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TAXATION TIMES

December 2021

A low-angle, upward-looking photograph of several modern glass skyscrapers. The buildings are reflected in each other, creating a complex geometric pattern of lines and reflections. The sky is a pale, overcast blue.

Taxation Times is a monthly newsletter published by UJA specifically with an intent and object to simplify and provide clarity on certain provisions of the Income Tax Act, discuss the implications of various amendments and circulars notified time and again, understand the judicial precedents as decided by various courts and interpret these.

The Taxation Times is an initiative to keep you abreast with the latest development in the realm of the Direct Taxes in India.

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Introduction

As we roll out this edition of the Taxation Times, we would have already sailed into 2022. As we step into the new year with fresh resolutions & new goals – let's not forget the valuable lessons which the year gone by has taught us.

Almost 2 years into the pandemic, every organization has evolved in some way or another. Some organizations have resumed working from office while others have either shifted to a permanent work from home / hybrid model of working. The pace of digitization & automation has been accelerated and certain trends arising out of the pandemic are becoming the new normal. As we look forward to 2022, let's hope it begins with itself new opportunities for growth & well - being.

Coming back to December 2021's Taxation Time's here's what we have in store:

- > An article elaborating types of Permanent Establishment & it's implications;
- > Case laws from different Courts;
- > Tax News from around the world;
- > Tax Compliance Calendar for January 2022;
- > Notifications/Circulars from December 2021.

We hope that you find this edition of the Taxation Times useful. In case you have any feedback or need us to include any information to make this issue more informative, please feel free to write to us at info@uja.in

Happy Reading!

Best Regards,
UJA Tax Team



Neha Raheja
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Types of Permanent Establishment & its implication in India

The concept of a Permanent Establishment ('PE') was introduced in the Income Tax Act 1961 ('ITA') as a part of the statutory provisions of transfer pricing by Finance Act 2001. Thereafter, the Finance Act 2002 inserted the definition of PE under s. 92F(iia) to include a fixed place of business through which the business of the enterprise is wholly or partly carried on.

As per s. 90 of the ITA, the Central Government has the power to enter into an agreement with other country for avoidance of double taxation or for exchange of information or for the recovery of Income Tax under this Act. These agreements are generally called as Double Taxation Avoidance Agreements (DTAA) or tax treaties.

India has signed DTAA with majority countries. These treaties provide for income that would be taxable in either of the contracting states, depending upon the understanding of the nations, and conditions for taxing and exemption from tax.

As per s. 90(2) of the ITA, if the provisions of the DTAA are more beneficial to the taxpayer than the provisions of the ITA, then the provisions of the DTAA will prevail. Thus, the provisions of the DTAA will supersede the provisions of the ITA to the extent they are more beneficial to the taxpayer.

Article 5 of the DTAA elaborates provisions of PE:

For the purpose of a DTAA, the term "Permanent Establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried out. A PE includes:

- a. A place of management, a branch, an office, a factory, a workshop, a warehouse;
- b. A building site or construction, installation or assembly project in connection with sale of machinery;
- c. An agent (not being an independent agent) habitually concludes contracts on behalf of the foreign company, regularly delivers goods on behalf of the enterprise or habitually secures orders for & on behalf of the foreign company.

To simplify, a Permanent Establishment in India is as under:

1. Fixed Place PE
2. Service PE and
3. Construction PE/Installation PE
4. Dependent Agent PE

Fixed Place PE: Elements of a Fixed Place PE include –

- a. Existence of a fixed place of business of a foreign company which is at the disposal of the foreign company;
- b. The place of business is more or less for a fixed period and the said place in total or in part is at the disposal of the foreign company;
- c. Business of the foreign company is carried on wholly or partly through this fixed place.

Any space or premises which belongs to the Indian subsidiary of the foreign company & **the same is at the disposal of the foreign company, it can be established that the Indian subsidiary is a PE of the foreign company.**

The **Delhi High Court in Lucent Technologies International Inc. [2009] 28 SOT 98 (Del)** has held that a foreign company has a PE in India by virtue of employees of its sister concern being made available to the Indian subsidiary to carry out the project.

In **Rolls Royce Plc [2009] 122 TTJ 359 (Del)** The premises of a wholly owned subsidiary in India were available to all the employees of the UK company in respect of business operations in India & the UK Co. had a place of business at its disposal and a PE in India.

Service PE : Elements of a Service PE are as under :

In **Rolls Royce Plc [2009] 122 TTJ 359 (Del)** The premises of a wholly owned subsidiary in India were available to all the employees of the UK company in respect of business operations in India & the UK Co. had a place of business at its disposal and a PE in India.

- A service PE entails providing of services through technicians or personnel which do not constitute Fees for technical services.
- Such services exceed the specified period of time as mentioned in the tax treaties.
- Merely the presence of an employee in a third country does not simply constitute a PE if such employee renders services to the parent company and not to the third party.

In **Tekmark Global Solutions LLC [2010] 38 SOT 7 (Mum)**, it was held that *deputation of personnel by the US company to the Indian company, without providing any further service cannot create a PE in India.*

The Mumbai Tribunal in the case of **Morgan Stanley International** has stated that the deputed employees created a service PE in for the taxpayer in India, since they continued to be on the payroll of the taxpayer or continued to have lein on their jobs with the taxpayer and they rendered services on behalf of taxpayer in India.

Installation PE / Construction PE : Elements of a Construction PE are as under :

- As per the OECD Model Convention, an installation project constitutes a Construction PE if it lasts more than 12 months and under the UN Model Convention, if it exceeds 6 months.
- While constituting a construction PE, the following points are generally included :
 - a Includes period for any preparatory work;
 - b A site exists until the work is completely finished or the project is abandoned;
 - c Temporary interruptions such as bad weather or shortage of labour are not to be excluded;
 - d Even if there are several contracts, a building site should be considered as a single unit.

The Mumbai Tribunal in the case of **J. Ray McDermott Eastern Hemisphere Limited (2012) 54 SOT 363 (Mum)**, it was hereby held that *the duration in respect of each contract is less than 9 months, it will not constitute a service PE in terms of Article 5 of India – Mauritius tax treaty.*

In **Tion Woon Project & Contracting Pte [2011] 338 ITR 386 (AAR)**, it was held that *the time period of independent installation & assembly projects cannot be aggregated to determine a construction PE under India – Singapore tax treaty.*

Agency PE : Elements of an Agency PE are as under :

An agency PE is attracted if an agent appointed by a foreign enterprise in India is a dependent agent. A dependent agent shall be considered as a PE of a foreign enterprise if such an agent:

- a. Such an agent has the authority to conclude contracts on behalf of the foreign company & to decide the final terms.
- b. The agent is dependent on the foreign company.
- c. The agent is authorized to act on behalf of the foreign company.
- d. The agent habitually concludes contracts on behalf of the foreign company

However, an agent will constitute an agency PE if he is an agent of independent status i.e

- a. He acts in his ordinary course of business;
- b. His activities are not wholly or exclusively devoted to the foreign company on behalf of whom he is acting as an agent.

The **Hon'ble Mumbai ITAT** in the case of **Reuters Limited Construction House (2011)** has stated that *even though an agent acts independently in the course of his business, if his activities are devoted wholly & mostly to the foreign company, then such agents constitute a Dependent Agency in India.*

What happens when it is established that a foreign company has a PE in India?

1. The net income of the PE in India is taxable at 40% + surcharge.
2. The PE will have to obtain a PAN, TAN, GST Registration etc. in India.
3. The PE will be liable to file it's return in India, withholding tax provisions become applicable
4. FEMA provisions and Companies Act provisions to the extent become applicable.

Case Law

“The AO disallowed INR 23,00,000/- towards cost of improvement incurred by the taxpayer merely on the basis of enquires taken by the inspector from the neighbors of the taxpayer. The CIT(A) restricted the disallowance to INR 5,00,000/- stating that the inspector ought to have undertaken the enquiries from the builder who constructed the building as against the neighbors. The ITAT upheld the order of the CIT(A) restricting the disallowance to INR 5,00,000/- and deleting the disallowance of INR 18,00,000/-”

Facts

The taxpayer¹ had purchased an old flat and incurred a sum of INR 23,00,000/- towards renovating the house. The said amount incurred was claimed by the taxpayer under s. 54 of the Income Tax Act 1961 ('ITA'). The Ld. Assessing Officer ('AO') had asked the taxpayer for bills & vouchers in connection with the expenditure incurred by him. The taxpayer did not furnish any vouchers but submitted that the same must be allowed.

The Ld. Assessing Officer ('AO') deputed an Income Tax Inspector ('inspector') to make an enquiry to verify if any renovation had been undertaken by the taxpayer. The inspector visited the taxpayers house & made enquiries with the neighbors. The neighbours said that they were not aware of any improvements done by the taxpayer. On the basis of the reports submitted by the inspector, the Ld. AO came to the conclusion that the taxpayer has not undertaken any improvement at the house purchased & therefore, he disallowed the entire amount.

The Ld. CIT(A) sustained the addition to the extent of INR 5,00,000/- and deleted a disallowance of INR 18,00,000/-.

Aggrieved, the Revenue has preferred an appeal before the Hon'ble Income Tax Appellate Tribunal.

Issue

Is the taxpayer eligible to claim deduction under s. 54 of the ITA in respect of cost of improvement incurred?

Held

1. The taxpayer was residing at Mumbai & purchased a flat at Chennai & subsequently repairs were carried out at the house. The Counsel for the taxpayer submitted that the taxpayer had

undertaken repairs to the property almost 5 years ago & therefore, he is not able to produce evidence before the AO. It was further submitted that the entire works/ repairs were carried on by the taxpayers relatives & since he was residing in Mumbai, he was unable to collect the bills and vouchers.

2. The ITAT on perusal of the Assessment Order & the Inspectors report observed that the inspector has enquired with the neighbors & the neighbors stated that they were not aware of the improvements carried out by the taxpayer.
3. Merely, based on the enquiries made with the neighbors, the inspector concluded that the taxpayer has not carried out any improvement work and disallowed the entire expenditure claimed by the taxpayer. The Ld. CIT(A) stated that if the AO intended to know exactly about the improvement work carried out by the taxpayer, he should have enquired with the builder who constructed the building along with the neighbors. Also, considering all other factors & also taking into consideration that the taxpayer is not residing in Chennai and residing in Mumbai, he disallowed INR 5,00,000/- for lack of evidence & directed the AO to allow the benefit under s. 54 of the ITA to the extent of INR 18,00,000/-. The Ld. CIT(A) laid emphasis on the following decisions wherein it was upheld that strict proof is not necessary for reaching a decision in Income Tax matters – CIT V/s Smt. Vimlaben Bhagvandas Patel, Anraj Narain Dass v/s CIT, Laxmin Co V/s CIT, Devi Das Madhav Prasad V/s CIT²
4. The ITAT upheld the order of the CIT(A) to be fair & reasonable and to allow to the taxpayer the benefit of s. 54 to the extent of INR 18,00,000.

1 ACIT V/s Sambandam Dorairaj [2021] 133 taxmann.com 40 (Chennai Trib)

2 CIT V/s Smt. Vimlaben Bhagvandas Patel [1979] 118 ITR 134 (Guj), Anraj Narain Dass V/s CIT [1951] 20 ITR 562 (Punj.), Laxmin Co V/s [1959] 37 ITR 461 (All.), Devi Dass Madhav Prasad V/s CIT [1967] 63 ITR 356 (All)

“ Employee contribution to PF & ESI paid after the due date of the respective Acts but before the due date of filing the return of income is an allowable deduction & the same cannot be disallowed under s. 43B or s. 36(1)(va) of the ITA for AY 2019 – 2020. Explanation to s. 36(1)(va) introduced vide Finance Act 2001 is applicable w.e.f AY 2020 – 2021 and does not apply retrospectively.”

Facts

The taxpayer³ filed its return of income declaring a total income of INR 38,767,430/- which was processed under s. 143(1) of the Income Tax Act 1961 ('ITA'). The CPC issued intimation making a disallowance of INR 21,55,855/- towards employee contribution to ESI & PF. On an appeal, the Ld. CIT(A), NFAC confirmed the disallowance made under s. 143(1) on account of the taxpayers failure to pay employees contribution to PF/ESI within the prescribed due dates as per s. 36(1)(va) of the ITA. Against the order of the CIT(A), the taxpayer has preferred an appeal before the ITAT.

Held

1. Before the ITAT, the Ld. Authorized Representative ('AR') for the taxpayer submitted that the taxpayer had deposited the employees contribution of PF/ESI though with delay of few days from the due dates mentioned in the respective Acts, however the same was deposited well within the due date of filing the return of income. It was submitted that the fact is not under dispute & where such contribution has been deposited before the due date of filing the return of income, no disallowance under s. 36(1)(va) of the ITA can be made. Several case laws have been relied upon in support of the aforesaid view. Explanation added to s. 36(1)(va) of the Finance Act 2021 will take effect from 1st April 2021 & will apply from AY 2021 – 2022 & subsequent years. It was further submitted that the adjustment is beyond the scope of s. 143(1) of the ITA.
2. The Ld. Departmental Representative ('DR') submitted that as per the details furnished in the tax audit report, the payment of employees contribution to PF/ESI amounting to INR 21,15,855/- was not made as per the prescribed due dates under s. 36(1)(va) of the ITA and since these have not been disallowed in the return of income filed

by the taxpayer, the variance between the tax audit report & ITR has been duly flagged by the CPC in the computerized & disallowance under s. 143(1)(a)(iv) on the basis of the fact furnished by the taxpayer was made which clearly falls within the ambit of prima facie adjustment to be carried on under s. 143(1)(a)(iv) of the ITA. Further, attention was invited to the explanation to s. 36(1)(va) of the ITA introduced vide Finance Act 2021 wherein it was submitted that the law has always been very clear i.e employees contribution to specified fund will not be allowed as a deduction under s. 36(1)(va) if there is a delay in deposit even by a single day as per the due dates mentioned in the respective legislation. Also, the amendments are clarificatory in nature & therefore applicable with retrospective effect.

3. The Hon'ble Jaipur ITAT in the case of its own decision KP Airtech⁴ has held that where PF/ EPF/ CPF/ GPF etc. if paid after the due date under the respective Acts but before the filing of the return of income under s. 139(1), cannot be disallowed under s. 43B or under s. 36(1)(va) of the ITA. The said decision has subsequently been followed in CIT V/s Jaipur Vidyut Vitran Nigam Ltd,⁵ CIT V/s Udaipur Dugdh Utpadak Sahakari Sangh Ltd,⁶ CIT V/s Rajasthan Renewable Energy Corporation Ltd⁷ and these decisions clearly and consistently have held that where PF & ESI has been paid after the respective due dates under the Acts but before filing of return of income under s. 139(1), the same cannot be disallowed under s. 43B r.w.s 36(1)(va) of the ITA.

3 Dhabriya Polywood Ltd V/s ADIT, CPC, Bangalore (2021) 133 taxmann.com 135 (Jaipur – Trib)

4 K.P. Airtech V/s Dy CIT [IT Appeal No. 41 and 42/JP/2021, dtd. 16.08.2021]

5 CIT V/s Jaipur Vidyut Vitran Nigam Ltd 363 ITR 307

6 Pr. CIT V/s Rajasthan State Beverages Corporation Limited (2017) 84 taxmann.com

7 PCIT V/s Rajasthan Renewable Energy Corporation Ltd.

4. In the instant case, employees contribution to ESI & PF collected by the taxpayer from its employees has been deposited well before the due date of filing of return of income under s. 139(1) of the ITA. Further, it is noted that the Ld. CIT(A) has referred to the explanation to s. 36(1)(va) & s. 43B introduced by the Finance Act 2021 and has also referred to the rationale of the amendment as explained in Memorandum to Finance Bill 2021, however, he has simply failed to consider the express wordings in the said Memorandum which says “these amendments will take effect from 1st April 2021 and will accordingly apply to AY 2021 – 2022 and subsequent assessment years.” In the instant case, the impugned assessment year is AY 2019 – 20 and therefore, the said amendment cannot be applied to the instant case. Therefore, in light of the aforesaid discussion, the deposit of employees contribution to PF & ESI before the due date of filing return of income but after deposit in respective due dates ought to be deleted.

Tax in the News

Cyprus to proceed with tax reform in 2022

<https://knews.kathimerini.com.cy/en/news/cyprus-to-proceed-with-a-tax-reform-in-2022>

Panama adapts laws on exchange of information for tax purposes to international standards.

<https://mnetax.com/panama-adapts-laws-on-exchange-of-information-for-tax-purposes-to-international-standards-46431>

Elon Musk to pay over \$11 billion in taxes this year; continues to sell Tesla stock to gather money.

<https://www.financialexpress.com/market/elon-musk-to-pay-over-11-billion-in-taxes-this-year-continues-to-sell-tesla-stock-to-gather-money/2386818/>

Belgium and France sign new tax treaty

<https://mnetax.com/belgium-and-france-sign-new-tax-treaty-46420>

The OECD has released the Model Rules paving the way for roll out of the new global tax regimes that will subject multinational corporations to a minimum tax of 15% from 2023. The rules set out the mechanism for implementation of the regime adopted by 136 countries.

<https://economictimes.indiatimes.com/news/economy/policy/oecd-paves-way-for-new-global-tax-regime-roll-out/articleshow/88398752.cms>

Corporate Tax Rates around the World, 2021

<https://taxfoundation.org/corporate-tax-rates-by-country-2021/>

The newly agreed global minimum corporate tax to prevent multinational firms from avoiding the legal cess regime is riddled with clauses to ensure that profits stay with rich nations.

<https://www.downtoearth.org.in/news/economy/global-corporate-taxation-the-new-bare-minimum-80383>

OECD countries tax revenues fell in 2020, but less than their GDPs

<https://mnetax.com/oecd-countries-tax-revenues-fell-in-2020-but-less-than-their-gdps-46360>

Circulars, Notifications & Press Release

Circulars

CBDT notifies one-time relation for verification of all income tax return e-filed for AY 2020-21 which are pending for verification and processing may be completed by 28th February, 2022.

<https://www.incometaxindia.gov.in/communications/circular/circular-no21-2021.pdf>

The Central Government makes 'the e-Verification Scheme, 2021' and will come into force on the date of publication in the Official Gazette.

<https://www.incometaxindia.gov.in/communications/notification/notification-137-2021.pdf>

CBDT notifies the time limit of issuance of intimation u/s 143(1) for AY 2020-21 to 30th June, 2022.

<https://www.incometaxindia.gov.in/communications/circular/circular-no21-2021.pdf>

The CBDT inserts Rule 2DD of Income-tax Rules, 1961 called as the Income Tax Amendment (34th Amendment) Rules, 2021 Computation of exempt income of specified fund for the purposes of clause (23FF) of section 10 of Income Tax Act, 1961.

<https://www.incometaxindia.gov.in/communications/notification/notification-138-2021.pdf>

Notifications

Central Government hereby notifies provisions of amendments in agreements between the Government of the Republic of India and the Government of the Kyrgyz Republic for the avoidance of double taxation, shall have effect in the Union of India

<https://www.incometaxindia.gov.in/communications/notification/notification-135-2021.pdf>

The Central Government makes 'd the Faceless Appeal Scheme, 2021' and will come into force on the date of publication in the Official Gazette.

https://www.incometaxindia.gov.in/communications/notification/notification_no_139_2021.pdf

The CBDT inserts Rule 21AK of Income-tax Rules, 1961 called as the Income Tax Amendment (33rd Amendment) Rules, 2021 in respect to conditions for purpose of clause (4E) of section 10 of Income Tax Act, 1961.

<https://www.incometaxindia.gov.in/communications/notification/notification-136-2021.pdf>

Upcoming Compliances for November 2021

7 January 2022

Due date for deposit of Tax deducted/collected for the month of December, 2021.

Due date for deposit of TDS for the period October 2021 to December 2021 when Assessing Officer has permitted quarterly deposit of TDS under section 192, section 194A, section 194D or section 194H

30 January 2022

Quarterly TCS certificate in respect of quarter ending December 31, 2021

Due date for furnishing of challan-cum-statement in respect of tax deducted under section 194-IA, 194-IB & 194M in the month of December, 2021

14 January 2022

Due date for issue of TDS Certificate for tax deducted under section 194-IA, 194-IB 194M in the month of November, 2021

31 January 2021

Quarterly statement of TDS for the quarter ending December 31, 2021

Audit report under section 44AB for the assessment year 2021-22 in the case of an assessee who is also required to submit a report pertaining to international or specified domestic transactions under section 92E

The due date for filing of audit report for Assessment Year 2021-22 has been extended vide Circular no. 17/2021, dated 09-09-2021

15 January 2022

Due date for filing of audit report under section 44AB for the assessment year 2021-22 in the case of a corporate-assessee or non-corporate assessee (who was required to submit his/its return of income on October 31, 2021)

The due date for filing of audit report for Assessment Year 2021-22 has been extended vide Circular no. 17/2021, dated 09-09-2021

Quarterly statement of TCS for the quarter ending December 31, 2021

Due date for furnishing of Form 15G/15H declarations received during the quarter ending December, 2022

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