KNAV
PARTNERS BEYOND BOUNDARIES

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In this edition of our thought leadership publication, we have tracked the progress of some significant cases decided by the appellate forums across the country along with an important notification, a miscellaneous communication and important press releases issued by the Central Board of Direct Taxes.

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Transfer Pricing

Case Law 1: Nivea India (P.) Ltd. Vs. ACIT [2018] 92 taxmann.com 165 [TMum]

In a case where there is no agreement or arrangement between the assessee and its associated enterprise ('AE') for incurring advertising, manufacturing and publicity ('AMP') expenses, the transaction does not constitute as an international transaction ('IT') and a transfer pricing ('TP') adjustment cannot be made.

Facts of the case:

The assessee is principally engaged in the sale of products in India. The AE supplied raw material / packing material / semi-finished goods / finished goods to the assessee as certain products were manufactured by the assessee and certain others were imported.

During assessment proceedings, the transfer pricing officer ('*TPO')* held that as AMP expenditure incurred by the assessee is significantly high, it translates to development of brand and leads to creation of valuable marketing intangible for the AE. The TPO stated that the assessee had incurred these expenses for the benefit of the AE as the assessee is merely a beneficiary and not the legal owner of brands in India. Therefore, the TPO was of the view that the assessee should be compensated by the AE for its marketing efforts.

The assessee preferred appeal before the Hon'ble Dispute Resolution Panel ('*DRP*'). However, the Hon'ble DRP upheld the TPO's order.

Aggrieved, the assessee preferred an appeal with the Hon'ble Tribunal.

Decision of the Hon'ble Tribunal:

The Hon'ble Tribunal was of the view that the assessee was a new entrant in the field of manufacturing and sale of cosmetic and personal care. The assessee had to incur expenses to create brand awareness in order to establish its foothold in the country.

Further, the Hon'ble Tribunal observed that there is a fine difference between product promotion and brand promotion. In the instant case, the assessee incurs AMP expenditure on the new products and not the brand.

The Hon'ble Tribunal stated that the AMP expenses incurred benefitted the assessee by creation of market share and increased turnover. The AMP expenses were wholly and exclusively for the promotion of business of the assessee, and not an expenditure on behalf of AE.

Therefore, the Hon'ble Tribunal held that the said transaction was not an IT and consequently, no TP adjustment could be made.

International Tax

Case Law 1: Samsung Electronics Co. Ltd. Vs. DCIT (Int. Taxation) [2018] 92 taxmann.com 171 [TDel]

A fixed place Permanent Establishment ('PE') of the assessee cannot be constituted in absence of any business conducted by assessee through expatriated employees nor any income derived by them though activities of these employees.

Facts of the case:

The assessee is based out of South Korea and is a tax resident of Republic of Korea, engaged in manufacturing and sales of various categories of televisions, home appliances, telecommunication terminals, semi-conductors as well as other state of the art information technology products for global markets. It has two wholly owned subsidiaries in India i.e. SIEL and Samsung R&D. The assessee had seconded expatriate employees which were rendering services to the subsidiary company.

Pursuing a survey conducted on the premises of the Indian subsidiary companies, the Assessing Officer ('*the AO*') issued a notice u/s 148 of the Income tax Act, 1961 ('*the Act*') to initiate reassessment proceedings for six AYs beginning from AY 2004-05. In the draft assessment order, the AO contended that the seconded expatriate employees were rendering services to SIEL on behalf of the assessee and, therefore, created a fixed place PE of the assessee in India under Article 5 of the India-Korea Double Taxation Avoidance Agreement ('*DTAA*'). Accordingly, the AO added an estimated income of 10% on the remuneration paid to such expatriate employees during the years under consideration to determine the profits attributable to tax in India by applying clause (iii) of Rule 10 of the Income Tax Rules, 1962 ('*the Rules*').

In addition to this, the AO rejected the objections filed by the assessee in response to the draft assessment and further, proposed to treat the subsidiary to be an agency PE as well as a service PE since the subsidiary was a place of management for the assessee's south east operations.

On reference to the Hon'ble DRP, following points were observed:

1. The subsidiary was incorporated under the laws governing the companies in India, it filed its returns as per the domestic revenue provisions and other statutes. Also, IT were reported by the subsidiary per the TP provisions in India.
2. In respect of the seconded employees, the assessee had no significant control over the posting of the seconded employees to various projects etc. Everything was decided pursuant to the tripartite agreement between the assessee, the Indian subsidiary and the seconded employees.

Based on the findings of the Hon'ble DRP, the Hon'ble DRP rejected all the contentions of the AO except that it can be treated as the fixed place PE. Pursuant to the directions of the Hon'ble DRP, the AO passed the final assessment order.

Aggrieved, the assessee as well as the revenue preferred cross appeals before the Hon'ble Tribunal.

Decision of the Hon'ble Tribunal:

The Hon'ble Tribunal noted that the entire dispute revolved around status of the expatriate employees working with the subsidiary and the nature of the functions performed by them i.e. whether they are the employees of the assessee and placed within the subsidiary to carry out business operations of the assessee or they are seconded employees of the subsidiary and the subsidiary is the economic employer who exercises full control over them.

On an analysis of the submissions / information / documents, the Hon'ble Tribunal highlighted the following key points:

1. The services rendered by the expatriate employees included providing information relating to models / design to the liking of the Indian consumers, plans and strategies etc.
2. None of the activities carried out by the employees would directly constitute that the business of the assessee had been carried out in India.
3. All the activities carried out by the expatriate employees had been related to the specificity of the products, stock verification, designs according to the preferences of the Indian consumers, the market strategies to be adopted etc. and were clearly within the ambit of the business of the Indian subsidiary. Such a communication would primarily benefit the Indian subsidiary, and would help the assessee to sustain its supply chain management and optimize purchase orders at a right timing or to acquire the most promising manufacturing technologies.
4. The benefits from the services were offered to tax in India by the Indian subsidiary.

Also, a plain reading of Article 5 of the DTAA suggests that in order to constitute a PE, there must be a fixed place of business available to the assessee, through which the business of the assessee is wholly or partly carried on.

Grounded on the definitions and the findings as above, the Hon'ble Tribunal held that the expatriate employees were merely discharging the functions of the subsidiaries towards the holding company. Further, there were no proofs as to any management activity like pricing decision making, decisions relating to launch of the product being conducted in the subsidiary by the expatriate employees.

The findings of the AO that the employees of the subsidiary had been conducting business in India was therefore, reversed by the Hon'ble Delhi Tribunal.

The Hon'ble Tribunal ruled in favor of the assessee and directed to delete the advance payments added by the AO to taxable income.

Domestic Tax

Case Law 1: ACIT Vs. Shri Shrey Sharma Guleri Prime Channel Software Communications (P.) Ltd. [2018] 92 taxmann.com 43 (TMum)

Where assessee sells basement and realizes capital gain which is invested in acquiring a house property, and there is sufficient evidence that the basement is part and parcel of residential unit/house, in the form of photographs, property tax bill and electricity bills issued by BSES/Rajdhani Power Ltd., the assessee is entitled to claim exemption u/s 54 of the Act.

Facts of the case:

In the case of the assessee, during the assessment proceedings u/s 143(3) it was revealed that the assessee had sold a basement flat and realized capital gain of INR 1,24,08,721, which was invested in acquiring two house properties in the same building. The stand of the AO was that the basement does not fall within the purview of "residential flat" as envisaged u/s 54 of the Act. Accordingly, the AO taxed the gain arising therefrom, not allowing the assessee the deduction u/s 54 of the Act.

The argument of the revenue was that the basement in the house cannot be termed as a residential house within the provisions of section 54 of the Act. On the other hand, the assessee pleaded that basement is part and parcel of the residential unit, therefore, it cannot be termed as a separate unit.

Decision of the Hon'ble Tribunal

The Hon'ble Tribunal stated that the only issue which required adjudication whether the basement is part and parcel of a residential unit. The Hon'ble Tribunal opined that when a sanction is approved by the municipal Authorities / competent authorities, naturally such approval is granted with the basement and even today above certain limit stealth parking has been made

mandatory, keeping in view the traffic problem in the bigger city like Delhi. Normally, the basement is used as a residential unit and if there is any violation there is a separate provision of taking action by the Municipal Authorities. Even if it is used as a residential unit by the domestic helps or used as a play ground like table tennis, it cannot loose its character as a residential unit.

Further, the Hon'ble Tribunal noted that there is uncontroverted finding in the impugned order that there was evidence on record to show that the basement referred as "A-2 / 30" of Sufdarjang Enclave was a habitable unit. The assessee produced the photographs of the basement clearly revealing, independent entry gate, stair case, living room, bed room, dining, wash basin, toilet, kitchen and mini-drawing room.

The Hon'ble Tribunal further stated that if the AO was apprehensive of some mala-fide, nothing prevented the AO to make an actual site / building visit and should have examined the factual matrix. The assessee also produced the evidences like property tax bill and electricity bills issued by BSES / Rajdhani Power Ltd. evidencing that the basement was infact used as a residential unit. The Hon'ble Tribunal concluded that such evidences cannot ignored.

Thus, the Hon'ble Tribunal held in favour of the assessee and stated that the assessee is entitled for exemption u/s 54 of the Act.

Case Law 2: Jasvinder Hans Vs. ACIT [2018] 92 taxmann.com 172 (TAmr)

Wherein the assessee opines that the fair market value ('FMV') of the property is less than the stamp value adopted for the purpose of computation of capital gains u/s 48 of the Act, it is incumbent on the assessee to request the AO to refer the matter to a Valuation Officer ('VO'). It is not the procedure of the law that the AO himself will assume the assessee to be prejudiced, and would be obligated to refer the same to the VO himself.

Facts of the case:

The assessee sold a house property for a consideration of INR 11,00,000 and subsequently offered the capital gains earned, as computed u/s 48 of the Act. During the assessment proceedings, the AO invoked section 50C of the Act, and substituted the consideration with the value adopted for stamp duty purposes, amounting to INR 12,00,000. Accordingly, an addition of INR 1,00,000 was made by the AO in the capital gains computed by the assessee.

The assessee preferred appeal before the Hon'ble Commissioner of Income tax (Appeals) ('*CIT(A)*'), wherein the assessee claimed that while substituting the consideration, no opportunity was granted by the AO to the assessee during the assessment proceedings prior to invoking section 50C of the Act. However, even though the Hon'ble CIT(A) opined that it would have been advisable for the AO to confront the assessee, the Hon'ble CIT(A) upheld the AO's decision stating that the re-computation was well within the provisions of section 50C of the Act and not ultra-virus.

Aggrieved, the assessee further preferred an appeal before the Hon'ble Tribunal.

The assessee argued that the AO was duty bound to confront the assessee before invoking section 50C of the Act thereby satisfying the principle of natural justice. The assessee disagreed that the mechanism for referring the matter to the VO for resolving any dispute as to valuation, as provided u/s 50C(2) of the Act, was only to be triggered when the assessee himself makes such a claim. However, there was no doubt in the fact that the assessee in the present case had made no such claim. Further, the assessee argued the very fact that a notice u/s 143(2) of the Act had been issued implies that the assessee is to be called upon to state his case whenever any adjustment to the returned income is to be made.

Decision of the Hon'ble Tribunal

The Hon'ble Tribunal observed that that it is for the assessee to exercise the right for seeking reference u/s 50C(2) of the Act, and in the absence of any such claim, it would not be presumed that the assessee had been prejudiced. The Hon'ble Tribunal explains that where the stamp value is disputed under the Stamp Act, the resolution of the said dispute itself redresses the grievance on account of application of stamp value. The law thus provides for an in-built mechanism (in section 50C(2)(b) of the Act) for the redressal of the prejudice contended to be caused by the substitution of the actual consideration by deemed consideration, thus, saving the provision from a charge to its vires. In a scenario wherein the assessee opines that the FMV is in fact lower than the stamp value, then the same could be challenged (for its correctness) both under the Stamp Act as well as, where not disputed there-under, before the VO, adhering to the principles of equity and fair procedure.

The Hon'ble Tribunal opined that the observation by the Hon'ble CIT(A) of it being advisable for the AO to confront the assessee, is, in view of his categorical finding of the AO being not obliged to do so under law, without any significance, and is merely an '*obiter dicta*', and would not operate to override the express provision of law.

Based on the above, the Hon'ble Tribunal concluded that the assessee's case was misconceived and without merit. The Hon'ble Tribunal held that there has been no violation of either the principles of natural justice, or of the procedure as laid down in the law by the AO.

Thus, the Hon'ble Tribunal decided in favour of the revenue.

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Case Law 3: Prasar Bharati Vs. CIT [2018] 92 taxmann.com 11 (SC)

Payment to various accredited advertising agencies to secure more business was in nature of commission paid, thereby being liable to deduction of tax at source ('TDS') u/s 194H of the Act.

Facts of the case:

The assessee, Prasar Bharati Doordarshan Kendra, functions under the Ministry of Information and Broadcasting, Government of India and is engaged in the running of the TV channel. It has been regularly telecasting advertisements of several consumer companies.

The assessee entered into an agreement with several advertising agencies. In terms of the agreement, the advertising agency was required to make an application to the assessee to get the 'accredited status', to enable them to do business with the assessee of telecasting the advertisements of various consumer products manufacturing companies on the assessee's TV Channel. The agreement between the assessee and the advertising agency required the assessee to pay the agency a commission of 15%, the same to be wholly retained by the agency. The agency was to give minimum annual business of INR 6,00,000 to the assessee in a financial year failing which their accredited status was liable to be withdrawn.

The assessee paid substantial amounts as commission to various accredited agencies, in line with the terms of the agreement. However, the assessee did not deduct TDS u/s 194H of the Act, on such commission payments. The AO was of the view that the assessee had violated the law and consequently, the AO invoked the provisions of section 201(1) of the Act.

On appeal, Hon'ble CIT(A) confirmed the AO's order. Aggrieved, the assessee preferred an appeal before the Hon'ble Tribunal.

The Hon'ble Tribunal ruled in favour of assessee. Aggrieved, the revenue preferred an appeal before the Hon'ble High Court.

The Hon'ble High Court ruled in favour of the revenue. Aggrieved, assessee preferred an appeal before the Hon'ble Apex Court.

Decision of the Hon'ble Supreme Court:

The assessee argued before the Hon'ble Apex court that the relationship between the assessee and the accredited Agencies was not that of principal and the agent but it was in the nature of principal-to-principal. Further, the assessee also submitted that the Agencies purchased the air time from the assessee and then sold it to their customers after retaining 15% commission given to them by the assessee.

The Hon'ble Apex Court observed that the agreement specifically used the expression 'commission' in all relevant clauses. Further, Hon'ble Apex Court observed that the terms of the agreement indicate that both the parties intended that the amount paid by the assessee to the agencies should be paid by way of 'commission', also considering the tenure and the nature of transaction.

The Hon'ble Apex Court was of the view that the transaction in question did not show that the relationship between the assessee and the accredited agencies was principal to principal rather it was principal and agent. The Hon'ble Apex Court, on a reading of the definition of 'commission' as per the Explanation appended to section 194H of the Act, was of the view that, the inclusive definition gave a wide meaning to the expression 'commission', and consequently, the transaction in question did fall under the definition of the expression 'commission'.

In view of above, the Hon'ble Apex Court upheld the Hon'ble High Court's order and concluded that the payment by the assessee to the advertising agencies is liable to TDS u/s 194H and that the AO rightly invoked section 201(1) against the assessee.

Recent important press releases, a notification and a miscellaneous communication issued by the central board of direct taxes ('*CBDT*')

1. Press release dated January 6, 2018 - Relaxation in the provisions relating MAT for companies undergoing insolvency

In case of companies against whom an application for corporate insolvency resolution process has been admitted under the Insolvency and Bankruptcy Code, 2016, the amount of total loss brought forward (including unabsorbed depreciation) shall be allowed to be reduced from the book profit for the purposes of levy of MAT u/s 115JB of the Act with effect from AY 2018-19.

The link to visit the press release is provided hereunder:
https://www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/681/Press-Release-Relaxation-provisions-relating-levy-MAT-8-1-2018.pdf

2. Miscellaneous communication CBDT F no. 225/270/2017/ITA. II dated March 27, 2018 – Extension of time limit to link PAN with Aadhar.

Vide this miscellaneous communication, the CBDT has extended the due date for linking of Aadhar and PAN while filing of the income tax return through the E-filing portal upto June 30, 2018.

The link to visit the press release is provided hereunder:
https://www.incometaxindia.gov.in/Lists/Latest%20News/Attachments/234/ORDER-UNDER-SECTION-119-MiscComm-27-3-2018.pdf

3. Press release dated April 5, 2018 - Clarification regarding applicability of standard deduction to pension received from former employer.

The CBDT via this press release has provided clarification that an individual receiving pension from his former employer is also eligible to claim standard deduction of INR 40,000 from his income taxable under the head 'Income from Salaries'.

The link to visit the press release is provided hereunder:
https://www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/701/Press-Release-Clarification-regarding-applicability-standard-deduction-pension-received-former-employer-5-4-2018.pdf

4. Notification No. 4 of 2018 dated April 5, 2018 of Directorate of Income Tax (Systems)

The notifications spells out the procedure for registration and submission of Statement of Reportable Account as per section 285BA of the Act read with Rule 114G of the Rules.

The link to visit the notification is provided hereunder:
https://www.incometaxindia.gov.in/communications/notification/system-notification-4-of-2018.pdf

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