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INTERNATIONAL TAXATION

TRANSFER PRICING - SECONDARY ADJUSTMENT – MORE AMBIGUITY THAN CLARITY

Contributed by CA Suresh Babu S |

Transfer pricing provisions in India and globally seek to ensure that there is no shift of profits or funds as against the functions being performed, risks absorbed and capital deployed in a specific jurisdiction i.e.,correct allocation of taxable profits amongst tax jurisdictions. In cases where the underlying transaction was not undertaken at arm's length, a primary adjustment is made to the taxable profits of the taxpayer to align the transfer price with the arm's length price ("ALP"). This primary adjustment may be made by the tax payer (voluntarily) or by the tax authorities.

Thus as per the Indian tax laws, currently, there is no concept or issue of remittance of the difference between the transaction price and the arm's length price. There would only be a single TP adjustment that increases the taxable income of the taxpayer and Income tax would likely be required to be paid on such notional TP adjustment. In effect, the Associated Enterprise (AE) would effectively retain the excess/differential funds due to any Transfer Pricing (TP) disconnect.

International Scenario:

The secondary adjustment rules are an internationally recognised including the United States, Canada, France and other EU Member States, albeit in different forms/approaches. Recently, in 2016, the UK Government also sought consultation from stakeholders on whether a secondary adjustment rule should be introduced into the UK's transfer pricing legislation and if so, in what form.

Secondary adjustments may take the form of constructive dividends, constructive equity contributions or constructive/ deemed loans. While a rule based on constructive dividends would treat the excess profits transferred to the overseas company as a deemed dividend (which may be subject to withholding tax), an equity contribution rule would treat the excess profits as deemed equity contribution.

The OECD Transfer Pricing Guidelines for Multinational Corporations and Tax Administrations ("OECD Guidelines") define the term secondary adjustments as "an adjustment that arises from imposing tax on a secondary transaction". A secondary transaction is further defined as *"a constructive transaction that some countries will assert under their domestic legislation after having proposed a primary adjustment in order to make the actual allocation of profits consistent with the primary adjustment"*

Indian Scenario: Union Budget 2017:

The Indian government has introduced the concept of secondary adjustments (Sec 92 CD &CE) under the TP provisions. The Budget specifies that where a primary adjustment to transfer price:

I) has been made by the Assessing Officer and accepted by the tax payer; or
ii) has been made by the tax payer suo-moto in the return; or
iii) Is determined under APA/ MAP/ safe harbour

then secondary adjustment is required to be done.

The Union Budget specifies that the amount of difference between arm's length price as determined and actual transaction price (referred as "excess money" = ALP in primary adjustment – actual transfer price of international transaction) is not received by the taxpayer from the AE within the prescribed time, then such excess money shall be deemed to be an advance made by the taxpayer to the AE and interest shall be computed on such advance. The time limit for repatriation to India and manner of computation of such interest including rate & method will be prescribed.

However, the following proviso has also been supplemented to the above proposed new section:

"Provided that nothing contained in this section shall apply, if,–
(i) the amount of primary adjustment made in any previous year does not exceed one crore rupees; ***and***
(ii) the primary adjustment is made in respect of an assessment year commencing on or before the 1st day of April, 2016."

Thus, the above proviso specifies that the new proposal would not be applicable if the amount of primary adjustment is less than Rs 1 Crore in any financial year on or before FY 2015-16.

Questions that need answers in the form of clarification–
There is certain ambiguity in the above mentioned provisions as follows:

1. Applicability of threshold of Rs 1 crores for future years?
2. Applicability of these provisions for past years (where adjustment is more than 1 crores)?
3. Applicability of these provisions for AY 2017-18?
4. Applicability of the above said provisions in scenarios where non filing of appeal by taxpayer pursuant to unfavourable HC/ITAT order?
5. MAT implications and is the interest calculations on cumulative basis?
6. How will the section impact counterparty if transfer price is not acceptable in overseas jurisdiction?
7. Does it make any difference that there is no corresponding amendment in Section 4,5 and 9 of ITA?
8. Does it make any difference if F Co ceases to be AE at a later date, while being AE on the date of transaction?
9. Whether interest needs to be computed from the date of primary adjustment or when the assessment is completed?
10. Cases where the AE also has a presence in India (say, in the form of Permanent Establishment)?
11. Window period of getting funds into the country and the manner of computation of interest?

As mentioned above, there is a need to have clarity on the ambiguity and already representations on this matter are being made before the CBDT/ Finance Ministry to get appropriate clarifications.

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FEMA

PROJECT EXPORTS - FEMA REGULATIONS

Contributed by CA Murali Krishna G |

Introduction:

Export of engineering goods on deferred payment terms and execution of turnkey projects and civil construction contracts abroad are collectively referred to as 'Project Exports'.

Project export contracts are generally of high value and exporters undertaking them are required to offer competitive credit terms to be able to secure orders from foreign buyers in the face of stiff international competition. Indian exporters offering deferred payment terms to overseas buyers in respect of export of goods and those who have been awarded turnkey, civil construction contracts by overseas parties have to secure prior approval at post award stage from Authorised Dealer ("AD") / Exim Bank for credit terms to be offered, third country imports etc. Regulations relating to Project Exports and Service Exports are laid down in the Project Exports Manual ("PEM") issued by RBI.

RBI vide its A.P. (DIR Series) Circular No. 39, dated 14th January, 2016 has done away with the limits on the delegated powers of AD and has updated the PEM.

Exporters who have secured orders for undertaking supply contracts on deferred payment terms, those who have secured turnkey/civil construction contracts abroad or for export of services in the area of management, technical consultancy, etc. where execution of the contracts involves grant of fund-based and/or non-fund-based facilities from the Indian banking system or where deferred payment terms are to be offered require approval from Authorised Dealer / Exim Bank.

.Meaning of "Deferred Payment exports"

Contracts for export of goods against payment to be received partly or fully beyond the period statutorily prescribed for realisation of export proceeds (at present 9 months) are treated as deferred payment exports. Ordinarily, contracts providing for deferred payment terms will be allowed only for export of engineering goods (capital goods and consumer durables).

Meaning of "Turn Key Project"

Projects involving rendering of services like designing, civil construction and erection and commissioning of plant / factory along with supply of machinery, equipment and materials

Meaning of "Civil Construction Contracts"

Execution of civil construction contracts abroad involving mainly erection and civil construction work and supply of construction materials and equipment going into the civil works. It may also include turnkey engineering contracts, process and engineering consultancy services and Project construction items (excluding steel & Cement) along with civil construction contracts

Export of Services

Contracts for export of consultancy, technical and other services by Indian companies/firms generally fall in the following categories:

(a) Preparation of project/feasibility reports, drawings, designs, etc.
(b) Supply of technical know-how/engineering services in different fields.
(c) Operation, maintenance and supervision of manufacturing plants, buildings and structures, etc.
(d) Management contracts for commercial concerns.

Period of Deferred Credit

The periods for which credit may be offered for export of goods, consumer durables, turnkey contracts and civil construction contracts will depend on merits of individual case and may be determined by the exporter and his banker in mutual consultation on the basis of commercial judgement.

However, consumer durables and miscellaneous engineering goods listed in the PEM should ordinarily be exported on cash terms. Four major factors viz. anticipated life of the goods to be exported, extent of foreign competition, nature of the foreign market and the contract value constitute the criteria for determining the overall terms of credit.

Approval from AD / EXIM Bank

Each project export contract or Service Export Contract involving Deferred Payments need to be approved either by AD/ EXIM Bank in India. Such approval need to be obtained on post award stage but before actual execution of the project.

After entering into Engineering or Civil contract, the exporter should submit to his AD bankers an application in form DPX-1 (in respect of turnkey and deferred payment supply contracts) or in form PEX-1 (in respect of civil construction contracts), as the case may be, in six copies along with six copies of the contract. Now ADs are permitted to approve the contract without any limit. However, in case the participation of EXIM Bank or ECGC is involved for credit facilities or insurance etc., then the AD need to furnish the details of contracts etc., to them accordingly

In case of export of Service Contracts, requiring furnishing a performance guarantee to the overseas employer in respect of the project as a whole especially for contracts in the field of erection/installation of plant and machinery as well as services like electrical or air-conditioning installations associated with civil construction work. The details of contract need to be submitted to AD in Form TCS-1 in six copies along with six copies of contract for necessary post-award clearance

Follow-up of Turnkey / Construction Contracts/ Service Contracts

Exporters and all their Indian sub-contractors executing turnkey contracts or civil construction contracts or Service Contracts of specified nature, abroad should furnish progress reports in form DPX 2 on a half-yearly basis (June and December) to concerned approving authority. The final Report in Form DPX 2 should clearly indicate the fact of completion of the project and full compliance with the requirements relating to completed projects

Foreign Currency Accounts/Site Offices Abroad/ Agency Commission/Financial Requirements

Project/ Service exporters may avail of facilities such as opening of foreign currency accounts, temporary site offices, payment of agency commission and availing of temporary overseas borrowings subject to the conditions as may be stipulated Exim Bank/AD. The project exporters may also be permitted to open temporary liaison offices overseas in connection with the execution of the contract abroad by the authority approving the relative project export proposal subject to the conditions as may be specified by the said authority.

Third Country Purchases

While granting package approval for turnkey/civil construction contracts involving purchase of machinery/equipment/materials from third country sources, the AD or Exim Bank will indicate the extent upto which such purchases may be made.

Ordinarily, the third country purchases should be paid for separately by the overseas project authority or by the Indian exporter out of advance/down payment received from the project authority. Where the payments for the contract are receivable on deferred payment basis, the exporter should, as far as possible, try to secure matching deferred payment terms in respect of third country purchases required for the project to avoid a net outlay of funds in foreign exchange.

Export of Construction Equipment and other equipment from India

Exporters executing turnkey/ construction/ service contracts abroad should normally take from India construction and other equipment required for performance of the contracts. AD may permit, on application, export of equipment from India on the condition that it will be re-imported into India on completion of the contract and if let out /sold, the full hire charges/sale proceeds will be promptly repatriated to India.

Exporters will also be permitted to purchase construction etc. equipment abroad, where necessary.

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AUDIT

IND AS and IFRS - A COMPARISION

Contributed by CA Sandeep Das

India has chosen the path of IFRS convergence and not adoption. Though Ind AS has come a long way and is now quite close to IFRS, certain differences between the IFRS and Ind AS still remain. We call them carve-outs or carve-ins. International Financial Reporting Standards (IFRS) are principal based standards, Interpretations and the framework adopted by the IASB (International Accounting Standard Board). India being member country is bound to adopt these standards. Any changes in IFRS would have impact on the on the books of Indian companies to bridge the gap Company Law Board suggested for solution through IND AS which is nothing but IFRS. The benefit of these standards isthat any changes in IFRS would not impact IND AS directly.

The carve outs/ins in some key areas are summarized below:

Presentation

Under Ind AS, the breach of a material provision of a long- term loan will be classified as current except where before the approval of the financial statements for issue, the lender had agreed not to demand payment as a consequence of the breach. A similar exemption is unavailable in IFRS. Consequently, adjusting events under Ind AS 10 has been modified to include events where the lender had agreed to not demand payment as a consequence of the breach of material provision of a long-term loan, before the approval of the financial statement for issue.

The option to present other comprehensive income in a separate statement is not available under Ind AS. Accordingly, only one statement comprising both profit or loss and other comprehensive income will be presented. The single statement approach requires all items of income and expense to be recognised in the statement of comprehensive income, while the two-statement approach requires two statements to be prepared, one displaying components of profit or loss (separate income statement) and the other beginning with profit or loss and displaying components of other comprehensive income. IFRS provides an option eitherto follow the single-statement approach or to follow the two- statement approach.

Ind AS also does not allow the presentation of expenses by function; only the classification of expense by 'nature' is permitted. Under IFRS, this is a policy election.

IFRS allows the option to present inflows and outflows of interest and dividends in the operating activities section of the cash flow statement. Ind AS does not have this option for non-financial entities. Interest and divided inflows and outflows are required to be reported in the investing and financing sections of the cash flow statement respectively.

Under IFRS, EPS is not required in separate financial statements if both consolidated and separate financial statements are presented. Under Ind AS, the disclosure of EPS is required in both consolidated as well as separate financial statements.

Under Ind AS, where any item of income and expense, which is otherwise required to be recognised in profit or loss in accordance with Ind AS, is debited or credited to the securities premium account or other reserves, the amount in respect thereof shall be deducted from profit or loss from continuing operations for the purpose of calculating EPS. There is no such provision in IFRS.

Acquisitions:

Under IFRS, the bargain purchase gain or negative goodwill arising on business combinations is recognised in profit or loss. Under Ind AS, the bargain purchase gain can be recognised either in other comprehensive income or capital reserve but not in profit or loss. Similar to business combination, bargain purchase gain on the acquisition of an associate is also not recognised in profit or loss.

Under Ind AS, common control transactions are to be accounted based only on the book values of assets and liabilities. IFRS also allows a fair value option.

Leases:

Under Ind AS, where the escalation of operating lease rentals is in line with the expected general inflation so as to compensate the lessor for expected inflationary cost, rentals are not required to be recognised as an expense on a straight- line basis. Under IFRS, this is considered contingent rent if linked to the index.

Derivatives:

Ind AS introduces an exception to the IFRS definition of a 'financial liability'. Ind AS classifies a conversion option embedded in a convertible bond denominated in a foreign currency as an equity instrument if it entitles the holder to acquire a fixed number of the entity's own equity instruments for a fixed amount of cash, and the exercise price is fixed in any currency. This is not provided in IFRS. Therefore, it will not be required to be fair valued at each balance sheet date under Ind AS. Under IFRS, this conversion option is treated as a derivative liability. This is one of the most significant differences between Ind AS and IFRS.

Property, Plant and Equipment:

Under Ind AS, investment property is to be accounted using only the cost model, with the disclosure of fair value. Under IFRS, both cost and fair value options of accounting are available.

IFRS permits the treatment of property interest held in an operating lease to be classified as investment property, if the definition of investment property is otherwise met and a fair value model is applied. In such cases, the operating lease will be accounted as if it were a finance lease. However, there is no such option under Ind AS.

Government Grants:

IFRS gives an option to measure non-monetary government grants related to assets (tangible and intangible) either at their fair value or at nominal value. Ind AS requires the measurement of such grants only at their fair value.

IFRS gives an option to present the grants related to assets either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset. Ind AS requires the presentation of such grants in the balance sheet as deferred income.

Related Parties:

Under IFRS, certain relationships are specifically mentioned and considered to meet the definition of close members of the family of a person. These relationships are expanded in Ind AS to include brother, sister, father and mother of a person.

Under Ind AS, the related-party disclosures do not apply where providing such disclosures will conflict with the entity's duties of confidentiality provided under a statute or by a regulator or similar competent authority. IFRS does not provide such an exemption.

Associates:

When it is impracticable, Ind AS 28 allows the exemption from use of uniform accounting policies to perform equity method accounting of associates. IFRS does not allow this option.

Others:

Under IFRS, standards on segment information and EPS are applicable to only those companies which are listed or are in the process of being listed. Ind AS does not provide any such exemption for the applicability of standards. In the absence of any exemption under the Companies Act, 2013, and the rules made thereunder, all companies applying Ind AS will have to apply standards on segment information and EPS.

Companies will need to carefully evaluate the Ind AS transition provisions and accounting policy elections, in case they wish to bring their Ind AS financial information closer to IFRS. This may be more important for those entities planning international fund raising or listing, as they may require IFRS compliant financial statements for that purpose.

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INDIRECT TAX AND DIRECT TAX

IMPACT ON JDA - DIRECT TAX AND INDIRECT TAX

Contributed by CA Ramprasad T & CA Sri Harsha

Brief about Joint Development Agreements:

It is very common that the builder/developers enter a development agreement with the land owners for construction of residential/commercial apartments. This would be a win-win situation both for the land owner and builder/developer since the said arrangement would save huge cash flow for the builder, since he is not required to purchase the land. For the land owner, the exploitation of the land shall be the blessing with builder/developer having construction expertise, which the land owner generally lacks.

These type of agreements are referred as to Joint Development Agreement (for brevity 'Agreement'/'JDA'. In such agreement, the land owner contributes the land and developer undertakes the responsibility of obtaining approvals, property development and marketing of the project with the help of his financial resources.

The land owner parts his rights in the land to the builder/developer and such builder/developer guarantees certain portion of the built up area to the land owner in consideration of the land obtained for exploitation. With the above major benefits, there are number of JDA's entered for majority of the infrastructure projects.

Impact under Income Tax & Allied Laws on JDA:

As stated above, the developer himself does not buy the land/property from the owner. The developer is not the transferee or buyer of the flats as per the Transfer of Property Act, 1882 (for brevity 'TOPA') under the Joint Development Agreement. The sole ownership lies with the owner of the land, but the landowner grants the developer along with development rights, a license to enter the land for development but not as a transferee/buyer. The license/authority to enter the land is typically given by way of a power of attorney issued in favor of the developer.

The general power of attorney should be registered on appropriate value stamp paper with the concerned authorities (registrar) to be legally binding on both parties.

The license gives way to the developer to gain approvals and raise debt by way of mortgage or appoint third parties for advertisement.

Applicability:

There is no specific section in the Income Tax Act, 1961 which directs the taxation of transactions arising out of Joint Development Agreements. [1]

[1] FA 2017 propose to address taxation of transaction from Joint Development Agreement from Land Owner's Point of View by introduction of Section 45(5A) w.e.f 01-04-2017 and TDS provisions by virtue of new section 194-IC w.e.f 01-04-2017.

The taxation of income arising out of the agreement is determined by provisions of Section 2(47) of Income Tax Act, 1961 which defines the term 'Transfer' for computation of income under the head 'Capital Gains' (since the Land Owner holds the land or building, which is given to the developer under the agreement, for earning income or as an investment).

Section 2(47)(v) states that any *transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882)- (TOPA).*

For this purpose, 'immovable property' shall mean

(i) any land or any building or part of a building, and includes, where any land or any building or part of a building is to be transferred together with any machinery, plant, furniture, fittings or other things, such machinery, plant, furniture, fittings or other things also.

Explanation—For the purposes of this sub-clause, "land, building, part of a building, machinery, plant, furniture, fittings and other things" include any rights therein;

(ii) any rights in or with respect to any land or any building or a part of a building (whether or not including any machinery, plant, furniture, fittings or other things therein) which has been constructed or which is to be constructed, accruing or arising from any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement of whatever nature), not being a transaction by way of sale, exchange or lease of such land, building or part of a building ;

In nutshell, it refers to Land or Building or part thereof and rights attached to it. Since the possession of land or building will be handed over to the developer under the agreement it is covered by the clause (v) of section 2(47).

<u>Year of Taxation:</u>

Now the question is the year of taxability. Whether it is taxable in the year in which the agreement is handed over or year in which land owner gets his share in constructed property along with the monetary consideration, if any, received.

The Honorable Bombay High Court[2] held that ***the object of entering a Development Agreement is to enable a professional builder/contractor to make profits by completing the building and selling the flats at a profit. Section 2(47)(v) read with section 45 which indicates that capital gains is taxable in the year in which such transactions are entered into even if the transfer of immovable property is not effective or complete under the general law.***

The Chennai ITAT[3] held that to invoke the ruling of Bombay High Court Judgement in Chaturbhuj Dwarkadas Kapadia vs CIT (supra) it is necessary to demonstrate that the conditions U/S 53A of TOPA are satisfied. It further held that handing over the possession of the property is only one of the conditions U/S 53A of TOPA and it is not the absolute condition.

[2]Chaturbhuj Dwarkadas Kapadia vs. CIT
[3]Coromandel Cables Pvt Ltd vs Asst. CIT

The issue of taxation arising out of JDA was decided in various cases based on the facts and the terms of the agreement. There was no certainty in the matters of year of taxability and the amount of consideration while computing the income.

Proposal in the FA 2017 to fix the 'Year of Taxation':

New section is proposed to be introduced for determination of tax liability arising from Joint Development Agreement by Section 45(5A) in the hands of Individual or HUF.

The new section provides that transfer of land or building or both under JDA will be subject to tax as per this section in the year in which in Certificate of Completion (CoC) is issued by the Competent Authority in respect of the project or any part of the project.

Valuation:

The stamp duty value on the date of issue of said certificate as increased by monetary consideration[4] shall be deemed to be the full value consideration received or accruing as a result of the transfer of the capital asset.

However, if the land owner transfer his share in the project on or before the date of issue of CoC the capital gain shall deemed to be income of the previous year in which such transfer takes place as per normal provisions of the Act i.e. section 2(47)(v).

Issues – Taxability of Un-registered JDA and Consequences under Allied Laws:

The provisions of new section 45(5A) will apply in case where the agreement is registered. Now the question is, to apply normal provisions of the Act, other than Section 45(5A), whether registration of agreement is mandatory?

Registration and Other Related Laws (Amendment) Act 2001 (w.e.f 24-09-2001) provides that ***the documents containing contracts to transfer for consideration any immovable property for the purpose of Section 53A of TOPA shall be registered if they have been executed on or after the Commencement of the Registration and Other Related Laws (Amendment) Act, 2001.***

If such documents are not registered on or after such commencement, then they shall have no effect for the purpose of Section 53A of TOPA.

Further the Punjab and Haryana High Court[5] held that unless registration of JDA, it was not enforceable under general law and transaction would not fall u/s 2(47)(v) of Income Tax Act, 1961.

As per Explanation to Section 2(9) Benami Transactions (Prohibition) Amendment Act, 2016benami transaction shall not include *any transaction involving the allowing the possession of any property to be taken or retained in part performance of a contract referred to in section 53A of TOPA if, under any law for the time being in force, -*

[4] As mentioned in the Memorandum to the Finance Bill 2017

[5] C.S. Atwal vs CIT

(I) ………..
(ii) ………..
(iii) The contract has been registered.

Considering the above developments registration of JDA is mandatory. However, the provisions of proposed new section will apply only JDA is registered and land owner doesn't sell his share in the project before the issue of CoC.

The question that remained un answered is what are the tax implication of un registered JDA?*[considering the latest developments in various applicable laws referred to above as well as the judgement of Punjab and Haryana High Court that the provisions of section 53A of TOPA are applicable only in case of registered JDA besides treating it as benami transaction].*

Impact under Service Tax on JDA:

Applicability:

The taxability of services provided to the land owner in a Joint Development Agreement is a part of huge on-going litigation in this industry. The entire issue has come up before the service tax authorities and trade after the judgment passed by the Honourable Apex Court in the case of Faqir Chand Gulati vs Uppal Agencies Pvt Ltd 2008 (12) STR 401 (SC), where in the apex court has stated in the light of the facts mentioned therein, that the builder is a service provider and land owner is a consumer and deficiency in construction service provided by the builder will fall under the ambit of Consumer Protection Act, 1986.

From the above judgment, where in it was stated that the association of builder and land owner cannot be regarded as a Joint Venture and naming the builder as service provider and land owner as customer, has given a clue for the service tax authorities taxing the services provided by the builder to the land owner.

The trade has displayed huge resistance in accepting the said transaction subjected to service tax. However, as time evolved, the trade is now fighting the valuation method prescribed by the Board and accepting the taxability of the transaction. Till this point of time, there was only one judgment delivered by the Chennai CESTAT in the case of LCS City Makers Pvt Ltd vs Commissioner of Service Tax, Chennai 2013 (30) STR 33 (Tri-Chennai) = 2012-TIOL-618-CESTAT-MAD, where it was held that transaction between the builder/developer and land owner falls under the ambit of service tax since there is no difference between the land owner and ultimate customer once joint development agreement is entered into.

Valuation:

Even assuming the transaction is taxable right from the inception of the taxable services category, there is no valuation methodology prescribed for payment of service tax on the services provided by the builder/developer to the land owner. It was only in 2012, the Board has come up with a Circular 151/2/2012-ST dated 10.02.2012, laying down the methodology for valuation of service component in the services provided to the land owner in the light of JDA.

Leaving apart from the validity of the circular, let us understand the methodology enshrined over there. Before approaching the circular, let us understand the basic valuation section in the Finance Act, which is Section 67. The said section deals with the valuation of the taxable service. As per Section 67 of the Act, the value for the service shall be determined as under:

- ❖ Where consideration is in money - the gross amount charged for the service provided or to be provided;
- ❖ Where consideration is not wholly or partly in money – such amount in addition to the service tax charged, is equivalent to the consideration;
- ❖ Where consideration is not ascertainable – the amount as may be determined as per the rules namely, Service Tax (Determination of Value) Rules, 2006.

Since, in the transaction between the land owner and builder/developer, the later shall not receive the consideration either in the form of money or partly in money and partly in kind. However, the question now to be answered is whether the consideration is ascertainable or not. If the consideration is not ascertainable, the resort to valuation rules has to be made. The answer to the availability of the consideration is purely dependent on the terms and conditions set out in the JDA.

Even in certain instances where consideration is not clearly spelt, an effort has to be made to adopt the value of land or development rights involved for calculation of service tax. Only when the value of land or developmental rights are not available then a resort has to be made to the valuation rules. The value of land can be arrived by adopting an independent valuer so as to represent the true value of the land. However, the service tax authorities might not accept such value but the same has to be on reasonable grounds and not a mere rejection.

Assuming the value of land or developmental rights are not ascertainable, then as discussed, the resort has to be - Rule 3 of Service Tax (Determination of Value) Rules, 2006 deals with the valuation of the when consideration of the service is not ascertainable. As per the said Rule, the value has to be determined as per the procedure laid under:

- ❖ Value shall be equal to the gross amount charged by the service provider to provide similar service to any other person in the ordinary course of business – where gross amount charged is the sole consideration.

- ❖ Where the value cannot be determined as per above - the service provider shall determine the equivalent money value of such consideration which shall, in no case be less than the cost of provision of such taxable service.

As discussed above, the Board's Circular 151/2/2012 – ST dated 10.02.2012, wherein the valuation as prescribed is as under:

- ❖ Value of the similar flats sold by builder/developer to the ultimate customers;
- ❖ 2In case the prices of flats/houses undergo a change over the period of sale (from the first sale of flat/house in the residential complex to the last sale of the flat/house), the value of similar flats as are sold nearer to the date on which land is being made available for construction should be used for arriving at the value for the purpose of tax.

However, it has to be kept in mind that the valuation prescribed by the Board has to be resorted as a final measure since the board circular has presumed that the value of land/development rights are not ordinarily ascertainable and hence a direct resort to the similar value as laid down in Rule 3 of the Service Tax (Determination of Value) Rules, 2006 has been taken.

Further, the Board's Circular (supra) states that the value of land/developmental rights in land may not be ascertainable ordinarily and accordingly the value of similar services has to be taken for the purposes of payment of service tax on the land owner's share. However, post amendment in Finance Bill, 2017 to the Income Tax Act, 1961, the said act has fixed the consideration for payment of Income Tax by the Land Owner which is stamp duty value of property pertaining to the land owner's share as on the date of certificate of completion + monetary consideration received by the land owner from the builder.

When the valuation of development rights is very clear and ascertainable for the purposes of Income Tax Act, 1961, the Board has to come up with another Circular stating that the valuation for the purposes of Income Tax would suffice for the purposes of service tax also. This would make the taxation uniform and hassle free for the builder and land owner.

Point of Taxation:

Board's Circular also clarifies that the builder is liable to pay service tax when the possession or right in the property of the said flats are transferred to the land owner by entering into conveyance deed or similar instrument (eg. Allotment letter). That is to say if the development agreement consists of identification of flats belonging to land owner and builder, the builder has to pay service tax irrespective of actual construction being done, which is against to the intention of Point of Taxation Rules, 2011.

With the amendment being made in the Income Tax Act, 1961 vide Finance Bill, 2017, fixing the year of taxation of development rights as the year in which certificate of completion is obtained for the land owner's share, similar amendment has to be brought in the service tax laws also.

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WOMEN AT WORKPLACE

Contributed by S V Ramachadra Rao

In developing countries like India, women's participation in the workforce has been remarkably low as compared to men. However, the role of women in employment has been increasing in recent years and it has now been widely accepted phenomena. The parents and the society are now approving the employment of both married and unmarried girls. The parents of a girl child do recognize the need of preparing her for a vocational or professional role besides preparing her to cope with calamities.

This has also brought in a change in the basic orientation of the female. Employment and career have become an important part of her life. She is gradually becoming achievement oriented with independent aspirations and is trying to achieve them.

The new economy industrial organisations have thrown open considerable employment opportunities to women and now it is a reality that the men and women have to work together shoulder to shoulder to achieve organisational objectives.

The increased women participation in workplaces made it necessary for the Legislature to enact The Sexual Harassment at Workplace (Prevention, Prohibition and Redressal) Act, 2013 for the prevention of sexual harassment against women at workplace. The main objective of the act is protection of Women, prevention and redressal of sexual harassment complaints.

Sexual harassment has been termed as a violation of basic fundamental rights of women under Article 14 and 15(3) that deal with Right to Equality and Right to Life and to live with dignity under Article 21 of the Constitution of India.

Sexual Harassment is also considered as violation of the right to practice any profession or to carry on any trade, occupation or business under Article 19(1) (g) of the Constitution of India.

Any of the following unwelcome acts or behaviour whether directly or by implication constitute sexual harassment as per the Act:

1. Physical contact and advances or
2. A demand or request for sexual favours or
3. Making sexually coloured remarks or
4. Showing pornography or
5. Any other unwelcome physical verbal or non-verbal conduct of sexual nature.

In one of the recent decisions, HR Manager who was guilty of sexual harassment was directed to pay compensation and the company was directed to pay salary for the non-workingperiod to the complainant women. The details of the matter are as under:

A former employee of I P Infusion Software India Private Limited had said that she was sexually harassed by Mr. Bharat Chandrashekhar, Senior Manager HR, while she was in service. She appealed to the labour department after the company's internal complaints committee quashed her petition.

The women complained Mr. Chandrashekhar had commented on the colour of her nail polish and tried touching her fingers inappropriately. Once referring to a job applicant, Mr Chandrashekhar had allegedly said the person was interested in joining the company because he had seen the complainant and got attracted to her.

Mr. T Srinivas, Additional Labour Commissioner in his order dated 27.12.2016 directed the company to hold back Mr. Chandrasekhar's annual salary increment and other monetary benefits for three years from January 1, 2017. He directed the company to deduct Rs. 50,000/- from Mr Chandrasekhar's salary every month for 60 months, and pay the same to the complainant.

In case Mr. Chandrasekhar leaves the company, then the amount should be deducted from the money payable by the company to him and the same should be paid to her. And if the company fails to do so, then it has to pay the amount to the petitioner on its own.

The Addl. Labour Commissioner also held the company guilty of creating an atmosphere conducive for sexual harassment and directed the company to pay Rs. 4,80,000/- towards her monthly salary for the period between September 2015 to December 2016. ***(Source of information – Labour Law Reporter February 2017)***

The above orders demonstrate the powers vested under the act, if any authority under the act is taking a decision on sexual harassment complaints and an eye opener for men who knowingly or unknowingly act or react to situations while working / partying with their women colleagues. The men at work need to respect women and observe absolute restraint in their behaviour to protect themselves from the long arms of the law.

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GST

JOB WORK UNDER GST— RATIONALE OF JURISPRUDENCE & POTENTIAL ISSUES

Contributed by CA Sri Harsha & CA Manindar

INTRODUCTION:

Under the present Excise Laws, the job worker who undertakes manufacturing activity are kept outside the tax net if the principal manufacturer undertakes the obligation to discharge excise duty on the finished goods sold to customers. These provisions require to reverse the credits availed by principal manufacturer on goods sent to job work if the processed goods are not received back or sold from job worker's premises within the stipulated period. Similar provisions are provided under GST Model Law to ensure that supply of inputs and capital goods to Job worker are outside the tax net if the goods are received back or sold by principal within the stipulated time. This article wishes to bring in the rationale of this jurisprudence and potential issues that may likely to emerge considering the taxation approach under GST.

Jurisprudence of Excise Laws:

Before we proceed to discuss about the Job work provisions under GST laws, we would quickly re-capitulate the existing provisions relating to job work under Central Excise. Thus the various aspects of this jurisprudence are discussed as under;

a) **Privilege to send inputs/capital goods to Job worker by availing CENVAT Credit:** In terms of Rule 4 of CENVAT Credit Rules, 2004, the principal manufacturer is allowed to send inputs/capital goods on which CENVAT Credit is availed to the premises of Job worker without reversing any CENVAT Credit for further processing, repairing, re-conditioning etc. Similarly, the principal manufacturer is allowed to avail CENVAT Credit of inputs/capital goods that are directly sent to the job worker without the same being received in his premises. The said privilege is subject to the condition that the inputs that are sent to the premises of job worker or products received therefrom should be received back by principal manufacturer within one hundred and eighty days. In case of capital goods, the time limit is two years. If the goods sent to job worker are not received back within the stipulated period, the principal manufacturer is required to reverse the earlier availed CENVAT Credit. If the goods are received subsequently after the reversal of earlier availed CENVAT Credit, then the principal manufacturer is allowed to retake the CENVAT Credit on such goods.

b) **Exemption for manufacturing by Job worker:** Notification 214/1986-CE exempts the manufacturing process undertaken by Job worker provided that the principal manufacturer gives an undertaking before AC/DC having jurisdiction over Job Worker that the processed goods will be used for further manufacturing or removed by discharging the appropriate duties.

c) Tax implications on Job work charges:

a. If the process employed by job worker amounts to manufacture as defined section 2(f) of the Central Excise Act, 1944, the said activity would come within the ambit of Central Excise Law. On the entire value addition including that of job worker, the Principal manufacturer is liable to pay excise duty. It is because of this reason, though job work charges collected by job worker is a service transaction, the same is not subject to service tax by keeping it under negative list of services under Section 66D (recently said entry in negative list is moved to mega exemption notification).

b. If the said process does not amount to manufacture as defined under section 2(f) of the Central Excise Act, 1944, then the job work charges are liable to service tax. However, if the process employed though not a process amounting to manufacture but is an intermediate process, exemption is available under Entry 30 of Notification No 25/2012-ST dated 20.06.2012 which states that intermediate production process undertaken on job work basis is exempt if the said process is in relation finished goods on which appropriate duty is payable by principal manufacturer.

With this understanding over the existing job work provisions under the Central Excise law, we now move on to the provisions under the Revised Model GST law.

Jurisprudence under GST Laws:

We now proceed to examine the jurisprudence relating to job work transactions under the GST law as prescribed under section 55 of Revised Model Law.

a) **Job work charges taxed as services under GST:** In terms of Schedule II (deals with matters to be treated as supply of goods or services) read with section 3(2), any treatment or process which is being applied to another person's goods is treated as supply of services and are accordingly subject to GST tax. Unlike the present regime, where job work charges are subject to service tax only if the process employed by job worker does not amount to manufacture, Job work charges under GST regime are always subject to GST.

b) **Supply of inputs/capital goods to job worker without paying GST:** Principal is allowed to send his inputs/capital goods without payment of tax to a job worker for job work and from there send to another job worker and likewise. This privilege is subject to the condition that the principal shall—

I. Bring back such inputs/capital goods after completion of job work without payment of tax to any of his place of business within one year (three years in case of capital goods) of their being sent out.

ii. As an alternative, supply such inputs/capital goods after completion of job work from the place of job-worker to any person within India on payment of tax or for export without payment of tax within the time limit specified above. Principal is allowed to supply the goods from the premises of job worker only if the principal declares the job worker's place of business as additional place of business or the job worker is registered separately under GST.

iii. If the said inputs/capital goods are not received back from Job worker premises or are not supplied as per point (ii) above, within the time limit specified above, it shall be deemed that such inputs/capital goods had been supplied by the principal to the job worker on the day when said inputs/capital goods were originally sent out for job work.

c) **Supply as waste and scrap:** Any waste and scrap generated during the job work may be supplied by the job worker directly from his place of business on payment of tax by job worker if he is registered or by the principal if job worker is not registered.

With this understanding of the provisions of section 55, we now proceed to examine the potential legal issues that may prop in if the said section is being implemented in the present state.

Issue 1: Whether inputs/capital goods supplied to job worker constitutes Supply under GST?:

One of the fundamental differences between Section 55 of Model GST Law and Rule 4 of CENVAT Credit Rules, 2004 is that Rule 4 provides for removal of inputs/capital goods to Job worker without reversing the availed CENVAT Credit on inputs/capital goods. On the other hand, Section 55 provides for removal of inputs/capital goods to job worker without payment of tax on such inputs/capital goods. Further, the said section 55 contemplates for payment of tax in the event the inputs/capital goods are not received back or sold by principal from the premises of job worker within the stipulated time period. This implies that section 55 is legislated on the ploy that sending of inputs/capital goods to job worker constitutes supply.

Unlike the condition of reversing CENVAT Credit under Rule 4, section 55 is stipulating the requirement to pay tax. Inthis context, it is required to examine whether sending of inputs/capital goods to job worker where no consideration is involved necessarily constitutes a supply as defined under Section 3 and thereby satisfies the levy under section 8.

On perusal of the definition of Supply under section 3, sub-section (1) provides that 'Supply' includes all forms of supply of goods such as sale, transfer, barter, exchange, license, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business. Further the said sub-section provides that supply includes those specified in schedule I even made or agreed to be made without a consideration. The items listed in schedule I are reproduced as under;

(a) Permanent transfer/disposal of business assets where input tax credit has been availed on such assets
(b) Supply of goods or services between related persons, or between distinct persons as specified in section 10 when made in the course of or furtherance of business
(c) Supply of goods by a principal to his agent where the agent undertakes to supply such goods on behalf of the principal and supply of goods by agent to principal where the agent undertakes to receive such goods on behalf of the principal.

In view of the definition of 'Supply', transfer of goods from one to another shall be treated as supply only when consideration is involved and the transfer constitutes sale, barter etc. Transfer of goods which does not involve any consideration may constitute supply only if the said transaction is covered under schedule I. In case of job work, sending of inputs/capital goods to job worker does not involve any consideration. Therefore, the same may not constitute supply unless the said transaction is covered under schedule I.

On perusal of the items specified in schedule I, clause (a) provides that permanent transfer or disposal of business assets constitutes supply if input tax credit is availed on such assets. This clause may not be applicable to the case of Job work as the principal temporarily sends inputs/capital goods to Job worker. The same does not constitute permanent transfer/disposal of business assets even in case where the principal has not received back the sent goods within the stipulated period.

Sub-clause (2) is relevant only if supplies happen between related persons or specified persons. The said clause is not applicable to Job worker who is neither a related person nor a specified person. The other relevant entry in the present context is sub-clause (c) which provides that supply of goods by Principal to his agent where the agent undertakes to supply such goods on behalf of the principal. This would mean supply of goods by Principal to agent would be deemed to be a supply if the agent undertakes to supply such goods to others on behalf of the principal. In case of Job work transactions, the job worker may undertake the responsibility of sending the processed/resultant goods directly from their premises to the customer on behalf of the Principal. However, in the humble opinion of the paper writers, even by considering the job worker as agent of principal, the same may not amount to supply as job worker never undertakes to send the goods as such in the condition in which they are originally received like a consignment agent/selling agent. He can only undertake to send the processed/resultant goods.

In view of the above discussion, the transaction of sending the inputs/capital goods by principal to job worker is not a supply within the meaning of Section 3. In such an event, the said transaction does not attract levy under section 8. In such a case, the essential question that arises is can section 55 require the principal to pay tax by deeming the said transaction as supply which is in contrary to levy under section 8? Further, it must be kept in mind that Section 55 does not override section 3 and section 8.

Even if we proceed by assuming that sending of inputs/capital goods to job worker amounts to supply, this may lead to another complication. Let us assume that principal sends material of Rs. 1000/- to job worker. The goods are not returned to the principal within the stipulated time period. In such an event, assuming that GST is at 10%, the principal pays a tax of Rs. 100. If the job worker is a registered taxable person under GST, then he can take input credit of the same. Subsequently, after the stipulated time period, the said goods are returned by job worker to the principal. In such case, the return of goods by job worker to principal will also be treated as supply and he can charge GST and send back the originally paid tax of principal (Rs. 100) as input tax credit to him. Suppose in the same example, if the job worker is an unregistered taxable person, he cannot avail input credit of GST originally paid by principal (Rs. 100) upon expiry of stipulated time period and also he cannot charge any GST while returning the goods to the principal. Further, the principal is required to pay GST on the processed goods when sold to his customer. This may result into breakage of input credit chain which is against the spirit of GST.

In the humble opinion of the paper writers, this legal anomaly is required to be put to rest. Otherwise, this will lead into a vociferous litigation. This can be put to rest by either of the following ways;

a) By amending section 55 so as to demand the reversal of input credit availed on inputs/capital goods sent to job worker if the goods are not received or sold from the premises of job worker within the stipulated time period.

b) By incorporating the transaction of sending of inputs/capital goods to job worker as supply in schedule I. This will entitle the Revenue to treat this transaction as supply and accordingly collect tax if the principal does not receive back the inputs/capitalgoods within the stipulated time period. However, this option may lead to breakage of input credit chain in manner described above, if the job worker is not a registered taxable person. In order to overcome this, there should be an appropriate enabling provision in section 55 which should entitle the principal to take re-credit of the GST originally paid by him, where the inputs/capital goods are received back subsequently after the stipulated period from a job worker who is not a registered taxable person under GST.

Issue 2: Whether waste and scrap during job work disposed of by job worker can be treated as supply by principal?:

Sub-section (5) of section 55 provides that any waste and scrap generated during job work may be supplied by job worker directly from his place of business on payment of tax by him if he is registered or by principal in case he is not registered.

Practically, many of the principals who undertake to process their goods through job worker may not claim any title/right on waste and scrap. It is the job worker who sells the waste and scrap in those cases. Principal is not associated with that transaction in any manner. In such cases, assuming the job worker is not required to be registered; can the tax be demanded from the Principal?

In the humble opinion of paper writers, principal is not legally bound to pay tax because unlike the case of sending processed/resultant goods by job worker directly from his location to customer as an agent of principal, the job worker is not affecting supply of waste and scrap as an agent of the principal. In such cases, demand of tax from principal would be without the authority of law after all the GST law requires the person affecting supply to pay tax.

Conclusion:

In view of the foregoing discussion, it appears that section 55 if implemented status quo may lead to inappropriate results. The value addition by job worker i.e. job work charges is subjected to GST as service which will be available as input tax credit to the principal. The principal upon sale of finished goods (either received back from Job worker or sold directly from premises of Job Worker) will pay GST. Thus the entire value addition created by both Job worker and Principal will be subject to GST automatically even in the absence of section 55. The only precaution to be taken in case of Job work is to ensure that inputs/capital goods removed should be received back or sold by principal within a reasonable period i.e. the revenue should exercise reasonable control over inputs/capital goods sent to Job worker to ensure that there is no evasion of tax or defer the tax payment by camouflaging the removal of goods as removal to Job worker. Thus appropriate amendments are required to the existing section 55 to enshrine this intent.

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TECHNICAL SESSIONS:

S.No.	Event	Date	Speaker	Venue
1	Companies Amendment Bill and Recent updates in Companies Act, 2013	10/03/2017	CS DVK Phanindra	SBS - Hyd
2	Demonetisation vis-a-vis Auditor's Report	17/03/2017	CS Bhyrav MHS	SBS - Hyd
3	Recent Issues in Service Tax	24/03/2017	CA Manindar K	SBS - Hyd
4	Derivatives vis-a-vis FEMA Regulations	31/03/2017	CA Murai Krishna G	SBS - Hyd

Note:

The timings for the above events shall be from 16:30 hrs to 18:30 hrs. We request the recipients of "SBS Wiki" who are interested to attend the above events to send confirmation of your participation two days in advance to make appropriate arrangements. The relevant material will be hosted at slideshare shortly after the session. The link to download is *http://www.slideshare.net/Team-SBS*

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Budget Changes - Indierct Taxes by CA Manindar K

Insights into Insolvency and Bankruptcy Code by - CA Rajesh D

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