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CASC BULLETIN

INDEX

Date	Topic	Speaker
17.10.2024 (Thursday)	Key aspects in Corporate Tax computations & Returns (ITR - 6)	CA. B.B. Sathyamurthy
24.10.2024 (Thursday)	Transfer Pricing Form 3CEB	CA. Ranjani Shrinivasan

The meetings will be held at CASC at 6.30 p.m. and will be preceded by fellowship over High Tea at 6.00 p.m

CASC Annual Members are requested to renew their subscription for 2024 - 2025

EDITORIAL

573 Direct Tax Cases Disposed Off

The Supreme Court has disposed off 573 direct tax cases where the tax effect is less than Rs.5 crores in view of the revised monetary limit of filing of appeals. The Ministry said, Union Budget 2024-25 provided for an enhanced monetary limit for filing appeals related to Direct Taxes, Excise and Service Tax in the Tax Tribunals, High Courts and Supreme Court. The Ministry of Finance informed this adding that the significant milestone aligns with the government's efforts to reduce tax litigation, expedite the resolution of tax disputes and promote 'Ease of Living' and 'Ease of Doing Business'. For filing appeals for Income Tax Appellate Tribunal, the monetary limit was increased from Rs.50 lakhs to Rs.60 lakhs, for High Courts, it was increased from Rs.1 crores to Rs.2 crores and for Supreme Court it was raised from Rs.2 crores to Rs. 5 crores. Government have taken steps to involve more officers for hearing and deciding of the income tax appeals, where the tax amount involved is

significant. Let's hope the pendency to be reduced to a greater extent in the upcoming days!!!

GST on Sweets & Savories

Few days back we all could have witnessed the video that was going viral on all social medias. It was all about the addressing by the owner of a very famous Restaurant in a meeting held with the Hon'ble Finance Minister. He said, "There is 5%GST on sweets but 12% on savories, and 18% on cream-filled buns, whereas there is no GST on plain buns! Customers often complain, saying that 'Just give me the bun, and I will add the cream and jam by myself'. When the same are supplied in hotels as composite supplies then it attracts GST @ 5% without ITC. He also said that the computer crashes when we try to input different GST % in a single bill. Even the GST officials are confused, as all items have the same input but different tax rates. This inconsistency is causing issues for both shopkeepers and customers. We had many supporters to his and speech at the same time we had many critics very strongly. But the real issue behind this is the simplify tax structures which we all expect.

AI and Automation

Our Profession is now at the inflection point, where several forces shaping its future trajectory. New technologies like AI, automation and Blockchain will disrupt existing audit and tax processes, but at the same time, they will also open up opportunities to add more strategic values. When our routine tasks get automated, we will have more space for business insights, advanced analytics and holistic advisory services which can tailored to each of our client's requirements. AI and automation can provide a foundation for substantially increasing efficiency and increasing clients and employee satisfaction.

Extended Deadline

The Income Tax department has extended the deadline for submitting various audit reports for the Assessment year 2023-2024 to 07.10.2024. The original deadline was 30.09.2024. This has allowed taxpayers, an additional time to fulfil their compliance obligations. The extension was made in response to technical issues reported on the e-filing portal. In a circular dated September 29, 2024, the CBDT acknowledged the slow

functioning of the portal and exercised its powers under Section 119 of the Income Tax Act to extend the deadline.

Appeal

We, at Chartered Accountants Study Circle, request members to contribute articles for the bulletin and you may contact the editorial board regarding the same. We have been regularly conducting technical programmes every month. Members are requested to attend the programmes conducted by CASC and are also requested to send their suggestions and / or value additions to the services provided by CASC including this Bulletin. The same can be sent as hard copy to the office of the CASC or emailed to admin@casconline.org or to any of the members of the Management Committee of the CASC. Any member interested in using the CASC platform for addressing our members on technical topics may kindly feel free to contact us by way of email at admin@casconline.org.

For and behalf of Editorial Board

Bhuvaneswari.R.V.

CA. BHUVANESWARI R.V

GLIMPSES FROM THE JOINT PROGRAMME ON TAX AUDIT FOR STUDENTS HELD ON 03.09.2024

GLIMPSES FROM THE MONTHLY MEETING
held on 12.09.2024 by CS.T.H.VIJAY PRASAD on
"Common Mistakes in the Preparation of FS of Private Limited Companies"

PRESENT MEMBERS OF THE MANAGEMENT COMMITTEE OF THE CHARTERED ACCOUNTANTS STUDY CIRCLE IN ALPHABETICAL ORDER

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2. Earlier issues of the bulletin are also available on the website in the "News" column.

The soft copy of this bulletin will be hosted on the website shortly.

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CA. V.V. SAMPATHKUMAR

Penalty: The matter in appeal to the first appellate authority was rejected on 23.05.2023 on the ground of limitation. In a WP, the petitioner referred to the impugned order and pointed out that penalty was imposed in spite of noticing that the petitioner had discharged the liability even prior to the issuance of the show cause notice. The submits that the petitioner's reply was considered before issuing the impugned order and also submits that the petitioner lodged a statutory appeal against the order and prayed that no interference is warranted. On perusal of the impugned order, it is evident that the petitioner had remitted sums towards ineligible ITC in respect of IGST and towards ineligible ITC in respect of CGST. Such remittances were made in 2017 and 2018, which is prior to the issuance of the SCN. Stating so, the impugned order dated 22.11.2022 is set aside only in so far as the imposition of penalty is concerned and remitted the matter back to respondents.

Ms.Good Leather Shoes Private Limited Vs The Deputy Commissioner of GST & Central Excise, Chennai North Commissionerate, Purasaiwalkam Division, Chennai-40 W.P.No.18064 of 2024 DATED: 31.07.2024

Non-participation: Tax proposal was confirmed because of the tax payers' failure to reply to the show cause notice. By taking into account the assertion that such non-participation was on account of not being aware of proceedings, the interest of justice warrants reconsideration subject to putting the petitioner on terms. Stating so, the impugned order is set aside on condition that the petitioner remits 10% of the disputed tax demand as agreed to within a period of two weeks from the date of receipt of a copy of this order with other conditions.

M/s. Sagaya Annai Associates, Vs 1. CTO, and 2.AC(ST), Sriperambudur Assessment Circle. 3.DC(ST), Kancheepuram Zone, Kancheepuram 631 501. W.P.No.18247 of 2024 DATED: 31.07.2024

Natural Justice: The petitioner is a Club registered as a Society under the Tamil Nadu Societies Registration Act, 1975. The Club possesses a FL-II licence for supply of liquor to its members and their guests in accordance with the rules of the Club. The

petitioner asserted that the supply of liquor by the Club to its members and their guests is not liable to tax. In support of this submission, the petitioner relied upon the judgment of the Hon'ble Supreme Court in State of West Bengal v. Kolkata Club (2019) 19 SCC 107. The impugned order was issued in these facts and circumstances on 29.01.2024. A notice was issued to the dealers and the reply was furnished by the dealer on 22.12.2023 was not accepted. The reply of petitioner was referred to in the impugned order but the contentions raised in the reply were not dealt with by the AO. Hence, the impugned order dated 29.01.2024 is set aside and the matter is remanded for reconsideration. **Tvl. Little Star Recreation Club Vs 1. The State Tax Officer, Pollachi (West) Assessment Circle 2. Joint Commissioner (State Tax), Intelligence, Coimbatore-641 018. W.P.No.16600 of 2024 DATED: 25.06.2024**

Credit Note: By referring to the relevant part of the impugned order, writ petitioner submits that the discount offered by the supplier was erroneously construed as a service provided by the purchaser to the supplier. Ld Additional Government Pleader points out that this WP only insofar as defect no.3 is concerned. As regards other defects, the petitioner has

carried the matter in appeal before the appellate authority. Ld AGP contends that such practice should not be encouraged and submitted that the petitioner should be relegated to the statutory remedy. The Officer while passing the impugned orders states that the word discount received relates to good performance done by the taxable person by way of increasing the sale and thereby to boost the total turnover of the supplier / company, which resulted in increase in goodwill of the company and also helps the company to market their products and if the company is in the stock market the value of the share of the company will automatically goes up. The taxable person in this end by performing a good sale have provided a service to the supplier and the supplier / company got the benefit of goodwill and sound marketability in the trading world. The Hon'ble court stated that the assessing officer concluded that the taxable person is providing a service to the supplier while taking the benefit of a discount by facilitating an increase in the volume of sales of such supplier. This conclusion is ex facie erroneous and contrary to the fundamental tenets of GST law. Therefore, this conclusion warrants interference and this issue requires re-consideration.

Stating so, the impugned order is set aside only insofar as defect no.3 relating to reversal of Input Tax Credit for the value of credit notes issued by the supplier is concerned. As a corollary, defect no.3 is remanded for re-consideration by the original authority. **M/s. Shivam Steels vs Assistant Commissioner (ST)(FAC), Hosur (South)-III Assessment Circle, W.P.No.15335 of 2024 DATED: 25.06.2024**

TNVAT Act 2006, Rectification: Scope and ambit of Section 84 of the TNVAT Act is limited. Unless there are errors apparent on the face of the record, he submits that such jurisdiction cannot be exercised. Petition u/s 84 was rejected after noticing that the invoice number mentioned in the C form does not tally with the invoice number in the commercial invoice. The petition was further rejected on the ground that the C form mentions the commodity as iron ore. The invoice number mentioned in the C form appears to tally with that in the excise invoice. In order to understand the nature of the commodity, it may be necessary to examine all the relevant documents, such as the contract and invoice. It also appears prima facie, that such examination may be possible even within the confines of the limited jurisdiction exercised

under Section 84. The impugned order dated 09.02.2024 is set aside and the matter is remanded for reconsideration.

M/s. Andritz Separation (India) Limited, Vs The Assistant Commissioner (ST), FAC, Nolambur Assessment Circle, Writ Petition No.15719 of 2024 DATED: 25.06.2024

Inadvertent Error: The show cause notice and other communications were uploaded in the "View Additional Notices and Orders" tab on the GST portal, but not communicated to the petitioner through any other mode, the present writ petition was filed. An inadvertent error was committed while filing the return in Form GSTR 3B for the month of August 2017-2018. Petitioner had filled up the inward supplies liable towards the reverse charge column instead of all other Input Tax Credit (ITC) column. On examining the impugned order, it is evident that the tax proposal relates to RCM purchases. For reasons set out above, the impugned order is set aside on condition that the petitioner remits 10% of the disputed tax demand as agreed to within a period of two weeks from the date of receipt of a copy of this order. The petitioner is permitted to submit a reply to the show cause notice within the aforesaid period. Upon receipt of the petitioner-s reply and upon being satisfied that 10% of the disputed tax demand was

received, the 1st respondent is directed to provide a reasonable opportunity to the petitioner, including a personal hearing, and thereafter issue a fresh order within a period of three months from the date of receipt of the petitioner-s reply. In view of the assessment order being set aside, the bank attachment is raised. **M/s.Sri Visalam Traders, Vs 1. The Deputy State Tax Officer – 2, Royapettah Assessment Circle, 2.The Manager, Canara Bank, P H Road, Chennai-7. Writ Petition No.15791 of 2024 DATED: 25.06.2024**

Documents not taken note: The assessing officer does not appear to have taken note of the documents submitted while confirming the tax proposal. However, as contended by Ld Additional Government Pleader, the petitioner has also failed to subsequently participate in proceedings or file the reconciliation statement in GSTR 9C. For reasons set out above, the impugned order dated 28.12.2023 is set aside on condition that the petitioner remits 5% of the disputed tax demand as agreed to within two weeks from the date of receipt of a copy of this order and remanded the matter with to the assessing officer. **M/s. Murugan Metals Vs The State Tax Officer (ST), Moore Market Assessment Circle, W.P.No.16582 of 2024 DATED: 25.06.2024**

Rate of tax, Trade payables, ITC: For tax proposal relating to the rate of tax on road works, the petitioner has placed on record notifications which indicate that the tax rate on road works is 12%, even if the service is not provided directly to the government. As regards trade payables it appears that impugned order was passed by assuming that 5% of the trade payables reflected in the financial statement were not paid within 180 days period. This conclusion is entirely speculative. In respect of tax proposal relating to excess input tax credit being availed, in respect of supplies where the difference in ITC is more than Rs.5 lakhs, the petitioner should have produced certificates from the chartered accountants of the suppliers concerned. This does not appear to have been done by the petitioner. For these reasons, the impugned order is set aside on condition that the petitioner remits a sum of Rs.25 lakhs towards the disputed tax demand within 15 days from the date of receipt of a copy of this order. Subject to being satisfied that the said amount was received, the respondent is directed to provide a reasonable opportunity to the petitioner, including a personal hearing, and thereafter issue a fresh order within three months from the date of receipt of a copy of this order. **M/s. JSR Infra Developers Pvt. Ltd., Vs 1. State Tax Officer, Gudiyatham East Circle, 2. Assistant Commissioner (ST), T-Nagar**

Assessment Circle, W.P.No.14415 of 2024 DATED: 24.06.2024

Input tax Credit: The petitioner submits that ITC was denied to the petitioner in spite of the petitioner submitting the relevant tax invoice, e-way bill and bank statement. In fact, learned counsel points out that the supplier had filed returns during the relevant period, and that these supplies are reflected in the GSTR 2A and relied upon several judgments, including the judgment of the Madurai Bench of this Court in DY Beathal Enterprises v. State Tax Officer, order dated 24.02.2021 in W.P(MD) No.2127 of 2021. Ld Counsel for respondent submitted that mere reflections of inward supplies in GSTR-2A, does not satisfy the condition of Section 16(2)(b) of the CGST Act 2017/TNGST Act 2017 for the inward supply transactions, since the suppliers issued fake invoices and passed on the fake input tax credit without movement of goods to the recipients. Stating so the Court concluded that re-consideration is necessary subject to putting the petitioner on terms and the impugned order dated 07.03.2024 is set aside subject to the condition. **M/s. S.S.Metals, Vs The State Tax Officer, Alandur Assessment Circle, W.P.No.15381 of 2024 DATED: 24.06.2024**

(The Author is a Chennai based Chartered Accountant in Practice. He can be reached at vvsampat@yahoo.com)

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- **GST – ORDER CONFIRMING DEMAND ON ACCOUNT OF ADDITION OF TURNOVER AS PER THE PROFIT & LOSS ACCOUNT AND TURNOVER AS PER THE ANNUAL RETURN IN GSTR 9 WHEREAS THE SCN WAS DEMANDED TAX ON THE TURNOVER DIFFERENCE BETWEEN PROFIT & LOSS AND GSTR 9 RETURN – EXCESS DEMAND NOT SUSTAINABLE**

CA. VIJAY ANAND

In Renaatus Projects Pvt. Ltd. v. STO, Chennai 2024(87) GSTL 70/(2024) 19 Centax 313 (Mad.), the petitioner is a company engaged in undertaking works contracts and turnkey projects, including Government projects, in Tamil Nadu, Puducherry and Mauritius. SCN was issued demanding tax on the difference between the turnover as per the Profit & Loss Account and the turnover as per the Annual

Return in GSTR 9 wherein the assessee could not participate as they were unaware of the same. Finally the demand was confirmed by adding the turnover as per the Profit & Loss Account and the turnover as per the Annual Return in Form GSTR 9 against which a writ petition was filed before the high court which observed as under:-

- On perusal of the impugned order, it is evident that the respondent added the total turnover as per the profit and loss account and the turnover as per the annual return in GSTR 9 when the tax proposal pertains to turnover difference, the difference between the turnover as per the profit and loss account and the turnover as per the GSTR 9 should have been taken into consideration. To that extent, the impugned order calls for interference.

- The record discloses that sufficient opportunity was provided to the petitioner by issuing intimation dated 20.09.2023, show cause notice dated 27.09.2023 and about three reminders in December 2023. The explanation of the petitioner that it was unaware of proceedings cannot be accepted especially in view

of the petitioner being a large corporate entity.

- However, substantial liability was imposed on the petitioner without taking into consideration documents on record such as the GSTR 9C reconciliation statement.

- Consequently, it is just and necessary to provide an opportunity to the petitioner to contest the tax demand, albeit on terms.

Hence, the impugned order was set aside subject to the condition that the petitioner remits a sum of Rs.2.50 crore within four weeks and the petitioner was permitted to submit a reply to the show cause notice by enclosing all relevant documents. Upon receipt of the petitioner's reply and upon being satisfied that Rs.2.50 crore was received towards the disputed tax demand, the adjudicating authority was directed to provide a reasonable opportunity to the petitioner, including a personal hearing, and thereafter issue a fresh order within three months from the date of receipt of the petitioner's reply.

- **GST- CONFIRMATION OF DEMAND HOLDING THAT THE DETAILED REPLY GIVEN BY THE ASSESSEE TO BE DEVOID OF MERITS**

WITHOUT ANY JUSTIFICATION – NOT SUSTAINABLE

In Rcube International v. STO 2024(87) GSTL 280/ (2024) 19 Centax 366 (Del.), the adjudicating authority confirmed the demand on the assessee holding that the detailed reply submitted by the assessee were devoid of merits without any justification. On a writ petition, the high court observed as under:-

- The impugned order mentions that the taxpayer has filed their objections/ reply online on portal through DRC-06 which has been examined thoroughly and was found to be devoid of merits. Therefore, following principle of natural justice before passing any adverse order, further personal hearing opportunity was given to the taxpayer for which neither the taxpayer nor their representative appeared for personal hearing despite giving sufficient opportunities, therefore, the undersigned is left with no other option but to reexamine the reply and documents available on the portal.

- The observation in the impugned order is not sustainable for the reasons that the reply dated 11.01.2024 filed by the Petitioner is a detailed reply with supporting documents. Proper Officer had to at least consider the reply on merits and then form an opinion. He merely held that the reply is devoid of merits without any justification which ex-facie shows that Proper Officer has not applied his mind to the reply submitted by the petitioner.

- Further, if the Proper Officer was of the view that any further details were required, the same could have been specifically sought from the Petitioner. However, the record does not reflect that any such opportunity was given to the Petitioner to clarify its reply or furnish further documents/details.

Hence, the impugned order was set aside and the matter was remitted to the Proper Officer for re-adjudication. The petitioner may file a further reply to the Show Cause Notice within a period of 30 days and, thereafter, the Proper Officer shall re-adjudicate the Show Cause Notice after giving an opportunity of personal hearing and shall pass a fresh speaking order in accordance with law.

- **GST – ORDER PASED OVERLOOKING ASSESSEE'S REQUEST FOR GRANT OF AN ADJOURNMENT DURING THE FIRST HEARING – CRYPTIC – SET ASIDE**

  In Sun & Sand Industries Africa Pvt. Ltd. v. STO, Avato, Department of Trade and taxes 2024(87) GSTL 391/ (2024) 18 Centax 531 (Del.) an SCN was issued to the assessee alleging excess claim of ITC and availing ineligible ITC for which the petitioner replied on 23.10.2023 seeking additional time for furnishing a detailed reply and an opportunity of personal hearing. A reminder dated 12.12.2023 was issued to the Petitioner providing a final opportunity for personal hearing, which was replied on 18.12.2023 seeking time to furnish reply and time to appear for personal hearing. However, the impugned order dated 19.12.2023 did not take into consideration the request submitted by the Petitioner for extension of time. On a writ petition, the high court observed as under:

- Section 75 (5) of the Act stipulates that, if sufficient cause is shown, the proper

officer shall adjourn the hearing, however, not more than three adjournments may be granted.

- However, it is not mandatory for the proper officer to grant three adjournments. Adjournment is not a right. Said provisions empowers the proper officer to grant upto three adjournments, if sufficient cause is shown. It would be dependent on the facts of each case whether sufficient cause has been shown or not for exercise of the discretion to adjourn.

- Be that as it may, the order is a cryptic one and a prayer is made on behalf of petitioner for one opportunity to file reply.

Hence, the impugned order was set aside and matter was remanded back to the proper officer for re-adjudication after giving an opportunity of personal hearing.

- **GST – GST PAID TO VENDOR FOR AN AGREEMENT WHICH WAS SUBSEQUENTLY CANCELLED – REFUND CLAIMED BY PERSON WHO BORNE THE TAX - ADMISSIBLE**

In Nam Estates Pvt. Ltd. v. JCCT (Appeals-I), Bengaluru

2024(87) GSTL 398/(2024) 18 Centax 466 (Kar.), pursuant to the Agreement dated 29.05.2017 entered into between the petitioner and its vendor by name viz., M/s. Mavin Switchgears and Control Pvt. Ltd., the petitioner paid advance of Rs.14,08,79,262/- to the aforesaid vendor as well as GST of Rs.2,53,58,268/-. Subsequently, the aforesaid vendor did not supply goods under the contract to the petitioner and the contract was cancelled and the petitioner called upon the aforesaid vendor to return/refund the entire advance amount. Since, the vendor did not refund/ repay the aforesaid amount of Rs.14,08,79,262/- back to the petitioner, the petitioner recovered the same by encashing the bank guarantee furnished by the aforesaid vendor. The petitioner filed a claim for the refund of GST which was rejected by the adjudicating authority and sustained by the Appellate Authority against which a writ petition was filed in the high court which observed as under:-

- A perusal of the rejection order indicates that the same is unreasoned, cryptic, non-speaking order without

assigning any reasons as to why the refund application was rejected. Further the appellate order indicates that despite several judgments having been referred to and relied upon by the petitioner, Adjudicating Authority / Appellate Authority confirmed the order passed on the ground that eligibility criteria under Section 54 of the Karnataka Goods and Service Tax, 2017, have not been met by the petitioner.

- The Appellate Authority has come to the conclusion that supplier/vendor was the person ought to have issued credit note and thereafter, it was open for the petitioner to seek refund and without doing so, the petitioner is not entitled to seek refund of the GST. In short the Appellate Authority has also come to the conclusion that it is for the vendor to file an appropriate application before the respondents/ authorities seeking refund and only thereafter, the grievance of the petitioner can be addressed for the purpose of refund.

- The payment of sum of Rs.14,08,79,262/- by the petitioner to the vendor, payment of Rs.2,53,58,268/-

towards GST by the vendor to respondents and refund of entire amount of Rs.14,08,79,262/-by encashment of the bank guarantee by the petitioner and other material on record would cumulatively indicate that there was no GST liability either by the petitioner or his vendor were concerned and by applying doctrine/ principles of unjust enrichment and restitution and since the aforesaid GST amount is lying with the respondents, who are retaining the same without there being any GST liability either by the petitioner or the vendor.

Hence, the high court allowed the petition along with the following directions:-

- Orders of the adjudicating and appellate authorities were set aside; and
- Refund application filed by the petitioner was allowed; and
- Concerned respondent/ authority were directed to refund the entire GST amount of Rs.2,53,58,268/- back to the petitioner within a period of eight weeks; and
- It was made clear that this order does not interpret any of the provisions of CGST Act and Rules and it is

made in the peculiar/special facts and circumstances obtaining in the instant case and this order shall not be treated as a precedent or have any precedential value for any purpose whatsoever.

- **GST – OBJECTIONS RAISED TO DEFECTS POINTED BY AUDIT – OVERLOOKING THE SAME SCN WAS ISSUED AND DEMAND CONFIRMED USING IDENTICAL LANGUAGE – DEMAND SET ASIDE**

In S.P.P.Silks v. STO, Erode 2024(87) GSTL 406/(2024) 18 Centax 308 (Mad.), pursuant to an audit of the petitioner's books of account, objections were raised in relation to audit observations which were not accepted by the assessee. Thereafter, an intimation was issued on 20.09.2023 in Form GST DRC-01 which was followed by a show cause notice dated 29.09.2023 to which the petitioner replied on 26.12.2023. The impugned order dated 29.12.2023 was issued thereafter confirming the demand using the same language as contained in the show cause notice. On a writ petition, the high court observed as under:-

- The show cause notice deals with about six defects wherein a conclusion was recorded instead of indicating the tax proposal and calling upon the petitioner to show cause in respect thereof.

- The impugned order deals with the same six defects and uses identical language as contained in the SCN without taking into consideration the petitioner's replies.

- The adjudication process would be robbed of meaning unless the authority undertaking adjudication acts in an objective manner without predetermining the issues arising for consideration.

- Since adjudication was not undertaken in such manner, the impugned order cannot be sustained. However, it shall be treated as a show cause notice and responded to.

Hence, the high court directed that the impugned order be treated as a show cause notice and permitted the petitioner to submit a reply thereto within 15 days upon receipt of which the second respondent was directed to provide a reasonable opportunity, including a personal hearing, and thereafter

issue a fresh order within three months from the date of receipt of the petitioner's reply after duly taking note of the observations set out in this order.

Hence, the matter was disposed off.

- **GST – REFUND OF IGST ON SOFTWARE DEVELOPMENT SERVICES PROVIDED TO OVERSEAS SUBSIDIARY – ELIGIBLE**

  In Vuram Technology Solutions Pvt. Ltd. v. ACGST (Appeals) Trichirapalli 2024(87) GSTL 491/(2024) 18 Centax 534 (Mad.), the petitioner has effected export of service to a subsidiary in Australia, namely Vuram Australia Pty Ltd., Docklands, Australia for which the petitioner discharged the GST liability by debiting tax from its Electronic Credit Ledger for a sum of Rs.3,39,457/-. The petitioner's claim for refund u/s 54/55 was rejected by the adjudicating authority and sustained by the appellate authority holding that the petitioner and its subsidiary are not merely establishment of a distinct person as per Explanation I in Section 8 of the IGST Act, 2017. Thereafter a writ

petition was filed before the high court, owing to the non constitution of the Tribunal, which observed as under:-

- The impugned order passed by the appellate authority concludes that the petitioner has satisfied the requirements of Section 2(6)(i) to (iv) of IGST Act, 2017 which is incorrect as the petitioner and its subsidiary are two distinct entities and therefore, it cannot be said that the petitioner has not satisfied the requirements of Section 2(6)(v) of IGST Act, 2017.

- The doctrine of the decision of the Authority for Advance Ruling in Segoma Imaging Technologies India (P.) Ltd., In re [2018] 100 Taxmann.com 221/[2019] 20 GSTL 611 (AAR-GST - Maharashtra) cannot be applied to the facts of this case.

- It cannot be said that the petitioner and its subsidiary are not merely establishment of a distinct person in accordance with the explanation I in Section 8 of the IGST Act, 2017.

- The issue stands clarified by Circular No. 161/17/2021-GST dated 20.09.2021 bearing Ref.F.No.CBIC-20001/8/2021-GST which

was followed in Xilinx India Technology Services (P.) Ltd. v. Special Commissioner Zone VIII [2023] 154 taxmann.com 312/99 GST 948/78 G.S.T.L. 24 (Delhi)/ 2023 (78) GSTL24 (Delhi).

- Furthermore, the Revenue cannot argue against its own circular, although such clarification in Circular of the Board are much binding on the petitioner nor on the Court.

- The view expressed in the said circular is correct and clarifies the legal position and therefore, there is no inclination to take a different view.

- Since the view taken by the Board is correct, the impugned order is liable to be set aside.

Consequently, the adjudicating authority was directed to process the re-fund claim of the petitioner together with interest payable in accordance with the provisions of the Act as expeditiously as possible.

Hence, the writ petition was disposed off.

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Admissibility of Input Tax Credit in respect of Rotary Car Parking System

CA. AMAN GOYAL

In the case of Re: M/s. Arthanarisamy Senthil Maharaj (referred to as "appellant") (Appeal No. 04/2024 AAAR, Order No. AAAR/9/2024 (AR) dated August 21, 2024) – Tamil Nadu Appellate Authority for Advance Ruling

Facts of the case:-

1. The Appellant is a proprietorship unit engaged in provision of taxable service falling under the category of 'Renting of Immovable Property Service' falling under Service Accounting Code 997212.

2. The Appellant had applied for Advance Ruling, seeking a clarification on the admissibility of Input Tax Credit (ITC) on the 'Rotary Parking System' falling under HSN code 8428. The AAR vide Ruling No. 07/ARA/2024 dated 30.04.2024 ruled that ITC is not admissible on the 'Rotary

Parking System' desired to be installed by the applicant.

3. Being aggrieved by the ruling, the appellant preferred the appeal before the Appellate Authority of Advance Ruling

Interpretation of Law by the Applicant:-

1. Supply of rotary car parking system involves two vital activities, viz., the goods falling under HSN 8428 90 90 and Installation service falling under SAC 995468, and accordingly is to be treated as a 'composite supply'. The installation of car parking system is for furtherance of business, as the provisioning of renting service is naturally dependent on the various allied services which are essential for enhancement of the quality of rental service.

2. There cannot be any justification in the denial of ITC on the plant and machinery, just because the civil foundation and structural support is created for the purpose of safety and stability. The credits are blocked only in respect of the activities relating to construction of an immovable property and not for the installation of parking system, which is a movable property.

3. The parking system is not attached to earth and therefore, the same cannot be construed to have attained the status of 'immovable property'. The commissioning of the parking system is an independent installation in the premises of the taxpayer and certainly not part of the building.

4. There can be no legal sanctity for the observations of the AAR to the effect that the car parking system falls within the meaning of Section 3 (26) of the General Clauses Act, 1897 (permanently fastened to anything attached to earth) and Section 3 (c) of the Transfer of Property Act, 1882 (attached to what is imbedded for the permanent beneficial enjoyment of that to which it is attached)

5. Car parking system can easily be dismantled by removal of bolts and screws with simple screwdriver technology for installation elsewhere to have the same characteristics and discharge of similar functions.

6. The specific exclusion of plant and machinery from the blocked credits and inclusion of civil foundation and structural supports as

plant and machinery would have the effect of liberating the parking system from the clutches of 'blocked credits', even if the activity of installation is to be construed as works contract service.

Question before AAAR:-

Whether the appellant is eligible to avail ITC on rotary car parking system or is the same blocked under the provisions of section 17(5)(c) & section 17(5)(d) ?

Observations & Ruling of AAR:-

1. Rotary Parking System, as the name suggests, is a system in its own, much more than an equipment, machinery or an apparatus, as it involves the functionality of various items like machines, equipments, motors, frame assembly, pallets, electrical panels, hydraulic power packs, operator boxes to floor/walls/columns and other electrical and electronic support system, a specialized civil foundation with steel structure to withstand the load, etc. Therefore, it could be seen that the overall system (Rotary Parking), takes shape and becomes operational only at the site of the appellant when all the

constituent parts are assembled first and installed over the civil foundation and steel framework specifically designed for this purpose.

2. Definition of "Foundation" in terms of the Tamil Nadu Combined Development and Building Rules, 2019, which means "part of the structure, which is in direct contact with ground and transmits loads over it". The term 'Structure' is also defined under TNCDBR, whereby "Structure" means something constructed or built having a fixed base on or other connection to the ground or other structure.

3. Further, the term "Structure" in the context of Civil Engineering refers to anything that is constructed or built from different interrelated parts with a fixed location on the ground and civil structures are manmade structures built by utilizing any material, viz., cement, steel etc., based on requirement and purpose of the structure. Rotary Parking system' ideally falls within the category of a 'civil structure', which is clearly excluded under the expression 'plant and machinery.'

4. When an immovable property, especially in the nature of a commercial/

residential complex is rented out, it is not just the building or part of the building that gets rented out. Rather, it includes the land appurtenant thereto which is incidental to the use of such building or part of the building, the common or shared areas and the facilities relating thereto, as well.

5. Service relating to 'Renting of Immovable property' includes the land, building, staircase, lifts, common basements, play areas, open parking areas, common storage spaces, water tanks, sumps, apparatus connected with installations for common use, all other portion of the project necessary or convenient for its maintenance, safety, etc., and in common use. The corollary is that all the common areas and facilities extended become part of the immovable property that is being rented out. Further, it is not the case here that rent is collected separately for the living space, and for the other common areas or facilities like lifts, basements, play areas, parking facility, water tanks, sumps etc., and that the same is collected for the single service, viz., 'Renting of Immovable Property'.

6. Rotary car parking system is attached to earth permanently, whereby it attains the status of an 'immovable' property, as the car parking structure as such cannot be moved in the same position from the place of erection, but that the same could be moved only after dismantling the constituent parts for re-erection at some other place.

7. The specific purpose behind installing the rotary car parking system within the premises of the taxpayer is to cater to the parking needs of the tenants, and their customers/invitees which in turn serves only the cause of the tenants. It is embedded to earth for the permanent beneficial enjoyment of the tenants of the complex for whom the premises along with facilities are rented out.

Ruling

Rotary parking system installed and commissioned at the premises of the appellant amounts to construction of an immovable property, whereby the input tax credit thereon becomes ineligible under Section 17 (5) (d) of the CGST/ TNGST Act, 2017.

ITC reversal under Section 17(3) in respect of transfer of title of goods in Free Trade & Warehousing Zone (FTWZ)

In the case of Re: M/s. Panasonic Life Solutions India Private Limited (referred to as "applicant") (TN/17/ARA/2024 dated July 25, 2024) – Tamil Nadu Authority for Advance Ruling

Facts of the case:-

1. The Applicant is a wholly owned subsidiary of Panasonic Corporation and is engaged in the business of manufacturing and supplying of various categories of products such as Consumer durables, Industrial Devices, Energy Systems, etc.

2. The Applicant had executed an agreement with 'Kerry Indev Logistics Private Limited' (hereinafter referred to as KILPL') for clearance/handling of goods from customs and for storage of imported goods in the FTWZ unit (located in Tamil Nadu, Chennai)

3. The Applicant secures space in the FTWZ unit (viz. of KILPL with whom the Applicant has entered into an agreement) for a fee to inter alia store the imported goods (viz. cleared without payment of applicable Customs duty) of the Applicant in the FTWZ unit. The Applicant has added the said place as Additional place of business in GST registration of Tamil Nadu.

4. The goods are cleared from the port by KILPL (viz, FTWZ unit) by filing Bill of Entry (BOE) on behalf of the Applicant. KILPL uses their IEC registration for the purposes of import of goods into India. The BOE filed by KILPL clearly mentions the name of the Applicant as the client on behalf of whom the goods are being imported by KILPL. As per the arrangement with the Applicant, the FTWZ unit (viz. KILPL) merely clears and warehouses the goods imported and in consideration, the FTWZ unit collects warehousing charges from the Applicant.

5. Prior to arrival of goods in the customs port, the Applicant would intimate KILPL in Chennai and provides copy of the purchase order and other documents for clearance of goods from the port and storage of the same in FTWZ unit. The title to the goods stored in FTWZ unit would remain with the Applicant during the storage.

6. In the warehousing facility of KILPL, no manufacture or processing activities is being carried out by the Applicant. On identification of the customers, goods would be sold by the applicant from

the FTWZ unit to the customers across India. The customer shall either clear goods from the FTWZ or shall make further transfer of such goods to other customers. The final customer (who decides to clear the goods) files the BOE and clears goods from the FTWZ unit upon payment of applicable duties.

7. Upon finalization of customer, the Applicant would raise a tax invoice (without tax) on the DTA customer in foreign currency. In case of supply to overseas entity, the Company issues an export invoice as export of goods without payment of tax under Letter of undertaking or Bond. The said invoices also refer the fact that the goods are being supplied from FTWZ unit (viz. of KILPL)

8. The Applicant reports the said transaction in their GST return as a non-GST supply in case of supply to DTA customer. Whereas in case of exports, the Company reports the transaction as export of goods without payment of tax.

Questions before AAR

1. Whether the transfer of title of goods stored in FTWZ Unit by the Applicant to its customers in Domestic Tariff Area (DTA) result in bonded warehouse transaction covered under para 8 (a) of Schedule III of the CGST Act, 2017?

2. If answer to the above question is negative, whether IGST is payable by the Applicant on goods stored in FTWZ unit and supplied to its customers in DTA unit, in addition to the customs duty payable [i.e. Basic Customs Duty (BCD) + IGST] by the customer in DTA on removal of goods from the FTWZ unit?

3. If the supply of goods lying in FTWZ unit is not covered under para 8 (a) of Schedule III of the CGST Act, whether any reversal of input tax credit of common inputs/ input services/Capital goods is required at the hands of the Applicant in terms of Section 17 (3) of the CGST Act, 2017?

Interpretation of Law by the Applicant:-

1. In terms of para 8 (a) of Schedule III of the CGST Act,

"Supply of warehoused goods to any person before clearance for home consumption" shall neither be treated as a supply of goods nor a supply of services. Further as per Explanation-2 of Schedule III of the CGST Act, for the purposes of paragraph 8, the expression "warehoused goods" shall have the same meaning as assigned to it in the Customs Act, 1962.

2. As per the Customs Act, 'warehoused goods' means goods deposited in a warehouse. Further, in terms of section 2 (43) and 2 (44) of Customs Act, "warehouse" means a public warehouse licensed under section 57 or a private warehouse licensed under section 58 or a special warehouse licensed under section 58A. in order to qualify as a "warehouse" in terms of the Customs Act, a license is required to be obtained in terms of the above sections. It is only when a particular area is licensed in terms of the above sections, said area qualify as "warehouse' and it is only then goods deposited in such area, qualify as "warehoused goods'.

3. As KILPL (viz. the FTWZ unit) has not been licensed as warehouse under section 57, 58 or 58A of the Customs Act and is registered as an SEZ unit, FTWZ is not a warehouse in terms of the Customs Act.

4. In terms of Section 2 (n) of the SEZ Act, FTWZ is a SEZ wherein mainly trading and warehousing and other activities related thereto are carried on.

5. In terms of Section 53 of the SEZ Act, FTWZ is a deemed foreign territory for the purpose of tariff and trade.

6. The SEZ Act and the SEZ Rules are the legal framework for FTWZ. Accordingly, FTWZ should be classified as a SEZ for authorized operations rather a "warehouse'.

7. By virtue of Instruction no. 60 dated 6 July 2010, the FTWZ unit is allowed to store goods on behalf of the DTA supplier and buyer and the same will be considered as an authorized operations as per Rule 18 (5) of the SEZ Rules.

8. Removal of goods from FTWZ unit to DTA unit is treated at par with import of

goods and accordingly, Custom duty is discharged by the end customer in accordance with Section 30 of the SEZ Act read with proviso to Section 5 (1) of the IGST Act read and Section 3 of the Customs Tariff Act.

9. Accordingly, transfer of title of goods by the applicant to customer while the goods are still lying in FTWZ does not tantamount to supply of "warehoused goods" to any person before clearance for home consumption and accordingly may not be covered under para 8(a) of Schedule III.

10. Para 8 (b) of schedule III is squarely applicable in the instant case, as applicant transfers the title of the goods to the customer while the goods are lying within the FTWZ unit i.e. before final clearance for home consumption by the end customer.

11. In terms of Section 17 (3), value of exempt supply shall not include the value of activities or transactions specified in Schedule III, except, inter-alia, the value of such activities or transactions as may be prescribed in respect of

clause (a) of paragraph 8 of the said Schedule i.e. "Supply of warehouse goods to any person before clearance for home consumption". In the instant case, supply of goods stored in the FTWZ unit should not fall under paragraph 8 (a) of schedule III. Accordingly, the Applicant would not be required to reverse ITC.

Observations & ruling of AAR:-

Free Trade Warehousing Zone (FTWZ) is part of SEZ scheme and it is a Customs bonded, warehouse. Warehousing of goods that are imported without payment of appropriate Customs duties are carried out in these zones. SEZ is a specifically delineated duty free enclave which is deemed to be a foreign territory for the purposes of trade operations and duties and tariffs.

Normally, the applicant imports goods and stores them in FTWZ till he finds a local customer who will purchase the goods and such purchaser clears the goods under the provisions of the Customs Act. In other words, the goods would become exigible to tax under the domestic enactments only when they are cleared and supplied

from FTWZ for home consumption to DTA.

Warehoused goods, as specified in clause 8 (a) of the Schedule III, covers the warehouses/ warehoused goods in respect of the FTWZ/SEZ, being discussed in the instant case, as well.

The impugned activities of the applicant get covered under clause (a) of Para 8 of the Schedule III to the CGST Act, 2017 (and not under clause (b) of Para 8 as claimed by the applicant, as clause (b) relates to activities in the nature of High Sea sales)

As far as the activities relating to 'transfer of title of goods by the applicant to customers in DTA', and multiple transfers within the FTWZ' are concerned, both these activities get squarely covered under para 8 (a) of Schedule-Ill of the CGST Act, 2017.

With the amendment to Explanation of Section 17 (3) of the CGST Act, 2017, apart from paragraph 5 of Schedule-Ill to the Act, clause (a) to paragraph 8 of the said schedule have been mentioned as an exception to Section 17 (3) of the Act. Accordingly, proportionate reversal of ITC of common

inputs/capital goods/services availed, if any, is required to be made by the applicant in terms of the amended Section 17 (3) of the CGST Act, 2017, and the rules made thereunder.

Ruling

1. The present transaction will get squarely covered under para 8 (a) of Schedule-Ill of the CGST Act, 2017.
2. Proportionate reversal of ITC of common inputs/ capital goods/services availed, if any, is required to be made by the applicant in terms of the amended Section 17 (3) of the CGST Act, 2017

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CORPORATE GUARANTEE – A DEEP DIVE

Nithya Srinivasan & Chitra Subramanian

Overview

With the rise of globalization and the blurring of national borders in business operations, financial transactions between Indian companies and their international counterparts have increased. Considering the current litigation landscape surrounding financial transactions, it is crucial to ensure that these transactions are conducted with full transparency, at an arm's length price, and with the necessary approvals. One common type of related party transaction is financial guarantees, where one entity guarantees the obligations of another group entity seeking funds from a financial institution. Often, these guarantees are provided without any consideration, leading tax authorities to scrutinize their reporting and tax implications more closely. Apart from direct tax implications, guarantee is viewed critically from indirect tax perspective – levy of GST on guarantee as a service. In transfer pricing, tax authorities

have become more aggressive on determining the arm's length application on such transactions, taxpayers face difficulties in determining the taxability and valuation of these arrangements.

Corporate guarantee involves a holding company assuring the financial obligations of a subsidiary or another affiliated entity within the same group. This guarantee helps the subsidiary to secure loans with competitive interest rates.

1. What is a Corporate Guarantee?

A financial guarantee involves a commitment by the guarantor to cover specific financial obligations if the guaranteed party fails to meet them. Various terms describe different forms of credit support within a multinational group, ranging from formal written guarantees to mere implicit support due to group membership (passive association). In this context, a guarantee is defined as a legally binding promise by the guarantor to fulfil the obligations of the guaranteed entity in the event of a default.

2. Transfer Pricing Perspective on Corporate Guarantees

Financial transactions are a significant source of transfer

pricing disputes between taxpayers and tax authorities. In MNC group, a guarantor provides guarantees to its affiliated entities because it has a vested interest in the subsidiary's performance. The provision of such guarantees by global multinational enterprises has led to contentious issues in financial transactions.

The Organisation for Economic Co-operation and Development (OECD) Guidelines in the 2022 edition has covered a new section on the financial transactions including guarantees. In order to evaluate the transfer pricing implications of a financial guarantee, it's crucial to first comprehend the specifics of the guaranteed obligations and their impact on all involved parties, accurately delineating the actual transaction. Some key aspects are given below:

Economic Benefits of Financial Guarantees

An understanding of the economic benefits that the borrower gains, which go beyond the benefits of mere group membership is critical. Financial guarantees can influence borrowing terms. For instance, having a guarantee might enable the borrower to secure a lower interest rate or access a larger loan amount due

to the lender's assurance of reduced risk.

Enhancement of Borrowing Terms: For a lender, a guarantee means that the guarantor legally commits to covering the borrower's debt in case of default, potentially lowering the lender's risk. This might allow the borrower to obtain loan terms as if they had the guarantor's credit rating rather than their own. Pricing methodologies for such guarantees are akin to those used in loan pricing.

Borrower's Cost Evaluation: If an intra-group guarantee reduces the borrower's cost of debt, the borrower might be willing to pay for the guarantee if it does not worsen their overall position. The costs associated with obtaining the guarantee should be compared with the cost of borrowing without the guarantee, considering any implicit support. The guarantee could also impact other loan terms, depending on the specific circumstances.

Increased Borrowing Capacity: When a guarantee allows the borrower to secure a larger loan than possible without it, the guarantee impacts both the borrowing capacity and the interest rate. This scenario raises two questions: whether part of

the loan should be considered as a direct loan to the guarantor (and subsequently as equity from the guarantor to the borrower) and whether the guarantee fee for the remaining portion is at arm's length. Analysis may reveal that the guarantee fee should apply only to the portion accurately deemed a loan, with the rest treated as a capital contribution from the guarantor.

Key considerations while providing a guarantee include whether group membership provides implicit benefits, whether an explicit guarantee qualifies as a shareholder activity or service, the associated costs of the guarantee, and the likelihood of securing a loan without the guarantee. Explicit guarantee is legal binding and usually provides the relevant rights to the creditor to enforce commitment.

Three types of explicit guarantees are commonly used 1) Downstream guarantees: a parent company issues a guarantee to external creditors for the benefit of one of its subsidiaries when that subsidiary enters into agreements with external creditors (typically used in decentralized business structures or when the location

of the subsidiary is more attractive for obtaining external financing); 2) Upstream guarantees: a group company issues a guarantee to external creditors for the benefit of its parent company where the latter enters into agreements with the external creditors (typically used when the external financing is obtained at a parent or holding level or when the parent company performs central treasury functions); and 3) Cross guarantees: Several group companies issue guarantees to external creditors for the benefit of each other with the effect that they can all be considered as one single legal obligor (typically used in cash pooling).

Implicit guarantee on the other hand is deemed to be present once the borrower is part of a MNC Group (passive association) and has the financial backing of the Group. This implicit group support or guarantee can enhance the credit rating, potentially lowering its financing costs (interest rates) or increasing its borrowing capacity. Since this incidental benefit arises from the controlled entity affiliation with the group, no payment is required for such implicit guarantees. Comfort letters/ letters of intent include a promise (generally not legally binding) provided, in most cases, by a parent company to

an MNE company which states that the former will oversee the latter's affairs in order to be in accordance with the group strategies and rules, and refrain from taking adverse actions that would compromise the financial stability of another group company. Agreements which include a declaration provided, in most cases, by the parent company to an MNE company which states that the former will provide the latter with additional capital to prevent the risk of its default. However, these generally do not transfer risk and generally are not considered as financial guarantees that require an arm's length payment.

3. Corporate Guarantees as International Transactions

Initially the definition of International Transaction was restricted to "*a transaction between two or more associated enterprises, either or both of whom are non residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service*

or facility provided or to be provided to any one or more of such enterprises."

Most of the taxpayers took a position that it was not an international transaction in the first instance and then went on to about the need for a consideration for such guarantee. The issuance of corporate guarantee was considered in the nature of shareholder activity/quasi capital and not having bearing on profits, income, losses or assets of an enterprise and thus could not be included in the provision of services. In the case of Micro Ink Limited *([TS-568-ITAT-2015(Ahd)-TP] - November 27, 2015)* ITAT deletes the Transfer pricing adjustment in respect of corporate guarantee considering the issuance of corporate guarantee was in nature of shareholder activity capital and thus could not be included within ambit of 'provision for services' under definition of 'international transaction' u/s.92B.Also in the case of Delhi Bench Tribunal in Bharti Airtel Ltd v. Addl. CIT*(I.T.A. Nos.: 5636/Del/2011 March 11,2014)*, found that guarantee provided by the assessee does not have any bearing on profits, income, loss or assets of the assessee and hence it is not international transaction.

The scope of definition of international transaction has been extended in Finance Act 2012 with retrospective effect from 1st April, 2002. Various international transactions that were earlier outside the scope of transfer pricing have been brought within the ambit of Indian Transfer Pricing regulations through inserting Explanation to section 92B. The expanded definition included the below:

c. Capital financing, including any type of long term or short term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

It gives substantial clarity to the statute that corporate guarantee is included under the ambit of 'international transaction' under Section 92B as the word 'guarantee' is used under explanation of clause (c) of Section 92B.

For the assessment years after the aforementioned amendment, Tribunals and Courts have ruled guarantee as an international transaction.

4. Benchmarking approaches

OECD guidelines describe several approaches to determining market values for circumstances in which the guarantee payment is considered appropriate.

Companies should consider adopting an appropriate benchmarking analysis for arriving at the Arm's Length Price of corporate guarantees fees. One could adopt any of the below 5 approaches to price corporate guarantees.

CUP Method

The CUP (Comparable Uncontrolled Price) method is applicable when there is external or internal comparables, such as independent guarantors providing guarantees for similar loans or when the same borrower has other comparable loans with independent guarantees.

To determine if controlled and uncontrolled transactions are comparable, all factors affecting the guarantee fee should be considered. These factors include the borrower's risk profile, the guarantee's terms, the underlying loan's specifics (e.g., amount, currency, maturity, seniority), the credit rating difference between the guarantor and the guaranteed party, and prevailing market conditions. When available, guarantees from uncontrolled transactions are generally the most reliable for establishing arm's length guarantee fees.

Conversely, there are financial instruments that can be used as proxies to determine the price of

these transactions, for example, letters of credit, bank guarantees, surety bonds (similar to guarantee rates), guarantee contracts.

The challenge with using the CUP method is the scarcity of publicly available information on sufficiently similar credit-enhancing guarantees between unrelated parties, as such guarantees are rare.

Yield Approach

This approach quantifies the profit the secured party receives from the guarantee in terms of lower interest rates. The method calculates the spread between the interest rate the borrower would pay without the guarantee and the interest rate payable with the guarantee.

First step involves determining the interest rate the borrower would have had to pay on his/her own merits, considering the impact of implicit support due to his/her membership in the economic group.

Then, determine the interest rate payable with the benefit of the explicit guarantee. The interest rate can be used in quantifying the benefit gained by the borrower as a result of the guarantee. In determining the extent of the benefit provided by the guarantee, it is important to distinguish the impact of an

explicit guarantee from the effects of any implicit support as a result of group membership. The benefit to be priced is not the difference between the cost to the unguaranteed borrower on a stand-alone basis and the cost with the explicit guarantee but the difference between the cost to the borrower after taking into account the benefit of any implicit support and the cost with the benefit of the explicit guarantee.

The result of this analysis establishes a maximum guarantee rate that the recipient of the guarantee will be willing to pay. The difference of the saved interest is shared between the guarantor and borrower. The interest differential attributed to the guarantor is the maximum guarantee fee payable by the borrower.

It should be noted that this approach is often used to price financial guarantees due to its simplicity and transparency.

Cost Approach

This method estimates the value of a guarantee by calculating the additional risk borne by the guarantor, which could be based on the expected loss or the capital required to support the risk.

Various models can estimate expected loss or capital

requirements. Some pricing models, like option pricing or credit default swap models, treat the guarantee as a financial instrument to approximate the default risk and determine the fee. The accuracy of these models depends on the assumptions used, and the cost method sets a minimum fee, which may not reflect an arm's length transaction on its own.

The most widely used models for market pricing under this approach are based on the premise that financial guarantee is equivalent to another financial instrument and sets the price of the alternative, for example, by treating the guarantee as a put option or a CDS. In this regard, publicly available CDS spreads data can be used to approximate the default risk associated with the loan and, consequently, the guarantee fee.

This approach sets a minimum fee that the guarantor should be willing to accept.

Valuation of Expected Loss Approach

This approach calculates the guarantee's value by estimating the probability of default and adjusting for the expected recovery rate. This valuation is then applied to the nominal

amount guaranteed to determine the cost of the guarantee, which can be priced using commercial models such as the Capital Asset Pricing Model (CAPM). Examples: probabilistic methods, Value at Risk

Capital Support Method

The capital support method is used when the risk profile difference between the guarantor and borrower can be addressed by adding capital to the borrower's balance sheet. First, determine the borrower's credit rating without the guarantee but with implicit support, then identify the amount of additional notional capital needed to match the guarantor's credit rating. The guarantee can then be priced based on the expected return on this additional capital, reflecting only the impact of providing the guarantee rather than the overall activities of the guarantor.

Companies should choose an appropriate benchmarking method for determining the arm's length price of guarantee fees.

5. Litigation and Corporate Guarantees

Given Corporate guarantee is litigative in nature it is advisable for the tax payers to have the supporting documentation. This should

include information on the nature of the corporate guarantee, its purpose (whether as a shareholder activity or service), how the funds are utilized, thorough benchmarking analyses, and other relevant comparable data.

Some taxpayers do not charge a guarantee fee or set it at a very low level arguing that such fees are related to shareholder activities. Others determine the rate for corporate guarantees on an ad hoc basis or rely on judicial precedents without considering the specific facts of their case.

In practice, tax officers often challenge these ad hoc corporate guarantee fee determinations by applying higher fee rates or comparing them to bank guarantee rates, which are generally higher. Currently, litigation concerning corporate guarantees focuses on determining arm's length pricing. Tribunal decisions generally support a corporate guarantee fee ranging from 0.5% to 0.85% as being at arm's length. Bombay High Court in *Everest Kento Cylinders Ltd ([TS-200-HC-2015(BOM)-TP] - May 8, 2015)* found that a 0.50% fee was appropriate based on the facts of those cases. Conversely, the Madras High Court in *Redington (India) Limited (T.C.A.Nos.590 & 591 of 2019 -*

10-12-2020) determined that a 0.85% fee was appropriate based on its case specifics. Numerous decisions from Income Tax Appellate Tribunals have also upheld the 0.50% rate.

6. Global Perspectives on Corporate Guarantees

The current US Treasury Regulations do not fully address transfer pricing for financial guarantees. There is ongoing review on whether guarantees should be treated as a service and how to apply valuation methodologies to ensure arm's length pricing. The IRAS in Singapore has expanded its guidance to include financial guarantees. Taxpayers must adhere to the arm's length principle for financial transactions, including guarantees, and follow the OECD Transfer Pricing Guidelines for pricing such transactions. Recently UAE has implemented Corporate Tax along with Transfer pricing. UAE has included Financial Guarantee in the transfer pricing regulations and hence tax payers in UAE need to be vigilant while considering corporate guarantee.

7. Global Jurisprudence

One of the most important cases isCanada vs. General Electric Capital*(2010 FCA 344)* is a landmark decision in the realm

of transfer pricing, particularly for financial transactions. It highlighted the complexities involved in pricing corporate guarantees and a strong credit rating(implicit support) even without the explicit guarantee can be consider when applying the arm's length principle. It also upheld the view that the valuation of the explicit guarantee was excessive. The pricing of the explicit guarantee should have been lower than the CRA's assessment due to the implicit support enjoyed.

In few rulings, justification was provided for not compensating the guarantee transaction when it linked to shareholder activity. In the case of Germany vs. Hornbach-Baumarkt AG*((Case No. 1 K 1472/13 august 2023)*, the ruling reinforced the principle that intra-group financial arrangements must be priced at arm's length, but it also established that companies can argue economic justification for non-arm's length transactions, especially when linked to shareholder interests. The decision emphasized the importance of providing sufficient evidence of economic necessity when defending intra-group transactions that deviate from the arm's length principle.

Also there are decisions which underlines the importance of understanding that intercompany agreements,

especially non-arm's length transactions such as guarantees, must meet tax authorities' documentation standards. In the case of *Poland vs. A. Sp. z o.o.(Case No. I SA/Rz 1178/18 (March 2019),* the decision reinforces the obligation for multinational companies operating in Poland to ensure proper transfer pricing documentation that reflects the full scope of financial interactions between related parties.

8. Interplay between GST and Transfer pricing

The application of GST to corporate guarantees has been a controversial topic. The primary issue has been whether providing corporate guarantees constitutes a service under GST regulations. Previously, under the service tax regime, courts suggested that corporate guarantees did involve a service component. With the introduction of GST, Rule 28(2) of CGST rules 2017 was established, setting the value of corporate guarantees at a maximum of 1% of the borrowed amount or the actual consideration, whichever is higher. It can be noted that reference of 1% cap is also present in the Safe Harbour rules issued by CBDT for transfer pricing. Indian tax

authorities, both direct and indirect, are coordinating to interpret the definition of corporate guarantees and determine the applicable percentages. Effective documentation is crucial for taxpayers to manage risks related to Transfer Pricing and GST and to avoid conflicts with tax authorities.

9. Conclusion

Corporate guarantees play a significant role in financial transactions and transfer pricing. The proper classification, valuation, and documentation of these guarantees are crucial for compliance and dispute resolution. Understanding the nuances of local and international regulations can help companies navigate these complex issues effectively.

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DECODING GLOBAL SANCTIONS : A CRITICAL GUIDE FOR GLOBAL BUSINESS NAVIGATION (PART II)

CA. RAJASEKARAN K

Global Sanction Regimes

Globally there are 3 regimes of sanctions:

- **UN Sanctions (The Big Boss) -** These are sanctions implemented by the United Nations Security Council (UNSC) in events threatening the peace and security. These are binding on all member states of the UN.

- **US Sanctions (The Big Brother)**

  These are sanctions primarily by the Office of Foreign Assets Control (US-OFAC) and may have either unilateral or bilateral binding with US' allies. Typically OFAC Sanctions are extensive and can go to the extent of crippling the financial system of the non-aligning nation. OFAC Sanctions are classified into 3 types viz Comprehensive Sanctions, Targeted Sanctions, SDN Sanctions (Specifically Designated Nationals & Blocked persons Sanctions)

- **EU Sanctions (The Little Brother)**

  These are sanctions implemented by the European Union members, with their unanimous consent, on nations or territories that act against the EU interests or its allies' interest. (*'Of course, an obedient little brother would follow the footsteps of the big brother'* – pun intended)

Types of Economic Sanctions

The most commonly used (or can we say misused?) sanction type is economic sanction which may take the following forms:

- **Trade Sanctions** – Restrictions on Export Import of commodities
- **Financial Sanctions** – Restricting access to financial assets or financial markets
- **Investment Sanctions** – Restrictions on Foreign Direct Investment (FDI) on certain sectors
- **Sectoral Sanctions** – Restrictions on certain specific sectors of an economy such as defence sector.

'Why' Sanctions?

The 'Why' of sanctions is predominantly two-fold – economic reasons and geo-political reasons, with the latter taking precedence in the modern world.

- **Economic Reasons** – Prevent domestic industries, Counter dumping, Safeguard indigenous tech advancements and IPRs, Ensure fair trade practices and pressurize market access
- **Geo-political reasons** – Foreign policy, Combat Terrorism or Arms proliferation, Disapproval of a regime

Sanctions and internal controls

The following will help in handling trade sanctions especially when dealing with such nations and ensure the same are addressed appropriately with minimal loss of resources.

Sanction-proofing internal controls

- Maintaining sanctions database
- Due diligence of sanction risk
- Clear escalation and approval chains
- Periodic training
- Effective tech utilization
- Appropriate documentation procedures

Sanctions management policy

- Clarity in roles and responsibilities
- Risk assessment and Compliance protocols

- Alignment with business goals
- Periodic Review and update mechanisms
- Developing Reporting mechanisms

Emerging Challenges – Beyond Trade Sanctions

- **Sustainability & ESG** – EU's CBAM, BRSR in India, Forest Conservation laws,
- **Labour laws** - US' Forced labour prevention laws, EU's Circular economy action plan, India's Plastic waste management rules
- **Data privacy** – India's DPDP Act, 2023
- **Geo-politics** – BRICS and BRICS+ nations forming their own bloc, De-dollarization efforts, BRICS' Alternative Development Bank, BRICS Common Currency

Key Takeaways

- Sanctions can mean both approval and punishment, with trade sanctions typically referring to restrictions on international commerce.
- Major sanction regimes include UN (binding globally), US (extensive reach), and EU sanctions, each with varying impacts and scope.

- Economic sanctions are most common, encompassing trade, financial, investment, and sectoral restrictions.
- Implementing robust internal controls and compliance policies is crucial for navigating the complex sanctions landscape.
- Emerging challenges like ESG requirements, labor laws, and geopolitical shifts (e.g., BRICS initiatives) are shaping the future of global trade restrictions.

Conclusion

In the high-stakes world of global trade, understanding sanctions is no longer optional—it's essential. From UN mandates to US-led restrictions, these economic tools shape international business landscapes. For companies navigating this complex terrain, robust internal controls and up-to-date compliance strategies are crucial. As sanctions evolve alongside emerging challenges like ESG and geopolitical shifts, staying informed and adaptable is key to thriving in the global marketplace.

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APPLICATION OF INCOME

CA. R. RAMACHANDRAN

The series of amendments in the last few years beginning with taxation and other laws (Relaxation and Amendment of certain provisions) Act 2020 has added more complexity to the provisions of Income Tax relating to Trust/Institutions.

In this article, let us discuss the provisions relating to application of Income as provided U/S 10 (23C), U/S 11(1)(a), 11(1)(b)

Section 10(23C) 22nd Proviso: [w.e.f. 1st April 2023 vide Finance Act 2022] Computation of income in case of non-compliance

- Finance Act 2022 has provided with effect from 01.04.2023 (i.e. financial year 23-24 onwards) the computation of income of any fund/trust/institution as referred to in sub-clause (iv) or (v) or (vi) or (via) in case of non-compliance of:

- 10th proviso which deals with maintenance of books of account where the income exceeds the maximum

amount which is not chargeable to tax or

- 12th proviso which deals with application of income out of corpus donations or
- 18th proviso which deals with inclusion of income from any activity in the nature of trade, commerce or business as provided in the first proviso to section 2(15).
- In such circumstances, the income chargeable to tax shall be computed after deduction for the expenditure (other than capital expenditure) incurred in India, for the objects of the fund/trust/ institution subject to the fulfilment of the allowing following conditions:
- such expenditure is not from the corpus; or
- such expenditure is not from any loan or borrowing or
- claim of depreciation is not in respect of an asset that has been allowed as application earlier or
- such expenditure is not in the form of any contribution or donation to any person
- Further, for the purpose of computation;
- amounts inadmissible under sections 40(a)(ia), i.e. amount inadmissible due to non-

deduction of TDS and 40A(3)/(3A), i.e. cash expenditure in excess of Rs.10,000/- shall also be considered;

- no deduction in respect of any expenditure or allowance or set-off of any loss shall be allowed under any other provision of this Act;

- no set off or deduction or allowance of any excess application pertaining to any year preceding to the previous year;

- Expenditure paid during the year shall alone be considered for computation irrespective of the previous year in which the liability has been created;

- Any sum that has already been claimed as application shall not be allowed again as deduction.

Accumulated Funds when Taxable

- When the income so accumulated is applied for purposes other than for which accumulated within the said period.

- Ceases to remain invested as per section 11(5)

- Credited or paid to another trust or institution registered

under section 12AA/12AB/ 10(23C). Since 1"April 2003.

- Until 31 March 2022, the amount not applied for the purpose for which accumulated was taxed in the year immediately following the expiry of the period

- However, **from 1st April 2023 vide Finance Act 2022 was amended.** Since 1 April 2003, the amount not applied for which accumulated is taxed in the year in which period of accumulation expired.

Any University / other Educational institution or Hospital /medical institution falls under 10(23C)(iv)/(v)/ (vi)/ (via) applies to income or accumulates it for application wholly and exclusively to the objects for which established and in case where more than 15% of its income shall in no case exceed five years.

The provision was introduced/ vide Finance Act (No.2) of 1998 w.e.f., 1stApril 1999.

The Period of accumulation was brought in/ substituted from 1st April 2003 vide Finance Act 2002

The Threshold of 15% was substituted from 25% vide Finance Act 2002 w.e.f., 1st April 2003

Where eighty five percent of income earned/derived by any trust/institution is not applied or not deemed to have been applied to a Charitable/ Religious purposes during the previous year but accumulated or set apart for application shall not be included in the total income of the previous year in which income is received provided such person furnishes a statement in prescribed form (Form No.10) and manner to AO stating the purpose for which accumulated and the period for which accumulated shall in no case exceed five year.

85% was substituted for 75% vide Finance Act 2002, w.e.f., 1st April 2003.

Section 11(1)(a):

Income from property held for Charitable or Religious purposes. Subject to provision of section 60 to 63 the following income shall not be included in the total income of the previous year of the person in receipt of the income.

Income derived from property held under trust wholly for charitable or religious purposes, to the extent to which such income is applied to such purposes in India; and, where any such income is accumulated or set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not

in excess of [fifteen per cent] of the income from such property;

This clause was substituted by taxation laws (Amendment) Act 1975 w.e.f. 1/4/1976. Earlier Clauses (a) and (b) were amended by Finance Act 1970 w.e.f. 1/4/1971.

Section 11(1)(b):

Income derived from property held under trust in part[3] only for such purposes, the trust having been created before the commencement of this Act, to the extent to which such income[3] is applied to such purposes in India; and, where any such income is finally set apart for application to such purposes in India, to the extent to which the income so set apart is not in excess of [fifteen] per cent of the income from such property **[For the meaning of the terms/ expressions "accumulated or set apart", "in part" and "such income"] [Substituted for "twenty-five" by the Finance Act, 2002, w.e.f. 1-4-2003]**

Since, 1stApril 2003, 15% was substituted for 25% vide Finance Act 2002 w.e.f., 1st April 2003.

Payment out of accumulated Funds to another trust registered U/S 10(23c)/11/12 shall not be treated as application from 1/4/ 2003 vide Finance Act 2002

Finance Act 2021 brought in amendment to Provisions of section 11(1)(a)/11(1)(b).

Following clause (iii) shall be inserted after clause (ii) of Explanation 4 to sub-section (1) of section 2024: 11 by the Finance Act, 2023, w.e.f. 1.4.2024:

Any amount credited or paid, other than the amount referred to in Explanation 2, to any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of clause (23C) of section 10, as the case may be, or other trust or institution registered under section 12AB, as the case may be, shall be treated as application for charitable or religious purposes only to the extent of eighty-five per cent of such amount credited or paid.

If income applied falls short of 85% (Earlier it was 75% until 31st March 2003), then the trust/ institution has the option to carry forward to next year for application. Such option to be exercised before the expiry of the time allowed under section 139(1) for filing the return of income in such form & manner by filing **Form 9A- [See rule 17(1)]**

Application for exercise of option under clause (2) of the Explanation to sub- section (1) of section 11 of the Income - tax Act, 1961. **[inserted w.e.f. 1st April 2016 vide Finance Act 2015**

The amount so accumulated as per explanation 1 to clause 11(1), shall not be contributed to another trust with a specific direction that they Shall form part of the corpus **w.e.f., 1st April 2018 vide Finance Act 2017.**

For the purpose of determining the amount of application under clause (a) or clause (b), the provisions of subclause (ia) of clause (a) of section 40 and sub-sections (3) and (3A) of section 40A, shall, mutatis mutandis, apply as they apply in computing the income chargeable under the head "Profits and gains of business or profession"]. **Since 1st April 2019 vide Finance Act 2018**

CORPUS DONATION/FUND

Corpus donation do not require application - 2(24)(iia) until 31.03.2021

However, application out of Corpus has undergone changes vide Finance Act 2021.

(Finance Act 2021) brought in certain amendments towards application of Corpus donation.

- Any expenditure or application made out of the corpus fund **will not be allowed as application.**

- Such amount shall be allowed as application **in the year in which it is deposited back to corpus** to the extent of such deposit or investment.

Rationale behind not allowing set-off of deficit against current years income:

Application for charitable and religious purposes can be out of three sources:

- Current year's income
- Accumulated & Unconditional own funds (Corpus of the organisation)
- Borrowed funds

Finance Act 2021 brought in certain restriction/condition w.e.f. 1/4/22

Application for Charitable or religious purpose towards objects of the trust out of Corpus donations received 11(1)d) shall not be treated as application of income.

w.e.f., 01/04/2022 Vide Finance Act 2021, that corpus donation received with a specific direction has to be invested or deposited in any mode specified U/s11(5)

w.e.f., 01/04/2022 vide Finance Act 2021, the application for charitable purposes from corpus shall not be treated as

application. The amount so not treated as application is allowed as application in the year in which such amount is deposited back.

w.e.f., 1"April 2023, the period for replenishing the corpus fund is restricted to 5years. If replenished beyond 5 years, will not be allowed as application. This restriction regarding application out of corpus shall apply for corpus fund received after 1 April 2021 and any application made after 1 April 2021, out of corpus fund received prior to 1"April 2021.

This restriction/Condition will not apply for Corpus donation received prior to 31/3/2021 and Corpus Fund as on 31/3/2021.

Corpus donation paid to another trust was allowed as application until 31 March 2017.

w.e.f., 1 April 2018, vide Finance Act 2017, corpus donation paid by a trust to another trust shall not be treated as application.

Vide Finance Act 2022 the corpus donation received after 1" April 2021 continue to enjoy Exemption under section 11(1)(d) is subject to the condition that

- It is applied for the purpose for which received.
- Does not apply such corpus for making contribution or donation to other trusts.

- Maintains such corpus separately
- Invests the same as per mode specified under section 11(5).

Borrowed Funds:

W.e.f., 1st April 2022, vide Finance Act 2021, application out of borrowed fund will not be allowed as application. But the same will be allowed as application in the year in which loan/borrowing is repaid.

However, 1st April 2023, the repayment period is restricted to 5 years. If repayment is made beyond 5 years, then it will not be allowed as application.

CONCLUSION

Before 01.04.2021 – The Provision relating to Corpus/ Borrowed Fund

- In any year if there is a deficit i.e. excess of expenditure over income, it would imply that the organisation has over spent out of either borrowed funds or its corpus.
- Such deficit, earlier, was allowed to be set-off against future income, but the Finance Act 2021 provided that effective from 1st April, 2021 such deficit cannot be set-off against future income.

- However, an organisation will be permitted to replenish the source of such deficit against income of future years i.e. (i) to repay the funds borrowed for such expenditure which created deficit, (ii) to create investments under section 11(5) to the extent of the deficit.

Amendment

- It is proposed that any application made out of corpus can be offset against future years income for a period of five years from the end of the year in which such corpus was applied for charitable purposes. It is further provided that this provision shall apply to all the application made from corpus after 1st April 2021, to the extent eligible.

Impact

- An organization cannot carry forward the deficit (application made out of corpus indefinitely), it has to create investments against such deficit within a period of five years.

- After the end of five years the right to create deposits against income shall stand forfeited.

- Further, if any deficit was there as on 31st March 2021, then the organization will not be allowed to claim it against any future year income w.e.f 01.04.2023

- If an organization has been sustaining its activity out of corpus fund up to 31st March 2021 and was not able to replenish its corpus on or before 31st March 2022 then such organization will erode its corpus to that extent. In that sense it is a unfair and arbitrary disallowance.

- Further, the five-year limit for reclaiming the corpus may have very adverse impact on many institutions which have a long gestation period or are compelled to continue there activities from corpus for multiple years.

- This amendment defies the intent of the provision which is to help a charity to protect its corpus from erosion.

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