FOCAL POINT

Newsletter from Raju and Prasad Chartered Accountants

January 2019 Volume 5, Issue 11

Dear Reader,

The Policy updates and Verdicts of Supreme Court and various High Courts are enclosed in this newsletter.

Attention of readers is invited to Article on Capital Expenditure vs. Revenue Expenditure by CA Ketan K Waghela, Recommendations made during the 31st GST Council Meeting, Acceptance of Probate of will or will for transmission of securities in demat mode by SEBI and the Decision of Honorable Supreme Court in Multi Commodity Exchange of India Ltd. v Deputy Commissioner of Income-tax.

Regards
For Raju and Prasad
Chartered Accountants
Your Knowledge Partners

M Siva Ram Prasad

Contact us:
Email : hyderabad@rajuandprasad.com
Website: www.rajuandprasad.com

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CAPITAL EXPENDITURE vs REVENUE EXPENDITURE

-Ketan K Waghela, ACA(Mumbai Branch)

The line of demarcation between capital and revenue expenditure is very thin and the ultimate conclusion on the nature of the expenditure is always a question of law and fact. There are numerous case laws widening line between these expenses. As the Act does not define the terms, one has to depend on their natural meaning on case to case basis.

Recently, the case law of Flipkart has created strife in the e-commerce industry and investors. However, on appeal, it was decided in favour of Flipkart by Income Tax Appellate Tribunal(ITAT). Summary of the case is as follows:

Contention of the Department:

Flipkart reported sales as net of trade discounts which are offered to the customers. The purchase and sales figures were for FY 2014-15 as follows:

Particulars	Amount
Purchases	Rs. 10335,73,05,882
Less: Stock Unsold	Rs. 741,83,06,836
	Rs. 9593,89,99,046
Less: Sale value	Rs. 9351,75,05,319
Gross Loss	Rs. 242,14,93,727

Flipkart India, despite being a wholesaler selling popular goods, reported losses at the gross-profit level. The company's motive was to capture market by creating marketing intangibles in terms of customer base, brands and trademarks, which, in turn, resulted in high valuation of business. During the assessment, department had taken a view that Flipkart

received an enduring benefit in the form of edge over competitors and brand building because of aggressive discounts (cash discounts to the extent of 3% of the turnover) or "predatory pricing".

Therefore, it embarked upon valuation of intangibles. It took the database for wholesalers dealing in consumer and electronic goods and arrived at the following conclusion –

"The market average of gross profit margin for wholesalers is 16.95%. Had the assessee not followed predatory pricing policy, its average sale price would have been Rs. 9593,89,99,046+ (16.95% of Rs. 9593,89,99,046) i.e. Rs. 11220,06,59,384. Assessee's real sales is Rs. 9351,75,05,319. The reduction in sales due to following assessee's strategy of selling at a price lower than Cost, the difference of Rs. 1868,31,54,065 between the price at which the assessee is selling and the price the normal wholesaler would have sold is the value of expenses incurred by assessee towards cost of marketing intangibles in the year. Therefore, the amount of Rs. 1868,31,54,065 has to be capitalized and depreciated at the rate of 25%."

Contention of Flipkart:

Flipkart contended that discounts are the expenses which the company incurs year on year basis to sell its products and retain its market share. Thus, entire amount of such expenses was claimed as revenue expenditure. Nothing in the Income Tax Act mandates that a product has to be sold at a particular price, and revenue not earned (by virtue of giving discounts) cannot be treated as capital expenditure i.e. tax cannot be charged on fictional / notional income.

Issue under consideration:

Flipkart has never shown profit in past several years but as we can see that the valuation of the Company is increasing. Contention of the

department was to tax Flipkart as it is creating its brand by retaining market share.

Department is trying to tax on notional income which here is increase in valuation. It views Flipkart as an anomaly since the company has been making losses while its valuation has been on the rise.

If the seller sells a product worth Rs.2000 and earns a profit of Rs.20 on it, Flipkart spends Rs.40-50 to advertise the product and build the brand.

Currently, companies report sales figures as net of trade discounts. Plant and Machinery, server cost, patent and other such expenses are capitalised in the books. If valuation methods as explained above are adopted by the department and value of marketing intangibles are capitalised, e-commerce companies like Flipkart, Amazon which generally reports losses will turn profitable. Thus, would be liable to pay taxes.

Industry experts say a verdict against Flipkart by higher appellate authorities could fundamentally change how E-Commerce Industry in India is taxed.

Treating discounts given by e-commerce companies as capital expenditure because it helps in building the brand, will affect anyone who offers discounts, even infrequently, including offline players. In fact, this can mean that any expense towards brand-building will be capital expenditure.

Note: This article is for educational purpose only.

Policy Watch

Indirect Taxes

Waiver of late fee payable for delayed filing of FORM GSTR-3B and GSTR 1 for the period July, 2017 to September, 2018 in specified cases

The Central Board of Indirect Taxes and Customs Vide Notification No 75/2018 and 76/2018 – Central Tax dated 31st December 2018 has waived the late fees payable for delay in filing GSTR 1 and GSTR 3B for the periods July 2017 to September 2018 if the above stated returns are filed after 22nd December 2018 and before 31st March 2019.

- http://cbic.gov.in/resources//htdocs-cbec/gst/notfctn-75-central-tax-english-2018.pdf;jsessionid=E269D84579FCDB6E5872AB4721EDDECF
- http://cbic.gov.in/resources//htdocs-cbec/gst/notfctn-76-central-tax-english-2018.pdf;jsessionid=0B5FA3B23134AC76B251E0E4E33854B1

Recommendations made during 31st GST Council Meeting

31st GST Council Meeting was held on 22nd December 2018. Major recommendations made were as follows:

1. The new return filing system to be introduced on a trial basis from 01.04.2019 and on mandatory basis from 01.07.2019.
2. The due date for furnishing the annual returns in FORM GSTR-9, FORM GSTR-9A and reconciliation statement in FORM GSTR-9C for the Financial Year 2017 – 2018 to be further extended till 30.06.2019.
3. The due date for furnishing FORM GSTR-8 by e-commerce operators for the months of October, November and December, 2018 to be extended till 31.01.2019.

4. ITC in relation to invoices issued by the supplier during FY 2017-18 may be availed by the recipient till the due date for furnishing of FORM GSTR-3B for the month of March, 2019.
5. Taxpayers who have not filed the returns for two consecutive tax periods shall be restricted from generating e-way bills.
6. Taxation of residential property in real estate sector has been referred to the Law Committee and Fitment Committee.

- http://cbic.gov.in/resources//htdocs-cbec/press-release/PressRelease_Goods-rates_%2031-GST-Meeting-22122018.pdf;jsessionid=6569BE3495D0811E6C49ED741A00B2D0
- http://cbic.gov.in/resources//htdocs-cbec/press-release/22181222_Press%20Release_31st%20GST%20Council%20Policy.pdf;jsessionid=2988F02337060E88934E0C84FCA722C7
- http://cbic.gov.in/resources/htdocs-cbec/press-release/Press%20Release_Goods%20and%20Services%20rates_%2031st%20GST%20Meeting%20combined.pdf;jsessionid=74FFAFFD9F52B3CB70C48F6E03EDC8A0

Extension of due date for furnishing ITC 04 till 31st March, 2019

ITC 04 is required to be filed by a tax payer by giving the details of goods dispatched to or received from job workers. Due date for filing the same is 25th of the month succeeding the quarter. The Central Board Of Indirect Taxes and Customs vide Notification No. 78/2018 – CT dated 31st December 2018 has extended the due date for furninshing ITC – 04 for the periods July 2017 to December 2018 till 31st March 2019.

http://cbic.gov.in/resources//htdocs-cbec/gst/notfctn-78-central-tax-english-2018.pdf

SEBI

Acceptance of Probate of Will or Will for Transmission of Securities held in dematerialized mode

In terms of SEBI (Listing Obligations and Disclosure Requirements) 2018, probate of will or will has been prescribed as documentary requirement for transmission of securities held in physical mode. With

regard to transmission of securities held in dematerialized mode, the same is dealt in terms of bye laws of the Depositories. In order to harmonize the procedures for transmission of securities in dematerialized mode with that of transmission of securities in physical mode, SEBI vide its Circular No.SEBI/HO/MIRSD/DOP/CIR/P/2019/05 dated 04-01-2019 has decided that for the purpose of transmission of securities held in dematerialized mode, will or probate of will would be accepted.

https://www.sebi.gov.in/legal/circulars/jan-2019/acceptance-of-probate-of-will-or-will-for-transmission-of-securities-held-in-dematerialized-mode_41548.html

Direct Tax

Procedure, format and standards for filing an application for grant of certificate for deduction of Income-tax at any lower rate or no deduction of Income-tax under section 197(1)/collection of the tax at any lower rate under 206C(9) TRACES portal

Earlier, Vide Notification No. 74/2018 dated 25-10-2018, Rule 28/37G of the Income-tax Rules, 1962 has been amended to provide for filing an application electronically for grant of certificate for deduction of Income-tax at any lower rate or no deduction of Income-tax. On 31-12-2018, The Central Board Of Direct Taxes vide Notification No. 8/2018 has laid down the procedures, formats and standards for grant of such certificate.

https://www.incometaxindia.gov.in/communications/notification/notification_8_2018_tds.pdf

RBI Updates

Micro, Small and Medium Enterprises (MSME) sector – Restructuring of Advances

With a view to facilitate meaningful restructuring of MSME accounts that have become stressed, Reserve Bank OfIndid vide its Circular No. RBI/2018-19/100 dated 01-01-2019 hasdecided to permit a one-time restructuring of existing loans to MSMEs classified as 'standard' without a downgrade in

the asset classification, subject to the following conditions:

1. The aggregate exposure, including non-fund based facilities, of banks and NBFCs to the borrower does not exceed Rs. 250 million as on January 1, 2019.
2. The borrower's account is in default but is a 'standard asset' as on January 1, 2019 and continues to be classified as a 'standard asset' till the date of implementation of the restructuring.
3. The borrowing entity is registered under GST Act on the date of implementation of the restructuring. However, this condition will not apply to MSMEs that are exempt from GST-registration.
4. The restructuring of the borrower account is implemented on or before March 31, 2020. A restructuring would be treated as implemented if the following conditions are met:
   a. all related documentation, including execution of necessary agreements between lenders and borrower / creation of security charge / perfection of securities are completed by all lenders; and
   b. the new capital structure and / or changes in the terms and conditions of the existing loans get duly reflected in the books of all the lenders and the borrower.
5. A provision of 5% in addition to the provisions already held, shall be made in respect of accounts restructured under these instructions. Banks will, however, have the option of reversing such provisions at the end of the specified period, subject to the account demonstrating satisfactory performance during the specified period as defined at paragraph 5 below.
6. Post-restructuring,NPA classification of these accounts shall be as per the extant IRAC norms.
7. Banks and NBFCs shall make appropriate disclosures in their financial statements, under 'Notes on Accounts', relating to the MSME accounts restructured under these instructions as per the following format:

No. of accounts restructured	*Amount (Rs. in million)*

8. All other instructions applicable to restructuring of loans to MSME borrowers shall continue to be applicable.

- Banks and NBFCs desirous of adopting this scheme shall put in place a Board approved policy on restructuring of MSME advances under these instructions within a month from the date of this circular. The policy shall, inter alia, include framework for viability assessment of the stressed accounts and regular monitoring of the restructured accounts.
- It is clarified that accounts classified as NPA can be restructured; however, the extant asset classification norms governing restructuring of NPAs will continue to apply.
- As a general rule, barring the above one-time exception, any MSME account which is restructured must be downgraded to NPA upon restructuring and will slip into progressively lower asset classification and higher provisioning requirements as per extant IRAC norms. Such an account may be considered for upgradation to 'standard' only if it demonstrates satisfactory performance during the specified period.
- 'Specified Period' means a period of one year from the commencement of the first payment of interest or principal, whichever is later, on the credit facility with longest period of moratorium under the terms of restructuring package. 'Satisfactory Performance' means no payment (interest and/or principal) shall remain overdue for a period of more than 30 days. In case of cash credit / overdraft account, satisfactory performance means that the outstanding in the account shall not be more than the sanctioned limit or drawing power, whichever is lower, for a period of more than 30 days.

https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11445&Mode=0

Verdicts

Direct Tax

Where for relevant years scrutiny assessments were pending and likelihood of substantial demands upon assessee after completion of scrutiny cannot be ruled out and any demand that would arise from processing of said assessments would have to be adjusted against refund claims, there was no merit in writ petition claiming for direction to Assessing Officer to expeditiously process said returns and issue refund for these years

- Decision of High Court of Delhi in Vodafone Mobile Services Ltd.v. Assistant Commissioner of Income-tax

Facts of the case:

1. The assessee-company (Vodafone) was engaged in providing telecommunication services.
2. Two amalgamations involving merger of certain Vodafone group companies were undertaken to re-structure business operations and increase operational efficiencies. The revised e-returns of income pertaining to assessment year 2014-15 and assessment year 2015-16, were filed claiming refunds of Rs. 1,532.09 crores and Rs. l,355.51 crores, respectively. The return of income pertaining to assessment year 2016-17, claiming refund of Rs. 1128.47 crores was also filed.
3. Vodafone requested the revenue for expeditious processing of the pending income-tax returns.
4. Thereafter, writ petition was filed by the petitioner 'vodafone' on account of inaction on the part of Assessing Officer in processing income tax returns for four assessment years 2014-15 to 2017-18 which would result in issuance of refunds aggregating to Rs. 4759.74 crores along with applicable interest under section

244A seeking a direction upon the Assessing Officer to expeditiously process the refund claim and issue refund under consideration as it was under financial stress.

5. Section 143(2) empowers the Assessing Officer to issue notice to the assessee to produce documents or other evidence, to prove the genuineness of the income tax return. Under section 143(1D) of the Act as introduced by the Finance Act, 2012 processing of a return under section 143(1)(a) is not necessary where a notice has been issued under section 143(2). This provision has now been amended by the Finance Act, 2016 (with effect from the assessment year 2017-18) to provide that if scrutiny notice is issued under section 143(2), processing of return shall not be necessary before the expiry of one year from the end of the financial year in which return is submitted.
6. The Assessing Officer has exercised discretion under section 143(1D) not to process the returns considering the fact that substantial demand would be raised on completion of scrutiny assessment of earlier years.
7. The revenue also argued that substantial outstanding demand ispending against the petitioner and that the likelihood of substantial demands after the scrutiny for the pending assessments, cannot be ruled out.

Judgement:

The Honorable High Court Of Delhi found no merit in the petitioner's argument and accordingly, the writ petition has been dismissed.

https://www.taxmann.com/filecontent.aspx?Page=CASELAWS&id=101010000000185535&isxml=Y&search=&tophead=true&tophead=true

SLP dismissed against High Court ruling that where on examination of special audit report, filed after passing of original assessment order, it was found that claims made by under section 80G were prima facie bogus and issue of a reassessment notice on basis of said report was justified

- Decision of Supreme Court Of India in Multi Commodity Exchange of India Ltd. v Deputy Commissioner of Income-tax

Facts of the case:

1. For the Assessment Year 2010-11, the Assessee company's income was assessed under section 143(3).
2. Later, in a report of Auditor (after completion of assessment) it was observed that claims made by assessee towards placement fees paid to its subsidiaries, advertisement expenses and donations paid to a charitable trust under section 80G were prima facie bogus.
3. The Assessee also could not substantiate their genuineness by providing relevant documents and evidences.
4. Thus, a reassessment notice was issued against assessee.
5. The Assessee later approached the High Court Of Bombay. The High Court, by its order held that since special audit report was a fresh tangible material which formed basis of Assessing Officer's reasonable belief that income chargeable to tax had escaped assessment, reassessment notice issued on basis of same was justified.
6. Aggrieved by the impunged order of the High Court, the assessee filed a Special Leave Petition with the Supreme Court Of India.

Judgement:

The Honorable Supreme Court Of India has held that the SLP filed against the order of the High Court was to be dismissed and it upheld the order of the High Court.

https://www.taxmann.com/filecontent.aspx?Page=CASELAWS&id=101010000000185620&isxml=Y&search=&tophead=true&tophead=true

Verdicts

Indirect Taxes - GST

No GST exemption on goods and service supply to Duty Free Shops (DFSs) at international Airports in India

- Decision of High Court of Madhya Pradesh in Vasu Clothing(P) Ltd. v. Union of India

Facts of the case:

1. The petitioner is a manufacturer and exporter of garments in India and specializes in manufacturing of highquality products for children with customer base in Middle East, South Africa and USA. He intends to supply

goods to Duty Free Shops (DFSs) situated in the duty free area at international airports. The petitioner is aggrieved by the fact that the benefit available to him under the erstwhile central excise regime of removing goods from his factory to DFS located in the international airports without payment of duty is not available to him under the GST regime.

2. Undisputedly, in light of the definition as contained under the IGST Act, 2017 a Duty Free Shop situated at the airport cannot be treated as territory out of India. The petitioner is not exporting the goods out of India. He is selling to a supplier, who is within India and the point of sale is also at Indore as the petitioner is receiving price of goods at Indore.
3. The petitioner cannot escape the liability to pay GST. It is true that our taxes cannot be exported but the facts remains that it is not the petitioner, who is exporting the goods or taking goods out of India. He is selling to a person, who is having Duty Free Shop (to a Duty Free Operator), which is located in India as per the definition clause as contained under the GST Act.

Judgement: In light of the aforesaid, as there is no reason to issue writ directing the respondents not to charge GST on the petitioner or to legislate on the subject granting exemptions as prayed by the petitioner and accordingly, the petition was dismissed by the High Court Of Madhya Pradesh.

https://www.taxmann.com/filecontent.aspx?Page=CASELAWS&id=101010000000185694&isxml=Y&search=&tophead=true&tophead=true

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