



**Tax Litigation in India**  
Changing landscape

April 2017

# Select decisions of the Supreme Court and the propositions laid down therein

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## Decision

Siemens Public Communication Network (P.) Ltd. v/s. CIT (2017) 77 taxmann.com 22 (SC)



## Discussion points

### Issue:

Taxability of subvention money received from the parent company

### Proposition:

Voluntary payments made by the parent Company to its loss making Indian company can be understood to be payments made in order to protect the capital investment of the Company. If that is so, we will have no hesitation to hold that the payments made to the Company by its parent Company cannot be held to be revenue receipts

Chennai Tribunal in the case of **Ucal Fuel Systems Ltd v/s. ACIT in ITA No. 725/Mds/2015** found logic in the infusion of funds and held that since there will be no comparable to benchmark such a funding, no arm's length interest can be imputed

# Select decisions of the Supreme Court and the propositions laid down therein



## Decision

DIT v/s. A. P. Moller Maersk A S (2017) 392 ITR 186 (SC)



## Discussion points

### **Issue:**

Taxability of FTS and reimbursements

### **Proposition:**

- Once it is accepted that IT system is an integral part of shipping business without which business cannot be conducted, it is only a facility allowed to be shared by the agents. Accordingly, the same cannot be taxed as technical services
- Once the character of the payment is found to be in the nature of reimbursement of the expenses, it cannot be income chargeable to tax

# Select decisions of the High Court and the propositions laid down therein

# Select decisions of the High Court and the propositions laid down therein



## Decision

CIT v/s. ZTE Corporation (2017) 77 taxmann.com 304 (Del)



## Discussion points

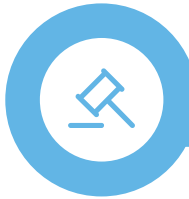
### Issue:

Taxability of software embedded in a hardware – whether taxable as “Royalty”

### Decision:

- The supplies of the software enabled the use of the hardware sold. It is undisputed that without the software, hardware use was not possible. The mere fact that separate invoicing was done for purchase and other transactions did not imply that it was a royalty payment

# Select decisions of the High Court and the propositions laid down therein



## Decision

Andrew Telecommunications India Pvt. Ltd. v/s. PCIT (2017) 77 taxmann.com 312 (Bom)



## Discussion points

### Issue:

Adjustment of refunds against disputed demand

### Decision:

- Stay of recovery of demand could be granted to the taxpayer subject to payment of 15% of the amount demanded after adjusting it from refund of previous year

Karnataka High Court in the case of **Flipkart India (P) Ltd. v/s. ACIT [2017] 79 taxmann.com 159** has held that arguments, if any, made on genuine hardship have to be considered / addressed before directing the tax payer to deposit 15% of the demand

# Select decisions of the Tribunal and the propositions laid down therein



# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Nagarjuna Fertilizers & Chemicals Ltd. v/s. ACIT [2017] 55 ITR(T) 1 (Hyderabad – Trib) (SB)



## Discussion points

### Issue:

Overriding effect of the provisions of the DTAA over the provisions of the ITA

### Ruling:

- Provisions of section 206AA of the ITA will not have an overriding effect for all other provisions of the ITA and the provisions of the Double Taxation Avoidance Agreement (DTAA) to the extent they are beneficial to the assessee will override section 206AA by virtue of section 90(2)
- The assessee could not be held liable to deduct tax at higher of the rates prescribed in section 206AA in case of payments made to non-resident persons having taxable income in India in spite of their failure to furnish the PAN

Finance Act, 2016 has inserted clause (7) to section 206AA of the ITA to provide that these shall not apply to non-residents *inter alia* in respect any other payments, subject to conditions as may be prescribed Rule 37BC of the Income-tax Rules prescribes conditions which provides relaxation from deduction of tax at higher rates u/s. 206AA

# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Burt Hill Design P. Ltd. v/s. DDIT (2017) 79 taxmann.com 459 (Ahd – Trib)



## Discussion points

Tribunal held that reimbursement by Indian subsidiary to its holding company in USA towards salary of seconded employees not subject to TDS u/s. 195 of the ITA

What is relevant is that the income embedded in the payments in question is taxable in India under the head "Salaries", and if so there are no withholding tax obligations u/s. 195

Whether the seconded employees continue to be in employment of the foreign entities or not is wholly irrelevant

# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Saira Asia Interiors P. Ltd. v/s. ITO (2017) 79 taxmann.com 460 (Ahd – Trib.)



## Discussion points

### Background:

- Taxpayer recorded certain liability in its books of account on 22 November 2010 towards technical know how to one of its group company in Italy
- Payment was made to the Italian company on 12 May 2011 after withholding tax which was deposited with the government treasury on 20 June 2011
- Tax authorities took a view that the taxpayer was liable to deduct tax at source at the time of credit, since the credit was earlier than the date of actual payment
- Accordingly, a tax demand was raised on the taxpayer which was upheld by the Commissioner of Income-tax (Appeals)

### Contentions of the Taxpayer:

Taxability of royalty under the India-Italy DTAA would arise only when the amount is actually paid / remitted and not at the time when the credit was made in the books of accounts

# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Saira Asia Interiors P. Ltd. v/s. ITO (2017) 79 taxmann.com 460 (Ahd – Trib.)



## Discussion points

### **Ruling:**

- Relying on the decision of the SC in the case of GE Technology Centre Pvt. Ltd. v/s. CIT (2010) 327 ITR 456, the ITAT held that the tax withholding obligation does not get triggered unless the income embedded in the payment is taxable under ITA
- In terms of Article 13 of the India-Italy DTAA , taxability of royalty is dependent on the payment by the resident of a contracting state and receipt of the same by the resident of the other contracting state
- Mere fact that the Indian resident credits in its books of accounts, the amount of royalty payable to an Italian resident, does not trigger taxability under Article 13 of the India-Italy DTAA

## Comparison of DTAA of various countries dealing with Royalty article

<b>India – Italy DTAA</b>	Royalties and fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.
<b>India – USA DTAA</b>	Royalties and fees for included services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State
<b>India – UK DTAA</b>	Royalties and fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.
<b>India – Singapore DTAA</b>	Royalties and fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Solar Turbines India Pvt. Ltd v/s. DCIT (ITA No. 1075/Mum/2016) (Mum - Trib.)

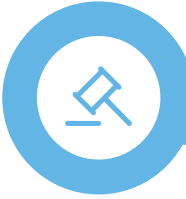


## Discussion points

### Background:

- Taxpayer was engaged in the business of designing, developing, installation, commissioning and servicing of gas turbines. It also provided annual maintenance service supply of spare parts to customers
- A contract was entered with PWD jointly and on behalf of its AE for supply of gas turbines and their installation, commissioning etc. Taxpayer had to bid for the contract as it was having the required eligibility criteria
- On the basis of contract, the Revenue authorities held that the contract was entered by the taxpayer on behalf of its AE or as an agent of the AE and hence the taxpayer was rendering marketing support services to its AE which needs to be benchmarked
- Revenue authorities roped in other direct sales of gas turbines by the AE to Indian customers for benchmarking the ALP and made an adjustment to the taxpayer's income which was confirmed by the DRP

# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Solar Turbines India Pvt. Ltd v/s. DCIT (ITA No. 1075/Mum/2016) (Mum - Trib.)

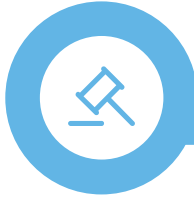


## Discussion points

### Decision:

- The basis of adjustment arose from the contract entered by the taxpayer with PWD
- Taxpayer was not manufacturing gas turbines but its AE was. AE also did not have any VAT registration certificate whereas the taxpayer was having the requisite certificate. Therefore taxpayer had to bid for the contract as it was having the required eligibility criteria
- Contract stated that OEM of gas turbines was the taxpayer's AE who had to provide gas turbines
- AE directly raised invoices on PWD for supply of gas turbines and payments were directly made by PWD to its AE
- There was no evidence to suggest that the taxpayer had provided any services to its AE for sale of gas turbines either to PWD and other Indian customers

# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Solar Turbines India Pvt. Ltd v/s. DCIT (ITA No. 1075/Mum/2016) (Mum - Trib.)



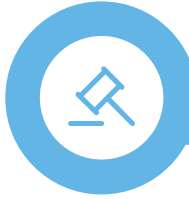
## Discussion points

### Decision:

- Contract required participation of OEMs which the taxpayer was certainly not
- In the absence of any material to show that the taxpayer had provided any marketing services to its AE, income cannot be notionally computed alleging provision of such services
- Adjustment cannot be made on presumption and surmises unless there is concrete evidence to establish that the taxpayer has rendered marketing support services to its AE



# Select decisions of the Tribunal and the propositions laid down therein



## Decision

Volvo India Pvt Ltd v/s. CIT (ITA No. 384/Bang/2013) (Bang. Trib.)



## Discussion points

### Issue:

Whether ALP of services rendered by AE can be determined at Nil?

### Ruling:

- It is now settled that ALP of services rendered by AE cannot be determined at Nil by questioning the necessity of benefits of expenditure incurred
- Onus lies on the taxpayer to prove that the services are actually rendered, and the taxpayer failed to discharge this onus despite being asked by the TPO
- Failure by the taxpayer to discharge the onus can be presumed that the taxpayer had no evidence to establish that services of management support are rendered by its AE.
- Since taxpayer had not made any efforts to controvert the findings of TPO, the action of the TPO/AO's adoption of ALP at Nil was upheld.

# Recent steps by tax department to reduce litigation

## Steps to reduce litigation

- Increasing the monetary limit for filing of appeals by the tax department
  - Appeal to the Income Tax appellate Tribunal – Rs. 1,000,000
  - Appeal to the High Court – Rs. 2,000,000
  - Appeal to the Supreme Court - 2,500,000
- Amendment in the Income-tax Act, 1961 to provide that the tax department cannot file appeal to the Income Tax Appellate Tribunal against the Directions given by the Dispute Resolution Panel;
- Introduction of 'The Direct Tax Dispute Resolution Scheme, 2016';
- Introduction of limited scrutiny assessment and modification in criteria for selection of cases for a Transfer Pricing assessment;
- Proposed addition of benches to the Authority for Advance Rulings

## Some Circulars issued by CBDT to reduce litigation

Issuance of Circulars clarifying position of the tax department on commonly litigated issues – examples:

- Levy of penalty in cases where additions made under the normal provisions of the Income-tax Act, 1961 but income returned and assessed under the Minimum Alternate Tax regime – prior to the amendment to the law;
- Meaning of the term “initial assessment year” for the purposes of claiming tax holiday;
- Allowance of a deduction for bad-debts;
- Deduction for employer’s contribution made to the employee benefit funds – beyond the due date prescribed under the relevant legislation.

# New Penalty Provisions

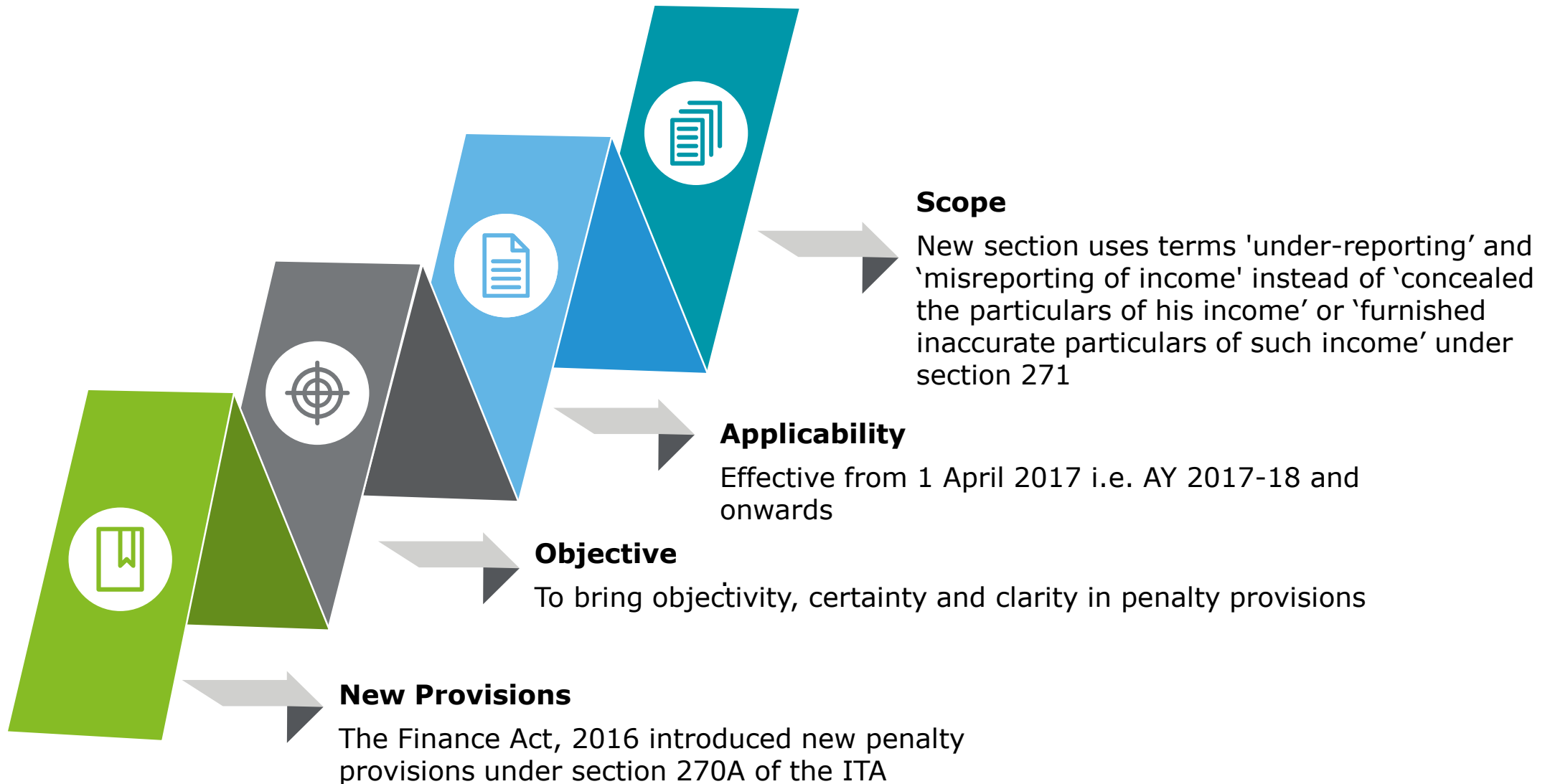
# Contents

## Penalty for under-reporting and misreporting of income

- Background
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- Immunity
- Issues under section 270A

# Background

## Background – New section introduced



**Whether applicable to ROI filed on or after 1 April 2016 or orders passed on or after 1 April 2016?**



# Under-reporting of Income

## Circumstances in which assessee has under-reported income – 270A(2)

Particulars	Return of income is filed	Return of income is not filed
Income computed under general provisions	Income assessed > income processed u/s 143(1)(a);	Income assessed > Maximum amount not chargeable to tax
	Income reassessed > income assessed or reassessed previously;	
Income computed under MAT/AMT	Deemed total income (DTI) assessed or reassessed u/s 115JB (MAT) or 115JC (AMT) > DTI processed u/s 143(1)(a);	Deemed total income (DTI) assessed u/s 115JB (MAT) or 115JC (AMT) > Maximum amount not chargeable to tax
	DTI reassessed u/s 115JB (MAT) or 115JC (AMT) > DTI assessed or reassessed previously	
Loss computed	Total income assessed or reassessed has the effect of reducing the loss or converting such loss into income.	

## Exclusions from under-reporting of income – 270A(6)

- Assessee offers an explanation which is bonafide and discloses all material facts to substantiate the explanation offered
- If income determined on the basis of an estimate, if accounts are correct and complete but income cannot be properly deduced due to method employed
- Where assessee himself has estimated a lower amount of addition or disallowance in computation of income and **disclosed all facts material to addition or disallowance**
- Addition made by TPO in conformity with arm's length price where assessee maintains documentation under Section 92D and has declared international transactions under Chapter X and disclosed all material facts relating to the transaction
- Undisclosed income is detected in search operations and penalty is leviable u/s 271AAB

## Computation of under-reported income – Section 270A (3)

- **Income assessed for first time:**

- ROI filed – Difference between income assessed and income determined u/s 143(1)(a)
- ROI not filed –

*A. In the case of a company, firm or local authority – Amount of income assessed*

*B. In a case not covered in A. above – Difference between income assessed and maximum amount not chargeable to tax*

- **Any other case** - Difference between income reassessed or recomputed and income assessed, reassessed or recomputed in preceding order

**“Preceding order” means an order immediately preceding the order during the course of which the penalty under sub-section(1) has been initiated**

## Computation of under-reported income – Section 270A (3)

**Where under reported income arises out of deemed total income under Section 115JB (MAT) or 115JC (AMT), the amount of under reported income shall be:**

**(A-B)+(C-D)**, where

**A** = Total income assessed as per general provisions of the Act (other than section 115JB/115JC)

**B** = Total income assessed as per general provisions of the Act **reduced by** under-reported income

**C** = Total income assessed as per provisions of Section 115JB or Section 115JC

**D** = Total income assessed as per section 115JB or 115JC as **reduced by** under-reported income

*(Where amount of under-reported income on any issue is considered under both normal provision and MAT/AMT, then such amount shall not be reduced from total income assessed while determining item D)*

**Similar to computation mechanism under Explanation 4 to section 271(1) as amended by Finance Act 2015**

## Tax payable on under reported income – Section 270A(10)

Circumstances	Tax payable
No ROI has been filed by the assessee and the income is assessed for the first time	Tax calculated considering Total Income = (Under reported income + Maximum amount not chargeable to tax)
In case total income determined under section 143(1)(a) or assessed, reassessed or recomputed in the preceding order is a loss	Tax calculated considering Total Income = Under-reported income
In any other case	<p><b>Tax payable = X-Y</b></p> <p>X=[tax on (under reported income + total income determined under section 143(1)(a) or assessed, reassessed or recomputed in the preceding order)]</p> <p>Y=(tax on total income determined under section 143(1)(a) or assessed, reassessed or recomputed in the preceding order)</p>

# Misreporting of Income

## Cases of misreporting of income – Section 270A(9)

- Misrepresentation or suppression of facts;
- Non-recording of investments in books of account;
- Claim of expenditure not substantiated by any evidence;
- Recording of false entry in books of account;
- Failure to record any receipt in books of account which has a bearing on total income; and
- Failure to report any international transaction or deemed international transaction or specified domestic transaction under Chapter X



# Quantum of penalty

Penalty payable in case of

- under reported income - 50% of tax on under-reported income - **Section 270A(7)**
- misreporting of income - 200% of tax on under-reported income - **Section 270A(8)**

Dual Penalty - Section 270A(11)

- Any addition or disallowance suffered or forming basis for imposition of penalty in case of a person for same or any other assessment year cannot be basis for levying penalty under 270A

# Immunity

## Immunity from penalty– Section 270AA

- To seek immunity from penalty under section 270A - File an application to Assessing officer
- **Following are the conditions to be adhered to:**
  - Payment of the tax and interest payable as per the assessment order u/s 143(3) or 147 within specified time
  - No filing of an appeal against assessment order
- Application to be filed in Form No.68 within one month from the end of the month of receipt of order
- Immunity not available for misreporting of income
- AO shall pass an order accepting or rejecting application made for immunity from penalty within a one month from the end of the month of the receipt of application
- No rejection of application - without providing opportunity of being heard

# Issues under Section 270A

## Section 270A – Analysis

- Introduction of new concepts of 'under reporting' and 'misreporting' likely to attract litigation – i.e. distinction between these two concepts is relevant for:
  - Deciding quantum of penalty
  - For granting immunity from penalty under Section 270AA
- Underreporting or misreporting?
  - Capital expenditure claimed by the assessee as revenue expenditure
  - Assessee does not deduct tax on FTS paid since it did not make available technical knowhow under India-US tax treaty – AO does not accept assessee's contention and disallows FTS due to non deduction of tax
  - Assessee fails to file return of income even though GTI was more than Basic exemption limit
  - Assessee fails to disclose a particular bank account in return of income
  - Wrongful deduction claimed by the assessee under chapter VI-A
  - Ad hoc / part disallowance made by AO since vouchers / evidence not produced

## Section 270A – Analysis

- Burden of proof on taxpayer to prove that his case doesn't fall under misreporting
- Where taxpayer is found to have misreported and under reported income – cannot seek immunity with respect to misreported income under Section 270AA to avoid penalty @200%
- Where penalty order contains 2 types of under-reported income – One type assessee accepts and other assessee wants a immunity – What is the mechanism in such case?
- Section 273B (which protects assessee from penalty if he proves that there was a reasonable cause) not amended to include 270A



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