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INTERNATIONAL TAX REVIEW

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ITAT RULINGS

The reimbursements of salary for seconded employees are not taxable as fee for technical services (FTS)

Facts

Assessee, a subsidiary of Goldman Sachs (Mauritius) LLC, engaged in providing back-end support services in the nature of information technology enabled services and software development services to the Goldman Sachs group entities. The assessee employed expatriate employees and paid part of their salaries, while the other part was paid by the overseas entity, which was later reimbursed at cost. The reimbursements made by the assessee were recorded as salary and payroll costs in the books of the assessee. Revenue held that the reimbursement of salary and other related costs made to the overseas entity would be covered under the definition of Fee for Technical Services (FTS)/Fee for Included Services(FIS) under Section (u/s) 9(1)(vii) of the Income Tax Act ('the Act') and respective Double Taxation Avoidance Agreement (DTAAs) and held assessee to be 'assessee-in-default' u/s 201(1) for non-deduction of taxes at source (TDS) u/s 195. Such findings were upheld by the Commissioner of Income Tax Appeals (CIT(A)). Aggrieved by such findings, the assessee preferred an appeal before Tribunal.

Ruling

The Tribunal perused and analysed the terms and conditions of the 'India Recharge and Cost Allocation' agreement between assessee and the overseas entity towards secondment of employees. Tribunal observed that the assessee entered into independent contracts with each seconded employee and the entire salary was subjected to TDS under Section 192. Further, the control and supervision of the seconded employees is with the assessee in India and upto 75% of the salary of expatriate employee was paid by the overseas entity that sent the employee on deputation, and the overseas entity continued to be the de jure i.e. legal employer, whereas assessee was the de facto employer that paid balance 25%. The Tribual observed that the definition of FTS under Section 9(1)(vii) excluded the consideration which would be income of the recipient chargeable under the head salaries. Therfore, if the seconded employee were regarded as an employee of the assessee in India, then the reimbursement to overseas entity, by the assessee would not be in the nature of FTS, but 'salary'. Accordingly, held that the reimbursements cannot be chargeable to tax in the hands of overseas entity and hence there would be no obligation to deduct tax at source at the time of making payment under Section 195.

Tribunal also refered to Article 12 of India-USA DTAA and observed that it excludes payments made towards services rendered by an 'employee' of the enterprise and payments made to 'individual or firm of individuals for service rendered by them in independent professional capacity from the purview of FTS, and as per Article 15 of the OECD Model Commentary, the seconded personnel are employees of the Indian entity being the economic employer. Further, the understanding as to who is the 'employee' in order to be excluded from, 'fees for technical services', cannot be inconsistent with the understanding of employee for the purpose of Article 15 on income from employment, especially when Article 15 is an anti-abuse provision. Tribunal noted that the liability

under section 195 to deduct tax at source when making payment to a non-resident arises, only if, sum paid is chargeable to tax in India and payment of salaries is not covered under section 195. Further, placed reliance on Authority for Advance Ruling (AAR) in Cholamandalam MS General Insurance Co (309 ITR 356), wherein it was held that merely supplying technical, managerial or personnel with managerial skills cannot be regarded as rendering technical services.

Furthermore, states that even if, the rendering of service by the seconded personnel constitutes a contract for service, the make available condition is not satisfied in the present case as there is no making available any technical knowledge or skill to the Indian entity while placing reliance on Karnataka HC ruling in De Beers India 2012) 21 taxmann.com 214 and Abbey Business Services India (2012) 23 taxmann.com 346, thus held that the same shall not constitute fees for technical services.

Source: ITAT Bangalore in Goldman Sachs Services Pvt. Ltd. vs. Deputy Commissioner of Income Tax, International Taxation, Circle 1(1), dated April 29, 2022, vide ITA No. 362 to 369 & 338 to 345.

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Citing practical difficulty in maintaining information for diamond merchants, Tribunal deletes penalty under section 271G.

Facts

The assessee engaged in the business of manufacturing of cutting and polished diamond and during the year under consideration carried out international transactions of purchase of cut/polished and rough diamonds and sale of cut/polished diamonds and rough diamonds to its Associated Enterprises (AEs) situated overseas. For determination of the arm's-length price of those transactions, the assessee applied Transactional Net Margin Method (TNMM) as the most appropriate Method. During the assessment proceedings, the assessee submitted two different working of segmental result for AE and non-AE transactions before the Transfer Pricing Officer (TPO). In one working, the assessee allocated expenses in the ratio of sales except manufacturing expenses, which were allocated in the ratio of 'Carat' sold to AE and non-AE.

According to the TPO this resulted into lower amount of expenses to AE transactions. In the second working the assessee identified the margins based on the grouping of finished products into sub-categories, based on quantity of diamonds, which was rejected by the TPO on the ground of being inconsistent with the approach for allocation of other expenses and hence not considered for the purpose of benchmarking. The TPO asked the assessee to submit the segment profitability separately for the AE and non-AE segment based on the actual direct cost. In view of the failure on the part of the assessee to provide segmental profit result of the AE and non-AE transactions, TPO initiated penalty proceeding u/s 271G of the Act on the ground that assessee had failed to furnish the details called for vide notice u/s 92D (3) of the Act. The TPO rejected the submission of the assessee of difficulty in maintaining the segmental profit of AE and non-AE looking to the peculiar nature of diamond trade. On further appeal, the CIT(A) deleted the penalty by taking into consideration the difficulty in identifying the rough diamond that gets converted into polished diamond, unless the single piece rough diamond happened to be of exceptionally high carat value, therein making tracing convenient. Thereafter, revenue filed an appeal out and identification of the polished diamond physically possible and against the relief provided by CIT(A).

Ruling

ITAT relied on coordinate bench ruling in assessee's own case, which in turn relied on ruling in D. Navinchandra Exports (P.) (87 Taxmann.com 306) Ltd to delete penalty u/s. 271G, considering the practical difficulties in furnishing segment wise details of AE segment and non-AE segment transactions in diamond industry. Accordingly, concurring with the observations of the CIT(A), Tribunal upheld the decision of CIT(A) in deleting the penalty-imposed u/s. 271G, and thereby dismissed Revenue's appeal.

Source: ITAT, Mumbai in Deputy Commissioner of Income Tax, Circle 5(1)(2) vs. Dharmanandan Diamonds (P) Ltd. vs dated May 19, 2022, vide ITA no. 4232 of 2019

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Tribunal quashed an assessment order passed basis invalid TP order as the threshold limit u/s 92BA was not breached.

Facts

During the assessment proceedings, a reference was made by the AO to the TPO in the instant case whereby the details of domestic transactions undertaken by the assessee with its AE were admittedly worked out at INR 4,94,91,268, despite the fact that Section 92BA was not applicable in the instant case. The assessee contended that the very reference to the TPO for passing the order was without sanction of law as the aggregate value of specified domestic transactions were less than threshold monetary limit of INR 5 crore at the relevant time as specified under Section 92BA. The order was however passed under Section 92CA(3) of the Act by the TPO. The assessee preferred an appeal before the CIT(A) and also highlighted that the time limit available for passing the assessment stood expired on 30.12.2016 whereas the assessing Officer passed the impugned assessment order on 31.12.2017 taking into account the extension of time limit under Section 153 of the Act for which reference was wrongly made to the TPO to elicitly gain time for assessment despite objections. On appeal, CIT(A) upheld the additions made by the AO. Subsequently, aggrived by such findings, the assessee filed an appeal before Tribunal.

Ruling

Tribunal held that in the instant case, considering that the transactions of the assessee aggregated to INR 4,94,91,268, the threshold monetary limit of INR 5 crore was not available to the AO to characterize the transactions with AE as SDT which enabled him to make a reference to the TPO. Therefore, Tribunal held that the order of TPO is a nonest and a nullity in the eyes of law. Further, Tribunal upheld that the time limit available for passing assessment stood expired on 30.12.2016 whereas AO passed the impugned assessment order on 31.12.2017 considering the extension of time limit u/s.153 for which reference was wrongly made to the TPO to illicitly gain time for assessment despite objections. Further, the extension of time under erstwhile provisions of Sec.153 for passing assessment order based on such nonest order from TPO was not available to the AO in the instant case. Accordingly, Tribunal held that the impugned assessment order passed was barred by limitation and hence bad in law and thus required to be quashed. Held the other grounds of challenges emanating from such assessment order as ipso facto infructuous.

Source: ITAT, Delhi in Garg Acrylics Ltd. vs Additional CIT, dated May 26, 2022, vide ITA No. 5214/Del/2018 and ITA No. 5915/Del/2018

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Reference u/s 92CA to TPO is invalid in respect of SDTs covered under the deleted Section 92BA (1) as once a clause is omitted by subsequent amendment, it would be deemed that the clause had never been part of the statute

Facts

Assessee, engaged in manufacturing of rear-view mirrors, rear view mirror cable assembles and other automotive component, undertook certain Specified Domestic Transactions (SDTs) which had exceeded the specified monetary limit. During the assessment proceedings for AY 2014-15, the AO referred the matter to the TPO for ALP determination. The assessee filed its response to the notice issued stating that the transactions with AEs are at arm's length and no adjustment is warranted. Further, the assessee strongly alleged that Section 92BA (1) of the Act has been omitted by Finance Act, 2017 and therefore, the impugned order should lapse and become invalid in law. In complete disregard of the assessee's arguments, the TPO passed his order and thereafter AO made additions in the assessment order. Assessee filed objections before Dispute Resolution Panel, however the findings of AO were upheld. Thereafter, assessee filed an appeal before the Tribunal.

Ruling

Tribunal accepted that the undisputed fact is that as per sub clause (1) of section 92BA, the assessee has undertaken transactions which exceeded the specified limit. Further, it is not disputed that vide Finance Act, 2017 w.e.f. 01.04.2017 the said sub-clause (1) of section 92BA had been omitted. Tribunal observed that the AO made a reference u/s 92CA of the Act having noted that the assessee entered specific domestic transaction as the case is covered u/s 92BA of the Act. Relying upon the observations of the coordinate bench, Bangalore in Texport Overseas Private Limited IT(TP)A No. 1722/2017, which was subsequently affirmed by the High Court (HC) in ITA No. 392/2018 along with ITA No. 170/2019, it was held that once a clause is omitted by subsequent amendment, it would be deemed that the clause had never been part of the statute. Thus, Tribunal held that the cognizance taken by the AO u/s.92CA is invalid and bad in law and thereby, order passed by the TPO and DRP were also not sustainable in the eyes of law. However, Tribunal opined that the applicability of Sec. 40A (2) provisions on the impugned transactions cannot be ruled out, therefore remitted the issue back to AO/TPO with a direction to examine the impugned transaction considering provisions of Sec.40A (2) after affording reasonable and sufficient opportunity of being heard to the assessee.

Source: ITAT, Delhi in SMR Automotive Systems India Ltd. vs DCIT, dated May 25, 2022, vide ITA. No. 6597/Del/2018

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Assessee can change the most appropriate method in the TP documentation at a later stage.

Facts

The assessee, engaged in the business of trading in pulses and handicrafts procured different varieties of pulses from its associated enterprise (AE) i.e., M/s P L Global Impex Pte Ltd (PLG Singapore). The AE under the assessee originally benchmarked the purchases made from TNMM. However, the TPO was not in agreement with the benchmarking of TNMM adopted by the assessee in the TP documentation and rejected the same and issued a show cause notice wherein he set out his own benchmarking. The

assessee submitted a response to the notice wherein various infirmities in the benchmarking undertaken by the TPO were highlighted. Further, assessee submitted that since the AE was selling the same pulses to unrelated parties as well, an alternative benchmarking using Comparable Uncontrolled Price Method (CUP) may be acceptable. However, the TPO rejected the same and proceeded to propose an adjustment using his own search methodology with TNMM. The CIT(A) noted that the assessee had furnished reliable internal CUP data of its foreign AE inter alia including month-wise statement of sales made by PLG Singapore to the assessee and unrelated parties along with sample invoices. Basis such observations, CIT(A) recorded his categorical finding that the prices at which pulses were being sold by PLG Singapore to the assessee were comparable with the prices at which the same variety of pulses were being sold to unrelated parties. Aggrieved by the order of Ld. CIT(A), the revenue appealed before Tribunal.

Ruling

The Tribunal held that the assessee cannot be estopped from changing its benchmarking methodology to CUP Method and establishing that TNMM was wrongly taken as the MAM in the TP documentation. In this context, reliance was placed in the decision of Special Bench in the case of DCIT Vs Quark Systems (P) Ltd (132 TTJ 1) in which the assessee was permitted to exclude the comparable which were wrongly included in the Transfer Pricing Study Report. Further, reliance was also place in the decision of the coordinate Bench of the Tribunal at Kolkata in the case of Almatis Alumina Pvt Ltd vs DCIT in ITA Nos. 726 & 2631/Kol/2017 which allowed a new Functions, Assets and Risk (FAR) analysis put forth by the assessee before the lower authorities adopting its AE as the tested party, as opposed to the assessee which was taken as the tested party in the TP documentation. This decision was affirmed by the jurisdictional Calcutta High Court, reported in 137 taxmann.com 202. Therefore, Tribunal upheld the order of CIT(A) and rejected the appeal of the revenue.

Source: ITAT, Kolkata in DCIT, Circle 8(2) vs R.P Comtrade Ltd. dated May 20, 2022, vide I.T.A. No. 207/Kol/2020 and I.T.A. No. 208/Kol/2020.

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VERENDRA KALRA & CO
CHARTERED ACCOUNTANTS

CONTACT DETAILS:

Head Office
3rd Floor MJ Tower,55 Rajpur Road, Dehradun
T +91.135.2743283, 2747084, 2742026
E info@vkalra.com
W www.vkalra.com

Branch Office
80/28 Malviya Nagar, New Delhi
E info@vkalra.com
W www.vkalra.com

For any further assistance contact our team at
kmt@vkalra.com