AmCham's Recommendations on Most Contentious Legal Tax Issues submitted to the Central Technical Committee (CTC) set up by CBDT, Ministry of Finance on 10th November 2015

Direct Taxes

Sr. no.	Topic	Remarks
1	Software payment - Whether software purchases qualify as "goods or services" and applicability of both GST and withholding	The Finance Act 2012 has amended Section 9(1)(vi) of the Act with effect from 1 June 1976, to include the software payments within the ambit of income deemed to accrue within India. Software related payments with the countries having tax treaty with India would be governed by the respective treaty Accordingly, the withholding tax implications will follow.
2	Treaty eligibility: Whether the fiscally transparent entities (such as partnership) are entitled to claim the treaty relief if the income is subjected to tax in the hands of its member resident of the same/ different country	Tax treaty of each country is specific with respect to terms and conditions or clauses agreed. Each treaty is to be interpreted accordingly. Further there may also be domestic law interaction.
3	Taxation of EPC contract: Guidance on taxation of offshore supply in case of EPC contracts	With a view to provide clarification in this regard, CBDT had issued instruction no 1829 dated September 21, 1989, wherein, it was clarified that companies forming the consortium for execution of power projects on turnkey basis will not constitute an AOP under the Act and offshore supply of goods by non-resident contractors engaged in execution of turnkey projects shall not be liable to tax in India, if the title to the goods is transferred outside India. However, in the year 2009, the said instruction was withdrawn on account of misuse of such instruction by various non-residents. The principles outlined in the aforesaid instruction have also been accepted by the Supreme Court in the case of Ishikawajima-Harima Heavy Industries Ltd and Hyundai Heavy Industries Co. Ltd. (2007) 161 Taxman 191 (SC). Further, Delhi HC in the case of Linde AG, Linde Engineering Division and Anr vs DDIT (supra) has also followed the aforementioned principles and held that offshore supply of goods by non-resident contractors are not taxable in India, if the title of such goods is transferred outside India. The HC further held that if the offshore services are inextricably linked to such offshore supplies, then such services are not taxable in India.

		However, the Revenue Authorities are taxing such non-residents as AOP at the withholding tax/ assessment procedure stage on the basis of a few favourable AAR rulings and withdrawal of the abovementioned circular. In light of the above, it is strongly recommended that the aforementioned instruction should be reissued and the clarification be made applicable to the infrastructure sector and EPC contracts. The reissuance of the "1989 clarification" would go a long way in instilling confidence amongst the non-resident contractors as regards the stability/ fairness of the Indian tax regime, which, in turn, would also encourage non-resident contractors to set up their manufacturing hubs in India and thereby result in a multiplier effect on the Indian economy.
4	Foreign tax credit - Mechanism to compute the FTC on foreign sourced income	FTC with most of the countries is governed by the respective tax treaty. In relation to non-tax treaty country, FTC is governed by the provisions of the Act. Different countries having different terms in their respective tax treaty cannot be benchmarked with one tax treatment for FTC.
5	AMP expense - The practice of disallowing AMP expenses in routine manner has to be stopped. Ordinarily, no AMP expense may be disallowed in the case of manufacturers. In case of distributors, the disallowance, if any, has to be the outcome of detailed analysis of facts and circumstances of the case and testing against appropriate comparables.	Based on international guidance on transfer pricing, bright line concept can be applied only to distributors, that too which are not limited risk distributors. However, Revenue authorities in India have applied the concept without appreciating the business model of the taxpayers. As a result, the concept has been applied even to licensed manufacturers. In case a normal distributor has been sufficiently compensated by way of a higher gross margin for the marketing functions, the issue of marketing intangibles should ideally not arise. Similarly, in the case of licensed manufacturer generally the transactions are limited to payment of royalty and minimal imports on routine cost plus basis. In such a case, if the royalty payout and import of materials are tested separately and demonstrated to be undertaken at arm's length, the question of marketing intangibles should not arise as the residual profits arising in the system would belong to the Indian entity.
6	In secondment of expatriate employees to India the concept of economic employer has to be recognized. If the expatriate employee entirely reports to the	The recent judicial trend shows remarkable exposure in terms of Permanent Establishment (PE) being alleged on secondment of the employees. However, in some situations, though employees are seconded they will not constitute a service PE in India for e.g. if a foreign company seconded its employees to an Indian company and the Indian company has control over such employees, payment of salary has also been

	Indian entity and all his costs are borne by the Indian entity, his presence must not be considered to be giving rise to service PE for the foreign entity in India nor should it be construed that the foreign entity is rendering any service to the Indian entity, even if the expatriate employee is maintaining his ultimate employment relation with the foreign entity.	made by the Indian company, employees directly report to the Indian company, etc. The Supreme Court in the case of Morgan Stanley observed that the concept of a service PE finds place in the U.N. Convention. It is constituted if the multinational enterprise renders services through its employees in India provided the services are rendered for a specified period. It is important to note that where the activities of the multinational enterprise entails it being responsible for the work of deputationists and the employees continue to be on the payroll of the multinational enterprise or they continue to have their lien on their jobs with the multinational enterprise, a service PE may emerge. The Delhi High Court in the case of M/s. Centrica India Offshore Pvt. Ltd. observed that there was no purported employment relationship between the Indian company and the secondees. None of the documents reveal that the latter can terminate the secondment arrangement. There was no entitlement or obligation, clearly spelt out, whereby the Indian company has to bear the salary cost of these employees. All direct costs of such seconded employee's basic salary and other compensation, cost of participation in overseas entities' retirement and social security plans and other benefits were ultimately paid by the overseas entity. The employment relationship remained independent and beyond the control of the Indian company. The secondees were originally employees of the overseas entities and they were not hired by that entity as a false façade, whose productivity is to be ultimately traced to the Indian company. They have only been seconded or transferred for a limited period of time to another organization, in order to utilize their technical expertise in the latter. The secondment agreement between the Indian company and the overseas entity, and the agreement between Indian company and the employees, envisages an end to this exception, and a return to the usual state of affairs, when the secondees return to the overseas entities. The High Court observed that OECD Model Commentary on Article 15 notes that ‘the situation is different if the employee works exclusively for the enterprise in the state of employment and was released for the period in question by the enterprise in his state of residence’. This was clearly not done in the present case. The Delhi High Court discussed the concept of economic employer and held that services rendered by the seconded employees constituted service PE in India.

		Recommendation It is recommended that an appropriate clarification / guidance can be issued recognizing the concept of economic employer while determining the service PE in India. If expatriate employee entirely reports to the Indian entity and all his costs are borne by the Indian entity, his presence should not be considered to be giving rise to service PE for the foreign entity in India. Further in such situations it should not be construed that the foreign entity is rendering any service to the Indian entity, even if the expatriate employee is maintaining his ultimate employment relation with the foreign entity. It may also be clarified that a 'Service PE' should arise only if **both** the following conditions are satisfied: (i) The activities of the overseas entity entails it being responsible for the work of expatriate employees, (ii) (a) The expatriate employees continue to be on the payroll of the overseas entity **OR** (b) The expatriate employees continue to have their lien on their jobs with the overseas entity.

Indirect Taxes:

1.	Issue:- Inclusion of sales tax collected and retained under the state incentive schemes in the 'assessable value' for payment of excise duty.	Fact: - The States provide various incentive schemes under the State VAT/Sales Tax Act and Central Sales Tax Act to retain certain percentage of the sales tax collected from the buyers on account of manufactured goods sold by them after getting an entitlement certificate issued under the tax incentive/ deferment scheme. The said tax amount collected by the Company was allowed to be retained by the Companies in lieu capital subsidy to be provided to the Companies for the quantum of investments done by the Company in the State. The sales tax allowed to be retained under such schemes is actually adjustable against the capital subsidy to be paid by the Government to the Company and is not supposed to be included in the transaction value which is subject to excise duty. However, excise department contended in the past that such sales tax concession has to be added to the assessable value for calculation and payment of excise duty. Current status: - Recently the Hon'ble Supreme Court has pronounced the following two judgments in against of the assessee: - CCE v. M/s Super Synotex (India) Ltd. [2014 (301) E.L.T. 273 (S.C.)]- The Supreme court held that the amount retained

		by assesse has to be treated as price of goods under basic fundamental conception of "transaction value" as substituted w.e.f. 1-7-2000 in Section 4 of Central Excise Act, 1944. Hence, assessee was bound to pay Excise duty on said sum. Further, the review petition filed in the aforesaid matter has also been dismissed by Supreme Court vide order dated 16th July 2014. - CCE v. Maruti Suzuki India Ltd. [2014 (307) ELT 625 SC] – Sale tax retained and not deposited to the authorities under the incentive scheme is to be included in the transaction value for payment of excise duty.
2.	Issue:- Applicability of differential VAT/CST, Excise Duty on Accessories cleared with main article, such as Battery, Battery Charger, Earphones cleared with mobile phones	Fact:- The Supreme Court in the recent judgment in the case of State of Punjab & Ors v. Nokia India Pvt. Ltd [2014-TIOL-100-SC-VAT], has held that mobile battery charger is not an integral part of the cell phone and therefore the mobile battery charger shall be chargeable to different rate of tax than mobile phones irrespective of the fact that chargers are supplied in a combo pack with mobile phones. Similarly, the excise authorities have also started issuing queries and seeking to levy excise duty on accessories sold in a composite package on the rationale that these products are classifiable under different Tariff heading vis-à-vis main article and will be assessed separately. Further, Custom department may also come with the separate assessment of accessories imported in the composite pack with main article.
3.	Issue:- Availability of CENVAT Credit on secondary transportation	Fact:-The Supreme court in the recent judgment in the case of CCE, Nagpur v. M/s Ispat Industries Ltd [(2014-TIOL-19-SC-CX)] relying on ratio laid down in the case of Escorts JCB, reiterated that the place of removal needs to be ascertained in term of provisions of Central Excise Act, 1944 read with provisions of the Sale of Goods Act, 1930 and held that merely because the transit insurance was in the name of the manufacturer, the transportation charges would not be includible in the assessable value. The Supreme Court also said that the buyer's premises cannot be considered as a place of removal. In the light of the judgement, availability of Cenvat credit of service tax paid on secondary transportation upto the buyer's premises in case of FOR destination price situation, becomes questionable.