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India tax konnect

January 2021

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Contents

Direct Tax

CBDT notifies the Faceless Penalty Scheme, 2021

On 12 January 2021, the CBDT notified[1] the Faceless Penalty Scheme, 2021 to facilitate the conduct of faceless penalty proceedings.

The Scheme specifies setting up of national faceless penalty centres (NFPC), regional faceless penalty centres, penalty units and penalty review units for the execution of penalty proceedings. All internal communication between units and communication with taxpayers will be done via electronic mode i.e. either via email or through a mobile app. Physical hearing will be allowed only in specified circumstances.

Appeals against penalty orders made by NFPCs under this Scheme will lie before the Commissioner (Appeals) having jurisdiction over the jurisdictional income-tax authority or before the National Faceless Appeal Centre.

Decisions

Provisions of Section 56(2)(vii) are not applicable on receipt of bonus shares

The Karnataka High Court[2] dealt with the applicability of Section 56(2)(vii) on receipt of bonus shares by a shareholder of a private limited company. The High Court held that the issuance of bonus shares does not involve any inflow of funds or increase in the capital structure of the company. It merely involves capitalisation of existing reserves. Further bonus shares do not enrich the shareholder. Profit derived by the taxpayer on account of receipt of bonus shares is adjusted by depreciation in value of equity shares held by him. Therefore, the provisions of Section 56(2)(vii) are not applicable on receipt of bonus shares by the taxpayer. The High Court also observed that the bonus shares were not issued in order to evade any tax.

Payments for grant of distribution rights of channels are not taxable as royalty or FTS under the India-USA tax treaty

The ITAT (Mumbai Bench)[3] dealt with the issue of taxability of distribution rights of channels granted by a foreign media company to an Indian entity. The Tribunal held that the distribution rights granted by the taxpayer to the Indian entity is only a commercial right/broadcast reproduction right and not a copyright and consequently consideration for the same cannot be treated as royalty or Fees for Included Services (FIS or FTS) under Article 12 of the India-USA tax treaty. The Tribunal observed that the technical explanation of the India-USA tax treaty issued by the tax authorities of USA was not an official protocol or clarification which has been mutually

[1] CBDT Notification Nos. 2 and 3/2021, dated 12 January 2021

[2] PCIT v. Dr. Ranjan Pai [ITA No. 501/Kar2016]

[3] NGC Network Asia LLC v. DDIT [ITA No. 8671/Mum/2004]

agreed upon between the two countries. Hence, the said technical explanation would not bind the Tribunal.

Consultancy services are not taxable as FTS in view of MFN clause under the India-Sweden tax treaty

The ITAT (Mumbai Bench)[4] held that in view of the Most Favoured Nation (MFN) clause under the India-Sweden tax treaty, the restricted scope i.e. 'make available' clause provided under Article 12(4)(b) of the India-Portuguese tax treaty would apply to the India-Sweden tax treaty. Therefore, the consultancy services provided by the taxpayer to an Indian entity are not taxable as FTS in India.

Transfer of partnership interest between two non-residents is not taxable in India as the value of Indian assets was not substantial

The AAR[5] dealt with the issue of taxability of indirect transfer of assets situated in India on transfer of partnership interest in a US based partnership firm (having 3 subsidiaries in India). The interest in the US based partnership firm was transferred by the taxpayer (another US based partnership firm) to a US based company. The AAR held that such transfer is not taxable in India under Section 9(1)(i) as the fair value of the Indian subsidiary i.e. assets situated in India was not substantial. It was 20.4 per cent of total assets of the US based partnership firm, which is less than 50 per cent. The AAR observed that during 2012 to 2016, the word 'substantially' appearing in Explanation 5 was not defined in the Act. However, Courts in various cases[6] have held that 'substantially' would mean at least 50 per cent. Subsequently, this position was clarified by introducing Explanation 6 in Section 9. Accordingly, the AAR held that the Explanation 6 is clarificatory in nature and would apply retrospectively. However, the AAR kept the valuation under the Income-tax Rules open for the Revenue to check if the percentage of value of assets derived from India exceeded 50 per cent of the firm's total assets. The AAR observed that ruling would not bind the tax department if assets in India contributed to more than 50 per cent of the value of firm's total assets.

CBDT Press Release/ Notification/Circulars

- On 30 December 2020, the government issued a press release[7] providing further time to taxpayers to furnish tax returns, Tax Audit Reports and declaration and orders under Vivad Se Vishwas Scheme. The due date for furnishing tax returns for the AY 2020-21 for the taxpayers (including their partners) who are required to get their accounts audited and companies [for whom the due date was 31 October 2020 and which was extended to 30 November, 2020 and then to 31 January 2021] and for the taxpayers who are required to furnish report in respect of international/specified domestic transactions has been further extended to 15 February 2021. The date for passing of order or issuance of notice by the authorities under direct tax laws has been extended to 31 March 2021.

- On 11 January 2021, CBDT issued an Order[8] rejecting representations for further extension of the due date since the due dates for filing of return/tax audit had already been extended on three occasions. Further, the Order noted that the extension provided by India is more generous as compared to other countries. Any further extension would adversely affect the return filing

[4] SCA Hygiene Products AB v. DCIT [ITA No. 7315/Mum/2018]
[5] BV Holdings (USA) LLC [AAR No. 1402/2012]
[6] DIT v. Copal Research Limited [2014] 371 ITR 115 (Del), GEA Refrigeration Technologies GmbH [2018] 401 ITR 115 (AAR) and Banca Sella S.p.A. [2016] 387 ITR 358 (AAR)
[7] CBDT Press Release, dated 30 December 2020
[8] CBDT Order, dated 11 January 2021

discipline and shall also cause injustice to those who have taken pains to file the return before the due date.

MLI/BEPS

- On 18 December 2020, OECD released 'Guidance on the transfer pricing implications of the COVID-19 pandemic' which intends to help taxpayers (in reporting the financial periods affected by the pandemic) and tax administrations (in evaluating the implementation of taxpayers' TP policies). The guidelines address four priority issues namely; (i) comparability analysis; (ii) allocation of losses and COVID-19 specific costs; (iii) government assistance programmes; and (iv) advance pricing agreements.

- In June 2020, the US Trade Representative (USTR) initiated an investigation of India's 2020 Equalisation Levy under the Trade Act of 1974 (the Trade Act). On 6 January 2021, the office of US Trade Representative (USTR) released its findings on this Section 301 investigation into India's Equalisation Levy (EL) and concluded that India's EL is discriminatory and restricts US commerce. On 7 January 2021, India issued a press release stating that India had already submitted its comments to USTR. India had participated in the bilateral consultation, emphasising that EL is not discriminatory. Government said that it will examine the determination / decision notified by the US in this regard and would take appropriate action keeping in view the overall interest of the nation.

Indirect Tax

Goods and Services Tax

a) Electricity Charges and incidental charges collected in addition to rent not liable to GST

The applicant in the instant case filed an application to seek ruling on whether electricity or incidental charges recovered in addition to the monthly rent is liable to GST. Upon perusal of the lease agreement the AAR made following observations –

- Agreement provides for a fixed value of supply for renting of premises for the space rented out and it also includes all the internal infrastructure. However, there is no specific clause regarding electricity charges.

- Further, vide a separate clause lessee is made liable to pay all charges in respect of electricity used.

Based on the above observation the AAR ruled[9] that electricity charges cannot form part of the value of supply for the sole reason that the rate for renting of premises has been fixed and the electricity charges are to be borne by the lessee as per the actual usage of electric power.

b) Amount forfeited on account of breach of contract for sale of land is liable to GST

The question before the AAR was whether an amount forfeited on account of breach of agreement of sale of land is liable to GST. The applicant contented that the said forfeited

[9] Gujarat Narmada Valley Fertilizers and Chemicals Limited [Advance Ruling no, GUJ/GAAR/R/93/2020]

amount since being on account of sale of land is not liable for GST.

The AAR observed[10] that the amount which was received was part of the terms and condition of an agreement entered by the customer and the applicant. This means that while entering into the contract the customer was aware about the terms and condition of the contract, the amount given as an advance would become forfeited by the applicant being settlement of exit of the contract. The purpose of payment of amount is an act of tolerance in the sense that when there is breach of the contract, the appellant is put to certain hardships, which he tolerates in return of the payment received as advance being forfeited. Therefore, the impugned transaction is a 'supply' under the provisions of the CGST Act and therefore taxable.

Service Tax update

a) Penalty, forfeiture of EMD and liquidated damages are not 'consideration' for 'tolerating an act' – CESTAT

On the question whether any penalty/liquidated damages that has been recovered pursuant to a commercial contract which contained clauses for levy of penalty for breach of the terms of the contract can be treated as 'tolerating an act', the CESTAT has held that such penalty are not in the nature of 'tolerating an act' and thus not liable to service tax.

Relying on the Hon'ble Supreme Court Judgements[11], CESTAT[12] stated 'consideration' must flow from the service recipient to the service provider and should accrue to the benefit of the service provider and that the amount charged has necessarily to be a consideration for the taxable service provided. There is marked distinction between 'conditions to a contract' and 'considerations for the contract'. A service recipient may be required to fulfil certain conditions contained in the contract but that would not necessarily mean that this value would form part of the value of taxable services that are provided.

In light of the above, there has to be a flow of consideration from one person to another when one person agrees to the obligation to refrain from an act, or to tolerate an act, or a situation, or to do an act. Thus, a service conceived in an agreement where one person, for a consideration, agrees to an obligation to refrain from an act, would be a 'declared services' for the purpose of levy of service tax.

An agreement has to be read as a whole so as to gather the intention of the parties. The penal clauses are in the nature of providing a safeguard to the commercial interest of the appellant and it cannot, by any stretch of imagination, be said that recovering any sum by invoking the penalty clauses is the reason behind the execution of the contract for an agreed consideration. It is not the intention of the appellant to impose any penalty upon the other party nor is it the

[10] Fastrack Deal Comm Pvt. Ltd. [Advance Ruling no. GUJ/GAAR/R/58/2020]
[11] Fateh Chand v. Balkishan Das [AIR 1963 SC 1405] and Commissioner of Service Tax vs. M/s Bhayana Builders [2018 (2) TMI 1325]
[12] South Eastern Coalfields Ltd. vs. Commissioner of Central Excise and Service Tax, Raipur [Service Tax Appeal No. 50567 of 2019]

intention of the other party to get penalized.

Based on the above observation the CESTAT held that penalty amount, forfeiture of earnest money deposit and liquidated damages received by the appellant is not towards 'consideration' for 'tolerating an act' and hence not leviable to service tax.

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