

LUTHRA & LUTHRA LLP

CHARTERED ACCOUNTANTS



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Highlights



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- CBDT clarified on disclosure of 'persons making substantial contribution' in Forms 10B & 10BB
- CBDT condoned Form 10-IC delay for AY 2021-22.
- CBDT notified Form 10-IFA for Sec.115BAE concessional tax-rate, applicable to new co-operative societies
- Philippines joins OECD / G20 BEPS Inclusive Framework, commits participation in Two-Pillar Solution
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News Highlights



CBDT notified Form 56F as CA's report for Sec.10AA deduction

CBDT, vide Notification No. 91/2023, notified Rule 16D with respect to Section 10AA deduction; As per the Rule, the report of a Chartered Accountant which is required to be furnished by the Assessee under Section 10AA(8) read with Section 10A(5) shall be made in Form No. 56F. The Rule is considered to have been enacted as of July 29, 2021 and onwards.

CBDT clarified on disclosure of 'persons making substantial contribution' in Forms 10B & 10BB

CBDT, vide Circular No. 17/2023, clarified on disclosure of person making substantial contribution to the trust or institution as per Section 13(3)(b). CBDT stated that for the purposes of Form 10B and Form 10BB, the details of the persons making substantial contribution 'may be given' with respect to those persons whose total contribution during the previous year exceeds

Rs. 50,000 and details of relatives of such persons 'may be provided, if available.

CBDT condoned Form 10-IC delay for AY 2021-22.

CBDT, vide Circular No.19/2023, condoned delay in filing Form 10-IC to avoid genuine hardship caused to Assessee seeking Section 115BAA concession. This condonation is applicable for the Assessment Year 2021-22, subject to the fulfilment of the following conditions:

(i) the Income Tax Return (ITR) is filed on or before the due date under Section 139(1)



(ii) Assessee have opted for item (e) in 'Filing Status' under 'Part A - Gen' of ITR-6,

(iii) Form 10-IC is electronically filed on or before January 31, 2024.

CBDT notified Form 10-IFA for Sec.115BAE concessional tax-rate, applicable to new co-operative societies

CBDT vide Notification No 83/2023, introduced Rule 21AHA and Form 10-IFA for newly established manufacturing co-operative societies seeking to avail concessional tax rate of 15% under Section 115BAE. The rule

specifies that the option in Form 10-IFA must be electronically furnished, either through a digital signature or an electronic verification code. Additionally, the notification empowers PDGIT (Systems) or DGIT (Systems) to outline the procedure for filing Form 10-IFA, and specify the data structure, standards, and manner for generating the electronic verification code to validate the form, also devise and implement appropriate security, archival, and retrieval policies concerning the furnished Form. It shall be applicable from the AY-2024-25 onwards.



Indian/Global Updates

Philippines joins OECD / G20 BEPS Inclusive Framework, commits participation in Two-Pillar Solution

The Philippines has officially become a member of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), aligning itself with global endeavors to combat tax avoidance. As a participant in the Inclusive Framework, the Philippines is committed to addressing tax challenges stemming from the digitalization of the economy. This commitment involves active engagement in the Two-Pillar Solution, a comprehensive initiative aimed at reforming international taxation rules to ensure that multinational enterprises contribute their fair share of taxes in all the jurisdictions where they operate. Additionally, the Philippines is actively involved in the implementation of the BEPS package, consisting of 15 measures designed to counteract tax avoidance, enhance the consistency of international tax regulations.

OECD / G20 BEPS IF releases Multilateral Convention for Amount A, Pillar One

The OECD/G20 BEPS Inclusive Framework has revealed the Multilateral Convention (MLC) text for Amount A of Pillar One, marking a consensus among members. Pillar One aims to reallocate taxing rights on a portion of profits from major multinational enterprises operating in market jurisdictions, irrespective of physical presence. This seeks to prevent digital services taxes, double taxation, and enhance international tax system stability. Anticipating an annual reallocation of about USD 200 billion in profits, Pillar One is projected to yield global tax revenue gains of USD 17 to 32 billion annually. A Minimum Tax Implementation Handbook for Pillar Two has also been released, aiding governments in adopting the global minimum tax. OECD Secretary-General Mathias Cormann highlights the progress toward implementing a fairer international tax system in the digitalized world.



Transfer Pricing / B E P S



OECD releases 2022 MAP Statistics, Awards and 2023 Consolidated Information on MAP

The OECD announced the release of the 2022 MAP Statistics, 2022 MAP Awards, and the 2023 Consolidated Information on MAP during the fifth OECD Tax Certainty Day. The MAP statistics cover a record 133 jurisdictions and nearly all MAP cases globally, aligning with the BEPS Action 14 Minimum Standard and the broader G20/OECD tax certainty agenda. Recognitions were given to the Netherlands and New Zealand for swift closure of TP and other cases, Canada for the smallest proportion of pre-2016 cases, and Luxembourg and Norway for effective caseload management. Awards were also presented to Denmark-Ireland for TP cases and Germany-Ireland for other cases, highlighting effective collaboration on joint caseloads. The Netherlands received the "most

improved jurisdiction" award, closing an additional 102 cases with positive outcomes compared to 2021. Additionally, the OECD introduced the first-ever edition of 'Making Dispute Resolution Mechanisms More Effective – Consolidated Information on Mutual Agreement Procedures 2023,' offering stakeholders a clear overview of published MAP information in each member jurisdiction of the OECD/G20 Inclusive Framework on BEPS.



Issue of the month



Foreign Tested Party

One of the initial step under transfer pricing analysis is identification of the 'tested party'. A tested party is an entity whose profit margins from the international transaction are tested for meeting the arm's length criteria. In any international transaction, there are a minimum of two enterprises, i.e. the Indian taxpayer and the foreign associate enterprise.

While determining the arm's length price using the Cost Plus Method, Resale Price Method, or Transactional Net Margin Method, it is necessary to choose one of the parties of the international transaction as a tested party whose profitability needs to be tested (i.e. mark up on costs, gross margin, or net profit margins) and compare the profitability of the tested party with the uncontrolled comparables. So, a question arises as to which of the two i.e., the Indian taxpayer or the foreign associate enterprise should be taken as the tested party for the comparison of profit level indicators with appropriate comparables.

The Income Tax Act 1961 ('the Act') does not define the term 'tested party' or lay down rules or guidelines on which of the two parties i.e. Indian taxpayer or the foreign AE is to be selected as the tested party.

So, various Hon'ble High Court and ITATs have placed reliance on the guidelines provided by the OECD, the UN Transfer Pricing Manual, and The Institute of Chartered Accountants of India ('ICAI')

Guidelines for Selection of Foreign Tested Parties

As per the OECD guideline, tested party is the one to which a transfer pricing method can be applied in the most reliable manner and for which the most reliable comparables can be found, i.e. it will most often be the one with the less complex functional analysis. In a similar manner UN manual clarifies tested party can be a local or foreign entity. A foreign entity should have the following attributes i.e.

- i. whose functions are less complex in nature
- ii. Data available can be used with minimal adjustment
- iii. Relevant and sufficient data on comparable is furnished



ICAI in its guidance note has provided that foreign entity can also be selected as the tested party.

As per the guidelines of the OECD, UN Manual, and ICAI, the foreign associate enterprise can be selected as a tested party if it has the least complex functions, for which profitability can be ascertained most reliably and whose functional profile and risk assumed can be easily documented and the reliable data on the comparable can be found in the public domain.

Case law relating to the Selection of Foreign Tested Party

PCIT vs Almatris Alumina (P.) Ltd (2022)

Hon'ble High Court of Calcutta observed that the tested party normally should be the least complex party to the controlled transaction and there is no bar for the selection of the tested party either local or foreign party. Neither the Act nor the guideline on transfer pricing provides so and the selection of the tested party is to further the object of the comparability analysis by making it less complex and requiring fewer adjustments.

Virtusa Consulting Services (P.) Ltd vs. DCIT, Company Circle 5(2)

Hon'ble High Court of Madras observed that there is no bar in the Act or in the transfer pricing guideline for the selection of tested party.

Ranbaxy Laboratories Limited vs ACIT

Hon'ble Delhi ITAT held that the tested party should be the party in respect of which reliable data for comparison is easily and readily available and fewest

adjustments in computations are needed. The object of the transfer pricing exercise is to gather reliable data, which can be considered without difficulty by both the parties, i.e., taxpayer and the revenue. It is also true that generally least of the complex controlled taxpayers should be taken as a tested party. But where comparable or almost comparable, controlled and uncontrolled transactions or entities are available, it may not be right to eliminate them from consideration because they look to be complex. If the taxpayer wishes to take foreign entity as a tested party, then it must ensure that it is such an entity for which the relevant data for comparison is available in the public domain or is furnished to the tax administration. The taxpayer is not then entitled to take a stand that such data cannot be called for or insisted upon from the taxpayer.

However, certain ITATs have taken a different point of view regarding selection of foreign tested party.

Aurionpro Solution Ltd. vs ACIT, Range -4(3), Mumbai,

Hon'ble ITAT held that the tested party is always the taxpayer and not the foreign entity as the effect of transaction on the income of the assessee is to be considered and not effect on the foreign entity. Hon'ble ITAT highlighted that the Transfer Pricing Regulations require an international transaction to be tested on the basis of income of the assessee, had a similar transaction been undertaken with a third party.

IZMO Ltd. vs DCIT circle 3(1)(1), Bangalore

Hon'ble tribunal rejected foreign entity as tested party because the geographical and other economic circumstances of the comparable companies outside India would be different, therefore cannot reflect the correct arm length price.

Comments

The concept of a tested party is the core of transfer pricing. However, due to a lack of guidance in Indian laws regarding the selection of foreign tested parties,

reliance has to be placed on OECD, UN transfer pricing manual. Selection of the tested party depends on the fact of the transaction and comparability analysis which differs according to the transaction, so the burden falls on the taxpayer to document the transaction fully, so as to justify the arm's length analysis.



Legal Corner



In the Supreme Court of India

Assessing Officer Circle Vs. M/S Nestle SA

Introduction and Brief Facts

India entered into a Double Tax Avoidance Agreement (“DTAA”) with various member countries of Organisation for Economic Cooperation & Development (“OECD”), i.e. France, Netherlands, and Switzerland, to provide for the rate and scope of taxability of income.

Subsequently, India entered into respective DTAA with Slovenia, Lithuania and Colombia as on 13th January 2003, 26th July 2011 and 13th May 2011, to provide for lower rate of taxation on dividend income at the rate of 5%. At the time of providing such favourable rate of taxation, these countries were not members of the OECD but became OECD members as on 21st July 2010, 5th July 2018 and 28th April 2020 respectively.

During the year under consideration, M/s Nestle SA (“the Assessee”) incorporated in Switzerland applied to the concerned tax officer for issuance of a lower withholding certificate for dividend income at a reduced rate of 5% instead of 10% as to invoke the Most Favoured Nation (“MFN”) clause in their tax treaties.

However, the concerned tax officer issued certificate showing a 10% withholding tax rate. Later, the decision was challenged before the Honourable High Court of Delhi (“Hon’ble HC”), wherein, the Hon’ble HC ruled in the favor of the Assessee stating that there is no need to issue any notification under section 90 of the Income Tax Act (“the Act”) for changing the terms or to alter the existing provision of the DTAA. Further, the MFN clause as mentioned in the India-Switzerland DTAA will be applicable from the date of membership of OECD of the third state (i.e. Slovenia, Lithuania and Colombia).

A batch of appeals was filed before the Honourable Supreme Court (“Hon’ble SC”), against the decisions of the Hon’ble HC regarding the interpretation of the MFN clause.



The questions of law that arose in the case was whether there is any right to invoke the MFN clause when the third country with which India has entered into a Double Tax Avoidance Agreement (“DTAA”) was not an OECD member yet (at the time of entering into such DTAA) and whether the MFN clause is to be given effect automatically or if it is to come into effect only after a notification is issued under section 90 of the Act.

Arguments of Revenue

The Ld. counsel argued that according to Article 253 of the Constitution of India, the Parliament has exclusive power to make legislation in respect of any DTAA or convention, entered into by India, with any other nation and without Parliamentary legislation, such treaties are unenforceable.

It was also argued that in the absence of any law, mere entering into a DTAA or convention or protocol cannot give rise to any right under the taxation laws having regard to the structure of section 90 of the Act (allowing the benefit of avoidance of double taxation where an Assessee earns income in more than one nation).

Further, the Ld. counsel pointed out that the mere entering of the countries into membership of OECD does not automatically grants the benefits under section 90 of the Act, to a country which had entered into DTAA with India. However, it would require a notification to be issued to give effect to such consequence.

Further, the Assessee placed reliance on use of the word “is” in Article 10(1) of the India-Netherlands DTAA. Article 10(1) states *“Dividend paid by a company which is a resident of one of the States to a resident of the other State may be taxed in that other State”*. The Assessee contended that ‘is’ signifies the time when the provisions of treaty are to be applied. However, responding to this contention the the Ld. Revenue Counsel argued that the word ‘is’ can have present, past or future meaning depending on the context in which it is used. The MFN clause clearly demonstrates that the other country is required to be an OECD member as on the date of the signing of the DTAA and not on any future date. Hence, the countries of Netherlands, France, and Switzerland can’t claim the benefit of MFN clause.

Arguments of Assessee

The Assessee argued that when the DTAA and the protocols including the MFN clause were already notified under section 90(1) and the same had come into force, there was no such legal requirement to notify any subsequent amendment to the DTAA which becomes operative automatically as a consequence of the trigger of the MFN clause to the DTAA.

Further, the Assessee urged that the MFN clauses in the DTAA’s and their protocols clearly oblige Indian revenue officers to grant the benefit that is given to countries which subsequently entered into DTAA’s with India, and were given favourable benefits, upon their entry into OECD.

Lastly, the word 'is' when it appears in the MFN clause can only mean that the third country need to be OECD member only when the benefit of the MFN clause is invoked.

Hon'ble Supreme Court Order

The Hon'ble SC held that a notification under Section 90(1) is a mandatory condition for a court, authority, or tribunal to give effect to a DTAA, or any protocol changing the terms or conditions of the said DTAA.

Further, when the signatory to an existing DTAA, points to the event of a third state entering into OECD membership, to claim the beneficial effect given to the third party state, does not automatically leads to integration of such term extending the same benefit and requires the terms of the existing DTAA to be amended through a separate notification under section 90 of the Act.

Lastly, the Hon'ble SC stated that the interpretation of the expression 'is' has present signification. Therefore, for a party to claim benefit of 'same treatment' clause, based on a tax DTAA between India and another state which is member of OECD, the relevant date to be considered is when the nation entered into a DTAA with India, and not a later date i.e. when such country becomes an OECD member.

Comments

The judgment lays down certain important principles, some contrary to popular opinion. In order to avail the benefit of MFN clause, it is mandatory for the countries to amend their existing DTAA by issuing a notification under section 90 of the Act by the concerned authority. Further, the benefit of the MFN clause with a state, will only be available to residents of other state if conditions prescribed in the DTAA with first state are met on the date of entering into DTAA with other state.



Glossary



Act	Income Tax Act, 1961
A.Y.	Assessment Year
AE	Associated Enterprises
ALP	Arm's Length Price
AO	Assessing Officer
BEPS	Base Erosion and Profit Shifting
CBDT	Central Board of Direct Taxes
TDS	Tax Deducted at Source
IFSC	International Financial Services Centres
ITO	Income Tax Office
TP	Transfer Pricing
PDGIT	Principal Director General of Income-tax
DGIT	Director General of Income-tax
NR	Non Resident
CIT	Commissioner of Income Tax
SC	Supreme Court
HC	High Court
DTAA	Double Taxation Avoidance Agreement
GIA	Gemological Institute of America
TRC	Tax Residency Certificate
MAP	Mutual Agreement Procedure

GET IN TOUCH

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