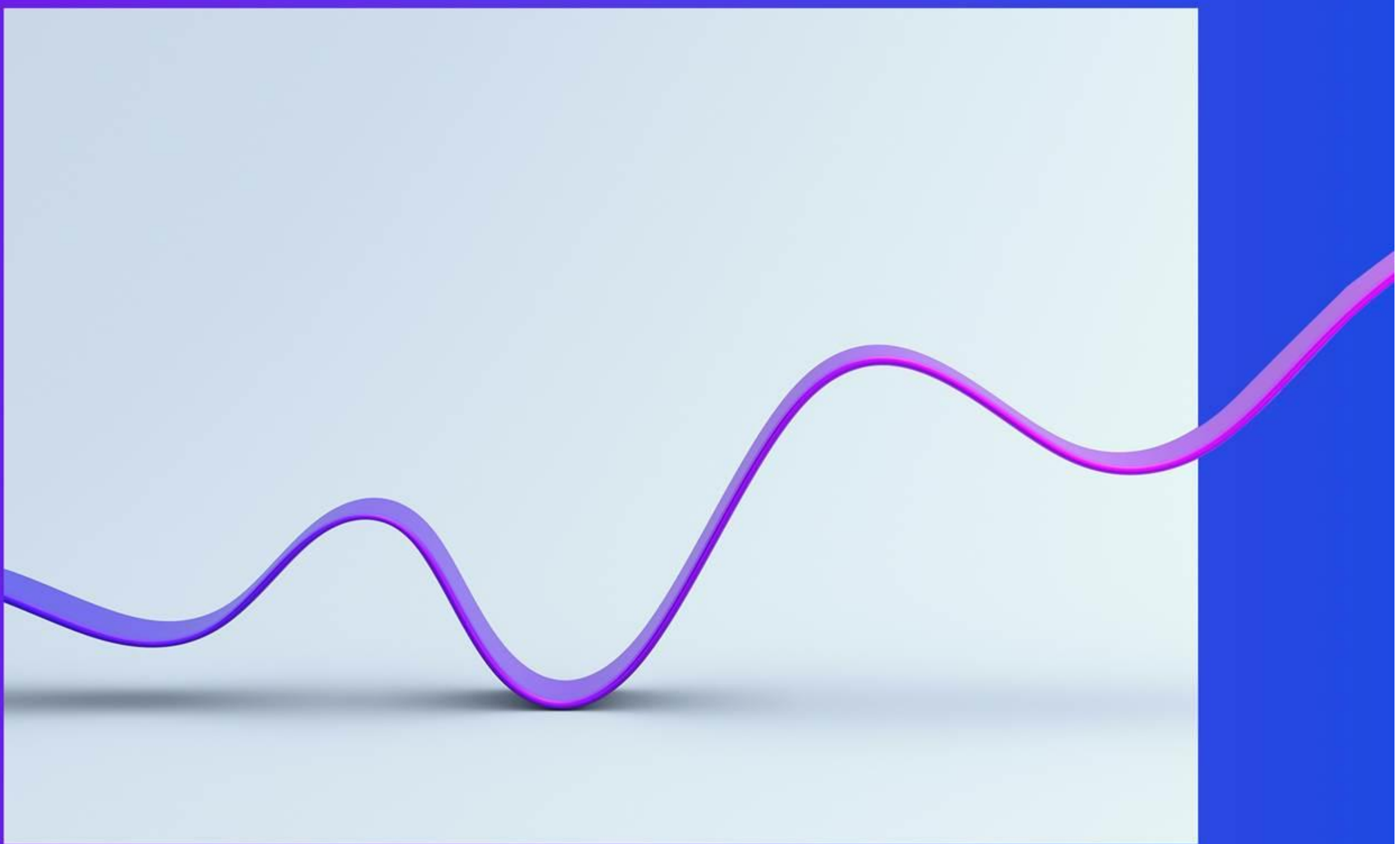
KPMG

India Tax Konnect

March 2024

kpmg.com/in



Contents

Direct Tax

1 Direct Tax

1.1 Decision - International Tax

Business support services provided by the UK company to its Indian group company are not taxable as fees for technical services – Delhi High Court[1]

A UK company provided business support services (BSS) to all its group companies across the world including its Indian group company. The services included management support, marketing support, taxation advice, etc. The cost incurred was allocated to all service recipients including the Indian company on a cost-to-cost basis using the cost allocation keys.

Article 13 of the India-UK tax treaty (the treaty), *inter alia*, provides that fees for technical services (FTS) means payment for any technical or consultancy services which 'make available' technical knowledge, experience, skill, etc.

Earlier, the Authority for Advance Rulings (AAR) had held that the payments for BSS were FTS under Article 13 of the treaty as the Indian company was able to use the know-how/ intellectual property generated from the BSS independent of the service provider and such services were 'made available' to the Indian company.

The Delhi High Court held that the payments for BSS were not taxable as FTS on the following grounds:

- The principle of *noscitur a sociis* mandates that the meaning of a word is to be determined by other words immediately surrounding it.
- In Article 13 of the treaty, the words 'consultancy services' followed the word 'technical'. Consultancy services which are not technical could not be considered as FTS.
- The BSS provided by the UK company are managerial in nature. They are not technical in nature as technical services mean services requiring expertise in a technology.
- Even if consultancy services were considered on a 'stand-alone' basis, only the services which *inter alia* satisfy 'make available' conditions are covered.
- After referring to the decision of *De Beers*[2], *Bio-Rad Laboratories (Singapore) Pte. Ltd*[3], it was held that the BSS did not 'make available' technical knowledge, experience, etc. Otherwise, there should not be any need to continue to provide the services and the contract must stand concluded once the services and the know-how, etc. are transferred to the Indian company.

1.2 Decisions - Domestic Tax

The effective date of transfer of shares is the 'date of actual transfer' after the fulfilment of conditions and not the 'date of agreement' – Mumbai Tribunal[4]

The taxpayer (a non-resident) entered into an agreement for the transfer of shares of a company to another Indian company (transferee). The transfer of shares and the payment of consideration were subject to the fulfilment of certain conditions. There was a right to rescind the agreement upon the non-fulfilment of conditions. The taxpayer received consideration from the transferee pursuant to the transfer of shares after the fulfilment of all the conditions.

The issue before the Tribunal was related to determining the effective date of transfer for computing the period of holding of the shares – whether it would be the date of the agreement or

---

[1] Writ Petition No.10788 of 2012 (Bom) – Source - Taxsutra
[2] *CIT* v. *De Beers India Minerals (P.) Ltd* [2012] 346 ITR 467 (Kar)
[3] *CIT* v. *Bio-Rad Laboratories (Singapore) Pte. Ltd*. [2023] 459 ITR 5 (Del)
[4] ITA No. 2545/Mum/2011 - Source - Taxsutra

the date when the transfer was effected. This would determine whether the gains arising from the transfer were long-term capital gains (LTCG) or short-term capital gains (STCG).

The taxpayer claimed that the effective date of transfer was the 'date of actual transfer of shares' and not the 'date of agreement'. As the taxpayer held the shares for more than 12 months as on the date of the transfer of shares, the capital gain was taxable as LTCG.

The tax officer held that the sale consideration was fixed on the 'date of agreement' and there was no change in such consideration subsequently. Accordingly, the date of sale was the 'date of agreement'. As the period of holding of shares was less than 12 months on the 'date of agreement', the capital gain was taxable as STCG. The tax officer relied on the CBDT Circular[5] and the decision of *Max Telecom Ventures Ltd*[6].

The Mumbai bench of the Tribunal observed that the effective date of transfer for deciding the holding period of share was the 'date of actual transfer of shares' after fulfilment of conditions of the agreement and not the 'date of agreement'. The Tribunal accepted the taxpayer's position that the capital gain was taxable as LTCG:

- In the case of *Mrs. Hami Aspi Balsara*[7], it was observed that the 'date of the contract of sale' would be the date of fulfilment of the conditions specified in the agreement and only upon the fulfilment of the said conditions, the contract of sale can be said to have been crystallised.
- The Tribunal distinguished the decision of *Max Telecom Ventures Ltd.* based on the facts of the case. In that case, the share purchase agreement was acted upon immediately on the execution of the agreement and it was not a conditional sale as in the instant case.

Deemed dividend is taxable only in the hands of a person who is a shareholder of the lender company: Chennai Tribunal[8]

The taxpayer (an Indian company) received a loan from its group company, IG3 (a closely held company)[9].

Out of 1000 shares of the taxpayer, 998 shares were held by an unrelated company and 1 share each was held by P and Q who were the promoters of IG3.

During the year under consideration, these shares were transferred to unrelated persons immediately before the grant of the above-mentioned loan.

The issue before the Chennai bench of the Tribunal was whether this loan can be regarded as a dividend under section 2(22)(e) of the Income-tax Act, 1961 (the Act).

As per section 2(22)(e), 'dividend' includes any payment by a closely held company by way of advance or loan to:

(a) a shareholder being the beneficial owner of equity shares holding not less than ten per cent of the voting power (first limb)

(b) any concern in which such shareholder is a member or a partner and in which he has a substantial interest[10] (second limb) or

It also includes any payment on behalf, or for the individual benefit, of such shareholder (third limb)

The tax officer held that the loan received by the taxpayer from IG3 was taxable as a dividend under section 2(22)(e) based on the following grounds:

---

[5] Circular No. 704, dated 28 April 1995

[6] *Max Telecom Ventures Ltd.* v. *ACIT* [2008] 114 ITD 46 (Amritsar)

[7] *Mrs. Hami Aspi Balsara v. ACIT* [2010] 126 ITD 100 (Mum)

[8] *DCIT* v. *Mukunda Land Developers Pvt. Ltd.* (I.T.A. No.642/Chny/2023) (Chen) - Source - Taxsutra

[9] Not being a company in which the public are substantially interested as defined in section 2(18) of the Act

[10] A person shall be deemed to have a substantial interest in a concern, other than a company, if he is beneficially entitled to not less than twenty per cent of the income of such concern

- The taxpayer was operating under the instructions of the promoters of IG3 (P and Q). The loan was received by the taxpayer on behalf of and for the benefit of promoters of IG3. Therefore, the third limb of section 2(22)(e) was attracted.
- The change in the shareholders of the taxpayer just before the grant of the loan was to avoid the applicability of section 2(22)(e).

The Tribunal, relying on the decision in *Ankitech*[11], held that the deemed dividend under section 2(22)(e) was taxable only in the hands of the person who is the registered as well as the beneficial owner of the shares.

The loan advanced by IG3 cannot be taxed in the hands of the taxpayer since the taxpayer was not the registered or beneficial shareholder in IG3 and thus, the first limb of section 2(22)(e) is not satisfied. Under the second limb of section 2(22)(e), the dividend can be taxable only in the hands of a common shareholder and it cannot be taxed in the hands of the loan recipient. The taxpayer was not the shareholder of the IG3 but was merely the recipient of the loan and thus the second limb did not apply to the taxpayer. The promoters of IG3 (P and Q) were not holding 10 per cent or more shares in IG3. Thus, whether they benefitted from the loans or not was immaterial as they did not satisfy the conditions of the third limb of section 2(22)(e).

The Tribunal observed that the Delhi High Court in the case of *National Travel Services*[12] taken a contrary view holding that it was not necessary that a shareholder must be a registered shareholder, and being a beneficial shareholder would suffice. The matter was appealed before the Supreme Court which agreed with observations of the High Court[13]. The matter was placed before the larger bench of the Supreme Court, but the appeal was withdrawn. Thus, the binding judgment on the issue of the expression 'shareholder' is that of *Ankitech*.

The relevant date for determining the shareholding is the date of advancing of the loan. Neither the taxpayer nor its shareholders were the shareholders of IG3 as on that date.

1.3 Notifications/circulars

CBDT issues circular clarifying tax implications arising from inter-trust donations: CBDT Circular[14]

The Central Board of Direct Taxes (CBDT), vide this circular, has clarified the tax treatment of non-corpus donations made by one eligible charitable entity to another in view of the amendment by the Finance Act, 2023.

Background

Income of an eligible charitable entity[15] is exempt from the tax subject to the fulfilment of certain conditions. One of the conditions is that at least 85 per cent of the current year's income is applied for the charitable purpose and the balance 15 per cent can be accumulated. If the charitable entity is unable to apply at least 85 per cent of its income, then it can accumulate or set apart the balance income. Such balance income should be applied within the next 5 years for the specified purpose and till that time such funds are to be deposited or invested in specified modes. Once 85 per cent of the current year's income is applied or accumulated, the entire 100 per cent income of such charitable entity is exempt.

The charitable entity is allowed to apply its income directly or by way of non-corpus regular donation to other charitable entities having similar objects.

---

[11] *CIT* v. *Ankitech (P.) Ltd* [2011] 340 ITR 74 (Del) affirmed in *CIT* v. *Madhur Housing & Development Co Ltd* [2018] 401 ITR 152 (SC)
[12] *CIT* v. *National Travel Services* [2011] 347 ITR 305 (Del)
[13] *National Travel Service* v. *CIT* [2018] 401 ITR 154 (SC)

[14] Circular No. 3/2024, dated 6 March 2024

[15] Any fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of clause (23C) of section 10 of the Act or any trust or institution registered under section 12AA or 12AB of the Act

The Finance Act, 2023 amended the relevant provisions[16] to provide that such eligible donations are to be treated as application for charitable or religious purposes only to the extent of 85 per cent of the donations. The balance 15 per cent of such donations are not to be treated as application for charitable or religious purposes.

The amendment posed practical challenges with respect to the tax treatment of 15 per cent of donations which are not to be treated as application for charitable or religious purposes. There was no clarity as to whether such 15 per cent of donations would be taxable or is eligible for 15 per cent accumulation. The latter option raises the challenge as the funds were already donated and would not be available with the donor entity for the deposit or investment.

Circular

- Eligible donations will be treated as application for charitable or religious purposes only to the extent of 85 per cent of such donations.
- For example, when a charitable entity donates INR100 to another charitable entity, it will be considered as application of INR85 (85 per cent) for the purpose of charitable or religious activity.
- The balance INR15 (15 per cent of such donations) will not be required to be invested in specified modes as the entire amount of INR100 has been donated to the other charitable entity and is eligible for exemption.

[16] Section 10(23C) and section 11

Foreign Exchange Management Act, 1999

2 Foreign Exchange Management Act, 1999

The Government of India eases norms for Foreign Direct Investment in the space sector

As per the existing Foreign Direct Investment (FDI) policy, FDI is permitted in the establishment and operation of satellites through the Government approval route only. In line with the vision and strategy under the Indian Space Policy 2023, the Government of India has eased the FDI policy on the space sector by prescribing liberalised FDI thresholds for various sub-sectors / activities.

The amendments in the FDI Policy[17] have divided the space sector into three broad categories and prescribed limits for foreign investment in each sub-sector as under:

Sr. No.	Sector / activity	Sectoral Cap	Entry Route
1	Satellite manufacturing & operation, satellite data products and ground segment & user segment	100 per cent	Upto 74 per cent – automatic route Beyond 74 per cent – Government route
2	Launch vehicles and associated systems or subsystems and creation of spaceports for launching and receiving Spacecraft	100 per cent	Upto 49 per cent – automatic route Beyond 49 per cent – Government Route
3	Manufacturing of components and systems/ sub-systems for satellites, ground segment and user segment	100 per cent	Upto 100 per cent – automatic route

The Indian investee entity will additionally be subject to the sectoral guidelines issued by the Department of Space from time to time. The above changes will take effect from the date of the FEMA notification.

[17] Press Note No. 1 (2024 series) dated 4 March 2024

Indirect Tax

3 Indirect Tax

3.1 High Court Decisions

Applications for refund of GST paid on ocean freight pursuant to the decision of the Supreme Court in Mohit Minerals cannot be rejected[18]

In May 2022, the Supreme Court in the case of Mohit Minerals had held that a separate levy on ocean freight in a CIF contract for the import of goods was in violation of section 8 of the CGST Act. The Supreme Court observed that the Indian importer was already liable to pay IGST on the 'composite supply' of goods plus services of transportation, insurance, etc.

After this decision, the Petitioner claimed a refund of IGST, interest and penalty paid under protest on ocean freight. GST authorities rejected the refund on the ground that refund as a result of levy being held unconstitutional can be claimed only by way of suit or a writ petition and not by virtue of section 54 of CGST Act as it would not fall under any category of refund prescribed therein.

The Gujarat High Court held that the refund claim cannot be rejected on the ground that the same is outside the scope of section 54 as the levy of IGST on ocean freight itself was held as unconstitutional and the Supreme Court's decision being the law of the land. Further, the principle of unjust enrichment was not violated as the Petitioner had submitted a CA certificate regarding the non-passing of tax burden to this effect.

Show cause notice under section 74 is bad in law once the entire duty and interest is discharged by the Assessee before the issue of SCN[19]

The Petitioner is engaged in the business of generation of electricity through solar plants. The GST Authorities conducted the audit for the period July 2017 to March 2019. The summary of the audit findings was communicated to the Petitioner. The Petitioner accepted the findings and paid the entire additional tax along with interest. The GST Authorities then issued the final audit report. Subsequently, the GST Authorities confirmed the demand section 74 (i.e., fraud, wilful misstatement or suppression of facts) on the grounds that there was an element of misstatement made by the Petitioner and there was suppression of fact until it was noticed in the course of audit which amounts to a fraud.

The Petitioner challenged this order by a writ petition. The contention of the Petitioner was that the entire proceeding initiated under section 74 is bad in law and the final order is liable to be set aside/quashed as its case squarely fell under section 73(5) and since the tax along with interest was already paid, all the proceedings should be deemed to be concluded.

The Telangana High Court allowed the writ in favour of the Petitioner. It held that if the conduct of the Petitioner did not fall within the purview of fraud, misstatement, and suppression of fact then the proceeding under section 74 was in excess of the jurisdiction. It further held that the Petitioner cannot be forced to undergo the entire process of litigation under the statute when the issuance of show cause notice is bad in law.

Show cause notice is not sustainable if an order in ASMT-12 is issued for the completion of scrutiny of returns[20]

The Petitioner is engaged in cash logistics business. The Proper Officer served a notice in Form ASMT-10 for scrutiny of returns for the FY 2017-18. The Petitioner furnished a satisfactory explanation to this notice. The Proper Officer dropped the proceedings under section 61 and issued an order (in Form ASMT-12). However, the Proper Officer issued a show cause notice and subsequently issued an assessment order. The Petitioner challenged the assessment order by way of a writ petition.

---

[18] *Jupiter Comtex Pvt Ltd* v. *Union of India* [2024-VIL-193-GUJ]

[19] *Rays Power Infra Private Limited* v. *Superintendent of Central Tax* [2024-VIL-202-TEL]

[20] *Radiant Cash Management Services Ltd*. v. *The Assistant Commissioner (ST), Chennai* [2024-VIL-238-MAD]

The Madras High Court examined the assessment order to verify if the demand was resurrected. It observed that the demand relates to the same assessment period. Further, the GST amount was also the same. The only difference was that of interest and penalty.

The Madras High Court held that upon issuance of an order in Form ASMT-12 (for scrutiny of returns) which recorded that no further action is required, the continuation of proceedings culminating in the impugned assessment order is unsustainable.

Input tax credit cannot be rejected merely because it is not claimed in Form GSTR-3B but claimed in Form GSTR-9[21]

The GST Authorities issued a notice and demanded tax along with interest and penalty under section 74 of the CGST Act 2017 for the years 2017-18 to 2019-20.

During the assessment, the Petitioner asserted that it is eligible for the input tax credit for each of the assessment years even though it had not claimed them in Form GSTR-3B. This was on the ground that the impugned amounts were reflected in Form GSTR-2B and consequently, the Petitioner had claimed them in Form GSTR-9. The Authorities rejected the input tax credit claimed by the Petitioner in Form GSTR-9 on the grounds that the Petitioner has not claimed the input tax credit in Form GSTR-3B.

The Madras High Court quashed the orders and remanded the matter for reconsideration. It held that when the registered person asserts that it is eligible for the input tax credit by referring to Form GSTR-2A and Form GSTR-9, the assessing officer should examine whether the input tax credit claim is valid by examining all relevant documents. Consequently, the input tax credit cannot be rejected on the grounds that Form GSTR-3B did not reflect the claim of input tax credit.

[21] *Sri Shanmuga Hardwares Electricals v. The State Tax Officer*, Attur Rural Assessment Circle, Salem [2024-VIL-180-MAD]

Contact:

Rajeev Dimri
National Head of Tax
T: +91 124 307 4077
E: rajeevdimri@kpmg.com

kpmg.com/in

Follow us on:

kpmg.com/in/socialmedia