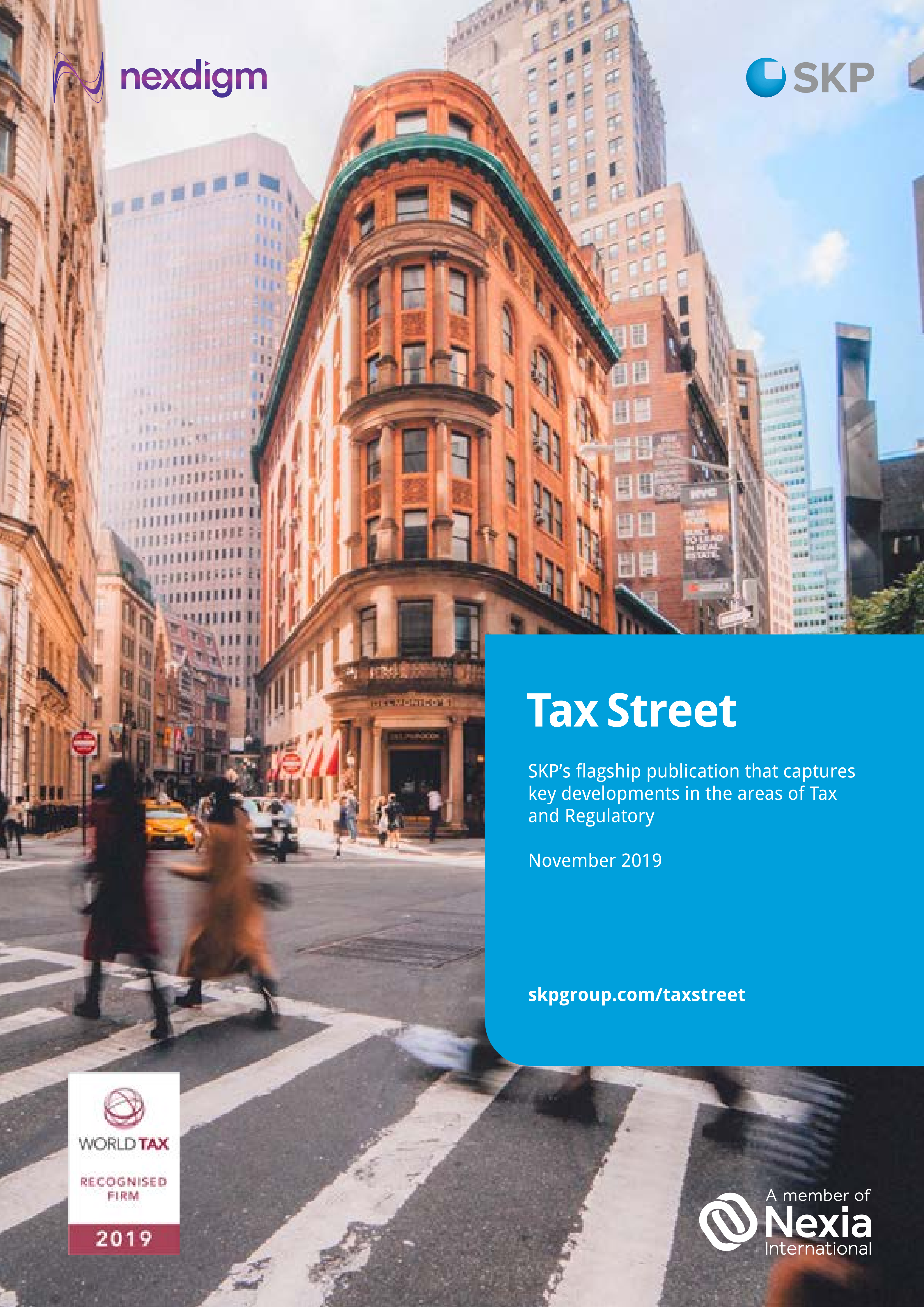

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SKP

# Tax Street

SKP's flagship publication that captures key developments in the areas of Tax and Regulatory

November 2019

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WORLD TAX
RECOGNISED FIRM
2019

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# SKP TAX STREET

# INTRODUCTION

We are pleased to present the latest edition of Tax Street – our newsletter that covers all the key developments and updates in the realm of taxation in India and across the globe for the month of November 2019.

- The **'Focus Point'** section covers the recently introduced ITC restriction in relation to invoices not disclosed by suppliers.
- Under the **'From the Judiciary'** section, we provide in brief, the key rulings on important cases, and our take on the same.
- Our **'Tax Talk'** provides key updates on the important tax-related news from India and across the globe.
- Under **'Compliance Calendar'**, we list down the important due dates with regard to direct tax, transfer pricing and indirect tax in the month.

We hope you find our newsletter useful and we look forward to your feedback. You can write to us at **taxstreet@skpgroup.com**. We would be happy to hear your thoughts on what more can we include in our newsletter and incorporate your feedback in our future editions.

Warm regards,
The SKP Team

# FOCUS POINT

## ITC claim restricted to 120% of GSTR-2A

The linkage of a recipient's input tax credit (ITC) with the outward supplies disclosed by the supplier is one of the intrinsic principles of the GST law. However, due to the absence of adequate IT capacity in the initial stages of implementation of the GST law, the government suspended the relevant provisions and allowed ITC on a self-declaration basis by the recipient through GSTR-3B.

Recently, the government, vide Notification No. 49/2019-Central Tax dated 9 October 2019, inserted Rule 36(4) to the CGST Rules, 2017 whereby ITC with respect to invoices or debit notes, the details of which were not uploaded by the supplier, is restricted to 20% of the ITC with respect to invoices or debit notes uploaded by the supplier, i.e., appearing in GSTR-2A. The provision can be understood through the following illustration:

| Particulars | Actual ITC | Eligible ITC as per amendment |
|---|---|---|
| Eligible ITC pertaining to invoices/debit notes uploaded by the supplier, i.e., appearing in GSTR-2A | 100 | 100 [No change post amendment] |
| Eligible ITC pertaining to invoices/debit notes not uploaded by the supplier, i.e., not appearing in GSTR-2A | 200 | 100*20% = 20; or 200; whichever is lower i.e. 20 |
| **Total eligible ITC to be claimed in GSTR-3B** | | **120** |
| **Restricted ITC under Rule 36(4)** | | **200-20 =180** |

## Government forced to introduce clarifications

The 37th GST Council meeting was held less than a month before the amendment was notified. However, no announcement was made post the council meeting in relation to its plans of implementing a restriction on ITC availment. Further, the amendment lacked clarity on various aspects such as the periodicity for which the restricted ITC had to be computed which led to confusion within the industry. Therefore, the government, vide circular No. 123/42/2019-GST dated 11 November 2019, issued the following clarifications:

- The restriction should be applicable only to invoices/debit notes on which ITC is availed after 9 October 2019.
- The restriction is imposed on the consolidated ITC, and not supplier-wise ITC.
- The calculation would be based on only those invoices which are otherwise eligible for ITC. Accordingly, those invoices on which ITC is not available, like, blocked credits under Section 17(5), would not be considered for calculating 20% of the eligible credit available.
- A taxpayer can avail ITC in respect of invoices/debit notes uploaded by the supplier only up to the due date of filing of GSTR-1 (i.e., taxpayers should download GSTR-2A on the 11th of every month to determine the amount of eligible ITC available for that month.)
- Taxpayers may avail full ITC in respect of a tax period, as and when the invoices are uploaded by the suppliers to the extent of 'Eligible ITC divided by 1.2.' This can be understood through the following illustration:

| Particulars | Month in which eligible ITC is being computed | |
|---|---|---|
| | Dec 2019 | Jan 2020 |
| Total ITC as per books | 10,00,000 | 10,00,000 |
| ITC in respect of invoices appearing in GSTR-2A | 6,00,000 | Say, 10,00,000/1.2=8,33,333 |
| ITC in respect of invoices not appearing in GSTR-2A | 4,00,000 | 1,66,667 |
| Eligible ITC to be claimed | 6,00,000 + 20% of 6,00,000 =7,20,000 | 8,33,000 + 20% of 8,33,333 =10,00,000 |

## Issues faced by taxpayers

While the above clarifications have answered some questions, there are certain inherent issues with the entire mechanism.

**Technical limitations of the GSTN portal**

- The government in its clarification stated that taxpayers must download GSTR-2A on the due date of filing monthly GSTR-1, i.e., the 11th of every month, to determine the amount of ITC available in that month.
- On most due dates, the GSTN portal is already overburdened with taxpayers filing monthly returns, which results in technical issues on many occasions.
- Adding the requirement to download GSTR-2A on the same day is an added and avoidable hassle for taxpayers.

**Postponement of ITC resulting in working capital blockage**

- Considering that most taxpayers file their GSTR-1 on the 10th or 11th of the month, it is unclear whether such data will be reflected on a real-time basis in GSTR-2A of the recipient.
- Further, certain suppliers are required to file GSTR-1 on a quarterly basis. Thus, supplies received from such suppliers would reflect in GSTR-2A of the recipient only on a quarterly basis.
- In these cases, there would be blockage of bona fide ITC otherwise available to the recipient taxpayers.

### Reconciliation issues

- Taxpayers have to undertake the tedious task of invoice level reconciliation every month to identify invoices/debit note not uploaded by suppliers.
- According to the Rule, taxpayers can avail 20% over and above the eligible ITC appearing in GSTR-2A. However, in such cases, reconciling such excess availment of 20% ITC against the corresponding invoices appearing in next month's GSTR-2A can turn into a herculean task. This can be further complicated by the fact that such invoices may be spread across GSTR-2A of 3-4 months.
- The government has simply mentioned that a taxpayer would be able to avail ITC in respect of invoices and debit notes only if the details of such invoices and debit notes are uploaded by the supplier in their GST returns.

However, in a practical scenario, there are several reasons for deviation between ITC register and GSTR-2A such as slight mismatches between document number, document date, taxable amount and tax amount. The government has failed to clarify whether ITC would be available in such cases.

### Interpretational issues

#### Rule applicable individually for each tax type or total ITC

- The rule is silent on whether the eligible ITC has to be determined on a consolidated basis, or for IGST, CGST, and SGST/UTGST separately. Logically, the eligible ITC should be determined individually for each type of tax. The relevance of this issue can be demonstrated through the following illustration:

| Particulars | Scenario 1 - Eligible ITC is computed separately for each tax type | | | Scenario 2 - Eligible ITC is computed on total ITC |
|---|---|---|---|---|
| | CGST | SGST | IGST | Total ITC |
| ITC as per purchase register | 400 | 400 | 1000 | 1800 |
| Invoices appearing in GSTR-2A | 200 | 200 | 1000 | 1400 |
| **Total eligible ITC to be claimed in GSTR-3B as per Rule 36(4)** | **200 + 200*20% =240** | **200 + 200*20% =240** | **1000** | **1400 + 1400*20% = 1680** |
| | **1480** | | | |

Thus, it can be seen that the eligible ITC can vary based on the approach adopted by the taxpayer. This can result in heavy interest liability if such an approach is disputed by the authorities at a later stage.

### Eligibility in respect of invoices 'not submitted'

- There are cases when the invoices are uploaded by the supplier, but the GSTR-1 is not filed. Such invoices appear in GSTR-2A of the recipient, but their status is denoted as 'not submitted'. There is no clarification on whether ITC in respect of such invoices can be claimed.

### Can authorities demand an invoice wise matching of ITC availed during assessment?

- The Rule allows an ad hoc claim of ITC. However, at the time of assessment/audit whether taxpayers would be required to provide an invoice-wise reconciliation of the ITC availed with the GSTR-2A of every month remains unclear.

## Conclusion

The linking of ITC of the recipient with the disclosure of invoices by the supplier is an integral part of the new return filing system to be implemented from April 2020. Therefore, the introduction of this rule provides an opportunity for businesses to amend their processes to ensure that there is constant communication with the suppliers for the timely filing of their GST returns.

However, the wide ambit of the rule has resulted in various practical and interpretational issues. Blockage of working capital of the recipient due to non-compliance of the supplier remains a key bone of contention. Further, considering that the interest on the wrong availment of ITC stands as high as 24% per annum, there is a risk that businesses will incur heavy costs for bona fide mistakes in the reconciliation of ITC with GSTR-2A.

# FROM THE JUDICIARY

## Direct Tax

### Is importing definition from the act into the tax treaty an automatic process pursuant to the provisions of Article 3(2) of India-Singapore tax treaty?

ACIT vs Reliance Jio Infocomm Ltd. [TS-710-ITAT-2019 (Mumbai)]

Taxpayer (Indian Company), had availed bandwidth services from RJS (Singapore Company) pursuant to bandwidth services agreement. The taxpayer did not withhold tax on payment made to RJS for availing bandwidth services on the premise that it had merely received access to bandwidth services without having access to any equipment deployed for the provision of such services. Further, the related infrastructure and process was always used under the control of RJS and not the taxpayer. Also, the amendments made to the act cannot be read into the tax treaty unless the latter has been amended.

However, the tax officer was of the view that provision of bandwidth services was covered under the term "process" according to the tax treaty. The tax treaty does not define "process", hence, pursuant to Article 3(2) of the tax treaty, recourse can be taken to the provisions of the act for understanding its meaning and the term "process" as defined by the act covers within its ambit, provision of bandwidth services. Hence, payment for such services was taxable as royalty under the act read with the tax treaty.

Held

The tax tribunal rejected the contention of the tax officer and inferred that the term "process" assumes importance for interpreting the term "royalty" under the tax treaty only. Further, given that the tax treaty has defined the term "royalty", it is not possible to invoke Article 3(2) for further dissecting each term used in the definition to explore the domestic law meaning of each expression used therein for arriving at conclusions about undertones of royalty.

The tax tribunal also inferred that even if the term "process" is established as an undefined tax treaty term, static interpretation may not be relevant since the aforesaid term was not defined in the act at that time. Further, the tax tribunal opined that which ever approach, i.e., static/ambulatory is adopted, for the purpose of Article 3(2), a unilateral treaty override, even if it is subtle, is not permissible at all. Further, relying on Article 26 of the Vienna Convention, the tax tribunal inferred that if ambulatory interpretation (upheld in the case of Siemens Aktiongesellschaft) reverses judicial precedents in favour of the residence jurisdiction, then such an interpretation has to be discarded as it patronizes and legitimizes unilateral treaty override which has never been the intention of the tax treaty draftsmen.

In light of the above, the payments for availing bandwidth services would not be covered within the ambit of the term "process" as per India-Singapore tax treaty.

#### SKP's Comments

This decision is very important as it clearly spells out that if royalty is defined in the treaty, you cannot look at the amended definition under the domestic law to interpret terms used within the definition.

The Tax Tribunal also clarifies that if certain retrospective amendments result in negative repercussions for the taxpayer or completely changes the meaning as provided under the treaty, the same should not be accepted as the same would mean that treaty was unilaterally amended.

The decision is very important in multiple contexts as tax authorities in many cases (like software cases, cases related to process, etc.) are trying to import amended definition from local laws.

### Should non-compete and non-solicitation fees received by the taxpayer be subject to tax in India under India-Qatar DTAA?

ITO vs Prabhakar Raghavendra Rao [TS-683-ITAT-2019 (Mumbai)]

The taxpayer, a non-resident individual was a Director as well as shareholder in SIPL, an Indian company. The taxpayer sold shares of SIPL to BVCPL (A Singaporean Company) and received the consideration. Further, the non-resident also received non-compete and non-solicitation fees from BVCPL pursuant to an agreement.

During the course of assessment proceedings, the taxpayer adopted a position that in the absence of permanent establishment/business presence in India, he was not liable to pay tax in respect of non-compete and non-solicitation fees received from BVCPL in India as per the relevant DTAA. The capital gains on sale of shares was offered to tax. However, the tax officer observed that the taxpayer had a business connection in India under section 9(1)(i) of the Income-tax Act, 1961 (the Act) since he held shares in SIPL. Further, the non-compete and non-solicitation fees deemed to accrue or arise in India and hence taxable in India.

Held

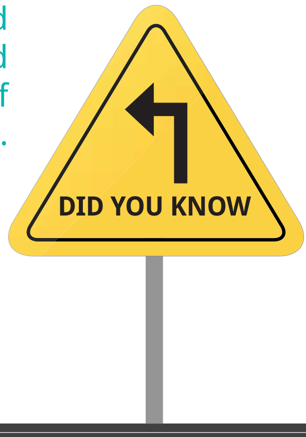
The Tax Tribunal rejected the contention of the tax officer and inferred that merely because the taxpayer had made investments in an Indian company, he cannot be said to have business connection in India. There is no restriction in law for non-residents to invest in shares of Indian companies. Tax consequence may arise once such investments were sold by him which has been duly offered to tax in India. As far as non-compete fees or non-solicitation fees were concerned, the tax tribunal held that such fees would have been taxable under the Act but not under the DTAA without having a permanent establishment in India. Since, non-compete fees were received post selling of shares in SIPL, the taxpayer did not have any business connection or permanent establishment in India, the tax tribunal held that such income was not taxable in India by placing reliance on the decision of Kolkata tax tribunal in the case of Trans Global PLC (158 ITD 230).

#### SKP's Comments

This decision clarifies that while the definition of business connection is wide but the same would not cover any kind of connection with India. The definition needs to be critically examined for determination as to whether there is any business connection in India or not.

Determination of a business connection is a fact-based exercise and the same needs to be contemplated on a case-to-case basis.

Indirect shareholding is covered by the fiction created by deemed dividend under section 2(22)(e) of the Income-Tax Act, 1961.



# Transfer Pricing

## Whether Indian Transfer Pricing Regulations can be applied to taxpayers exempt from paying tax?

Doshi Accounting Services Private Ltd – Special Bench[1]

The taxpayer is engaged in the business of providing Business Process Outsourcing services in the field of accounting and tax. The taxpayer provides these services from an STPI unit which was eligible for tax exemption u/s 10A of the act. The taxpayer has benchmarked the transaction of provision of services by adopting internal/external Comparable Uncontrolled Price (CUP) details. Transfer Pricing Officer (TPO) disregarded the applicability of the CUP method and instead adopted Transactional Net Margin Method (TNMM) to benchmark the transaction. Since the margin of comparable companies (33.10%) was higher as compared to the taxpayer (7.97%), TPO made an adjustment to the transfer price. DRP upheld the adjustment.

### Taxpayer's contention

- It was contended that the taxpayer enjoys the benefit of Section 10A exemption. Moreover, the effective tax rate in the UK would be higher as compared to India (0%) in the instant case. Hence, there was no motive/ incentive in shifting the profit from India to the UK.
- It was argued that the fundamental object of the Transfer Pricing provision is to ensure that India's tax base should not be eroded or profits taxable in India should not be shifted to other tax jurisdictions.
- It was contended that since none of the provisions (i.e. transfer pricing and tax exemption provisions) has an overriding effect on the other, tax exemption provision should be given preference.

### Income Tax Appellate Tribunal ('ITAT') ruling

- Courts are not required to look into the object or intention of the legislature by resorting to aids of interpretation where the language used is clear and free from ambiguity.
- The purpose behind the provision of transfer pricing is to determine true profits/income as if such international transaction has been entered with an unrelated party or non-AE, irrespective of the fact that the income of the assessee was eligible for exemption.
- Further, there is no express provision restricting the application of Transfer Pricing proviso where income is eligible for tax exemption under section 10A. On the contrary, there is a provision to section 92C(4) of the Act which prohibits the deduction under section 10A of the Act on the income to the extent enhanced as an effect of a determination of ALP.
- It was also observed that the assessee, though claiming the exemption under section 10A of the act, can also manipulate the ALP with an objective to avoid corporate dividend tax by shifting its profits to AE.
- Even though the income would be 'exempted income', it still fits in the definition of 'income' as used in Section 92(1) of the act. (The Vodafone India ruling shall not apply since there was no income or potential impact on income)
- Hence, it was held that transfer pricing provision is applicable even if the taxpayer is eligible for tax exemption.

Thus, ITAT dismissed the appeal of the taxpayer.

### SKP's Comments

In other cases having similar fact patterns, the taxpayers have appealed in higher courts such as the Bombay HC and Delhi HC.

It would be interesting to witness the judgment from Bombay/Delhi HC on this issue.

In the meantime, the judgment by Special Bench re-emphasizes the need to justify the arm's length price disregarding the fact that the income of the Indian taxpayer is exempt.

## Can CCDs be characterised as a loan? Can LIBOR be considered as benchmark rate for Rupee denominated CCDs?

Hyderabad Infratech Pvt. Ltd. – ITA No.1891/Hyd/2018

The taxpayer is an Indian company and has paid interest to AEs on Compulsorily Convertible Debentures ('CCD'). CCDs issued are denominated in Indian currency. Transfer Pricing Officer ('TPO') characterised the CCDs as loan and thereafter, determined the arm's length rate of interest to be LIBOR + 200 basis points. The Dispute Resolution Panel ('DRP') upheld the adjustment.

### ITAT ruling:

- ITAT has relied on the assessee's own ruling for AY 2013-14 and co-ordinate bench ruling in case of Adama India Private Ltd (ITA 497/Hyd/2016).
- It was observed that that as per DIPB, RBI and FEMA, CCDs are not loans and it should be reckoned as 'capital instrument'.
- Referring to the Hon'ble Supreme Court's ruling in case of Sahara India Real Estate Corporation Limited and Sahara Housing Investment Corporation Limited & Ors. vs

1. ITA No 1352/Ahd/2011, 1285/Ahd/2012, 1822/Ahd/ 2014 and 1874/Ahd/2014

What is a Special Bench? - In case of conflict of opinions by the division benches on the issues involved in an appeal, the appeals are sometimes heard by the special benches consisting of three or more members. Hence, Special Bench rulings generally carry more weight.

Securities and Exchange Board of India & Anr. (Civil Appeal No. 9813 of 2011), it was held that CCDs are 'Hybrid instruments'.

- In view of the above, it was held that CCDs cannot be characterized as loan.
- Further, considering the fact, CCDs are denominated in Indian currency, it was held that rate of interest should be determined based on the borrower country where the amount is consumed. Hence, LIBOR was rejected as benchmarking rate.

Thus, ITAT allowed the appeal of the taxpayer.

### SKP's Comments

Re-characterization of related party transactions by lower level tax authorities have been consistently rejected by the higher Courts/Tribunals.

## Can adjustments be carried out on account of differences in quality while adopting CUP method?

India Medtronics Pvt Ltd – ITA No.7263/Mum/2018 – AY 2014-15

The taxpayer is in the business of manufacturing, trading and marketing of drugs and pharmaceuticals. It has imported an Active Pharmaceutical Ingredient (API) used in the manufacturing process from its AE located in Switzerland. The taxpayer has used TNMM to benchmark the said transaction.

The TPO has however adopted CUP as the most appropriate method and made an adjustment to the ALP. DRP upheld the matter.

**Taxpayer's contention**

- The taxpayer contended that even if CUP was used to benchmark the transaction, an adjustment needs to be allowed on account of the quality of API.
- API imported from its AE was manufactured in German plant where quality control requirements are much more stringent than in India.
- The taxpayer also submitted independent laboratory test report conducted by Bee Pharma Ltd to verify physical superiority of the product.
- It was contended that the TPO himself had allowed a quality adjustment of 10% in AY 2011-12 (future year)

**ITAT ruling:**

- It was observed that as per Rule 10B(1)(a)(ii), the price of the comparable uncontrolled transaction "is adjusted to account for differences, if any...which could materially affect the price in the open market".
- As long as differences exist, whether having intrinsic value or merely in perceptions, they could "materially affect the price in the open market", these differences are required to be taken into account.
- Even though the generic product may be the same, the same generic product manufactured in a plant, with higher and more stringent quality control requirements, command a premium in the market and greater acceptability with the end consumers of the resultant end product.
- In view of the above and in line with TPO's action for AY 2011-12, ITAT has allowed to carry out quality adjustment at 10%.

The Revenue department filed the appeal before HC.

**HC held that:**

- HC dismissed the appeal of the department.

### SKP's Comments

This ruling emphasizes the need to maintain documentary evidence to justify differences in quality of products/services and reliable adjustment that may be made based on scientific methodology.

# Indirect Tax

## Would the activity of development and sale of land attract GST?

[Background: In view of para 5 of Schedule III of the CGST Act, 2017, the sale of land, subject to clause (b) of para 5 of Schedule II of CGST Act, 2017 i.e. sale of building should be treated neither as supply of goods nor supply of services.]

M/s Maarq Spaces Private Limited - Authority of Advance Ruling (AAR), Karnataka [KAR ADRG 119/2019]

### Facts of the case

- The applicant had entered into a Joint Development Agreement (JDA) for the development of land into residential layout along with specifications and amenities.
- The applicant will construct roads, lay sanitary pipes and drains, etc. and also bifurcate the land into sites and amenities.
- The revenue generated from the property would be shared with the landowners as per their agreement.

### Applicant's contention

- The activity of development undertaken was covered within the definition of 'composite supply' wherein the development activity was incidental to the sale of land.
- Therefore, the sale of developed plot was nothing but sale of land, and hence not chargeable to GST.

### Ruling

- The AAR observed that the applicant represented himself before the landowners as a person having experience and expertise as a land developer.
- The activities undertaken by the applicant are in the nature of development of land into a residential layout.
- Further, from the agreement it was clear that the applicant had no right in title of the land.
- Therefore, the activities undertaken by the applicant cannot be covered under Schedule III as sale of land, and hence would be chargeable to GST.

### SKP's Comments

In case of a joint development agreement, the developer of the land is essentially providing construction and related services to the land owner, and the developer does not have any legal title over the land. Accordingly, the AAR held that the consideration received for such activity cannot be treated as consideration towards the sale of land.

## In case of separate contracts for supply of goods and services in EPC contracts, would the taxability of goods and services be determined separately, or as a composite supply?

M/s Solarsys Non-Conventional Energy Private Limited - AAR, Karnataka [KAR ADRG 120/2019]

### Facts of the case

- The applicant is engaged in the operation of renewable energy power plants which also includes solar power plant set up.
- The applicant has received goods as well as services in terms of their solar plants being set up by EPC contractors.
- There are two separate contracts, one for the supply of goods and the other for supply of services.
- The goods for construction of solar power plants attract a concessional rate of 5% and related services are taxable at 18%.

### Ruling

- The artificial vivisection of the contract into two smaller contracts was not possible, since the two contracts were indivisible in nature.
- The supply of goods and services was covered in the definition of "works contract" and was to be treated as a single supply in spite of two different contracts.
- However from 1 January 2019, the government, vide Notification 24/2018 dated 31 December 2019, clarified that in solar power contracts, the values of goods and services should be deemed to be 70% and 30% respectively of the total value of contract for applying appropriate GST rates.

### SKP's Comments

The AAR has held that even if there are two separate contracts for the supply of goods and services, the overall transaction is an indivisible EPC contract for construction and installation of a solar power plant. The overall nature of the transaction cannot be modified by entering into separate contractual arrangement for the supply of goods and services.

## Should the supply of stores to foreign going vessels be zero-rated supplies?

M/s Shewratan Company Private Limited - AAR, West Bengal [2019 (11) TMI 715]

### Facts of the case

- The applicant is engaged in supplying stores like paint, ropes, spare parts, equipment, etc. to foreign-going vessels.
- In certain cases, such goods may be supplied directly from a customs bonded warehouse.

### Applicant's contention

- The applicant referred to Sections 88(a) of the Customs Act, 1962 which extends the exemption from import duty for warehoused goods taken on board of a foreign-going vessel.
- The applicant also referred to the ruling of the AAR, Andhra Pradesh in case of M/s Fairmacs Shipstores Private Limited wherein it was held that outward supplies made to foreign-going merchant ships would be treated as exports.

### Ruling

- The AAR stated that stores supplied to foreign-going vessels would neither be exports nor zero-rated supplies unless they were specifically marked for a location outside India.
- However, in lieu of Schedule III to the CGST Act, 2017, when such supply is of warehoused goods, then they shall neither be treated as supply of goods nor of services.

### SKP's Comments

In the present case, the AAR held that the condition under GST law of movement of goods outside India to be considered as exports was not fulfilled and hence, the activity was classified as taxable supplies.

However, in an earlier ruling by the AAR, West Bengal in case of M/s Fairmacs Shipstores Private Limited, a similar transaction was treated as export of goods.

In view of these contradictory rulings, it is expected that the matter will be litigated further.

# TAX TALK
## INDIAN DEVELOPMENTS

## Direct Tax

### I-T department to issue PAN instantly online

The Income-Tax department is set to launch a facility to instantly issue Permanent Account Number (PAN) using details from the Aadhaar database. The electronic PAN (ePAN) facility would be available free of cost and “on a near real-time” basis. Those looking for an ePAN will need to quote their Aadhaar and verify the details using a one-time password (OTP). Most of the basic information required for a PAN application would be easily taken from the database. Once a PAN is generated, the applicant will be issued a digitally signed ePAN, with a QR code which will capture the demographic data besides photo of the applicant. The information in the QR code will be encrypted to prevent forgery.

### Sunset clause: Commerce, finance ministries discuss SEZ tax benefit extension

Senior government officials confirmed that the finance ministry is currently assessing the proposal since the revenue department is not in favour of extending the SEZ sunset clause. A final call on the SEZ direct tax benefits extension is yet to be taken and the officials said that it will be taken up once the revenue department begins the budget discussions. Any tax incentive provided by the government lures taxpayers and plays a vital role in an investment decision. In view of the recent reduction of the corporate tax rate and reduction in MAT to 15%, tax arbitrage of SEZ has neutralized. In our view, considering that the government also has to work towards making the existing export benefit schemes compliant with the WTO scheme under FTP 2020-25, foregoing of certain incentives could be a real possibility for exporters including the non-extension of SEZ sunset.

### Digital tax on MNCs: India seeks changes in OECD math

India has sought changes in the Organization for Economic Cooperation and Development (OECD) proposal on digital taxation, saying it would deny the country its proper share of taxes from multinationals such as Google, Facebook, Uber, and Netflix, which generate substantial revenues locally. The government has proposed a more balanced principle for the taxation of such companies based on place of revenue generation. The OECD had on October 9 released a draft on taxing digital companies for public comment. Discussions on the proposal are to be held on November 21-22. All countries have to agree for the rules to be enforced.

The proposed OECD formulation will mean India getting little revenue despite the large digital and business presence of companies, the official said. This is because only “residual profit” will be apportioned among the countries where a company has its markets. The government is of the view that multinational companies derive large revenues from countries such as India via their digital presence, without having a physical one, and has questioned the distinction between “routine profits” which accrue due to physical presence and “residual” profit.

# Transfer Pricing

## CBDT has released APA annual report for FY 2018-19

Advance Pricing Agreement (APA) program was introduced in India more than 7 years ago (in 2012) and currently, it is in 7th annual cycle of examination and processing of applications.

In November 2019, the Central Board of Direct Tax (CBDT) released the 3rd annual report on India's APA Program for the period 2018-19.

The annual report carries forward the CBDT's unique initiative of the last two years to bring into the public domain various statistical and qualitative aspects of India's APA programme. Some of the key highlights are as under:

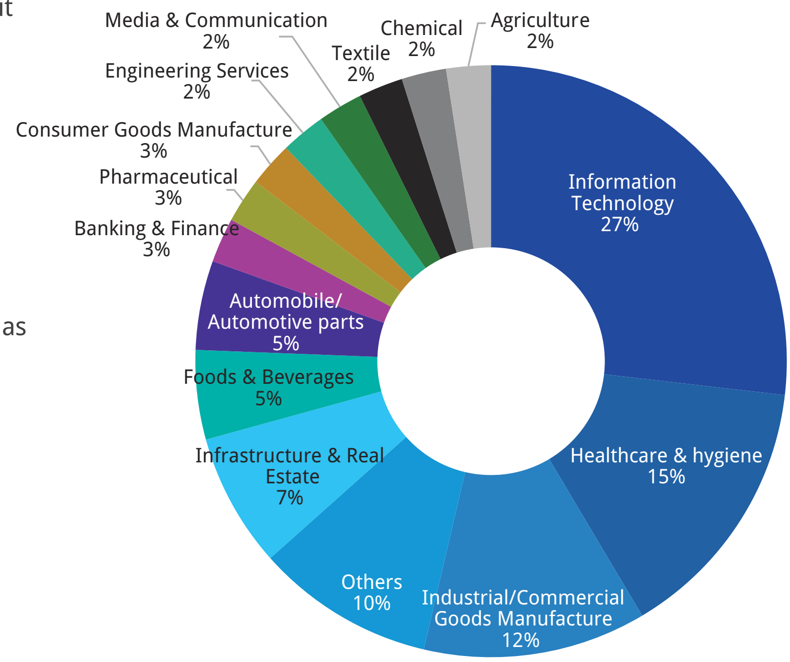
**Important statistics for FY 2018-19**

- New applications filed during the year- 170
  - Unilateral APA - 123
  - Bilateral APA - 47
- Applications signed during the year - 52
  - Unilateral APA - 41
  - Bilateral APA - 11

**Industry-wise bifurcation of signed APA**

The CBDT has released the industry-wise statistics of signed APA. Notably, the Information Technology and Health & Hygiene industries constitute more than 40% of the signed agreements. Diagrammatic representation is provided as under:

Distribution of Agreements — Industry wise – (2018–19)




**Signed Bilateral APA**

The CBDT has mentioned that more than 80% of signed bilateral agreements (31) have been signed with 4 countries, i.e., USA, UK, Japan, and Switzerland.

**Reasons for reduction in signed APA**

While the APA signed in FY 2018-19 has been decreased by 30%, CBDT has clarified the following reasons

- With more and more complex cases coming into the APA Programme, more time is required to analyze the covered international transactions
- The shortage of manpower in the APA teams has continued, which has slowed down the processing of applications.

## Indirect Tax

### Export benefit such as SEZ, EPCG, MEIS, etc. held to be non-compliant with WTO norms

A World Trade Organization (WTO) panel in its report has ruled that the export promotion schemes viz. Merchandise Export from India Scheme (MEIS), Duty Free Import Scheme (DFIS), Export Oriented Units (EOUs), Electronic Hardware Technology Park (EHTP), Bio-Technology Park (BTP), Special Economic Zone (SEZ), etc. are inconsistent with the agreement on Subsidies and Countervailing Measures (SCM), and accordingly should be withdrawn.

The key schemes considered by the WTO panel and its decision thereon are as follows:

| Sr. No. | Scheme and export benefit therein | Conclusion of the WTO panel | Conclusion of the WTO panel |
|---|---|---|---|
| 01 | Exemption from customs duties under EOU, EHTP, BTP and EPCG schemes | Inconsistent with the SCM agreement | 120 days of the adoption of report |
| 02 | Exemption from customs duties and IGST, and deductions from taxable income under the SEZ scheme | Inconsistent with the SCM agreement | 180 days of the adoption of report |
| 03 | Exemptions from customs duties under conditions 10, 21, 36, 60(ii), 61 of DFIS | Inconsistent with the SCM agreement | 90 days of the adoption of report |
| 04 | Duty Credit Scrips under MEIS | Inconsistent with the SCM agreement | 120 days of the adoption of report |
| 05 | Exemptions from central excise duty on domestically procured goods under EOU, EHTP and BTP schemes | Consistent with the SCM agreement | NA |
| 06 | Exemption from customs duties under conditions 28, 32, 33, 101 of DFIS | Consistent with the SCM agreement | NA |

### Government invites suggestion for RoDTEP scheme

Recently, the government had announced its plans to launch the Remission of Duties or Taxes on Export Products (RoDTEP) scheme to replace the existing MEIS and other export promotion schemes.

Now, in order to determine the burden of embedded taxes and formulate incentive rates under the proposed scheme, the Ministry of Commerce and Industry is inviting product-wise data/information from manufacturing units/exporters. Following product-wise data should be provided in a format set by the government:

- Details of the exported product;
- Details of common embedded taxes such as transportation, electricity, etc.;
- Details of embedded taxes on raw materials/inputs.

### Simplification of GSTR-9 (Annual Return) and GSTR-9C (Reconciliation Statement)

The government has brought in simplifications to annual return (GSTR-9) and reconciliation statement/audit (GSTR-9C) FY 2017-18 and FY 2018-19. Some of the key points are captured hereunder –

**Changes in GSTR-9 (Annual Return)**

- An option to disclose Table 4B to 4E [i.e., B2B supplies, exports/SEZ supplies (with payment of tax), deemed exports] net of credit/debit notes and amendments.
- Exempted, Nil-Rated and Non-GST supplies can be shown entirely in the “exempted supplies” row.
- The break-up of Input Tax Credit (ITC) availed in GSTR-3B into inputs, input services, and capital goods is made optional.
- The disclosure of HSN wise summary of outward and inward supplies is made optional.

**Changes in GSTR-9C (Reconciliation Statement)**

- The requirement of reconciliation of sales turnover as per the financials with the annual return is made optional.
- Reconciliation of the ITC availed and the expense wise disclosure of ITC availed is made optional.

The above relaxations have been provided by the government to the taxpayers to ensure that they finalize their GSTR-9 and GSTR-9C return quickly to meet the extended due date of 31 December 2019.

[Notification No. 56/2019-Central Tax dated 14 November 2019]

## Communications from the GST department to contain DIN

The government has directed that search authorizations, summons, arrest memos, inspection notices, and letters issued in the course of any inquiry by any officer should contain a computer-generated Document Identification Number (DIN). This should be applicable to documents issued on or after 8 November 2019.

Any communication not bearing the DIN and not covered under certain exceptions should be considered invalid and deemed to have never been issued. The recipient of the communication can ascertain the genuineness of the DIN by using the facility available on https://www.cbicddm.gov.in/MIS/Home/DINSearch

[Circular No. 122/41/2019 – GST dated 5 November 2019]

# TAX TALK
## GLOBAL DEVELOPMENTS

## Direct Tax

### Global Anti-base Erosion (GloBE) Proposal – A strong response to the multinational companies' practice of shifting profits to low/no tax jurisdictions!!

Recently, the Organization for Economic Cooperation & Development (OECD) released a public consultation document on GloBE Proposal under Pillar II before closing the window for stakeholders to submit their comments on Unified Approach under Pillar I. Pillar II is a more structured/well-researched proposal to achieve minimum global taxation. The questionnaire is inclined more towards determining the feasibility of using financial accounts for tax purposes.

Our Knowledge on GloBE Proposal

The GloBE Proposal calls for development of coordinated rules that may avoid the shifting of profits by multinational companies, resulting into no/low taxes. This would be achieved by requisite amendments in domestic tax laws as well as tax treaties which are as follows:

| | | |
|---|---|---|
| **Domestic Tax Laws** | Income Inclusion Rule | Allows countries to tax income from overseas branches/controlled entities if such income was not subject to a minimum effective tax rate. |
| | Undertaxed Payment Rule | Denies a deduction or grants source based taxation for payments made to related parties if such payments were not subject to a minimum effective tax rate. |
| **Tax Treaties** | Switch-over Rule | Allows countries to switch from exemption to credit method when profits attributed to a permanent establishment/derived from immovable property (not forming part of PE) are not subject to a minimum effective tax rate. |
| | Subject to Tax Rule | Grants or denies tax treaty benefits if an item of income was not subject to tax at a minimum rate. |

### Way Forward

The OECD has done a great job while drafting the GloBE proposal as this would ensure that multinational companies in the digital economy and beyond would end up paying a minimum rate of tax. The main objective of this proposal is to provide all the stakeholders involved the necessary tools to fight shifting of profits by multinational companies to low/no tax jurisdictions. One of the key propositions of this proposal, i.e., using financial accounts would entail problems for different countries as each country would have different methods to determine items of income and expenditure leading to gross complexities. To tackle such a situation, it would be imperative for the OECD to provide for clear and constant list of inclusions and exclusions in respect of items of income and expenditure so that financial accounts across the globe could be arrived at basis common accounting principles.

Another important aspect is the determination of a minimum rate of tax to be borne by the multinational companies. The OECD should come out with concrete factors for determination of the minimum rate of tax payable by multinational companies to avoid unnecessary clashes amongst countries across the globe. It is to be seen how this proposal would be implemented on a real-time basis by countries across the globe. It would also be interesting to see whether the OECD, along with all the stakeholders involved, provides for a tax credit mechanism to avoid double taxation.

## Transfer Pricing

### Ireland's Finance Bill 2019 provides transfer pricing related legislative changes

On 17 October 2019, Ireland's Department of Finance released Finance Bill 2019 which provides for legislative changes to tax laws effective from accounting periods beginning on or after 1 January 2020. Transfer pricing-related key developments vide Finance Bill 2019 are summarised below:

**a. Aligning transfer pricing laws with 2017 OECD transfer pricing guidelines**

Finance Bill 2019 has proposed to align transfer pricing laws of Ireland with OECD transfer pricing guidelines (issued on 10 July 2017) and other guidelines relating to Intangibles/ Transactional Profit Split Method

**b. Applicability of Transfer Pricing Regulations to small and medium-sized enterprise**

Finance Bill 2019 has indicated that Transfer Pricing Regulations may apply to small and medium-sized enterprises where"

- Aggregate consideration for related party transactions exceed EUR 1 million; or
- Value of transaction relating to acquisition/ disposal of asset is more than EUR 25 million.

However, it is proposed that small enterprise shall be exempt in preparation of Transfer pricing documentation.

For this purpose, small enterprise means an enterprise having:

- Less than 250 employees; **and**
- Either an annual turnover less than EUR 50 million or assets worth less than EUR 43 million

This is an annual test and applied at the group level.

Medium enterprise means an enterprise having:

- Less than 250 employees but more than 10 employees; and
- Either annual turnover is less than EUR 50 million but more than EUR 2 million; or
- Assets less than EUR 43 Million but more than EUR 2 million.

### c. New transfer pricing documentation requirements

Finance Bill 2019 has introduced compliances relating to Master file and Local file in case consolidated turnover of Group exceeds the prescribed threshold:

| Particulars | Threshold – Consolidated Group Turnover |
|---|---|
| Master File | EUR 250 million |
| Local File | EUR 50 million |

Further, it is proposed that documentation needs to be prepared on a contemporaneous basis, i.e., latest by filing annual corporate tax return. Accordingly, for a fiscal year ending on 31 December 2020, documentation needs to be prepared on or before 23 September 2021.

### d. New transfer pricing penalty provisions

Finance Bill 2019 has proposed following penalties for non-compliances as under:

| Particulars | Penalty amount |
|---|---|
| Failure to provide information/ documentation within prescribed time | EUR 4,000 |
| Failure to provide local file documentation within prescribed time | EUR 25,000 + EUR 100 per day |

### e. Extending transfer pricing rules to non-trading transactions

Finance Bill 2019 has proposed to extend transfer pricing law to non-trading transactions as well along with existing applicability to trading transactions.

### f. Extending transfer pricing rules to capital transactions

Finance Bill 2019 has proposed to extend Transfer pricing rules to capital transactions from 1 January 2020 in case the quantum of transaction exceeds EUR 25 Million.

### g. Grandfathered arrangements

Existing Irish transfer pricing rules allows exemption for certain arrangements/transactions entered into before 1 July 2010. Finance Budget 2019 has proposed to remove such exemption.

## UAE: Frequently Asked Questions ("FAQ's") released relating to Country-by-Country Reporting ("CbCR") in UAE

UAE had issued the Cabinet Resolution No. 32 of 2019 (the "Resolution") on Country-by-Country ("CbC") Reporting on 30 April 2019. For further details on CbC Reporting-related regulations in UAE, refer our tax alert Click here.

On 16 October 2019, the Ministry of Finance of UAE released list of 25 Frequently Asked Questions ("FAQs") to address the concerns of tax payers in relation to CbC Reporting.

FAQs have been divided in 3 groups as under:

- FAQs relating to general CbC Reporting consideration
- FAQs relating to CbC Reporting filing
- FAQs relating to CbC Reporting notification

Few of the important clarity provided by the recently released FAQ's are summarised hereunder:

| Questions | Answers |
|---|---|
| Can the OECD guidance on CbC Reporting be used to interpret the UAE CbC Reporting Legislation? | The OECD guidance on the implementation of CbC Reporting can be used to interpret the UAE CbC Reporting legislation to ensure a consistent and standard approach to CbCR across all implementing countries. However, if there is a conflict, the UAE CbC Reporting legislation takes precedence. |
| Duration for which CbCR should be kept by reporting entity in UAE? | The effective records should be kept by a CbC Reporting Entity for 5 years following the date on which the CbC Report is submitted to the Ministry of Finance. |
| When do the CbC Reporting requirements come into effect in the UAE? | CbC Reporting requirements come into effect for financial years starting on or after 1st January, 2019. Accordingly, for the financial reporting year starting on 1st January 2019 and ending on 31 December 2019, CbCR must be submitted latest by 31 December 2020. |

| Questions | Answers |
|---|---|
| What currency should be used for CbC Reporting purposes? | If separate entity statutory financial statements are used as the basis for reporting, all amounts should be translated to the stated functional currency of the MNE Group. The average exchange rates for the year should be used for currency conversion. The applied rates should be stated in the Additional Information section (Table III) of the CbC Report. |
| In which language should the CbC Report be submitted in the UAE? | The CbC Report should be submitted in English. |

Further, it has been mentioned that more specific guidance on completing CbC Reporting, filing of detailed CbC Reporting form, and filing of the CbC Reporting notification in the UAE shall be provided soon.

The FAQ's provided by the Ministry of Finance of UAE would help the taxpayers in effectively complying with the CbC Reporting related compliance in UAE.

## Thailand: Transfer Pricing disclosure form

Thailand's tax authority has released a disclosure form to be filled by the taxpayers in order to provide certain Transfer Pricing related information for the fiscal year beginning on or after 1 January 2019. The disclosure form is required to be filled by taxpayers having revenues of more than THB 200 million (apprx USD 6.6 million) for the accounting year. The said form is required to be submitted within 150 days from the end of the accounting year. Following information to be provided in disclosure form as under:

- List of related parties
- Quantum of related party transactions – Separate details to be provided for
  - cross-border transaction and domestic transaction
  - income and expenses transactions
- Classification of expenses transaction (such as transactions relating to purchase of raw materials, goods, land, building and equipment, royalties, management technical services, commission fee, and interest expenses)
- Consolidated financial information
- Business restructuring-related information
- Details in relation to sales, distribution, and transfer of intangibles between group entities.

## Costa Rica amends Transfer Pricing Documentation related regulations

On 13 November 2019, Costa Rica's tax authority released a new resolution laying down new guidelines for Transfer Pricing Documentation in relation to Master File and Local File compliances. With the new guidelines, the old resolution (2017) has been repealed.

The new resolution require taxpayers carrying out transactions with related companies to maintain documentation justifying their intercompany transactions in lines with independent party. The said documentation must be prepared based on OECD's BEPS Action Plan 13.

Important details to be covered are as below:

| Details relating to Master File | Details relating to Local File |
|---|---|
| a. Corporate structure<br>b. Group administration structure<br>c. Document showing the chain of suppliers of goods and services<br>d. List of the main markets<br>e. Group intangibles<br>f. Intragroup services<br>g. Financing<br>h. Description of the restructuring carried out during the last five years<br>i. A chart showing the total number of employees for each country<br>j. A copy of the statement of consolidated income for the most recent period | a. Administration structure of the local entity<br>b. Identification and documentation of other controlled transactions that may directly or indirectly affect the price of those transactions<br>c. Reasons as to why a multi-year analysis is applied<br>d. Audited financial statements of the previous three years |

## Indirect Tax

### Kenya imposes VAT on import of services by unregistered person

The Kenyan government has amended their Value Added Tax (VAT) law to levy VAT under reverse charge mechanism on the import of taxable services by persons otherwise not registered under the VAT regime. It remains to be seen whether the government intends to enforce this provision against individuals who are not involved in business and commerce.

# Compliance Calendar

**7 December 2019**

- Payment of TDS and TCS deducted/collected in November 2019

**10 December 2019**

- GSTR-8 for the month of November 2019 to be filed by taxpayers required to collect tax at source (TCS)
- GSTR-7 for the month of November 2019 to be filed by taxpayers required to deduct tax at source (TDS)

**11 December 2019**

- GSTR-1 for the month of November 2019 to be filed by registered taxpayers with an annual aggregate turnover of more than INR 15 million

**13 December 2019**

- GSTR-6 for the month of November 2019 to be filed by input service distributors

**15 December 2019**

- Payment of third instalment of advance tax for FY 2019-20 (75% of the estimated tax liability to be deposited on a cumulative basis)

**20 December 2019**

- GSTR-3B for the month of November 2019 to be filed by all registered taxpayers
- GSTR-5 for the month of November 2019 to be filed by Non-resident taxable person
- GSTR-5A for the month of November 2019 to be filed by persons providing Online Information and Database Access or Retrieval (OIDAR) services

**30 December 2019**

- E-Filing of Country-By-Country Report in Form No. 3CEAD in case of International group whose accounting year ends on 30 December 2018
- Due date for furnishing of challan-cum-statement in respect of tax deducted under section 194-IA for the month of November 2019
- Due date for furnishing of challan-cum-statement in respect of tax deducted under section 194-IB for the month of November 2019

**31 December 2019**

- GSTR-9 for the period from July 2017 to March 2018 to be filed by the regular taxpayers (voluntary if aggregate turnover is less than INR 20 million)
- GSTR-9A for the period from July 2017 to March 2018 to be filed by the persons registered under composition scheme
- GSTR-9C for the period from July 2017 to March 2018 to be filed by taxpayers with an aggregate turnover of more than INR 20 million

# UPCOMING EVENTS

# SKP IN THE NEWS

### How India May Approach the WTO Ruling

"The SCM Agreement seems to have a narrow application by allowing subsidies only in respect of inputs consumed in production of export products." – **Jigar Doshi**

Tax Sutra - November 25, 2019

Read more at https://bit.ly/2Dhshw7

### Three suggestions on how finance minister can reform the direct tax law

"Simplification of tax rules is a must, it should be done in such a way that it will be able to help the government as well as the taxpayers, and there should be no uncertainty, which right now is prevailing and results in lot of litigations."
– **Neeraj Sharma**

Live Mint - November 25, 2019

Read more at https://bit.ly/2DMvCnb

## Alerts

### Government announces the extension of GST annual return GST audit due date along with simplification of forms

Read here https://bit.ly/2XcUWeS

### Export benefit such as SEZ, EPCG, MEIS, etc. held to be non-compliant of WTO norms

Read here https://bit.ly/36YExiE

## Recent Developments under GST Regime

Assocham

Bengaluru, 6 December 2019

Jigar Doshi / Rebecca Pinto

Visit https://www.assocham.org/eventdetail.php?id=1804 for more details

## Webinar – Changing face of GST compliances and GST Audit

10 December 2019

Organizer – Nexdigm (SKP) and USISPF

Jigar Doshi / Rebecca Pinto

Register here https://bit.ly/2rXZrym

# About **SKP**

SKP is a multidisciplinary group that helps global organizations meet the needs of a dynamic business environment. Our focus on problem-solving, supported by our multifunctional expertise enables us to provide customized solutions for our clients.

Our cross-functional teams serve a wide range of industries, with a specific focus on healthcare, food processing, and banking and financial services. Over the last decade, SKP has built and leveraged capabilities across key global markets to provide transnational support to numerous clients.

We provide an array of solutions encompassing Consulting, Business Services, and Professional Services. Our solutions help businesses navigate challenges across all stages of their life-cycle. Through our direct operations in USA, India, and UAE, we serve a diverse range of clients, spanning multinationals, listed companies, privately owned companies, and family-owned businesses from over 50 countries.

Our team provides you with solutions for tomorrow; we help you think next.

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