier of the inputs and it is not because the inputs could not be used. Further, in case their inputs were treated as unusable or destroyed, the value would have written off by reflecting it on expenditure side of the profit and loss account and not as an income. The taxpayer submitted that they have complied with the condition of CENVAT Credit Rules, 2004, therefore, CENVAT credit cannot be denied to them.

In this background, the CESTAT held that once the quantity of inputs received in the factory are used in or in relation to manufacture of final product on payment of duty, CENVAT credit cannot be denied.

Trichem Enterprises Pvt Ltd vs CCE (2017-TIOL-540-CESTAT-AHM)

Duty on quality control samples cannot be demanded, when the record of control samples is maintained

In the present case, the taxpayer is engaged in the manufacture of excisable goods, namely, bournvita, drinking chocolate and flavoured chocolate falling under Chapter No. 18 of Central Excise Tariff Act 1985.

The department, on investigation found that the taxpayer is drawing excisable goods as quality control samples and no duty was paid on such quality control samples. Accordingly,

a Show-Cause Notice was issued demanding Excise duty on the quality control samples. The adjudicating authority has confirmed the demand, which was upheld by the learned Commissioner (Appeals). Hence, the present appeal is filed before the Mumbai Tribunal.

The taxpayer submitted that the issue whether the quality control samples are liable for Excise duty has been settled by the Larger Bench of this Tribunal in the case of Dabur India Ltd (2005-TIOL-171-CESTAT-DEL-LB). Further, the taxpayer submitted that the demand was raised on the basis of the record of quality control samples maintained by the taxpayer only. Therefore, there is no dispute that the record of the samples have been maintained and the same was relied upon in the show-cause notice.

In this background, the Mumbai Tribunal observed that the entire demand was raised on the basis of the record of the control samples maintained by the taxpayer and the Excise duty was also quantified from the said records, taking the quantity of control samples drawn from the production. Therefore, there is no dispute that the taxpayer have been maintaining records of control samples. The Larger Bench judgment is directly applicable in the facts of the present case. Accordingly, Excise duty is not chargeable on the control samples drawn by the taxpayer and accordingly, appeal was allowed.

Shree Warana Sahakari Dudh Utpadak Prakriya Sangh Ltd v. CCE [2017-TIOL-704-CESTAT-MUM]

Notifications/Circulars/Press Releases

Master Circular on Show Cause Notice, Adjudication and Recovery

The CBEC issued a Master Circular on the subject namely, show cause notices, adjudication proceedings and recovery to compile relevant legal and statutory provisions, circulars of the past and to rescind circulars, which have lost relevance. Annexure-I to the circular provides list of the eighty nine circulars which stand rescinded. Three circulars listed in Annexure-II have not been rescinded as they contain comprehensive instructions on the subject they address.

The Master Circular is divided into four parts namely, Show Cause Notice related issues, adjudication proceedings, closure of proceedings and recovery of duty and miscellaneous issues. The provisions of the Master Circular shall have overriding effect on the CBEC's Excise Manual of Supplementary Instructions to the extent they are in conflict.

Circular No 1053/02/2017 – CX dated 10 March 2017

Custom duty Notifications/Circulars/Press Releases

Exemption from drawal of samples for the purpose of grant of drawback to the AEO certificate holders

Exporters, who have been accorded 'Authorised Economic Operator (AEO)' certificate (Tier II & Tier III) in terms of

Circular No. 33/2016-Customs dated 22.07.2016 are now being exempted from the requirements of drawal of samples for the purpose of grant of Duty drawback, except in case of any specific information or intelligence.

Circular No 5/2017 – CX dated 28 February 2017

Acceptance of e-BRC of DGFT towards proof of realization of sale proceeds for exports with LEO date upto 31 March 2014 under Duty Drawback Scheme

As per CBEC circular no. 5/2009-Cus dated 2 February 2009, Bank Realization Certificate (BRC) may be submitted to customs authorities as proof of realisation of sale proceeds. Further, for exports with LEO date from 1 April 2014 onwards, an electronic system of reconciliation of sale proceeds (RBI-BRC module) is made functional by DG (Systems) in coordination with Reserve Bank of India (RBI).

In this regard, the issue of non-acceptance of e-BRC of DGFT by field formations cropped up since, it contains 'realised value' details but does not contain details of commission, freight, insurance etc. which are relevant for duty drawback purpose.

In light of the above, the Board has decided that for exports with LEO dates 12 August 2012 onwards till 31 March 2014, DGFT's e-BRC would be accepted, except in case of specific intelligence or information of misuse. This shall be subject to appropriate declaration by the exporter on back of DGFT e-BRC.

Circular No 6/2017 – CX dated 28 February 2017

Foreign Trade Policy – Public Notice

Amendment in procedure for seeking modification in IEC

When an IEC holder seeks modification/change of Head Office/Registered Office address in its IEC and which involves a shift in its jurisdictional RA, a request to that effect will have to be made to the new RA, to whose jurisdiction the applicant is shifting its office. The new RA shall make appropriate amendments, based on documents submitted to it by the applicant.

The new RA will also separately inform the RA, who had initially issued the IEC, of the changes made in the concerned IEC. Thereafter, the new RA shall allow the applicant to carry out necessary functions and also apply for eligible benefits as per FTP through its office.

Public Notice 59/2015 – 20 dated 21 February 2017

Harmonising MEIS schedule with Indian Trade Classification -Harmonised System (ITC – HS)

The Directorate General of Foreign Trade notified ITC (HS) - 2017 vide notification no. 36/2015-2020 dated 17 January 2017.

In pursuance to the above, DGFT re-notified MEIS Schedule, which showed the existing HS Codes, their description and rates of MEIS applicable with corresponding 2017 HS Codes and description of goods/products. The MEIS Schedule as per ITC (HS) 2017 would be effective for shipments made with effect from 1 January 2017.

Public Notice 61/2015 – 20 dated 7 March 2017

VAT - Decisions

Purchasing dealer cannot be denied benefit of input tax credit on purchases made against tax invoice, on the ground that the selling dealer's registration is cancelled or his transactions with other parties are doubtful

In the present case, VAT officer disallowed the input tax credit claimed by the taxpayer, who is a registered dealer, in respect of purchases made against tax invoices issued by selling dealers, for the assessment period 2007-08. Such credit was disallowed with the rationale that the selling firm's registration has been cancelled and the condition stipulated for claiming tax credit in Section 9(2) (g) of the Delhi VAT Act, 2004 (DVAT Act) has not been fulfilled.

The taxpayer approached VAT Tribunal, which analysed the provision Section 9(2) of DVAT Act, following the decision of Delhi High Court in Shanti Kiran India Pvt. Ltd. Vs. Commissioner Trade and Tax Department 2013. In case of Shanti Kiran India Pvt. Ltd., it was observed that section 9(1) of DVAT Act grants input tax credit to the purchasing dealers. Further, Section 9(2) of the said Act, lists out specific situations where the benefit is denied. The negative list, is restrictive and is in the nature of a proviso. It was also observed that, the interpretation of the said section that, the statutory authority for granting input credit is only to the extent tax is deposited by the selling dealer, is unsound and contrary to the statute. Further, the Delhi High Court also observed that, in the absence of any mechanism enabling a purchasing dealer to verify if the selling dealer deposited tax, for the period in question, and in the absence of notification in a manner that can be ascertained by men in business that a dealer's registration is cancelled the benefit of input credit, under Section 9(1) of the DVAT Act cannot be denied to the purchasing dealer.

Relying on the above case law, the Tribunal decided the matter in favour of the taxpayer. However, VAT department filed an appeal challenging the Tribunal's order on the basis of substantial question of law as to the correct interpretation of Section 9(2)(g) of the DVAT Act.

The Delhi High Court held that in view of the enunciation of law, which was followed by the Tribunal, the question of law does not arise, as it stands settled by the Division Bench in Shanti Kiran case. Accordingly, the appeal filed by the VAT department stands dismissed.

The Commissioner Department of Trade and Taxes Government of NCT Vs M/s K Steel Trader – Delhi HC

Notifications/Circulars/Press Release

Maharashtra

Circular has been issued prescribing various procedures to facilitate in respect of following matters:

- To claim deduction on account of goods return, rate difference and discount under MVAT law and CST Act
- Dealers getting error message while filing return in Form 232, to choose the combination of Form 233 CST to file their returns
- Waiver of late fee in connection to the dealers, who have paid taxes within due dates and submitted the returns for monthly return periods from April 2016 to February 2017 and quarterly returns for the period April 2016 to June 2016 and July 2016 to September 2016, on or before 31 March 2017
- Present process of refund application in Form e-501 for dealers registered before 25 May 2016 shall continue for return period upto 31 March 2016 and for the return period from April 2016, new application of refund is based upon the invoice wise annexures of sales and purchases. Further, for dealers registered after 25 May 2016, refund application shall be filed under New Automation system
- In case of obtaining e-CST declarations for dealers registered after May 25, 2016 in connection to returns for period from April 2016, application for e-CST forms will get auto generated from purchase annexure and further, in case of sales under section 6(2) of CST Act, transactions mentioned in sales annexure will be used to create requisition for CST forms.

Trade Circular No. 8T of 2017 Dated 16 March 2017

Personal tax



Notifications/Circulars/Press Releases

India's Social Security Agreement with Portugal to come into effect from 8 May 2017

The Social Security Agreement (SSA) between India and Portugal was signed on 4 March 2013. The Ministry of External Affairs issued a press release¹¹ notifying that the SSA between India and Portugal will come into effect from 8 May 2017.

This SSA has advantages for employees who are posted by their employer in another country. The India- Portugal SSA is the eighteenth SSA to come into effect.

The countries with which India already have effective SSAs are Belgium, Germany, Switzerland, Denmark, Luxembourg, France, Republic of Korea, Netherlands, Hungary, Finland, Sweden, Czech Republic, Norway, Austria, Canada, Australia and Japan.

Key potential benefits under the India- Portugal SSA

- Exemption from social security contribution in the host country
- Totalisation of contributory periods
- Export of benefits

http://mea.gov.in/pressreleases.htm?dtl/28078/India_Portugal_Social_Security_Agreement



11. http://mea.gov.in/press-releases.htm?dtl/28078/India_Portugal_Social_Security_Agreement

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