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Articles

Most favoured nation (MFN) clause 'no' more favourable

By **Sumeet Khurana & Ashish Karundia**

The recent decision given by the Authority for Advance Rulings ('AAR') in *Steria (India) Ltd.*[1] has unsettled the position, wherein it has held that 'Protocol' signed along with the treaty cannot be treated at par with the provisions contained in the treaty itself, though it may be an integral part of the treaty.

In the instant case, Steria (India) Ltd. ('Steria India/taxpayer') availed management services from Groupe Steria SCA ('Steria France') in respect of which payment was required to be made. Steria India argued that even though the services qualify as technical service ('FTS') under Income Tax Act, 1961 as well as India-France DTAA, tax is not required to be deducted at source, pursuant to Most Favored Nation ('MFN') clause in the Protocol annexed with the treaty. The taxpayer submitted that India-UK DTAA provides for a restricted definition of FTS and thus, Steria India is also eligible for such a beneficial treatment by virtue of the Protocol.

The AAR held as follows:

- Protocol or Memorandum of Understanding cannot be used to import words, phrases or clauses, that are not available in the treaty under consideration;
- Protocol cannot be treated at par with treaty; and
- 'Make available' clause cannot be read in Protocol, absent specific mention;

A critical analysis of the ruling is made in the following paragraphs.

Relevance of Protocol

The Protocol to India-France DTAA starts as *'At the time of proceeding to the signature of the Convention between France and India for the avoidance of double taxation with respect to taxes on income and on capital, the undersigned have agreed on the following provisions which shall form an integral part of the Convention".*[2] In a series of judgments, it has been held that a Protocol is an integral part of the tax treaty and it is to be given effect in the same manner as any other substantive part of the tax treaty.[3] Reference to comments made by various authors also substantiates the same.[4]

It can, therefore, safely be concluded that Protocol is to be given effect in the same manner as any other substantive part of the tax treaty and is always treated as an integral part of the treaty.

Protocol – Automatic application or requires legislative action

The AAR has held that the notification giving effect to paragraph 7 of Protocol to India-France DTAA was silent on inclusion of 'make available'

1 AAR No. 1055/2011 dated 2nd May, 2014.

2 Both treaty as well as the Protocol are signed by same persons on same day.

3 *DCIT* v. *ITC Ltd.* [2002] 82 ITD 239 (ITAT Kolkata.), *Sumitomo Corpn* v. *DCIT* [2008] 114 ITD 61 (ITAT Delhi), *Poonawalla Aviation (P.) Ltd.* [2011] 16 taxmann.com 120 (AAR), *Idea Cellular Ltd.* [2012] 20 taxmann.com 53 (AAR), *DCIT* v. *Gupta Overseas* [2014] 42 taxmann.com 42 (ITAT Agra).

4 Prof. Dr. Klaus Vogel, Ned Shelton and Roy Rohatgi.

clause in the definition of FTS. Such inclusion being absent, 'make available' clause cannot be read in India-France DTAA. Though AAR observed that India is under an obligation as per the terms of the Protocol to limit its rate or (of) scope, however, declined to comment citing 'outside its authority' as a reason.

The AAR, however, failed to notice the language of paragraph 7 to the Protocol contained under the India-France DTAA which suggests an *automatic application*. A reference to Protocol to India-Philippines and India-Swiss Confederation DTAAs would have made the picture clearer; the language of which explicitly spells out the necessity of a legislative action before the Protocol can be given effect to.

Unilateral amendment of treaty – valid?

AAR has opined that taxpayer can claim the benefit of Protocol originally notified only where notification amending the text of India-France DTAA is subsequently issued, as was done in the case of India-Netherlands DTAA. Even though we are of the view that no notification is required for bringing the Protocol into effect, let us see whether the unilateral act of amending the India-France DTAA by way notification is legally valid.

Per *Lord Denning "At any rate the Parliament itself cannot alter the wording of this Double Taxation Agreement without the consent of both the Parties to it"*[5]. Reference in this regard is also invited to the case of *WNS North America*[6], wherein it was held that a country who is party to treaty cannot unilaterally alter its provisions and any amendment to the treaty can be by means of deliberations between the two countries who signed it. We may point out here that unilateral amendment to treaty is different from treaty override by a contrary domestic legislation passed by Parliament.

In light of the above, it is clear that unilateral Act of Government of India to issue notifications curtailing the effect of Protocol has the effect of amending the treaty and is not legally valid.

'Rate or scope' and not 'rate of scope'

The AAR has held that paragraph 7 [infra] of the Protocol *only* puts a restriction on the 'rate of tax' and has nothing to do with the scope. A reading of paragraph 7 shows that both, rate and scope, are contemplated in the said paragraph and the usage of word *'of''* [rate of scope] is nothing but a printing error.

> *"7. .....India limits its taxation at source on dividends, interest, royalties, fees for technical services or payments for the use of equipment to a rate lower or a scope more restricted than the rate of scope provided for in this Convention on the said items of income, the* ***same*** *rate or scope as provided for in that Convention, Agreement or Protocol on the said items income shall also apply under this Convention....."*

Reference can be made to notification amending India-France DTAA wherein paragraph 7 of the Protocol is repeated where such printing mistake is avoided.[7]

The AAR's opinion that Protocol to India-France DTAA puts restrictions *only* on the rates,

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5 *Ostime (Inspector of Taxes)* v. *Australia Mutual Provident Society* [1960] 39 ITR 210 (House of Lords) rendered in the context of United Kingdom-Australia DTAA.

6 *WNS North America Inc.* v. *ADIT (IT)* [2012] 28 taxmann.com 173 (ITAT Mumbai).

7 Notification No. S.O.650 (E) dated 10-07-2000.

thus, with due respect, requires to be revisited.

The way forward…

Uniformity in laws helps in maintaining and/or restoring the confidence of the investors, boosting the economy and thereby benefitting the entire society. AAR should, therefore, endeavor to maintain uniformity in interpretation of tax laws and follow their earlier views *except* where there are strong grounds and reasons to take a contrary stand. In other words, there should be consistency and uniformity in interpretation of provisions as uncertainties can disable and harm governance of tax laws.

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How impartial is service tax law to partial constructions?

By **Chaitanya Bhatt**

Section 66E(b) of the Finance Act, 1994 enacted pursuant to the introduction of the negative list regime with effect from 1-7-2012 reads as under:

> "SECTION 66E. Declared services. — The following shall constitute declared services, namely :—
>
> .....
>
> (b) construction of a complex, building, civil structure or a part thereof, including a complex or building intended for sale to a buyer, wholly or partly, except where the entire consideration is received after issuance of completion certificate by the competent authority…"

Prior to 1-7-2012, the explanation added to the taxable category of 'commercial or industrial construction of complex service' under the erstwhile Section 65(105)(zzq) of the Finance Act, 1994 with effect from 1-7-2010 sought to achieve the same result that the present Section 66E(b) (supra) has achieved.

A brief background that led to the advent of the above explanation to Section 65(105)(zzq) would be of relevance here. Prior to insertion of the explanation, both the department and the assessees were of the view that any amount received towards sale of immoveable property by the seller to the buyer would not be subject to the levy of service tax since transfer of property in immovable property is not a service.

The Supreme Court in the case of *K. Raheja Development Corporation* v. *State of Karnataka* [2005 5 SCC 162], however, held that the transaction of sale of flat by the seller to the buyer would qualify as a works contract unless the agreement for sale of flat was entered into after the construction was complete. The aforesaid decision of the Supreme Court was, however, doubted in the case of *Larsen & Toubro Ltd.* [2008 (12) S.T.R. 257 (S.C.)] and the same was referred to the Larger Bench. Although the aforesaid decisions were concerned with the applicability of VAT, considering the fact that the decision of *K. Raheja* might get reversed and there would be uncertainty in such a scenario with respect to levy of service tax, a fiction by way of insertion of the above explanation was created in the service tax provisions with effect from 1-7-2010.

However, the Larger Bench of the Supreme Court in the case of *L&T Limited* v. *State of Karnataka* [2013-TIOL-46-SC-CT-LB] held that the activity of construction undertaken by the developer would be treated as a works contract from the time the developer enters into a contract with the flat purchaser. In other words, the Apex Court held that the consideration received towards portion of construction to be carried out after a unit is booked amounts to works contract only.

A view could be taken that even for the purpose of service tax, ongoing construction contracts are also in the nature of works contracts and the decision of the Larger Bench of the Supreme Court in the case of *L&T Ltd.* is, therefore, *mutatis mutandis* applicable. In other words, pursuant to the said Larger Bench decision, in respect of on-going construction contracts, service tax would be payable only on that portion of value of construction services that pertains to the period after the customer books the flat and not on all amounts received prior to receipt of completion certificate.

Contrarily, it is pertinent to note that, although construction contracts are certainly in the nature of works contracts, the service tax provisions both prior to and post 1-7-2012 always sought to levy service tax under two separate service headings viz. "construction of complex service" and "works contract service". Further, construction contracts are more specifically covered under the taxable category of "construction of complex service" rather than 'works contract service'. Furthermore, the decision of the Supreme Court in *L&T* was limited only to the VAT aspect and service tax was not discussed therein. Further, in so far as service tax is concerned, the scope and language of the explanation to construction of complex service (up to 30-6-2012) and Section 66E(b) of the Finance Act (with effect from 1-7-2012) as such make it unequivocally clear that in respect of construction contracts, all amounts received by the developer prior to receipt of occupancy certificate would be leviable to service tax.

Going further, a question arises as to whether Section 66E(b) is applicable in case of a building/complex which was intended to be constructed for oneself but subsequent to partial construction of the building/complex, such building/complex is sold off to a third party. For example, a person X is constructing a mall for himself. The construction started in August 2012 and half of the mall was constructed by April 2013. In May 2013, X decides that he does not want to continue to build the mall for himself and he decides to sell off the already constructed portion of the mall to Y for a consideration of Rs. 1 crore.

In the above illustration, would X be liable to pay the applicable service tax on the consideration of Rs. 1 crore received from Y in terms of Section 66E(b) of the Finance Act, 1994? If the answer is said to be in the affirmative, it is pertinent to note that the language of Section 66E(b) uses the term *"the construction of a new building which is intended for sale"*. Since X had commenced the construction activity in August 2012 and at that time, the intention of X was to build the mall for himself and not for Y, X at the time of transfer in May 2013 is only transferring the existing structure in an "as is where is" condition to Y. Y at his own discretion would decide whether to undertake further construction or not. Can it therefore be said that Section 66E(b) only

covers within its ambit those situations where the builder continues the activity of construction of the building after the buyer is located and hands over the building to the said buyer only in completed form?

In the scenarios discussed above, only a clarification/circular issued by the CBEC explaining the true intent, scope and interpretation of an otherwise apparently unambiguous Section 66E(b) would change the dynamics behind the taxability of construction contracts under service tax law.

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CENTRAL EXCISE

Ratio decidendi

Cenvat credit reversal not required on re-export of capital goods: Cenvat credit taken on imported capital goods is not required to be reversed at the time of their clearance as such for export. CESTAT, Mumbai holding as above noted CBEC Circulars issued in 1996 and 2000 allowing clearance of Cenvatted inputs or capital goods for export under bond. Tribunal's earlier decision in the case of *Essel Propack* was followed in this regard. [*Glass & Ceramic Decorators* v. *Commissioner* – Final Order No. A/140/14/EB/C-II, dated 19-2-2014, CESTAT, Mumbai]

Refund – No unjust enrichment when credit notes issued: Tribunal, Mumbai has held that refund of excise duty on account of quantity discounts given to dealers at the end of calendar year, is not hit by unjust enrichment if the duty amount has been refunded to dealers through credit notes. The Tribunal in this regard also held that reference to buyer under Section 12B of the Excise Act (*relating to presumption of passing of duty incidence to the buyer*) should mean the buyer who buys goods from the person who has paid duty and cannot be construed as having reference to the ultimate consumer of the product. [*Daimler Chrysler India Pvt. Ltd.* v. *Commissioner* – 2014-TIOL-825-CESTAT-MUM]

In another case relating to credit notes, CESTAT, Delhi has held that where there is subsequent reduction in prices, the refund of duty will not be hit by bar of unjust enrichment. The Tribunal in this case also held that in order to claim refund of duty on account of reduction in price pursuant to a clause in an agreement, the manufacturer is not necessarily required to resort to provisional assessment at the time of clearance of goods. [*Sankhla Udyog* v. *Commissioner* – 2014-TIOL-860-CESTAT-Del]

Value of bought-out tools or accessories not includible: Tribunal, Mumbai has held that value of bought-out items such as drill rods, pipes, etc. which are not parts of drilling rigs but are in the nature of tools, accessories or operating equipment and used in conjunction with rigs, is not includible in the assessable value of drilling rigs. The Tribunal in this regard relied upon an earlier order in the case of *Ingersoll Rand* and distinguished the order in the case of *Thermax Bobcock & Wicox Ltd.* [*Kores (India) Ltd.* v. *Commissioner* – 2014 (303) ELT 83 (Tri-Mum.)]

Cenvat credit on returned goods: Cenvat credit is not deniable on goods returned under Rule 16 of the Central Excise Rules, 2002 merely because evidence of transportation of rejected goods from the buyer's premises is absent. The Tribunal in this regard noted that the department had not disputed receipt of goods back from the buyer and that there was certificate in this regard from the buyer. It was held that mere fact of non-availability of evidence on transportation will not result in denial of credit. [*Jamna Auto Industries Ltd.* v. *Commissioner* – Final Order No. 51972/2014, dated 5-5-2014, CESTAT Delhi]

Rebate not available if duty paid after exports: Rebate of excise duty would not be admissible if such duty is paid after export of goods. The Delhi High Court in this regard held that one of the conditions for grant of rebate under Rule 18 of the Central Excise Rules, 2002 is that excisable goods shall be exported after payment of duty and the same was not satisfied in the instant case. The petitioner had paid the duty with interest in this case. [*Sandhar Automotives* v. *Joint Secretary, GOI* – Order dated 15-5-2014 in W.P.(C) 2469/2014, Delhi High Court]

Exemption to intermediate goods captively used in manufacture of ICB supplies: CESTAT, Delhi has held that exemption under Notification No. 67/95-C.E. would be *prima facie* available on aluminium slabs captively consumed in the manufacture of aluminium sheets which were supplied without payment of duty against ICB under Notification No. 6/2006-C.E. Observing that in terms of Rule 6(6) of the Cenvat Credit Rules, 2004, no Cenvat credit reversal was required in case of ICB supplies, the Tribunal while waiving pre-deposit and granting stay of recovery, came to the *prima-facie* view that condition under Notification No. 67/95-C.E. with respect to discharge of obligation under Cenvat Rule 6 was satisfied in the instant case. [*Bharat Aluminium Co. Ltd.* v. *Commissioner* – 2014 (303) ELT 580 (Tri-Del.)]

Valuation – MRP based valuation of television sets sold for free distribution to public: Assessment of television sets sold to another entity for public distribution should be done at MRP less abatement. Department's contention that sale to another entity should be treated as sale to institutional consumers and thus there would be no requirement to declare MRP on television sets, was rejected by CESTAT, Delhi on the ground that the other entity would not be covered under the definition of institutional consumers. [*PG Electroplast Ltd.* v. *Commissioner* – 2014-TIOL-861-CESTAT-DEL]

In a related case the Tribunal has held that valuation of TV sets, specified under Section 4A of the Central Excise Act, 1944, should be done under Section 4A only and not under Section 4 (Transaction value), even if such goods are sold to related parties. Reliance was placed by the Tribunal on Larger Bench decision in the case of *Indica Laboratories Pvt. Ltd.* [*Prisma Electronics* v. *Commissioner* – 2014 (303) ELT 589 (Tri-Del.)]

Cenvat credit admissibility when capital goods used outside factory: Cenvat credit is available on weighbridges (qualifying as capital goods under Credit Rules), which were taken by the assessee outside the factory for weighing sugarcane of farmers, during crushing season.

According to the Tribunal since weighment was an integral part of process of sugar industry, Cenvat credit should be available on weighbridges even if they are used outside the factory. [*Triveni Engg. & Inds. Ltd.* v. *Commissioner* – 2014 (303) ELT 129 (Tri-Del)]

CESTAT, Ahmedabad has also in a recent case, noting that temporary to and fro movement of capital goods is covered under Cenvat Rule 4(5)(a) and that reversal of credit on removal and re-credit on receipt was revenue neutral, allowed the credit on cylinders which were moved out of the factory frequently for refilling gas. [*Commissioner* v. *Aarti Industries Ltd.* – Order dated 9-5-2014 in Appeal E/186/2010, CESTAT Ahmedabad]

Chocolate clubs i.e. biscuits covered with chocolate classifiable under Heading 1905: Chocolate clubs *viz.* biscuits covered with chocolates are classifiable under sub-heading 1905 90 of the Central Excise Tariff Act, 1985 which covers *"Biscuits, waffles & wafers"* and not under Heading 1803 which covers *"Chocolate in any form…"*. CESTAT, Delhi in this regard held that the product in question is a preparation of biscuits. [*Munch Food Products Ltd.* v. *Commissioner* – 2014-TIOL-810-CESTAT-DEL]

Board games involving no skill and only chance classifiable as "games" and not "toys": Board games involving only chance and not involving any skill or involving very little skill do not cease to be a game. CESTAT, Chennai while observing the essential elements of a game as being played according to the rules where outcome is not predetermined; having an element of competitiveness; and where the outcome depends on skill or chance or both, held that the products, Chip N Dale, Duck Tale Disney and Rally are classifiable under "games". In this case, the department had sought classification under sub-heading 9504.90 of the Central Excise Tariff then attracting 16% duty while the assessee had classified the goods under 9503.00 claiming NIL rate of duty. [*Funskool (India) Ltd.* v. *Commissioner* – Final Order Nos. 40324-40326/2014, dated 23-5-2014, CESTAT Chennai]

Cenvat credit wrongly taken but not utilized - Penalty not payable: Madras High Court has held that penalty would not be payable in a case involving taking of ineligible Cenvat credit and its subsequent reversal when there was no mala-fide on the assessee's part and no ineligible credit was utilized to pay duty wrongly. The court in this regard noted absence of allegation of intention to evade. Further, relying upon Supreme Court decision in the case of *Ind-Swift Ltd.*, it was held that interest is leviable on credit wrongly taken, even if it is not utilized (prior to 17-3-2012). The court negated the argument of the assessee that reversal of credit before utilization would amount to not taking of credit. Supreme Court's judgement in the case of *Bombay Dyeing* [2007 (215) ELT 3(SC)] holding that reversal of credit before utilization is equivalent to non-availment of credit, was also distinguished by the court. [*Commissioner* v. *Sundaram Fasterners Ltd.* – 2014 (304) ELT 7 (Mad.)]

Exemption when required certificate procured after start of investigation: Exemption under Notification No. 10/97-C.E is not available if the required certificate from the

Project Director was obtained by the assessee only after start of investigation proceedings. The Tribunal observed that the notification providing exemption to scientific and technical instruments, apparatus & equipments, specifically required that the manufacturer should obtain certificate not below the rank of Deputy Secretary, Government of India and that obtaining such certificate is a substantial condition of the notification and not procedural in nature. Further, it was also held that optical cables of length 88 km cannot be said to be accessory or spare part of goods specified in the notification. [*Commissioner* v. *Starlite Indus. (I) Ltd.* – 2014 (304) ELT 111 (Tri-Mum.)]

CUSTOMS

Notification & Public Notices

Imports under FICCI/TAITRA Carnet exempted: Goods intended for display, demonstration, publicity or any other such pupose imported under FICCI/TAITRA Carnet, for exhibitions, fair, or for meeting for charitable purpose, etc., have been exempted from payment from basic customs duty and additional duty. According to Notification No. 10/2014-Cus., dated 12-5-2014 such exemption will be available if the event is sponsored or approved by Government of India or ITPO and the imported goods conform to the description, quantity, quality and other specifications as mentioned in the Carnet.

Free Trade Warehousing Zones in sector specific SEZs: Instruction No. 49 dated 12-3-2010 which provided that a unit in FTWZ in a sector specific SEZ can store goods required for development of zone or setting up of units or manufacturing and export/DTA sale of goods and services or finished products of the units in that particular specific zone stands amended. Instruction No. 80, dated 18-5-2014 now clarifies that a unit in an FTWZ in sector specific SEZ shall be allowed to provide services for products which are covered within the sector approved for sector specific SEZ to other SEZ/SEZ units.

Agencies authorised to issue Certificate of Origin: List of agencies authorized to issue Certificate of Origin (Preferential) under certain agreements such as India-Sri Lanka Free Trade Agreement (ISLFTA); ASEAN-India Free Trade Agreement (ASEAN-India FTA); India-Korea Comprehensive Economic Partnership Agreement (IKCEPA), etc., has been modified. DGFT Public Notice No. 59/2009-2014 (RE-2013), dated 15-5-2014 modifies Appendix 4D and includes Export Inspection Council and Marine Products Export Development Authority (MPEDA) in the list of agencies. Further, Public Notice No. 61, dated 3-6-2014 authorises Tobacco Board to issue this certificate for tobacco products, under Global System of Trade Preferences (GSTP). In respect of Certificate of Origin (Non Preferential), Trade Promotion Council of India has been authorized to issue the same. DGFT Public Notice No. 60(RE 2013), dated 15-5-2014 issued for this purpose amends Appendix 4C of the Handbook of Procedures.

Online complaint resolution system relating to EDI issues: An online complaint resolution system relating to EDI issues has been established by the DGFT. Users have to feed data in the

system to get the issues addressed, at the section of "EDI complaint resolution". A key number for each complaint will be generated which can be used for follow up. As per DGFT Trade Notice No. 25/2014, dated 4-6-2014, if the issue is not resolved in five (5) working days, email can be sent to DDG(NIC).

Ratio decidendi

Refund – Limitation to be calculated from date of communication of order: Limitation period provided under Section 27 of the Customs Act is to be calculated from the date of communication of finalization of provisionally assessed bills of entry and not from the date of such finalization of assessments. The Tribunal while holding so noted that the date on which a public order is served on the person is important for any remedial measure if such person is aggrieved over the order. [*Indian Oil Corporation Limited* v. *Commissioner* – Final Order No. 52096/2014-CU(DB), dated 30-4-2014, CESTAT Delhi]

Finalization of provisional assessment – Hearing to be granted: Provisionally assessed bills of entry are to be finalized after granting an opportunity of personal hearing to the importer. CESTAT, Bangalore in this case while remanding the matter back to the adjudicating authority had held that in terms of Section 122A of the Customs Act, 1962 adjudicating authority should grant an opportunity of personal hearing to the importer, if the importer so desires, before finalization of provisionally assessed bills of entry. The lower authorities in this case were of the view that no personal hearing was required as Customs Section 18, relating to provisional assessment, does not provide for grant of personal hearing. [*Sun Microsystems India Pvt. Ltd.* v. *Commissioner* – 2014-TIOL-731-CESTAT-BANG]

Conversion of free shipping bills to drawback shipping bills after export: Relying on the decision of Bombay High Court in the case of *Repro India Limited* [2007-TIOL-795-HC-MUM-CX], CESTAT, Ahmedabad has allowed the conversion of free shipping bills to drawback shipping bills after export of goods out of India on the ground that if duty drawback is not allowed to the appellant then it shall be forced to export taxes out of India. Tribunal in this regard noted that documents like ARE-1, shipping bills, etc. and the report of an independent laboratory (authorised by Government of India) indicated the goods to be furnace oil on which specific brand rate of drawback was fixed for the exporter. [*Essar Oil Ltd* v. *Commissioner* – 2014-TIOL-754-CESTAT-AHM]

Refund of redemption fine and penalty not barred by limitation: CESTAT, Mumbai has allowed the refund of redemption fine and penalty paid in excess while it held that limitation period of one year provided under Section 27 of the Customs Act, 1962 is not applicable to such refund claims. Redemption fine and penalty were reduced by the appellate authority and the refund claim was rejected on the ground of limitation as it was filed after the lapse of one year from the relevant date. [*Sunland Metal Recycling Industries* v. *Commissioner* – 2014-TIOL-870-CESTAT-MUM]

Limitation for demand cannot be prescribed by courts if statute is silent - Recovery of drawback by addendum to SCN upheld: Karnataka High Court has held that if limitation is not prescribed by the statute, the court cannot prescribe the same. It was argued by the petitioner that where statutory provisions do not prescribe any period of limitation, a reasonable period has to be read and hence the addendum to the SCN issued on 2-5-2002 after the SCN issued on 18-7-2001 was barred by limitation. The court however noting that the addendum did not structurally alter the nature of SCN held that the addendum was not a fresh SCN. [*Gemini Dying & Printing Mills Ltd.* v. *Commissioner* – 2014 (304) ELT 51 (Kar.)]

Joint Director, DRI has jurisdiction to issue demand notice post 2011: Gujarat High Court has held that post 6-7-2011, Joint Director of Directorate of Revenue Intelligence (DRI) has jurisdiction to issue show cause notice under Section 28 of the Customs Act, 1962. The High Court relied upon Notification No. 44/2011-Cus. (N.T.), dated 6-7-2011, which specifically assigns the functions of 'proper officer' for the purpose of Customs Section 17 and 28 to various officers including DRI officers. Reference was also made to Notification No. 40/2012-Cus. (N.T.), dated 2-5-2012, which assigns the functions of 'proper officer' under different sections of the Customs Act to various officers. It was pointed out that Notification No. 40/2012-Cus. (N.T.) does not assign the function of 'proper officer' for the purpose of Section 28 to the officers of DRI. The High Court however held that the subsequent notification is not in supersession of the earlier notification and both notifications must operate simultaneously. It is to be noted that the High Court did not give any finding or discuss as to whether show cause notices issued prior to 6-7-2011 are valid or not. [*Swati Menthol* v. *Joint Director, DRI* – 2014 (304) ELT 21 (Guj.)]

Service of adjudication order on CHA is not a valid service: CESTAT, Delhi has remanded the matter for fresh adjudication in a case where adjudication order was served on the appellant's CHA. The Tribunal in this regard relied upon the order of Supreme Court in the case of *Trivandrum Rubber*, holding that CHA is not an agent of the importer after clearance of goods. Earlier, the Commissioner (Appeals) had rejected the appeal filed by the assessee, after obtaining the adjudication order (subsequent to receipt of recovery notice), on the ground of being time barred. The Tribunal in this regard observed that service on the CHA is not a service on the appellant-importer. [*Jagdishbhai Ambalal Patel* v. *Commissioner* – 2014-TIOL-800-CESTAT-DEL]

Penalty under Section 114AA not imposable on imports made prior to its enactment: CESTAT, New Delhi has held that penalty under Section 114AA of the Customs Act, 1962, which was enacted vide Taxation Laws (Amendment) Act, 2006, cannot be imposed in respect of imports made prior to enactment of such provision, i.e. prior to 13-7-2006. The department had imposed penalty under the said provisions of the Customs Act in respect of imports made in October, 2005. [*Shri Sanjeev Kumar* v. *Commissioner* – 2014-TIOL-709-CESTAT-DEL]

SERVICE TAX

Ratio decidendi

Service tax liability cannot be shifted by private agreement between parties: The assessee had provided space for advertising and as per agreements with advertisers, the recipient of the service would be liable for tax. It also pleaded bona fide belief that the liability to remit service tax stood transferred to the recipient qua the agreements, for failure to file returns and remit service tax. The Tribunal held that there can be no transfer of the substantive and legislatively mandated liability to service tax from the service provider to the recipient. [*Delhi Transport Corporation* v. *Commissioner* – 2014-TIOL-898-CESTAT-DEL]

Valuation - Electricity supplied to service provider for plant maintenance, not includible: Evaluating the contention of the department that electricity supplied free by the manufacturer to the service provider who undertook maintenance of air separation plant set up by it, the Tribunal concluded that value of free electricity is not includible in gross value or consideration received for services. The decision was based on the ground that electricity is an input for manufacture of oxygen and the service provider did not get any benefit from the same so as to term it as an additional consideration. It held that electricity was not an input for the service provided by the appellant. [*Inox Air Products Ltd* v. *Commissioner* – 2014-TIOL-803-CESTAT-MUM]

Club or Association Service – Exclusion to services of charitable nature: Finding force in the argument of mutuality and exclusion to services of charitable and public nature under Club or Association Service (during the relevant period), the Tribunal held that services provided by the appellants to their respective members do not fall within the ambit of the club or association service. Thus the consideration received by the appellants, whether by way of subscription/membership fee or otherwise, for the same was held as not liable to service tax. [*FICCI* v. *Commissioner* – 2014-TIOL-701-CESTAT-DEL]

Offshore supply vessels in continental shelf & EEZ – Import of service not attracted: Agreeing with the arguments advanced by the assessee, the Tribunal held that reverse charge mechanism is not applicable in case of service rendered by offshore supply vessels in continental shelf and Exclusive Economic Zone. It was reasoned that even after amendment to the definition of "India" with effect from 1-7-2009, the term 'vessels' in 'installations, structures and vessels' does not mean a ship carrying goods and persons. Vessels in the definition cover those akin to installations and structures stationed at a location in the designated areas. The department had contended that the assessee was liable to pay service tax under reverse charge mechanism under 'Supply of Tangible Goods Service'. It was held that since the vessels were not in India when service was rendered, no liability arose to the assessee under reverse charge mechanism. [*Reliance Industries* v. *Commissioner* – 2014-TIOL-940-CESTAT-MUM]

Outdoor Catering service – Coverage when food sold to employees in canteen: Sifting through the argument that to determine liability under Outdoor catering service, it is essential to examine to whom the food was supplied, who consumed the same and whether sale was directly made to person who consumed them, etc., the Allahabad High Court has held that all that is essential is that a person must be engaged in providing services in relation to catering at a place other than his own. In the instant case, the assessee supplied food including beverages in the premises of an entity selling the same directly to employees and others who bought the same. The assessee contended without success that supply had not been to the entity as such, no service had been rendered and it had merely sold food and beverages to persons from the canteen run by it. [*Indian Coffee Works Cooperative Society* v. *Commissioner* – 2014 (34) S.T.R 546 (All.)]

CESTAT empowered to entertain appeals relating to rebate of service tax: In the absence of specific exclusion providing that appeal in relation to rebate does not lie with CESTAT, the amendment to Section 83 of Finance Act, 1994, without amending general provisions regarding matters appealable to CESTAT under Section 86 of the Finance Act, 1994, CESTAT continues to possess appellate jurisdiction to decide on matters pertaining to rebate. The Delhi High Court thus, held that in appeals relating to rebate on service tax can be decided by the Tribunal and set aside the impugned order wherein the Tribunal had cited lack of jurisdiction and declined to decide the matter on the ground that the proper remedy was to invoke revisionary jurisdiction in such matters. [*Glyph International Ltd.* v. *Union of India* – 2014 (34) S.T.R. 727 (Del.)]

Cenvat credit of service tax on repair service provided by third party: Cenvat credit of service tax paid on repair or maintenance service availed from third party for goods manufactured by assessee would be admissible particularly when the same were under warranty period and the charges therefor were included in assessable value of the relevant goods for excise duty purpose. In the instant case, the appellant had taken Cenvat credit of service tax based on bills/ invoices issued by the service provider who were providing maintenance / repair service of diesel engines cleared by the appellant within warranty period. The service provider attended to complaints during such warranty period on behalf of the appellant. [*Gujarat Forging* v. *Commissioner* – 2014-TIOL-774-CESTAT-AHM]

Cenvat credit admissibility when dealer also acting as authorized service station: In the present case, assessee was operating in dual role – first as a car dealer and also as an authorized service station. GTA service was utilized for transport of vehicle to the premises of dealer for his dealership business and not for the service of authorized service station. The Tribunal held that such GTA service cannot be treated as input service for the activities of the assessee relating to authorised service station. [*Assistant Commissioner* v. *Sree Siva Sankar Automobiles* – 2014 (34) STR 797 (Tri. - Bang.)]

Input service distribution - Principal cannot distribute credit to job worker: The appellant in this case, a job-worker, was manufacturing

goods on behalf of the principal and was discharging duty on its behalf. At issue was distribution of Cenvat credit by the input service distributor (principal) to the job worker. The Tribunal held that credit can be distributed by the manufacturing unit's head office/office to various manufacturing units belonging to the same entity and not to manufacturing units belonging to others. Thus, the principal cannot distribute credit to job worker. [*Sunbell Alloys Co. of India Ltd.* v. *Commissioner* – 2014 (34) STR 597 (Tri.-Mumbai)]

Repair service – Exclusion to particular goods when extendible to parts: When a statutory provision excludes particular goods from levy, can it be said that parts of such goods are also covered under such exclusion? According to the Kerala High Court, the answer is in the affirmative. In the case before it, the assessee was carrying on the activity of automobile repair including engine reconditioning, repair of engine parts and repair of vehicles and other vehicle parts as well. It was contended by the department that the exclusion in respect of repair of motor vehicles during relevant period was applicable only if the motor vehicle was brought to service provider but when the engine was dismounted and brought to service provider for repairing, such exclusion would not be applicable as the said exclusion was not for parts of motor vehicle. The High Court rejecting the contention of the department held that the motor vehicle included all its parts and if any service centre undertook maintenance or repair of any part of the motor vehicle, the same would also be entitled to get the benefit of the said exclusion. It further observed that when the statute clearly intended to exclude motor vehicle, it was clear that it excluded parts of motor vehicle also. [*Kuttukaran Trading Ventures* v. *Commissioner* – 2014-TIOL-825-HC-KERALA-ST]

VALUE ADDED TAX (VAT)

Notification & Circular

Cell phones - Amendment in Schedules to Haryana VAT Act: Haryana VAT Act, 2003 has been amended with effect from 23-5-2014 by Notification No. S.O.51/H.A.6/2003/S.59/2014. Major amendments made to Schedules A and C are:

- In Schedule A, S. No. 6 has been inserted which reads as "Cell Phones (including their parts and accessories) exceeding retail price of Rs.10000/-". The rate of tax prescribed against the same is 8%.
- In Schedule C, Entry No. 44 has been amended. The word 'cell phone' in the said entry has been replaced with "Cell phones (including their parts and accessories) having maximum retail price upto Rs. 10000/-".

Works contract for SEZ – Exemption under Tamil Nadu VAT clarified: By Circular No. 25/2014 dated 30-5-2014, it has been clarified that the works contract executed for a developer or co-developer of SEZ for authorized operations

is exempt from sales tax as per G.O. Ms. No. 193, CT & R (B2) dated 30-12-2006 read with Section 88(3)(i) of the Tamil Nadu VAT Act, 2006.

Ratio decidendi

Replacement of defective goods whether covered under 'sale': In this case, the respondent, engaged in the business of manufacturing and selling compressors used in air conditioners also accepted defective compressors outside the warranty period with certain fixed repair charges and replaced them at the option of the customer with a repaired compressor, off the shelf. Repair charges were levied at the time of replacement of the repaired compressor in exchange for the old defective compressor returned by the customer. The Department contended that repair charges were fixed and uniform all over India and, accordingly, that was the price at which repaired compressors were being sold to the customers.

The High Court observed that Section 2(28) of the Bombay Sales Tax Act, 1959 (BST Act), *inter-alia*, defines 'sale' to mean a sale of goods made within the State for cash or deferred payment or other valuable consideration. It noted that this was a transaction of cross transfer of property between a defective compressor and repaired compressor off the shelf of the respondent and there was no consensual agreement of sale supported by price or money consideration.

The Court observed that in order to constitute a 'sale', it was necessary that there should be (i) an agreement between the parties for the purpose of transferring title to the goods (ii) which is supported by monetary consideration; and (iii) the title in the property should actually pass in the goods. It held that there was no sale of the repaired compressor by the respondent to its customers who were merely given an option to not wait and instead take another second hand repaired compressor immediately in lieu of the defective compressor. The payment was only in the nature of repair charges and not a price for the sale of repaired compressor. Accordingly, the reference application of the applicant was rejected. It needs to be noted that this judgment has been delivered taking into consideration the peculiar facts of the case. [*Additional Commissioner of Sales Tax, VAT-III, Mumbai* v. *Kirloskar Copeland Ltd.* – 2014-VIL-120-BOM]

Works contract – Concessional rate of tax for materials used: In this case, the petitioner, a civil works contractor, was awarded a contract for construction of roads. The petitioner required cement, diesel oil, furance oil and lubricants for the manufacture of hot mix materials which was to be used in the construction of roads. As per relevant notification issued under Section 4 of the Uttar Pradesh VAT Act, diesel oil sold to a registered dealer for use in the process of manufacture of any taxable goods, was made liable to tax in the hand of the manufacturer or importer at the concessional rate of 4% provided that a certificate in Form-D was issued by the purchaser of diesel oil to its seller. The petitioner made an application for issuance and authentication of Form D but the same was denied and a show cause notice was issued contending that the petitioner was not a manufacturer.

The court noted the decision of the Supreme Court in the case of *State of U.P.* v. *PNC Construction* [2007 NTN (35) 451] in which

concessional rate of tax was allowed on the purchase of goods to be used in the manufacture of hot mix material. Relying on this decision, the court held that issuance and authentication of Form-D could not be refused by the Department for the purchase of diesel oil and furnace oil. [*P.N.C. Infratech Limited* v. *State of Uttar Pradesh* – 2014-VIL-144-ALH]

INCOME TAX

Ratio decidendi

No TP adjustment for interest not charged from AEs: The Indian subsidiary of a multinational group had receivables due from its Associated Enterprises (AEs) in relation to certain international transactions entered into by it. The Transfer Pricing Officer (TPO) made adjustment for notional interest on these receivables. The taxpayer argued before the ITAT that, as a policy it does not charge interest on sums outstanding beyond the specified dates, irrespective of whether the creditor was an AE or a non AE. The ITAT accepted this argument and deleted the addition of notional interest following the ruling of the Bombay High Court in *Indo American Jewellery Ltd*. [*Bausch & Lomb Eyecare (I) Pvt. Ltd.* v. *ACIT* – Order dated 23-5-2014 in ITA 3861/Del/2010, ITAT Delhi]

Notional income can be included in Profit Level Indicator (PLI): The taxpayer, engaged in manufacturing certain articles, had an in-house design and quality development department, which rendered services to AEs located in foreign countries as well as to other units in India. While consideration was charged from AEs located abroad, no invoice was raised for services rendered to other units of the taxpayer despite incurring costs for rendering such services. The TPO accepted TNMM as the most appropriate method and determined profitability of the assessee using actual revenue and actual expense figures. On appeal, the ITAT held that while computing the true profit of a particular division, it is necessary that the value should be assigned in respect of services rendered to other unit, though there is no actual realization and the PLI of the taxpayer was to be arrived at after including notional income. [*Pentair Water India Pvt. Ltd* v. *ACIT* – Order dated 17-4-2014 in ITA 02/PNJ/2013, ITAT Panaji]

No TP adjustment if intention to shift profits absent: The taxpayer was rendering back office services to its AE in USA, with a cost plus mark up of 11% and claiming deduction under Section 10A. The AE in USA was incurring losses. Profit Split Method (PSM) was adopted as the Most Appropriate Method (MAM) by the taxpayer to establish that the transaction was at ALP. On appeal the ITAT noted that though the taxpayer was earning profit in India, the AE has been incurring losses in USA, which showed that there was no intention to shift profits from India to USA. The ITAT also did not find any commercial prudence in shifting profits as USA was a higher tax jurisdiction. [*Hyperquality India Pvt. Ltd.* v. *ACIT* – Order dated 11-4-2014 in ITA No. 5630/Del/2011, ITAT Delhi]

No disallowance under Section 14A, if no exempt income is earned: The taxpayer had

invested in tax-free investments, however no income for the AY 2009-10 was earned therefrom. It claimed that in the absence of tax-free income, no disallowance under Section 14A read with Rule 8D should be made. The High Court, while dismissing the appeal of the Department observed that as the taxpayer did not make any claim for exemption of any income from payment of tax, therefore no disallowance under Section 14A can be made. [*CIT* v. *Corrtech Energy Pvt. Ltd.* – Order dated 24-3-2014 in ITA No. 239 of 2014, Gujarat High Court]

Reopening is impermissible even where the retrospective amendment is clarificatory: The claim of the taxpayer under Section 80IA(4) was accepted and assessed. Pursuant to the retrospective amendment to Section 80IA, the case of the taxpayer was reopened under Section 147 within 4 years. The taxpayer argued that the amendment was merely clarificatory. On these facts, the High Court following *Parikshit Industries* [352 ITR 349 (Guj)] and *Agrawal J.V.* [83 DTR 101 (Guj)] on the clarificatory nature of the explanation concluded that the reopening in the instant case was invalid as in the absence of any change in facts or law the same was based merely on a 'change of opinion'. [*Sadbhav Engineering Ltd.* v. *DCIT* – Order dated 9-4-2014 in ITA No. 5848-50 of 2010, Gujarat High Court]

Section 50B inapplicable when monetary consideration absent: The taxpayer, transferred its 'Lift Field Operations' undertaking to the transferee company pursuant to a scheme of arrangement sanctioned by the court under Sections 391 & 394 of the Companies Act, 1956. The tax authorities noted that transfer took place in exchange of preference shares and bonds issued by the transferee company. The taxpayer agitated that the transfer was not liable to tax as there was no 'cost of acquisition' ascertainable for the undertaking and also that the transaction is 'exchange' as against sale taxable as slump sale. The Bombay High Court, following *Motors & General Stores (P) Ltd.* [66 ITR 692 (SC)] held that 'sale' meant transfer for a monetary consideration and that an 'exchange' would not amount to a 'sale' therefore, Section 2(42C) read with Section 50B was held inapplicable. [*CIT* v. *Bharat Bijlee Ltd.* – Order dated 9-5-2014 in ITA No. 2153 of 2011, Bombay High Court]