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Direct Tax

India and US agree on a transitional approach on Equalisation Levy 2020

To address the tax challenges posed by the increased digitalisation of the economy, an Equalisation Levy (EL) was introduced in India. Various other countries had also introduced digital services taxes (DST) to tackle the challenges of the digitised economy. Introduction of these unilateral measures impacted the multi-national US technology companies. The USA found such unilateral measures unreasonable or discriminatory which burdens or restricts their commerce. The USA was planning to introduce various trade actions under Section 301 of the Trade Act, 1974 against the countries which have introduced such unilateral measures, including India.

On 8 October 2021, 136 out of the 140 member countries of the OECD/G20 Inclusive Framework approved a statement finalising a framework for a major international tax reform. The reform focuses on prevention of tax avoidance by Multinational Enterprises (MNEs), through a two-pillar approach, by addressing the gap in the existing tax rules. Pillar One provides for a new nexus rule to align the evolving digital economy and Pillar Two ensures that MNEs will pay a minimum tax in the each of the jurisdictions that they operate. Pillar One demands removal and standstill of DST and other relevant similar measures.

In line with this statement, on 21 October 2021, the USA, Austria, France, Italy, Spain, and the UK reached an agreement on a transitional approach to existing unilateral measures while implementing Pillar one. The agreement is reflected in the joint statement that was issued by those six countries. The joint statement describes a compromise reached by the countries on a transitional approach to the treatment of existing DSTs and other relevant similar measures during the interim period before new Pillar One rules come into effect.

On 24 November 2021, the Ministry of Finance of India has issued a press release[1] where India and the USA have agreed that terms of Joint Statement issued on 21 October 2021 shall apply between the USA and India with respect to India's charge of 2 per cent EL on e-commerce supply of services. The interim period in case of India will be from 1 April 2022 till the implementation of Pillar one or 31 March 2024, whichever is earlier. The final terms of the agreement shall be finalised by 1 February 2022.

[1] Press release issued by the Ministry of Finance of India, dated 24 November 2021

Decisions - International Tax

Income from Indian investment by UAE based settlor through a Jersey based Trust is not taxable in India under the India-UAE tax treaty: Bombay High Court[2]

Under the trust deed, the UAE settlor was provided right to re-assume power over the entire income arising on the investments made by the trust in the portfolio companies. There was a revocable transfer by settlor. Thus the entire income arising therefrom was assessed in the hands of UAE based settlor considering the provisions of revocable transfer of asset[3] under the Act.

The High Court held that as per the provisions of the Income-tax Act, 1961 (the Act) read with the India-UAE tax treaty, even if, the trust is based out and settled in Jersey, the income which arises to UAE based settlor by virtue of investment in Indian portfolio companies will be governed by the beneficial provisions of the tax treaty as UAE based entity was the settlor and sole beneficiary of the trust and resident of UAE. There was no attempt to reduce the tax liability by using the trust structure.

Even if the provisions of revocable transfer of asset are not applicable, the trustee will be assessed in a representative capacity and, accordingly the provisions of representative assessee[4] will be applicable.

Consequently, as per the provisions of the Act and Article 24 of the tax treaty, income arising on the investments in Indian Portfolio companies is not taxable in India.

Even though UAE based subsidiary was a paper/shell company, its profits are not taxable in India: ITAT Ahmedabad[5]

The profit earned by the UAE subsidiary company was predominantly on account of the import from the downstream subsidiary based in Democratic Republic of Congo (DRC) which was sold to a party based in China. Thus, the transaction was amongst the parties based outside India. Accordingly, such profit cannot be attributed to the taxpayer merely on the reasoning that the taxpayer is the holding company. The substance of the transaction shows that the profit was belonging to such foreign subsidiary companies.

The substance of the transaction shows that the profit was either belonging to the subsidiary in DRC or subsidiary in UAE. Even if the existence of the subsidiary in UAE is denied, such profit has to be attributed to the subsidiary in DRC. No doubt was raised by the tax department on the existence of the subsidiary in DRC which implies that the subsidiary company in DRC was functioning properly. Therefore, the profit related to the subsidiary company in DRC cannot be clubbed with the taxpayer company on the reasoning that the taxpayer had diverted the profit by using the colourable device.

Decisions - Domestic Tax

Taxpayer's petition challenging initiation of prosecution proceedings can be challenged before the Trial Court only: Madras High Court[6]

[2] Abu Dhabi Investment Authority and Others v. AAR (Writ Petition No. 770 of 2021) (Bom)
[3] Section 61 - any income arising to any person by virtue of revocable transfer shall be chargeable to tax as the income of the transferor.
[4] Under Section 160
[5] Rubamin Ltd v. DCIT (ITA No. 2929/Ahd/2014)
[6] Shri Raman Krishna Kumar v. DCIT (CRL OP No. 25561/2016 & CRL MP Nos. 12438 & 12439/2016)

The High Court dealt with the issue of initiation of prosecution against the taxpayer for non-furnishing of his tax return despite having taxable income. The taxpayer contended that such prosecution proceedings should be quashed at the initiation itself as the taxpayer's default was due to a bonafide belief that his employer would file his tax return.

The High Court held that once there is a default of non-furnishing of the tax return, prosecution is mandatory, given the presumption of culpability under the Act. While such presumption is rebuttable, the validity of claim of innocence and ignorance can only be established during a trial in a court of law. Accordingly, the High Court rejected the taxpayer's petition to quash the prosecution proceedings at the stage of initiation.

Notifications /Circulars/Press Release

- CBDT vide an Order[7] dated 26 October 2021 authorised the Director General of Income-tax (Systems) to upload information relating to specified sources, in the Annual Information Statement (AIS) in Form 26AS in the electronic filing account registered by the taxpayer. The information can be uploaded in designated portal, within three months from the end of the month in which the information is received by her/him. The information that is required include interest on tax refund, information about purchase of mutual fund and its dividend, foreign remittance information reported in Form 15CC, etc.

- CBDT vide Guidelines[8] dated 26 October 2021 clarified the term 'indirectly' for the purpose of claim of exemption under Section 10(23FE) with respect to sovereign wealth funds and pension funds (specified fund). If the loans and borrowings have been taken by the specified fund or any of its group concern, not specifically for the purposes of making investment in India, it shall not be presumed that the investment in India has been made out of such loans and borrowings. Further such specified fund shall be eligible for exemption under Section 10(23FE), subject to the fulfilment of other specified conditions, provided that the source of the investment in India is not from such loans and borrowings.

- CBDT notified[9] E-Settlement Scheme, 2021 which is applicable to pending settlement applications in respect of which the applicant has not exercised the option of withdrawal under Section 245M(1) and which has been allotted or transferred by the CBDT to an Interim Board. The proceedings before the interim board shall not be open to the public. No person other than the applicant, their employee, and concerned officers of the interim board or the income-tax authority or the authorised representatives, without the permission of the interim board, can attend the proceedings even on video-conferencing or video telephony. All communication between the Interim Board and the applicant, or his authorised representative, shall be exchanged by electronic mode.

- The Employees' Provident Fund Organisation (EPFO) vide Circular[10] dated 30 October 2021 declared the rate of interest of 8.5 per cent for crediting interest on Provident Fund accumulation for members of the Employees' Provident Funds Scheme for the Financial Year 2020-21.

[7] CBDT Order F.No.22S/1SS/2020/ITA-II, dated 26 October 2021
[8] CBDT Circular No. 19 of 2021, dated 26 October 2021
[9] CBDT Notification No.129/2021, dated 1 November 2021
[10] EPFO Circular No: NV-11/1/2020-INV

Indirect Tax

Instructions / Guidelines

Guideline for blocking of electronic credit ledger[11]

Recently, there have been several instances of blocking of electronic credit ledger, in response to which Writ were filed in several courts. The High Courts in some cases have emphasized the need for laying guidelines for invoking rule 86A of the CGST Rules. In view of the same, CBIC has issued guidelines with respect to powers under rule 86A of the CGST Rules. Gist of the guidelines is as follows:

i. There must be 'reasons to believe' after proper application of mind that credit of input tax available in the electronic credit ledger is either ineligible or has been fraudulently availed by the registered person, before disallowing the debit of amount from electronic credit ledger of the said registered person under rule 86A;

ii. The amount disallowed for debit from electronic credit ledger should not be more than the amount of input tax credit which is believed to have been fraudulently availed or is ineligible, as per the conditions / grounds mentioned in sub-rule (1) of rule 86A;

iii. Upon expiry of one year from the date of restriction, the registered person would be able to debit input tax credit so disallowed, subject to any other action that may be taken against the registered person.

[11] GST Policy Wing Instructions 20/16/05/2021-GST dated 2 November 2021

Advance Rulings

Pooling of contributions from members for administrative expense amounts to supply[12]

'Applicant' is engaged in humanitarian and charitable services. Administration and working of the 'Applicant' and implementation of policies are on the concept of mutuality. It arranges meetings for its members. In order to cover its expenditure for such meetings, it collects fees from its members. It does not provide any facilities / benefits to its members. Two separate bank accounts, one for administrative expenses and other for donations / charity are maintained. 'Applicant' contents that the doctrine of mutuality applies as there is no other commercial consideration whatsoever and two distinct persons are missing.

Maharashtra AAR held that the principles of mutuality on the fees collected from members will not be applicable in view of the amended section 7 of the CGST Act, 2017. The impugned activities performed by the 'Applicant' is a service rendered by the 'Applicant' to its members. The activity of providing facilities or benefits by an association to its members for a subscription is a business under GST Act. Fees / donation/ subscription amount (by whatever name called), collected by the 'Applicant' is nothing but the consideration for such 'supply' and is covered by the scope of the term 'business'.

Concessional rate of GST of 0.1% will not be applicable if export goods are not moved directly to Port, ICD, etc.[13]

'Applicant' is engaged in manufacturing of packing material. It supplies packing material (HDPE drums) to a merchant exporter on receipt of a purchase order, by raising invoice on the merchant exporter

[12] Rotary Club of Bombay Queen City [2021-VIL-426-AAR]

[13] Time Technoplase Limited [2021-VIL-402-AAR]

and delivers the subject material, under the instructions of the said merchant exporter, to the premises of the chemical manufacturer, who manufactures ethyl alcohol which is packed in the HDPE drums and then exported by the merchant exporter. 'Applicant' contends that it is entitled to concessional rate of GST of 0.1%, in terms of Notification No. 40/2017-Central Tax (Rate) dated 23 October 2017 and Notification No. 41/2017-Integrated Tax (Rate) dated 23 October 2017.

Karnataka AAR held that in order to avail the concessional rate of GST, the registered recipient is required to move the goods directly from the place of registered supplier to the Port, Inland Container Deport (ICD), Airport or Land Customs Station from where the said goods are to be exported, or to a registered warehouse from where the goods shall be further moved to the Port, ICD, Airport or Land Customs Station. In case the merchant exporter procures goods from different registered suppliers, the merchant exporter should move such supplies to the registered warehouse, aggregate such procured goods at the warehouse and should move the goods to the Port, ICD, Airport or Land Customs Station from where the goods are exported. In the instant case, the impugned goods are not moved directly to the Port, ICD, Airport or Land Customs Station or to a registered warehouse, which is a pre-condition for availing concessional rate of GST. Therefore, the 'Applicant' is not entitled to supply the impugned goods at the concessional rate of GST of 0.1%.

High Court Decisions

Exemption cannot be taken away by issuing clarificatory circular[14]

'Petitioner' is a manufacturer of fish meal which, one hand, is a finished product and at the same time, it can also be used as input. CBIC issued Circular No. 80/54/2018-GST dated 31 December 2018 clarifying that fish meal will attract 5% GST.

Department initiated proceedings on the contention that the exemption from GST to fish meal is confined only when it is meant for use as finished product and not as raw material for manufacture of cattle feed or poultry feed.

On analysis of the rate notifications, Madras High Court held that the impugned product is exempted. It further held that exemption provided by the Central Government by exercising its powers either under section 11(1) of CGST Act, 2017 or under section 6(1) of IGST Act, 2017 are the substantive right. Exemptions cannot be taken away or done away by issuing clarificatory circulars by CBIC, in exercise of its powers under section 168 of the CGST Act, 2017.

[14] Jenefa India vs. Union of India & Ors. [2021-VIL-763-MAD]

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