# ACHROMIC POINT KNOWLEDGE FORUM

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BY THE PROFESSIONALS FOR THE PROFESSIONALS

# Index

Some of Key Supreme Court / High Court Judgements Under

# INDIAN INDIRECT TAX LAWS

1. Constitutional validity based on place of supply of 'intermediary services' based on the location of the supplier - **Dharmendra Jani vs. Union of India [2021 (6) TMI 563 – Bombay High Court]**

The two-judge Bench of the H'ble Bombay High Court has given a split decision.

*Quick glance at the facts*

- The Petitioner undertook activities of marketing / promotion of goods sold by its foreign customers in India, solicited purchase orders for them and earned commission in convertible foreign exchange from its foreign customers.
- The Petitioner assailed the constitutional validity of the provisions in GST law for determining the place of supply of services of an 'intermedi-

ary' basis the location of the supplier on the ground that the services provided to a service receiver located outside India is treated as export of service and that levy of GST on export of service is ultra vires the Constitution of India.

*Judgement - Ujjal Bhuyan J. – place of supply under the law is unconstitutional*

- Honourable Justice noted that GST is a destination-based consumption tax and that Constitution does not empower imposition of tax on export of services out of the territory of India by treating the same as a local supply.
- Honourable Justice further noted that there is an express bar under Constitution that no law of a State shall impose or authorise imposition of a tax on supply of goods or services where such supply takes place in the course of import into or export out of India. Basis this it was held that the power of Parliament to make laws formulating principles for determining supply of goods or of services cannot be used to foil or thwart this express bar under the Constitution.
- Held that intermediary service is an export of service as understood in common parlance and supply takes place outside India. The provisions in GST law create a fiction deeming export of service by an intermediary to be a local supply and this is an artificial device created to overcome a constitutional embargo.
- The Honourable Justice finally held that provision in GST law for determining the place of supply of services of an 'intermediary' is foul of the overall scheme of GST laws and offends the Constitution of India.

***Judgement – Abhay Ahuja J. - place of supply under the law is constitutional***

- Honourable Justice noted that the examination of the Court begins with a presumption in favour of constitutionality and that Constitution empowers the Parliament to legislate on principles for determining the place of supply and when the supply would be in the course of inter-state trade or commerce, it was held that the provisions determining the nature of supplies or place of supply originates from such power to enact provisions.
- Held that it is not relevant in the circumstances that export and import are not defined under the Constitution or that the same would be of wide constructions.
- Honourable Justice held that the Petitioners submission that its service is an export of service is misplaced especially when there is a specific provision defining 'intermediary', and intermediary services being specifically dealt for determining place of supply; the question of application of general provision for determining place of supply would not arise.

The matter would now be placed before the Chief Justice of High Court for hearing.

2. Power of provisional attachment under the GST law - ***Radha Krishan Industries vs. State of Himachal Pradesh and others (Civil Appeal No. 1155 of 2021) – Supreme Court of India***

*Quick glance at the facts*

- The Petitioner manufactures lead according to the specific requirements of its clients. Search and seizure was undertaken for one of the supplier's of the Petitioner, and it was noticed that the supplier was availing input tax credit on the basis of fake invoices.
- Based on same the authorities also the input tax credit of the Petitioner without any notice. Notices were issued to two of the customers of the Petitioner, provisionally attaching the Petitioner's receivables from its two customers.
- The Petitioner filed their objections but were not granted an opportunity of being heard. The petitioner also

contested the exercise of power of provisional attachment under the GST law .

- The writ petition was dismissed by High Court solely on the ground that writ petition is not maintainable if there is an alternative remedy available in the law.

*Judgement*

- Dhananjaya Y Chandrachud J. held that the writ petition filed by the Petitioner before the High Court was maintainable since there was no alternative remedy available in the law. The power to order a provisional attachment of the property is draconian in nature and the conditions as prescribed in the statute ought to be satisfied to exercise the said power.
- Noted that the power must be exercised by the authorities only based on an opinion that it is necessary to attach the property to protect the interest of the revenue. Such opinion should be backed by tangible material and findings.
- The law itself provides dual safeguards to the person whose property is being attached – an entitlement to submit objections against the order of provisional attachment & an opportunity of being heard.
- The Commissioner in the instant case, not having granted an opportunity of being heard to the Petitioner, had misconceived the law and concluded that the opportunity of being heard was at his discretion. The civil appeal was thus allowed and order of the High Court was set aside.

3. Service tax on take-away of food parcels from restaurants / eateries? - ***Anjappar Chettinad A/C Restaurant & others vs. Joint Commissioner & others (W.P. No.13469 of 2020) - Madras High Court***

- *Quick glance at the facts*
- Petitioners run air-conditioned restaurants, wherein, take-away of food parcel was also offered.
- The authorities objected that service tax was not discharged on take-away of food parcels for a period up to June 2017.

*Judgement*

- Noted that sale of food and beverages involves both aspects of sale as well as service. Initially service tax was levied only on sale of food and beverages in all air-conditioned /

centrally heated restaurants / eateries.

- Noted that service portion in any activity, wherein, food or any drink was supplied, was a declared service under the service tax regime.
- Held that not all services rendered during sale of food and drinks are taxable. Specified services, commencing from the point where the food and drinks are collected for service at the table till the bill is raised, would be liable to service tax.
- Held that in the case of take-away of food parcels, there being an absence of the above specified services, such take-away parcels should not attract service tax. More so, consumption of the food and drinks does not take place in the restaurant premises. In which event, there is no service element involved. Also, noted that, take-away counters are generally positioned away from the main dining areas and may / may not be air-conditioned / centrally heated.

4. Eligibility of input tax credit by duty free shops - ***Flemingo Dutyfree Shop Private Limited vs. Union of India & others [WP (MD) No. 2129 of 2018 and WMP (MD) No. 2373 of 2018 & 2980 of 2019] – Madras High Court***

***Sandeep Patil vs. Union of India (Writ Petition No. 1511 of 2019) – Bombay High Court***

*Quick glance at the facts*

- Petitioner operates duty free shops at the international airport for which it has entered into a concession agreement / revenue share agreement with the Airport authority of India for grant of rights and use of the licensed premises of the duty free shops.
- Petitioner was paying GST on the concession fee / revenue share agreement to the Airport Authority of India. Writ petition was filed and there was an interim order restricting the Airport Authority to collect GST from the petitioner.

*Judgement*

- Noted that goods sold by duty free shops are either imported or purchased from Indian market and are stored in customs bonded warehouses and are removed from such warehouses only under the supervision of the Jurisdictional Commissioner, thus, for all intents and purposes are not sold for domestic purposes.
- Noted that duty free shops, situated at the international airports, though in common parlance, are situated in India, however, as per the Customs Act, 1962, such airports fall beyond the customs frontiers of India.
- Held that Article 286 of the Constitution of India restricts States from imposition of tax on sale of purchase of goods where the supply takes place in the course of import or export of goods out of India. Thus, States, cannot levy tax on any transaction that takes place when goods are in the course of import or export.
- Sale of goods to outbound passengers - The destination of the goods purchased by the outbound passenger is clearly a foreign destination. The outbound passenger only acts as a carrier on behalf of the duty free shops, until it reaches the final destination in a foreign country. Thus, sale of goods to outbound passengers qualifies to be an export, thus, zero-rated, under the GST law.
- Sale of goods to inbound passengers - Customs liability on import of goods arises at the point when the importer files the bill of entry for home consumption. Duty free shops sells such goods to the inbound passengers, who in turn, are required to file the bill of entry, pay the customs liability & clear the goods for home consumption. However, passenger baggage is exempt from GST in accordance with the Baggage Rules. Thus, duty free shops, not required to file the bill of entry for home consumption, are not liable to pay customs duty. W.e.f. February 1,

2019, supply of warehoused goods before clearance for home consumption would not be treated as a supply of goods or services, as per Schedule III of the GST law.
- Receipt of input services by duty free shops - Though duty free shops are located beyond the custom frontiers, it is still in the territorial waters of India. Thus, receipt of input services by duty free shops would be liable to GST. Accordingly, duty free shops are required to pay GST & claim input tax credit on the input services received by them, pursuant to which, their outward supplies being zero-rated, they can claim refund of unutilised input tax credit under the GST law.

5. Inclusion of actionable claims in the definition of goods & GST on lotteries - ***Skill Lotto Solutions Pvt. Ltd. vs. Union of India & others [Writ Petition (Civil) No.961 of 2018] – Supreme Court***

*Quick glance at the facts*
- Petitioner is an authorised agent for sale and distribution of State organized lotteries.
- Petitioner assailed the Constitutional validity of the provisions in the GST law for inclusion of actionable claims in the definition of goods, selective inclusion of lotteries as actionable claims and levy of GST on lotteries i.e., actionable claims.

*Judgement*
- Held that definition of goods under the GST law cannot be said to be violative of the definition of goods under the Constitution, since the latter is an inclusive definition. It is a settled position that an inclusive definition is always intended to expand the scope of the definition and should not be interpreted in a restrictive manner.
- Held that the Parliament has been empowered with wide powers to make laws with respect to GST. Inclusion of selective categories as actionable claims, for the purposes of GST law, cannot be said to be without any rationale. Even in the pre-GST regime, lotteries have been regulated and taxed by different legislations.
- Noted that to the extent that the lottery tickets evidenced the right to claim the prize, was not goods but an actionable claim. Purchaser does not pay for the right to participate in the lottery, instead it pays for the chance to win. Lottery ticket, per se, has not innate value. The right to participate being an inseparable part of the chance to win, is therefore part of an actionable claim.
- Held that value of supply of lottery should be determined as per the specified rule in the GST law.

**Amitabh Khemka**
*Lead Partner – Global Indirect Taxes*
**KNAV**

# GST ON SECONDMENT OF EMPLOYEES

In India, it is a common practice for the Indian subsidiary to issue the employees a separate employment contract till the subsistence of contractual relations. When multinational parent businesses delegate personnel resources to their subsidiaries, the remuneration is typically paid directly to the workers concerned in their local currencies by the home company (Parent). During a deputation or secondment, the employee works under the direction, supervision, and control of the deputed/seconded firm and is paid a salary and other benefits in accordance with their policies. The salary of the deputed/seconded employee is processed and paid by the deputed/seconded firm, and the amount is subsequently recovered from the deputed/seconded company.

**LEGALITY OF APPROACH**

This type of employee secondment agreement is legal because there is no legislation prohibiting an employee from working for more than one firm. In the case of a clear contractual position, it can be claimed that the secondee firm's wage reimbursement to the other company does not amount to supply, but rather to the employer-employee relationship, and should be covered under Schedule-III of CGST Act,2017. The nature of the degree of control required to build connections between employer and employee, on the other hand, must vary from business to business and is, by definition, impossible to define precisely. As a result, the proper route to follow would require focus on the contractual agreement reached between the two firms.

**SERVICE TAX APPLICATION**

The service tax's application has grown over time, with 119 services falling under its purview in 2012. The notion was based on the positive list of services, which stated which services were taxed under Section 65(105) of the Finance Act of 1994. In this case, the numerous services must be closely monitored to determine whether the service given is taxable under any of the listed services. With the release of

Budget 2012, a new service tax system was established, in which all services would be taxed unless they are designated under the negative list item or are otherwise exempt under any category.
Several jurists have stated that service taxes would be imposed if supply is defined as services provided by a manpower recruitment or supply agency. However, in a number of cases, different Tribunals and High Courts have ruled that the supplied supply does not qualify as Manpower Recruitment or Supply Agency Services. And with respect to the Service tax consequences on employee deputation, the legal situation following the implementation of the negative list system does not differ from the settled legal position that existed before to 2012. The exception in the definition of service strengthens the legal position that workers who provide service to their employer in the course of their job are not subject to Service tax.

## GST ACT AND RELEVANT PROVISIONS

To understand the relevance of GST implications on Secondment of employees, it is imperative to break down the provisions of the finance Act which define taxable services and the provisions concerning manpower recruitment. **Section 65(105) (k) of the Finance Act defines** *"taxable service" as any service provided or to be provided to any person, by a manpower recruitment or supply agency in relation to the recruitment or supply of manpower, temporarily or otherwise, in any manner". And accordingly, Section 65(68) of the Act defines manpower recruitment or supply agency" means any person engaged in providing any service, directly or indirectly, in any manner for recruitment or supply of manpower, temporarily or otherwise, to any other person"*

According to Para 1 of Schedule III of the Central Goods and Services Tax Act, 2017 ("CGST Act") along with Section 7, services provided by an employee to his employer in the course of or in relation to his employment are neither a supply of goods nor a supply of services. The ratio in the case of ***M/s Target Corporation India Pvt Ltd v. C.C.E., Bangalore*** states that an activity cannot be classified as "manpower recruitment or supply agency" when an employee-employer connection exists. demanding INR 28,37,08,191/- in differential Service tax on secondment of personnel by firms under agreement.

## JUDICIAL ASSESSMENTS ON GST CONCERNS

However, in the case of **Franco Indian Pharmaceutical (P) Ltd. V. Comm. of ST**, it was decided that if an employee signs a contract with one company and is later delegated to another group company, the cost shared will not be subject to service tax because the parties' conduct indicates that the employee will work for more than one company and there is no intent to earn revenue. The tribunal found that services provided in the course of employment were retained from the scope of the service tax levy, not only during the time under review but also now, under the negative list system. It further clarified that in order for anything to qualify as a supply, there must be reciprocity, meaning that the one offering the consideration expects something in return.
The Commissioner of Central Excise & Central Goods and Services Tax Authority in Jaipur held in a recent decision in ***M/s Imasen Manufacturing India Private Limited*** that payments given by an Indian business to its parent company for staff secondment are not taxable. The seconded employee's employer-employee connection with the Indian Company was verified by the Commissioner in his order. The findings of the Supreme court in the case of **Nissin Brake India Pvt. Ltd. Concluded that, discussed with respect to** taxability of secondment of employees under the service tax regime. When the Revenue attempted to tax such pay reimbursements as manpower supply services and requested service tax

under the reverse charge method, this case came to light. The main observations of the court were that the assessee supervises the delegated person, and the assessee also acts as an employer in terms of withholding tax compliance. Apart from the reimbursement of salaries at cost, the assessee did not pay any direct or indirect remuneration to its parent business for the deployment of workers.

In this situation, the foreign employees were placed on the payroll of an Indian business, with part of the salary paid by the Indian entity in India and part of the salary paid by the foreign holding entity in the employee's overseas bank account. The argument was that an Indian entity's reimbursement to a foreign entity was subject to service tax. The projection undertaken by judges was that the foreign group firm did not provide personnel services to the appellant. The ratio concluded that the nature of the transaction could not be determined by the manner of salary disbursement and as a consequence avoided the service tax liability for the same. This position was adopted in the case of **Volkswagen India (Pvt.) Ltd. Versus Commissioner of C. Ex., Pune.**

**CONCLUSION**

As a result, from these decisions, it can observed that supply covers a contribution to the employer-employee relationship, which is protected under Schedule III of the CGST Act and may not be subject to GST but may not be extended to claim any salary reimbursement of pay by the secondee business to the other company. However, contract provisions will play a significant influence in determining taxability. The taxability of GST transactions continues to be hampered by inconsistent judgments based on the broad definition of the term "supply," which encompasses all types of supply made for consideration in the conduct or advancement of business. When an employee is seconded, however, the receiving business takes on the role of the real and economic employer. As a result, based on the preceding decisions and draught explanation, the appellate authorities' purpose to categorize such arrangements as employer-employee relationships rather than manpower recruitment or supply agency services appears to be fairly obvious.

In all of these instances, the firms should engage into a formal employment transfer agreement in which the employee's effective control is transferred from the parent company to the group company. It is also required that the parent business waives all claims, obligation, liability, or other ties with the seconded employee during the period of secondment, and that the seconded employee be answerable to the group company to which he is assigned for all real and economic purposes. In such instances, the group business will pay the wage directly, and no money will pass from the group company to the parent, avoiding the application of GST.

However, due to globalisation, the notion of a company's recourse arrangement for employees is gaining prominence. As a result, the tax authorities are always scrutinizing this arrangement since the underlying connection puts doubt on its value. Clearer rulings and policy framework from the government is needed to provide appropriate clarity on such arrangements and transactions under the GST regime.

**CA MANEET PAL SINGH**
*Partner*
**I.P. Pasricha & Co**

# Demystifying Rule
## 86A of the CGST Rules The Untrodden Path


To ensure availability of funds to meet working capital crisis, especially for Micro, Small and Medium Enterprises ('MSME') Sector, the Central Government and Reserve Bank of India ('RBI') have taken certain heavy-weight monetary measures.

The above noble objective of one arm of the Government and RBI is getting frustrated in practice by the GST authorities. Even on trivial issues or minor lapses on the part of suppliers, GST Authorities block the credit utilization of bona fide recipients, thereby forcing the taxpayers to discharge their GST liabilities in cash. Rule 86A of the CGST Rules is a classic example of another arm of the Government giving such powers to the GST Authorities to curb the flow of funds to industry.

This is evident from a recent news article:

*'Indirect tax department has started blocking Input tax credit ('ITC') of the whole supply chain under GST framework even if one of the vendor or supplier has missed out filing requirements. This impacted several corporates and prompted some to consider legal recourse' - Economic Times; June 4, 2021.*

The use of such excessive and disproportionate powers by the GST Authorities compelled us to revisit Rule 86A of the CGST Rules. Together, let us take 'the Untrodden Path'.

*Rule 86A: Conditions of use of amount available in electronic credit ledger -*

*"(1) The Commissioner or an officer authorized by him in this behalf, not below the rank of an Assistant Commissioner, having reasons to believe that credit of input tax available in the electronic credit ledger has been fraudulently availed or is ineligible in as much as-*
*……*
*may, for reasons to be recorded in writing, not allow debit of an amount equivalent to such credit in electronic credit ledger for discharge of any liability under section 49 or for claim of any refund of any unutilized amount.*
*……."*

The use of the term “available” in the above Rule, when closely looked at, gives an altogether different context and meaning to the above Rule. Such an interpretation has hitherto not been taken in any decision or judgment.

In common parlance, the term 'available' indicates “anything which is at someone's disposal or which is at hand”. As per the Collins Dictionary, the term 'available' means “obtainable or accessible; capable of being made use of; at hand”. Law Lexicon also defines the term in a similar manner only.

By corollary, something which is not in presenti i.e. non-existent / not available, cannot be said to be available. Hence, notwithstanding the satisfaction of other conditions specified under Rule 86A, the ITC fraudulently availed, must be available in the Electronic Credit Ledger ('ECL') for any order to be passed under Rule 86A by the GST Authorities.

It is a settled Rule of Interpretation that every word used by the Legislature must be given its due meaning. It is trite that Legislature does not waste any

word and never says anything in vain. A simple exercise to test this Rule of Interpretation is to check whether by dropping the subject word, does the meaning of the provision remains intact or it undergoes change.

Moreover, generally, the words used by the Legislature need to be understood in their natural or ordinary sense. If the words of the statute are unambiguous, then it is inappropriate to expound a different meaning to such words beyond their natural and ordinary meaning. The words used in the provision are sufficient to say aloud the intent of the lawmakers.[1]

By applying the above Rules of Interpretation to Rule 86A, it is obvious that the term 'available' used therein carries its natural and ordinary meaning. If the term 'available' is dropped from the Rule 86A, then the interpretation of Rule 86A would be different from the interpretation this Rule would have with the term 'available' remaining in it. Therefore, the term 'available' as used in Rule 86A must be given its due meaning.

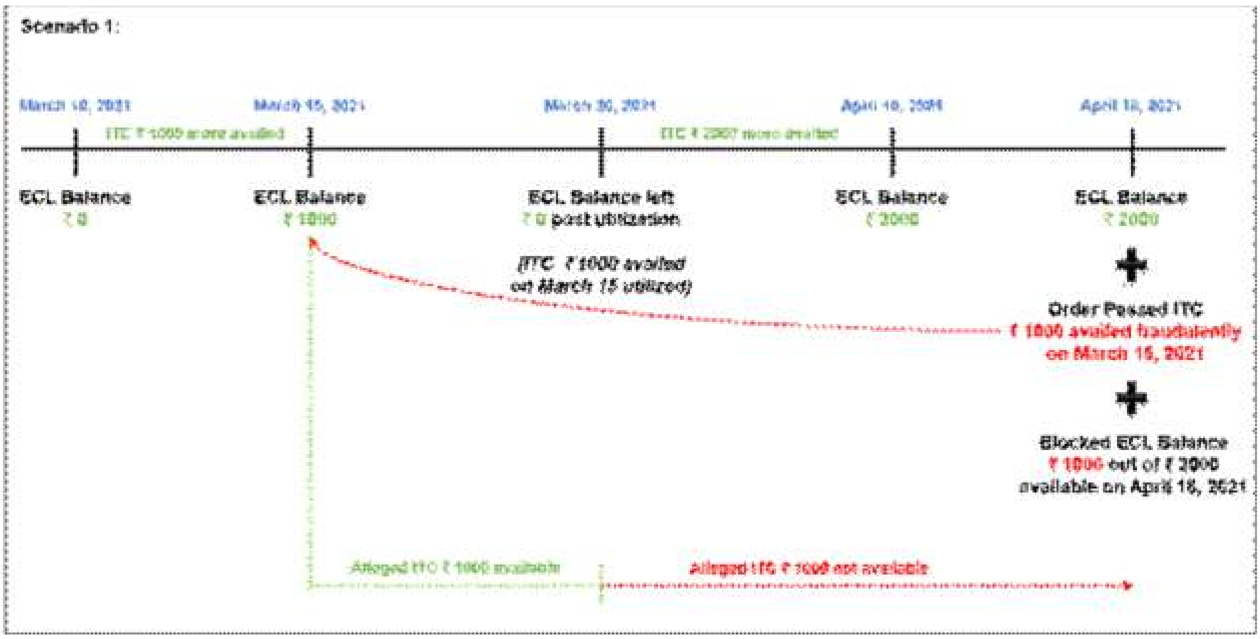
Power to block ITC under Rule 86A is akin to the power of attachment of property under Section 83 of the CGST Act. Both the provisions require the Commissioner to have reason to believe under specified circumstances to block ITC or attach property provisionally for a period of one year. Recently in the case of Radha Krishna Industries[2], the Supreme Court held that the power under Section 83 is draconian and needs to be interpreted restrictively. The

*[1]. G.P. Singh: Principles of Statutory Interpretation*
*[2]. Radha Krishan Industries v. State of Himachal Pradesh [2021-VIL-50-SC]*

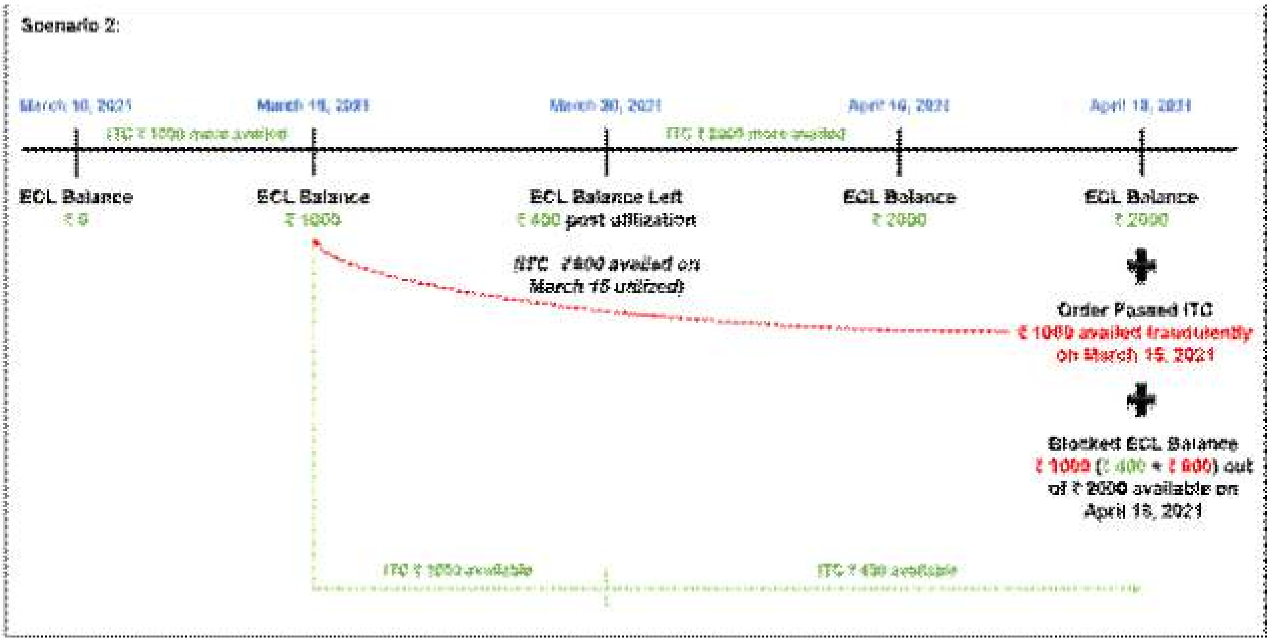
provision must be construed on its plain terms without any intendment.

From the above ruling, we can draw an analogy to interpret Rule 86A. Resultantly, words used in Rule 86A must be interpreted restrictively only. Accordingly, the term 'ITC available' as used in Rule 86A must necessarily refer to availability of that ITC which is sought to be blocked in terms of Rule 86A. If any part of the ITC which is sought to be blocked in terms of Rule 86A has already been utilized and is therefore not available on the date of passing Order under Rule 86A, then no Order under Rule 86A can be passed. Moreover, an Order under Rule 86A cannot block any other ITC which is availed by the taxpayer after the subject ITC for which Order under Rule 86A pertains to. This is explained by plotting different scenarios as under:

**Examining Rule 86A from the optics of the term 'Available' (presuming all other conditions are satisfied)**




***Remarks*** *- Order passed blocking ITC of Rs.1000 is inappropriate as the alleged fraudulently availed ITC was not available in ECL as on April 18, 2021 inasmuch as ITC of Rs.1000 was utilized for discharging output tax liability on March 20, 2021. Therefore, on April 18, 2021, no fraudulently availed ITC of Rs.1000 was available for blocking. Order dated April 18, 2021 blocking ITC of Rs.1000 out of ITC of Rs.2000 availed during March 20, 2021 to April 10, 2021 is not tenable as ITC of Rs.2000 has not been held to have been availed fraudulently*




***Remarks*** *- The Order issued blocking ITC of Rs.1000 is inappropriate to the extent of Rs.600 as the alleged fraudulently availed ITC was not available in ECL as on April 18, 2021. The alleged ITC to the extent of Rs.600 was utilized for discharging output tax liability on March 20, 2021. However, the Order is appropriate to the extent of Rs.400 as ITC of Rs.400 is out of the fraudulently availed ITC of Rs.1000 on March 15, 2021 and the same was available in ECL on the date of passing Order i.e. April 18, 2021.*

**Concluding Remarks:**

Apropos Rule 86A, GST Authorities can block the use of ITC by taxpayer by alleging it to be fraudulently availed. But they can restrict utilization of only that portion of ITC which is available in ECL on the date of passing Order out of the ITC which is availed in contravention of Rule 86A. Utilization of no other ITC can be restricted as Rule 86A needs to be interpreted strictly. Interestingly, Section 83, albeit declared a draconian provision, still provides for post facto opportunity of being heard to the taxpayer. Whereas Rule 86A, though a reflection of Section 83, does not provide for any opportunity of being heard to the taxpayer. Our interpretation of Rule 86A herein is like sailing through unchartered waters and walking an untrodden path. It would be interesting to see how the term 'available' in Rule 86A is interpreted by the Courts.

The article was first published on Taxsutra.

**Dharnendra Kumar Rana**
*Partner*
**NITYA Tax Associates**

**Parul Gupta**
*Senior Research Associate*
**NITYA Tax Associates**

**Mohit Pugalia**
*Associate*
**NITYA Tax Associates**

# How Organizations Prepare for Transformation

*Why do business organizations go through the demanding process of transformation?*

Typically, because they want to improve on multiple aspects of their business to gain a competitive advantage or address a significant challenge.

This process has become even more critical for several industries during the recent pandemic when many businesses needed to adapt to a new working environment to survive.

In this sense, even though a disaster might occur, organizational transformation can act as a catalyst by changing behavioral patterns of employees, introducing more robust processes or by introducing a new technology into the organization. In many cases, these forms of transformation improves a company's lifespan. Every organization is at different stages in its transformation journey. The degree to which they are entrenched in this process depends on internal and external factors unique to their business venture.

While there are several parameters to streamline if one has to execute a successful transformation, a key parameter nowadays is technology.

**Technology does not Entail Transformational Readiness**

At times, people confuse transformation with the implementation of technology.

Organizations often assume buying the latest software will give them profitable results, but they miss the mark because they often fail to prepare in the right manner.

Though artificial intelligence, machine learning, and automation may facilitate a transformation, it is not the only criteria.

Expecting technology to immediately provide significant results without preparing to invest in understanding deeper problems or training/streamlining employees to the new technology is similar to going to a gym and not knowing how to properly use the equipment.

Your transformation requires knowledge of impact areas, a customized, phased approach, and time to integrate with other systems. Merely purchasing automation software or new technology without full knowledge or preparation for its application often results in inaccurate outputs, excessive time for implementation, and other inconsistencies.

**What Transformational Readiness Actually Constitutes**

When an organization wants to execute a transformation, its leaders must inspect each and every aspect of the new microcosm before going forward with implementation.

Let's look at the key consideration points before undertaking an organizational transformation:

**Understanding core problems and their interlinkages:** It is necessary to understand the main challenges that the organization is facing before undertaking a transformation. In most cases, the transformation can substantially help. However, without understanding the main challenge, the kind of transformation may not be accurately identified.

**Project Plan:** Before you begin your transformation journey, you need to have a comprehensive project plan that covers priority processes, people training, investment, and identify the roles and responsibilities of the leadership team spearheading this change.

**Budget:** Procure a firm commitment from the organization on the budget. You need a clear-cut budget for process transformation which covers the cost of the new tools and technology, customization costs, new compliance requirements, trainings, and other contingencies.

**Vendor Selection:** A trustworthy vendor is essential when opting for any form of transformation. You need to assess the vendor's approach, existing client base, and ability to understand your unique organizational needs.

**Allocating Resources:** You need to identify champions from your team who will support the transformation process. Ideally, these should be members of the leadership team or organizational influencers. This will help create a ripple effect throughout the organization when the identified influencers begin to exhibit changed behavior, adopt more efficient processes, or imbibe new technologies into their daily routine.

**Tool selection:** Once you have identified the processes than need to be transformed, you have identified the opportunity to deploy a technology to help make the process efficient. It is essential to have a clear idea of what you are looking for, your unique business-specific nuances, non-negotiable features, etc. The selection of the right tool is half the battle won.

**Upskilling:** While business transformations will result in freeing up the bandwidth of your human resources in the long-run, it is essential that these resources are made aware of the requirement and correct usage. Upskilling must be accounted into the transformation process before expecting significant returns. The increased competency also allays fears of unemployment while simultaneously building a better functional team.

**Implementation Partner:** One of the biggest challenges in organizational transformation is the rarity of in-house experts who can oversee the whole process with assurance. This person/team must have a holistic understanding of the technology, the lay of the land, as well as the distinct business requirements of your organization. They are also expected to work collaboratively with your team. It is preferable to join forces with an experienced partner who knows the intricacies of business transformation.

So, what is the key to a successful transformation?

In short:

Identification, commitment, and expertise.

**Partnerships are the Key to Business Transformation**

Businesses will continue to ply their trades in different countries, business verticals, and sometimes even in new industries altogether. The key differentiator in this situation will be an organization's transformation. In this context, a well-thought-out strategy and allocating the right resources can help you gain a strategic edge.

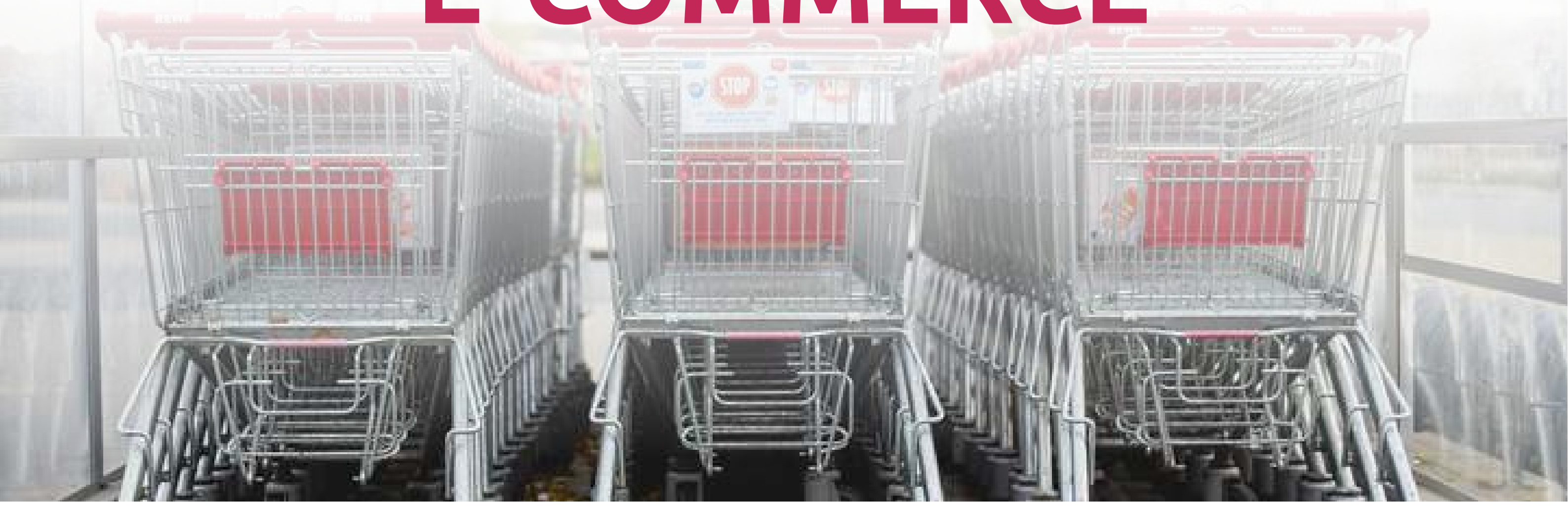
However, this alone is still not enough.

Businesses need a partner who can fit or adapt to the culture, style, and the needs of your organization or new venture. For companies looking to set up in a high-potential market, the management team needs to be completely committed to the purpose and ensure it is communicated to the entire organization or process for their transformation to succeed.

Even in this pandemic era, organizational transformations can have a positive impact if they are able to take care of all aspects mentioned above. An organization's fragility can be overcome with transformation frameworks whose intricacies are well-established and have thoroughly understood. Once a collaboration is in place, the results will follow.

**Alpana Shirgaonkar**
*Senior Executive Director-Business Process Management*
**Nexdigm (SKP)**

# PROPOSED CHANGES TO E-COMMERCE RULES AND THEIR IMPACT ON E-COMMERCE




**Backdrop**

The Consumer Protection (E-Commerce) Rules, 2020 ("Rules") is a year old now. During its short lifespan so far, it has remained in the news as well as subjected to multi-faceted analysis, given the various stakeholders who get affected by it (in addition to the end consumer). The latest round in the evolution of this law is owing to the Consumer Affairs Ministry's proposed amendments thereto ("Proposed Amendments"). Given how far reaching the Proposed Amendments could be if brought into law, various industry bodies and stakeholders provided their comments.

While the public window for providing inputs closed a couple of weeks back, we are now in the more significant period of how the government evaluates the feedback (often competing) that it would have received. Therefore, it may be a good time to review some of the implications of the Proposed Amendments, from the vantage point of e-commerce entities.

**Definition of E-Commerce Entity**

At the outset, the revised definition in the Proposed Amendments should be considered. The proposed change casts a wider net to cover 2 (two) additional categories of persons. First, a person engaged by an e-commerce entity for fulfilment of orders would now be counted as an e-commerce entity as well. Plain reading of the language seems to bring within its fold third party logistics entities as well. In addition, any "related party" of an e-commerce entity per the Companies Act, 2013 ("Act"), would also be an e-commerce entity. This could be a large envelope, covering the related party entities of the wide swathe of business houses who might be owning (or even operating or managing) an electronic facility/platform but also has other diverse business interests.

**Steps Difficult to Action**

The Proposed Amendments introduce new concepts as well as new governance and grievance redressal mechanism. Provided below are a few illustrations, which would demonstrate how some of the steps in the Proposed Amendments may be difficult to implement or not even required.

***Flash Sale***

Flash sales by e-commerce entities have been prohibited. Often, this is a practice in the marketplace model, and it is

sometimes argued that it creates an unequal playing field for entities with deep pockets. However, it can hurt inventory-based e-commerce entities as well, some of whom may have a genuine need to clear inventory and improve cashflows. Furthermore, while the definition of "flash sale" proposed has the expected references to reduced prices and high discounts, there is an added qualifier – such sales have to be organised fraudulently intercepting ordinary course of business using technology, to enable only certain seller(s) managed by the e-commerce entity to undertake sales. Presently, there are no metrics for what would constitute "fraudulent interception" and "ordinary course of business".

***Cross Sell***

Practically, it is a business development strategy across sectors. Although some may consider it invasive in the e-commerce space with pop-ups and suggestions for the user, it is a business development tool nevertheless. There are also viewpoints favouring prompts on a website for complimentary products to those already purchased, as they can sometimes be convenient even for users. The Proposed Amendments mandate disclosures on cross-sell data by the e-commerce entity to users. While this is a good to have, it may not be of particular benefit to users or their purchasing needs.

***Mis-Selling and Misrepresentation***

"Mis-selling" has also been introduced as a prohibited activity, premised upon deliberate misrepresentation of information to a user. However, when defining misrepresentation, one criterion states: "causing, however innocently, a consumer to purchase such goods or services, to make a mistake as to the substance of the thing which is the subject of the purchase". The use of "however innocently" creates an absolute burden of compliance that is naturally difficult to achieve. Furthermore, its usage also appears contradictory to the notion of "deliberate misrepresentation".

***Clamp Down on Misleading Users***

There are additional embargoes to prevent a user being misled. Illustratively, the prohibition on an e-commerce entity from allowing display or promotion of misleading advertisements. While this is no doubt good for a user, it has wide ramifications for a marketplace e-commerce entity ("MECE") as it may become liable for incorrect information from a seller, whose accuracy the MECE has no control over.

Another example is for the e-commerce entity to not mislead users by manipu-

lating their search result/index. Once again, it is difficult to test for what could be construed as manipulation and whether such search result/index indeed misled a user (because search results would have to appear in some sequence or the other).

***Deeper Compliance and Grievance Redressal***

The Proposed Amendments mandate the appointment of a Chief Compliance Officer and a Resident Grievance Officer. The purpose of having the former is not certain, given the exis-

tence of a nodal person already under the Rules who is in charge of ensuring compliance with the statute. Furthermore, it may not be easy to recruit for the proposed position, which carries individual liability for non-compliance with a legal regime that remains uncertain. In addition, there is also the obligation to appoint another nodal contact person for 24 x 7 coordination with law enforcement (being in a sector that may not require 24 x investigation/prosecution). Similarly, it is unclear whether the Resident Grievance Officer is the same as grievance officer that already provided for in the Rules.

**Extra for MECE**

There are a host of noteworthy obligations that are proposed specifically for an MECE.

***For Related Party and Associated Enterprise***

For instance, the obligation to ensure that none of its related parties or associated enterprises are enlisted by it for sale to consumers directly. While the restriction of B2C sale is understandable, there is inexplicable inconsistency in defining “related party” per the Act but “associated enterprise” with a much wider import than the Act's definition of “associate company”. One possible reason may be that the Proposed Amendments intend to snap certain business models that could be considered circumvention of the spirit if not the letter of the existing law.

The entity would also have to ensure that its related parties/associated enterprises do nothing that the entity itself would not be permitted to do. One such example is related parties and associated enterprises of the MECE are not supposed to listed as sellers on the marketplace platform.

***Unfair Trade Practice***

There is also an obligation to ensure that any information the MECE collects through its platform is not used for unfair advantage of its related parties and associated enterprises. There are questions that this raises. For instance, can it be presumed that the information is supposed to be only of users, since the parent law is for consumer protection; and could information of other third-party sellers be used? Would data/information that a user or a third-party seller has consented to sharing with the MECE be off limits for data analytics? What would constitute "unfair advantage"; and would superior data gathering and analytics as a means of business development be construed as such?

***Information for Display***

There are obligations to display information like country of origin and best before/use before dates on the MECE. It has to be noted that such information is also obtained from sellers, and inaccuracy therein could create liability on the MECE.

***Fall Back Liability***

This concept proposes to make the MECE liable to a user who faces losses due to commissions, omissions and negligent conduct towards such user by a seller registered for the marketplace platform, while such MECE has no control over acts/omissions of the seller with respect to the user.

***No Sale to Seller***

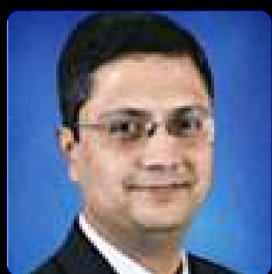
This could be the single most impactful proposal located in a sea of changes suggested under the Propoesd Amendments, as it goes beyond liability and compliance burden and cuts into a widely practiced business model for marketplace e-commerce. Under this, there appears to an effective prohibition on MECE selling any other goods or services to a seller registered on its platform.

**Concluding Remarks**

Clamps on customer attraction tools such as flash sale, cross sell and advertisements would discourage consumers from engaging with a marketplace platform. Prohibition on sale of goods and services to registered sellers disincentivises a seller from tying up with an MECE. Potentially, MECEs running multimillion-dollar operations may be reduced to narrow revenue streams generated through end consumer purchase convenience fee. The absence of safe harbours against acts or omissions by unrelated entities is a significant liability on top of this. Added to this is the uncertainty of being able to implement requirements that are unclear and subjective.

More harmonisation is also suggested with procedures and liability regimes under FDI laws as well as competition laws; absent which, compliance will once again be challenging for an e-commerce entity.

There may be plenty to contemplate before the Proposed Amendments become binding law. In present form, they propose significant challenges in business viability as well as implementation, even with best intentions.



**Saurya Bhattacharya**
*Partner*
**HSA Advocates**

# Grappling with Increasing **TDS** Compliances

**Interplay between Section 194Q and 206C(1H) and Related Controversies**

Finance Act, 2021 had introduced a new Section 194Q in the Income tax Act, effective from 1st July 2021, related to tax deduction at source by a buyer on purchase of goods. Prior to this, Finance Act, 2020 had introduced the provisions related to Tax collection at source (TCS) in respect of sale of goods by a seller and the said provision was effective from 1st October 2020. Thus, at present, there are two provisions of tax deduction and tax collection on the same transaction. Erstwhile, the transactions of purchase and sale of goods were not within the ambit of tax deduction or collection at source (TDS/ TCS) except for a few specific transactions related to sale of alcoholic liquor, scrap, tendu leaves etc. which was within the purview of TCS. However, as law evolved, more and more transactions got included within the purview of TDS/ TCS, thereby, increasing compliances. In fact, the amendments and the compliances related thereto, are against the Government's commitment via the ***'Taxpayers Charter' to reduce cost of compliances and treating taxpayer as honest.***

**Provisions of Tax Deduction at Source on Purchase of Goods [Section 194Q]: Applicable w.e.f. 1st July 2021**

The provisions of section 194Q provides that 'any person, being a buyer who is responsible for paying any sum to any resident (hereafter in this section referred to as the seller) for purchase of

any goods of the value or aggregate of such value exceeding fifty lakh rupees in any previous year, shall, at the time of credit of such sum to the account of the seller or at the time of payment thereof by any mode, whichever is earlier, deduct an amount equal to 0.1 per cent of such sum exceeding fifty lakh rupees as income-tax'.

The section defines "Buyer" as a person whose total sales, gross receipts or turnover from the business carried on by him exceed ten crore rupees during the financial year immediately preceding the financial year in which the purchase of goods is carried out.

**Provisions of Tax Collection at Source on Sale of Goods [Section 206C(1H)]: Applicable w.e.f. 1st October 2020**

As stated aforesaid, vide Finance Act 2020, the Government already had included the provisions of TCS [by inserting sub-section (1H) in section 206(C)] effective from 1st October 2020 on the same nature of transaction (i.e., sale of goods) as under:

'Every person, being a seller, who receives any amount as consideration for sale of any goods of the value or aggregate of such value exceeding fifty lakh rupees in any previous year, other than the goods being exported out of India or goods covered in sub-section (1) or sub-section (1F) or sub-section (1G) shall, at the time of receipt of such amount, collect from the buyer, a sum equal to 0.1 per cent of the sale consideration exceeding fifty lakh rupees as income-tax'.

The section defines "seller" as a person whose total sales, gross receipts or turnover from the business carried on by him exceed ten crore rupees during the financial year immediately preceding the financial year in which the sale of goods is carried out.

**Interplay between Section 194Q and section 206C(1H)**

Section 194Q specifically provides that if tax is deductible under any other provisions of the Act or is collectible under section 206C {other than the transaction on which 206C(1H) is applicable}, provisions of 194Q shall not be applicable. In other words, if a transaction is subject to both section 194Q and section 206C(1H), tax will be deductible under section 194Q.

On the other hand, Section 206C(1H) provides that if the buyer is liable to deduct tax at source under any other provision of the Act on the goods purchased by him from the seller and has deducted such amount, then section 206C(1H) shall not be applicable.

The language of the exceptions under these two sections are worded in a way that section 194Q is given precedence, however section 206C(1H) imposes a condition that only if section 194Q is applicable and the buyer has also deducted the tax at source, only then section 206C(1H) is not applicable. This would have led to a situation whereby in case of a purchase on which section 194Q is applicable and the buyer

defaulted on deduction of tax at source, both TDS and TCS could have become applicable. To address this interplay and also to address the situations wherein TCS has already been collected due to the fact that the provisions of section 206C(1H) came into force prior to the applicability of section 194Q & sellers have already made modifications to their accounting software to this effect, the Board vide Circular No. 13 dated 30th June 2021 has clarified that "if, for any reason, tax has been collected by the seller under sub-section (1H) of section 206C of the Act, before the buyer could deduct tax under section 194Q of the Act on the same transaction, such transaction would not be subjected to tax deduction again by the buyer". Though the clarification is a welcome move to address such situation, however, for the cases where buyer has defaulted in deducting tax as per law or the parties to the transaction mutually agree that only the seller collects the tax at source, can the buyer be relieved from his statutory obligation under law by taking shelter of a circular. Can a circular override the provisions of law!

**Other issues relating to application of Section 194Q**

- **What is included in Goods** – The term 'Goods' is not defined in the Act and hence, has a wide meaning. Taking import from various other laws (including Sale of Goods Act as well as in GST law and Customs law) and as per general parlance, the term 'Goods' would mean and include every kind of property, more particularly, movable property and including crops, shares, stocks, etc. So, one has to keep in mind the provisions of section 194Q while buying any type of goods and not necessarily traded goods, raw material etc. It will include even stationary, consumables, fixed assets, off-market transactions in security and any other goods bought during the course of business if the threshold is achieved.

- **Credit of TDS in case of advance/ purchase return** – TDS under section 194Q is applicable on payment or credit, whichever is earlier. In case TDS under section 194Q is done on an advance payment during the year or tax has been deducted at source and thereafter a purchase return is made which is not adjusted during a particular financial year, there could be a challenge in claiming credit of TDS under section 199 because the income pertaining to the transaction, on which tax has been deducted, is not included in taxable income of that year. This will impact the cash flow of the seller.

- **Issues pertaining to threshold for computing turnover** – Though the circular addresses certain aspects related to the threshold of turnover of the immediately preceding year, however, there is still not much clarity:
  - Circular clarifies that turnover from non-business activity will not be included, but interpretation of the term 'non-business activity' could be a subject matter of litigation.
  - Whether GST is to be considered while computing the turnover/ gross receipts.

- **Company having various branches, different accounting software but common vendors** – If a taxpayer has multitude of branches across the country with different TAN and the accounting is not centralised, but there is a common vendor, the aggregation of transactions for effecting the compliance of TDS provisions would be a dreary task.

- **Strenuous checking by Tax Auditor** – With almost the entire debit side of the profit & loss account of the taxpayer under the ambit of TDS (given the wide meaning of the term goods), it would be a taxing job for a tax auditor for absolving his duties.

With such commotion around the application of these sections, the consequences of non-compliance are tremendous. A bonafide non-deduction of tax at source, because of manifold interpretations, would lead to a 30% disallowance of the expenditure and will also result in treating the taxpayer as an assessee-in-default resulting in levy of interest, penal consequences & prosecution. To add on to this, another burden on the deductor is the compliance of newly inserted section 206AB/ 206CCA which provides for an even higher rate of tax deduction/ collection if the deductee/ collectee is a defaulter in filing tax returns. The burden of ensuring this compliance is also on the deductor/ collector. Even though the government has come up with a functionality to check the list of such defaulters, the said task is onerous owning to frequent procedural checks.

The concept of deduction and collection of tax at source was introduced to reduce certain acts of tax evasion to ensure that some portion of tax is collected by the government in advance. However, law has evolved in such a way that it is causing undue difficulty to honest taxpayers and the Government has exonerated itself from this. Mere issuance of a Circular, clarifying certain questions, has in fact added to the confusion and some still remain unanswered. Evidently, the Government did not anticipate the practical difficulties in implementing and compliance of the current TDS provisions and therefore, one hopes that the Government takes the Taxpayers Charter seriously and remedial steps are taken to ease the doing of business rather than increasing cost of compliance for businesses.

**Aditi Gupta**
**SCV & Co. LLP**

Production Linked Incentive Scheme

# MANUFACTURING IN INDIA

Production linked incentive scheme (PLI scheme) aims to boost domestic manufacturing in India under the initiative of the Government of 'self-reliant India'. The aim is also to make manufacturing companies in India an integral part of global supply chains. The scheme is expected to result in a minimum production worth more than $500 billion in five years.

The scheme provides incentives to entities for enhancing their domestic manufacturing. PLI scheme offers incentives on incremental sales for specified products manufactured in India.

Thirteen sectors have been identified for PLI scheme. The scheme for respective sectors is implemented by the concerned ministries and departments.

| Sr. | Sectors | Sector vision | Outlay | Incentive |
|---|---|---|---|---|
| 1 | Automobile & Auto components | Enhance competitiveness and globalization of the industry. | 57,042 | 4% - 8% (likely) |
| 2 | Mobile Manufacturing and Specified Electronic Components | Electronics permeates all sectors of the economy, and the electronics industry has cross-cutting economic and strategic importance. | 40,951 | 1%-4% |
| 3 | Advance Chemistry Cell (ACC) Battery | Consumer electronics, electric vehicles and renewable energy sectors expected as major consumers for ACC batteries. | 18,100 | Max. 20% |
| 4 | Pharmaceutical drugs | To increase production of high value goods such as biopharmaceuticals, complex generic drugs, patented drugs or drugs nearing patent expiry, cell based / gene therapy drugs. | 15,000 | 3% -10% |
| 5 | Telecom and Networking Products | To become a major original equipment manufacturer of telecom and networking products. | 12,195 | 4% - 7% |
| 6 | Food Products | Growth of sector to provide better price for farmers and reduce high levels of wastage. | 10,900 | 4% - 10% |
| 7 | Textile Products | To boost production and export of Manmade Fibre segment and Technical Textiles. | 10,683 | 4% - 8% (likely) |
| 8 | Critical Key Starting materials / Drug Intermediaries & APIs | To boost domestic manufacturing of identified products. | 6,940 | 5% - 15% |
| 9 | Speciality Steel | Enhancing manufacturing capabilities for value added steel. | 6,322 | 4% - 12% |
| 10 | White Goods (AC's & LED) | High potential of domestic value addition and global competitiveness. | 6,238 | 4% - 6% |
| 11 | Electronic / Technology product | Promotion of data localization, Internet of Things Market in India, projects such as Smart city and Digital India to increase demand for electronic products. | 5,000 | 3% - 5% |
| 12 | High Efficiency Solar PV Modules | To reduce import dependency and boost manufacturing in the country. | 4,500 | Specified rates |
| 13 | Manufacturing of Medical Devices | To provide financial incentive to conquer the deficiencies in domestic manufacturing of medical devices. | 3,420 | 5% |

*(Outlay is INR in crores)*

For nine sectors, notification and guidelines are issued. Currently, schemes is open for Pharmaceuticals upto July 31,2021 and for White Goods (AC's & LED) upto September 15,2021. Notification and guidelines (both) are awaited for Advance Chemistry Cell Battery, Automobile and Auto Components, Textiles Products and Speciality Steel.

According to a Cabinet statement, savings, if any, from one PLI scheme of an approved sector can be utilised to fund the scheme for another approved sector.

*Salient Features of the PLI Schemes*

- The scheme specifies the target segment and the eligible products supported by the scheme. The eligibility of the applicant requires to be reviewed basis the specified products. Application may be target-segment wise, or product-wise.
- The schemes provide the threshold criterions for investments and incremental sales over the tenure of the scheme. The selected applicant is required to commit the investment amount, potential manufacturing capacity and locations, projected revenue, and incremental sales at the time of applying for the scheme.
- Investment criteria includes companies making a brownfield or a greenfield investment for the manufacturing facility, eligibility of expenditure on plant, machinery, equipment, research & development, and transfer of technology, etc. Generally, a year or two is provided for set-up of the manufacturing facility.
- The incentives offered by majority PLI schemes are a percentage of the incremental sales of the eligible product over the base year. The base year is F.Y. 2019-20 for majority of the sectors. The incentives are provided over the 5-year tenure of the scheme. A cap on the maximum incentive is provided for each selected applicant.
- The selected applicant is required to apply for disbursement of the incentive which may be submitted on a quarterly / half-yearly or annual basis. Certification for multiple details along with specified documents are to be submitted with the disbursement form. The disbursement process will involve verification of the claim, approval of the disbursement, and final disbursement.

The incentives offered under the PLI's generally recoup 50-100% of the investments made. Clear-cut and unambiguous guidelines promise a guaranteed incentive to the applicant. The schemes provide large and small investment criteria thereby rendering support to the MSME sector. Thus, the PLI schemes having a direct correlation between the incentives and upscaling of manufacturing capacities, makes it attractive to investors. The schemes implemented have received successful response from the industry.

*The entities opting for the PLI scheme, should also evaluate the incentives / benefits available under the State's Investment / Industrial Policy.*

**Amitabh Khemka**
*Lead Partner – Global Indirect Taxes*
**KNAV**

# TAXATION OF SOFTWARE

## A JOURNEY FROM DUSK TO DAWN

***"Puzzle pieces don't always connect, do they?"***

—— *Ellen Hopkins* ——

*Information Technology ('IT') industry contributed 8 percent to India's Gross Domestic Product ('GDP') in 2020. IT has changed our lives completely in the past 50 years from wired to wireless, brick and mortar to digital, physical to virtual. It has replaced the manner of communication and is involved in every walk of life from medicine to outer space, agriculture to artificial intelligence; almost everything has become smart.*

IT industry involves massive infrastructure in the form of world wide web, a network of cables, transmission and receiving equipment, satellites, operating equipment like computers et al. The backbone of IT however remains the software, a set of machine-readable commands which operate the equipment using the infrastructure to perform a desired function. Interestingly, Indian software industry has a potential to reach US$ 100 Billion by year 2025.

Taxation of software has throughout been a vexed issue in India. With a paradigm shift to GST regime, 'Taxation of software' has witnessed a 'journey from dusk to dawn'. Previously, a constant attempt was made by tax authorities to treat software as goods as well as service for levying both sales tax and service tax (despite being mutually exclusive) on the same aspect of transaction under varied scenarios. This resulted in cascading effect and posed a major challenge for taxpayers who mostly adopted conservative position by charging both taxes.

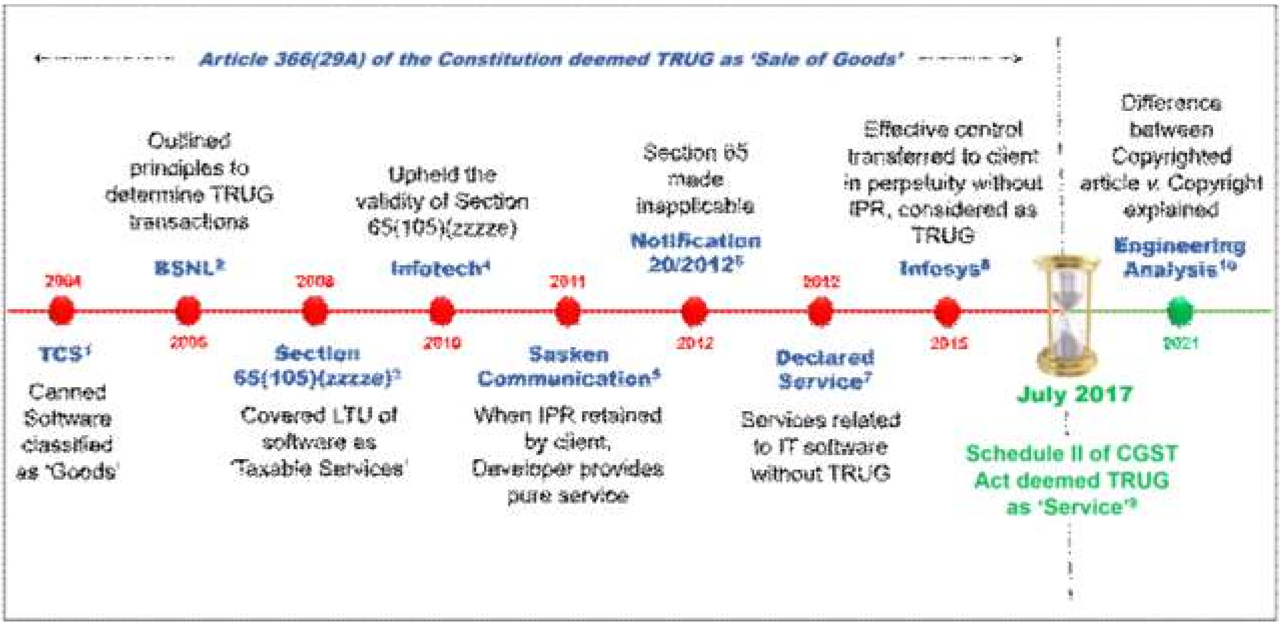
The dispute regarding classification of software was settled in the landmark judgement of TCS[1], wherein the Supreme Court classified canned software as 'goods', being capable of extraction, consumption, and use, which can be transmitted, transferred, delivered, stored etc. Medium of transmission had no influence on the classification of software. A catena of decisions dealt with various aspects relating to taxation of software without resulting in much respite for the taxpayers.

The epicenter of conflict shifted from classification to categorization of software. Clause (d) of Article 366(29A) of the Constitution of India, 1950 deemed 'Transfer of right to use goods

[1]. Tata Consultancy Services v. State of Andhra Pradesh [2004-VIL-06-SC-CB]

('TRUG')' as sale. On the other hand, 'License to use ('LTU')' goods were considered as a service under the Finance Act, 1994 leviable to service tax. All sales tax / VAT laws of states incorporated TRUG as deemed sale leviable to sales tax / VAT.

Ownership of any property is bundled with a set of rights, like right to possess, right to use / enjoy, right to consume, to destroy, or transfer, etc. While being the owner of a property, a person may transfer certain rights without transferring the ownership. In a transaction involving transfer of title in property, all the rights of owner are transferred to purchaser. On the other hand, in a transaction involving TRUG, delivery of possession of underlying goods by the transferor to the transferee is sine qua non, which is not the same as mere custody of goods.




Terms being essence of an agreement, play a predominant role in determining tax implications. Complex software agreements are more prone to litigation owing to underlying transactions in intangible goods and incorporeal subject matter. Agreements should have explicit clause to specify whether the transaction pertains to transfer of Copyright per se or transfer of Copyrighted Article.

'Copyright' and 'Copyrighted Article' are distinct subject matters. Ownership of Copyright is different from ownership of Copyrighted Article in which copyrighted work is embodied. Further, the right to commercially exploit (reproduce, replicate, etc.) and mere right to use computer software are distinct rights. When the former is transferred, it amounts to parting of copyright i.e. Intellectual Property Right ('IPR'). However, there is no transfer of copyright in the latter case. This distinction has been affirmed by Supreme Court in Engineering Analysis[10].

The concept of 'TRUG' and 'LTU' can be understood using an example. If one buys a Microsoft Office license, the person acquires a right to use and enjoy the licensed software. However, no rights vest with the buyer to replicate or commercially exploit the software or to further sub-license the software to any other person as all such rights vest with the owner (Microsoft). Microsoft retains the right to reproduce and sell more licenses, make changes in the software and/or transfer the IPR in the software itself. Therefore, the buyer acquires TRUG (software) which is nothing but a Copyrighted Article, whereas the Copyright remains with Microsoft. On the other hand, if the buyer purchases a software license which restricts the use by buyer, and control over the software remains with the owner, then in such a transaction, the buyer merely acquires LTU of software for want of effective control.

*[2]. Bharat Sanchar Nigam Limited v. Union of India & Ors. [2006-VIL-07-SC-LB]*

*[3]. Section 65(105)(zzzze) of Finance Act, 1994 read as - to any person, by any other person in relation to information technology software including:*

*i. development of information technology software*

*ii. ------*

*iii. adaptation, upgradation, enhancement, implementation, and other similar services related to information technology software*

*iv. -------*

*v. providing the right to use information technology software for commercial exploitation including right to reproduce, distribute and sell information technology software and right to use software components for the creation of and inclusion in other information technology software products*

*vi. -------*

*[4]. Infotech Software Dealers Association v. Union of India [2010-VIL-123-MAD-ST]*

*[5]. Sasken Communication Technologies Limited v. Joint Commissioner of Commercial Taxes (Appeals) [2011-VIL-67-KAR]*

*[6]. Notification Number 20/2012 - Service Tax dated June 5, 2012*

*[7]. Section 66E of the Finance Act 1994 specified 'Declared services'. Following are relevant entries:*

*c) temporary transfer or permitting the use or enjoyment of any intellectual property right*

*d) development, design, programming, customization, adaptation, upgradation, enhancement, implementation of information technology software*

*f) transfer of goods by way of hiring, leasing, licensing or in any such manner without transfer of right to use such goods*

*[8]. Infosys Limited v. Deputy Commissioner of Commercial Taxes [2015-VIL-394-KAR]*

*[9]. Schedule II of CGST Act effective from July 1, 2017. Relevant entries of Entry 5 are reiterated below:*

*c) temporary transfer or permitting the use or enjoyment of any intellectual property right*

*d) development, design, programming, customization, adaptation, upgradation, enhancement, implementation of information technology software*

*f) transfer of the right to use any goods for any purpose whether or not for a specified period for cash, deferred payment or other valuable consideration*

*[10]. Engineering Analysis Center of Excellence Private Limited v. Commissioner of Income Tax & Anr. [2021-VIL-37-SC]*

*Basis the principles laid down in various landmark judicial pronouncements under the erstwhile regime, various transactions in software have been plotted in the table below together with their tax positions in the erstwhile regime as also under GST for better understanding:*

| Scenario | Nature of Transaction | Implications under Erstwhile Regime | Implications under GST Regime |
|---|---|---|---|
| With recipient (right to use software without right of commercial exploitation - Copyrighted Article) | TRUG | Sale of goods - Article 366(29A) of the Constitution | Supply of service - Entry 5(f) of Schedule II |
| With supplier (recipient has mere access to use the software with limitations) | LTU | Provision of service - Declared service as per Section 66E of Finance Act | Supply of service |
| Remarks - The above transactions involve transfer of bundle of rights and not all rights vested with the owner. If there would have been a transfer of all rights, then the transaction would have amounted to transfer in title, which is classifiable as supply of goods. | | | |
| B. Development / Upgradation / Customization of Software | | | |
| IPR vest with recipient | Pure service | Provision of service - Declared service as per Section 66E of Finance Act | Supply of service - Entry 5(d) of Schedule II |
| IPR vest with supplier | TRUG / LTU (depending upon effective control as discussed in (A)) | If TRUG - Sale of goods<br>If LTU - Provision of service | If TRUG - Supply of service - Entry 5(f) of Schedule II<br>If LTU - Supply of service |
| Remarks - A transaction will tantamount to 'pure service' when the substance of contract provides that software which would come into existence post development, will be absolute property of the recipient since inception. | | | |
| C. Implementation / Installation Services of Software | | | |
| Mandatorily required to be provided along with main supply as under (A) and (B) | Ancillary to main supply | Classification as main supply | Classification as principal supply (being composite supply) |
| Recipient has an option to avail these services from 3rd party vendors | Pure service | Provision of service - Declared service as per Section 66E of Finance Act | Supply of service - Entry 5(d) of Schedule II |
| Remarks - In scenarios where contract provides an option to recipient to avail implementation / installation services from 3rd party vendors, such supplies will qualify to be an independent supply of services. | | | |
| D. Transfer of IPR (Copyright) | | | |
| Temporary transfer of IPR | Pure service | Provision of service - Declared service as per Section 66E of Finance Act | Supply of service - Entry 5(c) of Schedule II |
| Permanent transfer of IPR# | Transfer in title | Sale of goods | Sale of goods - Entry 1(a)[11] of Schedule II |

*[11]. Entry 1 of Schedule II of CGST Act has been reiterated below:*
*a) any transfer of the title in goods is a supply of goods*
*b) any transfer of right in goods or of undivided share in goods without the transfer of title thereof, is a supply of services*

#From the above table, disputes as regards categorization of software transactions between TRUG and LTU appear to have been settled under GST regime justifying its journey from dusk to dawn. Still the sun is hazy due to confusing multitude of entries in GST rate notifications.

On reading the relevant entries in the rate notifications, applicable GST rate is 18% for -

'

- *Permanent transfer of IPR* in respect of IT software' (Goods rate notification[12])'
- Temporary or *permanent transfer* or permitting use or enjoyment of *IPR* in respect of IT software' (Services rate notification[13])

The above entries in Goods and Services rate notifications show a clear overlap of transactions relating to permanent transfer of IPR in respect of IT software. Surprisingly, Schedule II of CGST Act specifically covers 'permanent transfer of title' as 'goods' and nowhere treats the same as 'service'. Qua the software, title is transferred through transfer of IPR. Still the transaction of permanent transfer of title has been prescribed in Services rate notification. In Authors' considered view, this entry in Services rate notification is erroneous inasmuch as it is contrary to Schedule II deeming the transaction of permanent transfer of title as 'goods' as also the entry under Goods rate notification. It will be interesting to wait and watch how the revenue authorities and Courts would classify the transactions of permanent transfer of title (i.e. IPR) in respect of IT software.

**Concluding remarks:**

With the advent of GST, classification disputes in software transactions have been settled to a large extent. But there still exists an ambiguity regarding classification of transaction as 'LTU' in absence of any specific entry under Schedule II of CGST Act and no entry under Services rate notification except for online download of software. The conundrum further continues due to overlapping entries in Goods and Services rate notifications as regards permanent transfer of title (i.e. IPR) of IT software. It will be interesting to see how this unfolds in coming times and when software transactions will see clear sunny skies.

*The article was first published on VATinfoline Multimedia [VILGST].*

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*[12]. Entry number 452P to Schedule III of Notification Number 1/2017 - Central Tax (Rate) dated June 28, 2017 states 'Permanent transfer of IP right in respect of Information Technology software'*

*[13]. Entry number 17(ii) of Notification Number 11/2017 - Central Tax (Rate) dated June 28, 2017 states 'Temporary or permanent transfer or permitting the use or enjoyment of IP right in respect of IT software'*


**Dharnendra Kumar Rana**
*Partner*
**NITYA Tax Associates**


**Parul Gupta**
*Senior Research Associate*
**NITYA Tax Associates**


**Mohit Pugalia**
*Associate*
**NITYA Tax Associates**


# Future of **GST**

*Litigations, Disputes and the entire conundrum*

**Four years of GST**

As the GST rolls over to its fifth year, the experts are deliberating on the hits and the misses of the past four years. The achievements and the delinquencies of the regime and the improvement areas are the discussions that are hovering in each conversation that happens amidst the tax experts. Another point which makes its way in these conversations is the future of GST. How does that look? In the hindsight, one may feel that the focal point or the focus of the GST Council was to streamline the compliances and automate them to the largest extent possible. This is evident from the fact that E-way bill, E-invoicing, dynamic QR code etc. have been introduced in the last four years. Moreover, the upgradation of varied

functionalities of the GSTN portal are evidences of the Government's inclination to improve the compliance experience for the taxpayers of the country. All these steps have led to streamlining of compliances with an added advantage of automation. The importance of technology and automation is not hidden. Interestingly, in the last couple of years, the Government has not only implemented automation in compliances, but has made it an integral part of its functioning especially in taxation departments whether it be assessments, litigation or refunds. The extent of use of technology is such that various departments of Ministry of Finance are now exchanging data for better administration and investigating loopholes in data furnished by assessees.

Apart from stabilising compliances, the Government has also been able to achieve other significant accomplishments which include widening of tax base thereby increasing the number of taxpayers to almost double of what it was[1]. Increased revenue collections even after the atrocious two waves of Covid-19 is another feather in the cap for the Government. However, the increased revenue can be partially said to be a result of multiple scams and frauds that have been unearthed in the past year.

If one was to identify areas which still need to be worked upon, there are plenty. One such area is the AARs, which are set up as a quasi-judicial system interpreting tax laws to provide clarifications to applicants. However, rather than providing clarifications to taxpayers, the AARs are doing exactly the opposite. Differing rulings from different state authorities is giving nightmares to taxpayers. The fact that there is no judiciary member on the AAR also raises question on the independence of the body.

Further, the frequency and the number of amendments made to the law in the past four years is mind boggling. It may actually require a software just to track these amendments and give out the impact as it beyond human powers to do so.

Furthermore, the non-inclusion of petroleum products under GST, the compensation cess fiasco, rationalisation of tax rates, problem of inverted duty structure on multiple products, are some issues but the list seems to be never ending.

Now, as we move ahead on the curve, the question is what is next?

***What's Next?***

In any tax regime once the day-to-day issues and the regular hiccups are addressed, it can be said that it is on its progression to become mature. While GST still cannot be said to be mature still, but it is safe to say that the natural progression has begun. The next step that is awaiting us all is, heavy duty litigations.

Although GST was a much-awaited reform in the country, one cannot say that it was incorporated in its true spirit. In order to obtain consensus from all states, major tweaking was done to the legislature. Also, the GST law borrows

[1] *https://www.thehindu.com/business/Economy/4-years-of-gst-regime-tax-base-has-doubled-says-nirmala-sitharaman/article35070507.ece*


ample of concepts from the erstwhile regimes which has made it prone to identical errors and drafting omissions which persisted in the earlier regimes as well. Thus, the issues that we were living with, also continue under GST on piece-meal basis. Moreover, some provisions of the law are more inclined towards punishing the law evaders than serving the honest taxpayers. In the past two years, multiple amendments made to the law suggests that the lawmakers are adamant to punish the fraudsters, even if it comes at a cost of adversely impacting the motivation of honest taxpayers. These amendments seem to have created more problems than they might have solved. This is because these are half baked with very little thought being given to the drafting, ancillary impacts and legislative backup which leads to multiple writ petitions being filed against such provisions.

*Some examples of amendments/ provisions which have already transpired into burning litigations under GST are:*

- Levy of IGST on Ocean Freight on import of goods under Reverse Charge Mechanism (RCM) was struck down by the Gujarat High Court. The revenue has filed an appeal against the said decision before the Supreme Court. Meanwhile, the assessee filed a refund claim for the IGST paid under RCM. However, the said refund application was rejected on the grounds that the law has not been amended and thus refund application would not sustain. Against such rejection order, the assessee again approached the HC. The HC has issued a notice to the revenue returnable in August, 2021.

- Issue of Transitional Credit seems to be a never-ending tussle. Even after four years of GST, there are multiple writ petitions which have been decided/ undecided in favour of/ against the taxpayers. However, no definitive conclusion has been reached as yet.

- The carry forward and utilization of Swachh Bharat Cess (SBC) and Krishi Kalyan Cess (KKC) under GST was allowed by the Madras HC; although, the division bench reversed this ruling. Further, a retrospective amendment was made to Section 140 wherein it was explained that 'eligible duties and taxes' excludes any cess which has not been specified in the Section. While the CBIC has made its view clear by introducing the retrospective amendment, the taxpayers are awaiting the matter to reach the Supreme Court to hear its verdict.

- The fundamental basis of GST was seamless credit mechanism and few credit blockages. However, the way things are moving, we are set to end up not only in a situation where substantial ITC is disallowed but also where the ITC rules would become incomprehensible. Rule 36(4), Rule 86A, Rule 86B and proposed Section 16(2) (aa) have created an unfathomable situation for taxpayers where it may take superhero powers to decode and execute the provisions in practical scenarios. Further, there are multiple writs pending in various HCs on the constitutional validity of

these provisions since they deny taxpayers their vested rights.

- The GST AAR mechanism has invited plenty of scornful comments. Right from the non-independent constitution of the AARs and AAARs to differing rules by different state AARs to not having a centralized National Appellate Tribunal for Advance Ruling (NAAAR) till date, this is a pandora's box. It's been two and half years since the NAAAR was announced vide Union Budget 2019; however, NAAAR has unfortunately not seen the light of the day. Even when NAAAR was proposed, there was a discussion on the limited scope of the rulings that it was supposed to pass - contrary rulings passed in case of distinct persons! Not sure what purpose NAAAR would have served due to the limited scope. Further, there has been no action on its constitution or no announcement on when it would come into play.

- In respect of Anti-profiteering provisions quoted as a transitory provision, one can only wonder how long will this transition period continue; especially when the revenue has fought hard against allowing transition credit to taxpayers in courts. While the time period to allow transitional credit has lapsed according to revenue, the transitory provision of anti-profiteering has been given a fresh lease of life of another two years. This step just exposes the outlook of the revenue wherein on one hand the credits that are an assessee's substantial right can be taken away after the transitory period (as this is against the revenue's interest) citing lapse of time limit, on the other hand the Government has extended the life of anti-profiteering provision (as it is in favor of the revenue). With the recent office memorandum that was issued with regards to investigations to be conducted if suppliers do not pass the benefit of GST rate reduction on covid relief items, it seems that the NAA is nowhere near its conclusion. Only a few months away from its sunset date, the Government is signaling towards another extension for the anti-profiteering authority (citing Covid as one of the major reasons). One will have to wait and watch when the Government brings the cat out of the bag!

- Absence of an appellate forum in any regime can deny justice to citizens. Surprisingly, even after four years under GST, there is no appellate court in place. GSTAT or the GST Appellate Tribunal was approved in 2019, but regrettably, the approval has only been on paper. There has been some incongruity even on the constitution of the GSTAT which does not include any judicial member. How can one expect a fair judgment from a body which only includes revenue officers! This has led to every appeal reaching the High Courts. It is no secret that the Courts are laden with legacy cases and are struggling to conclude


them. Absence of a much-needed appellate forum could worsen the situation further. As it is said – Justice delayed is Justice denied!

- Writ petitions -Left, right and Centre: Before the GST regime came into picture, write petitions were a rare sight. However, under the GST regime, writ petitions are being filed at every nook and cranny. The already burdened judiciary of the Country is facing a wave of writ petitions due to absence of an appellate tribunal under GST. Another reason for filing writ petitions is the challenge to constitutionality of multiple provisions of the law. Whether it be taxability of intermediary transactions or the provision of Detention, seizure, and release of goods and conveyances in transit, there are many provisions in the law which have been challenged in the High Courts as being unconstitutional. Even worse, multiple writ petitions are filed on the same subject at various High Courts, thus increasing the number of pending litigations unnecessarily. The industry and taxpayers cannot be blamed for such petitions. They are entitled to fair process of appeal.

***Conclusion***

While above are only a handful issues, the litigations just seem to have begun. There is a long list of such issues which, with time is only getting longer. With assessments and departmental audits being conducted, even more litigations are to follow. Moreover, GST has also witnessed its first amnesty scheme this year after merely four years of it being live. Amnesty schemes are usually rolled out after a decade of any law in force. However, the Government must have realised the need to bring in the amnesty scheme at this point in time to ensure that taxpayers can start with a clean slate post the pandemic.

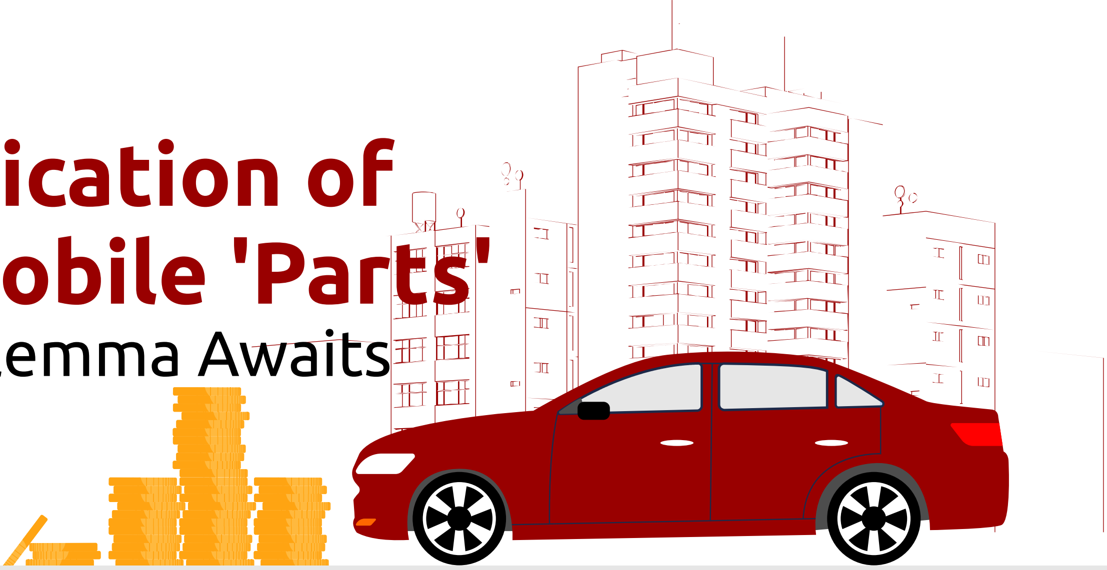
While it is a fact that none of the tax regimes are perfect; however, having the same issues persistently, rolling over from one tax era to another, is what makes it worrisome. This only means that the Government neither had the answers to the gravest of issues then, nor is it able to find them now. Constantly increasing litigations will neither benefit the taxpayers, nor the Government; it will only increase the chaos and the turmoil. This certainly goes against the Government's agenda of 'ease of doing business'. The Government needs to take reckonable steps in order to hit two birds with the same stone – to reduce litigations by resolving conflicts and bringing GSTAT to life soon and to improve the ease of doing business ranking in the world bank index which can attract FDI's in these times of financial hardships!

**Jigar Doshi**
*Founding Partner*
**TMSL**

**Nikita Maheshwari**
*Manager*
**TMSL**

# Classification of Automobile 'Parts'

## A New Dilemma Awaits



**Introduction**

Internationally, classification of goods and determination of rate of tax under Indirect tax is much simpler, as most nations have two rate tax structure. The same subject matter in India has always been sophisticated. Such complexity is primarily attributed to multi-tax structure in old regime as well as GST regime, where revenue constantly seeks classification in higher tax category. Methodology for determining classification has been persistent across different regimes, which is in principally based on International convention of Harmonized System of Nomenclature ('HSN').

Classification of 'parts and accessories' of motor vehicles is one of controversial topics under Indirect tax regime. No one is at fault for this, since classification requires a careful study of the Customs Tariff Act, 1975 ('CTA'), different Sections, Chapters, Section Notes and Chapter Notes, and a detailed perusal of HSN Explanatory Notes to rule out overlaps. Over the years, jurisprudence pertaining to their classification had largely evolved. But even now, both revenue and taxpayers often struggle to determine the correct classification and tax rate of product in question, and often end up concluding incorrectly.

This editorial aim to critically examine Supreme Court's decision in case ***Westinghouse Saxby Farmer Ltd v. CCE, 2021-VIL-33-SC-CE*** and its impact on automobile industry.

**Classification of 'part' to be determined only as per its sole or principal use?**

Recently, in ***Westinghouse's*** case, the Supreme Court held that 'relays' used in railway signaling equipment are classifiable under **Heading 8608** as 'Signaling, safety or traffic control equipment for railway' as per its predominant or sole or principal use. The Court rejected revenue's contention that product is specifically covered under Heading 8536 and Note 2(f) of Section XVII of the Central Excise Tariff Act, 1985 ('CETA')[1] specifically excludes electrical machinery or equipment covered by Chapter 85. The Court principally relied upon Note 3 of Section XVII and held that parts suitable for use solely or principally with an article in Chapter 86 cannot be taken to a different Chapter (upholding concept of group classification).

In authors' view, reasoning adopted by the Supreme Court appears to be erroneous. Note 2(f) of Section XVII of CETA clearly excludes goods of Chapter 85, but Court pronounced its decision basis Note 3 only, completely disregarding Note 2. Such interpretation will render Note 2 redundant. Further, HSN Explanatory notes also clearly provide that both Note 2 and Note 3 should be read cumulatively to determine classification of any product. However, it seems that the HSN Explanatory Notes were not placed before the Court for its consideration.

*[1] Section Notes of CETA and CTA are pari-materia*

**Entangling already untangled (earlier jurisprudence overruled)**
The verdict is likely to have ripple effect for automobile industry and has actually unsettled already settled jurisprudence involving on the principles of classification. The Supreme Court in the case of ***Intel Design Systems (India) P. Ltd v. CC&CE, 2008-VIL-72-SC-CE*** held that electric traction vehicles, fuses, switches and other electrical apparatus are classifiable under Chapter Heading 8536 even when they are used specifically, solely or principally with the armored vehicles of Chapter Heading 8710. The Supreme Court observed that for a product to be classified as 'parts' of Heading 8710, it needs to fulfil two conditions. Firstly, such 'part' must be identifiable for use solely or principally for vehicles of Heading 8710. Secondly, such 'part' must not be excluded by the provisions of Notes to Section XVII of CETA. As discussed above, these conditions are echoed in HSN Explanatory Notes. Several other decisions have adopted similar reasoning while determining final classification.

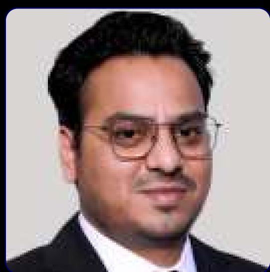
Surprisingly, this decision has not been referred by the revenue in Westinghouse's case. This will however not be of much relevance now, since the earlier judgements were of division bench and Westinghouse's case is of Larger Bench (3 judge). Hence, Westinghouse's case which will have an overriding impact on prior jurisprudence of lower bench.

**Impact on automobiles and railway sector**
While this judgment offers relief to railway parts manufacturers (which attracts lower GST rate), it will raise new classification disputes for parts of motor vehicles. Consequent to Supreme Court's decision, all parts of motor vehicles will be classifiable in Heading 8708 (barring parts wherein Supreme Court's decision can be distinguished or some reasonable basis). Automobile sector will be adversely impacted, since Heading 8708 attracts higher customs (BCD) and GST rate.

In authors' view, taxpayers are suggested to analyze impact of this decision while simultaneously seeking clarification from government. Leading automobile industry associations have approached Government in light of this ruling and sought relief, but representations from all corners will further the case and may attract Government's attention sooner. Taxpayers may also consider taking a conservative stand for future (to limit their exposure), while continuing to litigate the past.

*The article was first published on VATinfoline Multimedia [VILGST].*

**Deepak Suneja**
*Partner*
**NITYA Tax Associates**



**Rohit Kumar**
*Senior Associate*
**NITYA Tax Associates**

**Tanya Rani**
*Executive*
**NGKA & Associates LLP**

# International Treaties v. Indian Legislations vis-à-vis Rules of Origin Under Trade Agreements

*"Sovereignty must be redefined if states are to cope with globalization"*
***-Richard N. Haass***

**INTRODUCTION**

Conventional International Laws (Treaties) and Customary International Laws (State Practices) many a times lock horns. While the former is based on a consent between the State parties, the latter is formed when a State acts in a certain way due to domestic legislations or judicial pronouncements.

Recently, the India enacted Section 28DA in the Customs Act, 1962 ('Customs Act') empowering the Government to administer the Origin Rules under various Free Trade Agreements ('FTA'). Consequently, the Government has issued Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020 ('CAROTAR') enforced w.e.f. September 21, 2020.

The legality of Section 28DA and CAROTAR has become a matter of intense deliberations amongst the importers as well as International Trade professionals.

This write-up intends to shed some light on Indian jurisprudence on similar conflicts.

**LEGAL BACKGROUND**

Article 253 read with Entry 14 in List I of Seventh Schedule to the Indian Constitution empowers Parliament to make laws for the Government to enter into and implement treaties, agreements, and conventions with foreign countries.

In the absence of any such law, Article 73 extends the powers of Central Government to the constitutional

limits.

Till date, Parliament has not enacted a single standard law under Article 253. As a consequence, it is entirely left to the Executive to decide upon entering into any such arrangement and its implementation in the Country. The Central Government resorts to the Parliament only to enforce such arrangement and usually, the Parliament accepts what the Government needs.

This time, however, the Parliament interfered in the interest of the nation. Under the FTAs, India faced majorly three following setbacks:

**(I)** Fraudulent Certificates of Origin ('COO');
**(ii)** Trade Deficit with Countries where it was not expected; and
**(iii)** Unfavourable decisions by Indian Courts making FTA sacrosanct

To dilute these setbacks in future, the Parliament enacted Section 28DA empowering Government to take measures beyond what is stipulated under FTAs, thereby, raising the captioned question of law.

**POTENTIAL DISPUTES**

Of course, the biggest dispute may arise as to the validity of CAROTAR as against the observance of International commitment / obligations as required by Article 51(c) of the Constitution.

Secondly, the CAROTAR provides that the notified Rules of Origin will have the overriding effect. Can the same be said against the parent Section 28DA?

The conflicts are real and probably arise in the future as it did in the past. Of course, the list of contradiction is too large to share in a small write-up, but the ensuing paragraphs cover two such instances.

Firstly, Section 28DA(10) having non-obstante clause provides that the preferential treatment may be refused without verification where the COO is produced after the period of its expiry. However, the South Asian Free Trade Area ('SAFTA') provides that the COO submitted after its expiry shall be accepted when the failure to observe the time-limit results from force majeure or other valid causes beyond the control of the exporter.

Second instance is where Section 28DA(10) provides that preferential treatment may be rejected where complete description of goods is not contained in the COO. Indian-ASEAN FTA, however, provides that a minor discrepancy in the COO will not invalidate the COO where the origin of a product in not in doubt.

Now, it is a trite that Rules cannot override the substantive law. The

question, therefore, is not whether Section 28DA will prevail or the Rules of Origin. The question of law, instead, arises as to 'whether, in the garb of Section 28DA, the government can challenge its own Rules wherein it acknowledges the supremacy of Rules of Origin over CAROTAR?'

**INTERNATIONAL JURISPRUDENCE / LAW – TREATIES v. DOMESTIC LEGISLATIONS**

Internationally, some countries consider international law as the law of land without having transformed into a national law (known as Principle of Monism). For instance, Constitution of the United States of America states that notwithstanding anything in the constitution, all treaties with the authority of the United States, shall be the supreme law of the land and the judges in every state shall be bound thereby.

The British law is just the opposite. The Privy Council in the celebrated decision in Attorney General for Canada v. Attorney General for Ontario (AIR 1937 PC), stated that while treaties bind the State as against the other contracting parties, Parliament may refuse to perform them and so leave the State in default. In a unitary State whose Legislature possesses unlimited powers, the problem is simple. Parliament will either fulfill, or not, treaty obligations imposed upon the State by its Executive. The nature of the obligations does not affect the complete authority of the Legislature to make them law if it so chooses.

Further, Vienna Convention on the Law of Treaties, 1969 ('Vienna Convention') provides that a State cannot be excused or be relieved from compliance with the treaty entered into by them on the basis of or by reference to inadequate national law. Notable that, India has not yet signed the Vienna Convention and therefore, not binding on the Government.

From the above, it is clear that the Principle of Monism is not accepted by all the countries and the national Legislature holds the supreme powers in many jurisdictions globally.

**INDIAN JURISPRUDENCE – TREATIES v. DOMESTIC LEGISLATIONS**

Indian Courts have been following the Doctrine of Dualism in the matters concerning the captioned dispute. In ***Vishaka v. State of Rajasthan AIR 1997 SC 3011***, the Hon'ble Supreme Court noted that regard must be had to international conventions and norms for construing domestic law when there is

no inconsistency between them and there is a void in the domestic law.

Further, in the case of ***National Legal Services Authority v. Union of India [WP(C) No. 400 of 2012],*** the Apex Court held that if the parliament has made any legislation which is in conflict with the international law, then Indian courts are bound to give effect to the Indian law, rather than international law. However, in the absence of a contrary legislation, municipal courts in India would respect the rules of international law.'

Also, Supreme Court in J***olly Verghese v. Bank of Cochin (1980 (2) SCC 360)*** held that Article 51(c) of the Constitution obligates India to "foster respect for international law and treaty obligations in the dealings of organized peoples with one another". Even so, until the municipal law is changed to accommodate the Government, what binds the court is the national law and not the international law.

It is clear that judiciary in India follows an approach of Dualism whereby treaties or international laws will be upheld in the absence of a conflicting domestic legislature.

Since, Section 28DA of the Customs Act is having certain conflicts with the FTAs, it is to be seen how the Hon'ble Supreme Court will see this conflict under the taxation laws.

**CONCLUSION**

Importers in India right now are concerned with the demand of Bank Guarantees by Customs Authorities that the captioned dispute is not bothering much. The dispute, however, is inevitable going forward when the assessments will be finalized.

The Doctrines of Monism and Duality will be examined in greatest of depths on the validity of CAROTAR as against the international commitments of India.

The Customs Authorities may rest their case on the argument of Indian sovereignty to uphold the validity of Section 28DA and CAROTAR over the international commitments or obligations basis various Supreme Court decisions.

It is the taxpayers now who need to find some sharp arguments which can shake the present jurisprudence on the subject.

To conclude in the words of Mr. Bolger (Ex-PM of New Zealand) "In an interdependent world, pure sovereignty – the complete control of one's own affairs – is not possible".

***The Author's Article was first published on idt.taxsutra.com***

**YOGESH GABA**
*MANAGING PARTNER- INDIRECT TAX*
**GABA & Co**

# DEPARTMENT LOSES BATTLE AGAINST ITC REVERSAL ON MANUFACTURING LOSS

## But will there be any winners at end of war??

**Introduction**
In a recent survey carried by our firm on social media, around 85% of the people voted that issue of Input Tax Credit ('ITC') eligibility has not settled even after 4 years of GST. Not surprisingly, the industry is encountering a reality mismatch and fears that disputes relating to ITC will fill Courts in coming times.


The main reason for disputes on ITC stems from restrictions placed under Section 17(5) of the Central Goods and Services Tax Act, 2017 ('CGST Act') on eligibility of ITC; and absence of clarity on intention and scope of such coverage. This article revolves around Section 17(5)(h), which inter-alia denies ITC on **goods lost or destroyed** and dispute raised by the department on its coverage. The department denies ITC on goods lost during manufacturing activity (manufacturing normal loss), stating that Section 17(5)(h) will apply in this case.

Manufacturing loss is unavoidable and occurs majorly due to inherent nature of production operation. Inputs at time of processing may be wasted, spoiled or scrapped, and thus lost. One can also recall the cost accounting principles wherein normal loss is considered as part of direct costs.

In indirect taxation, disputes regarding availability of credit on 'manufacturing loss' were raised in the erstwhile regime too. The issue has now opened its wings in GST law as well.

**Chronicle of credit reversal on manufacturing loss in erstwhile regime**
Many VAT laws had similar provisions requiring reversal of ITC in case of goods lost, destroyed, stolen etc. Section 19(9)(iii) of the Tamil Nadu VAT Act, 2006 disallowed ITC on inputs destroyed at an intermediary stage of manufacture. Rule 7(3) of the Delhi VAT Rules, 2005 required reversal of ITC where inputs or manufactured goods were lost or destroyed. Similar provision existed in the Uttar Pradesh VAT


Rules, 2008.

The erstwhile regime had experienced ample jurisprudence where the Courts consistently held that situation of inputs consumed in manufacture is different from situation where inputs or intermediate goods are destroyed. The Courts under VAT regime thus held that credit reversal will not trigger on inputs consumed in manufacture and suffer some loss in the process. Similarly, under Central Excise as well, the Courts held that goods issued to manufacturing process and destroyed / lost thereafter will be considered as used in manufacturing process and will not warrant any credit reversal.

**Recent decisions of Madras High Court and AAAR in GST**

In case of ***ARS Steels & Alloy International Private Limited v. STO, 2021-VIl-484-MAD***, the Petitioner incurred loss of some portion of inputs during manufacturing process. The department demanded reversal of ITC on inputs lost during manufacturing process under the garb of Section 17(5)(h). The High Court observed that Section 17(5)(h) **will cover situations of quantifiable loss of inputs which involve external factors or compulsions**. The High Court held that the loss occasioned by consumption during manufacture is inevitable and hence, is inherent to the process of manufacture itself. Accordingly, ITC reversal under Section 17(5)(h) will not attract.

Similar view was expressed in the case of ***General Manager Ordinance Factory Bhandara, 2020-VIL-36-AAAR***. The Appellate Authority for Advance Ruling held that inputs once consumed in testing cannot be said to be destroyed. Once inputs are used in manufacturing process, they cease to exist and lose their identity. Thus, such inputs cannot be later considered as destroyed, lost or stolen.

We concur with the views of Madras High Court in ARS Steels and AAAR in General Manager Ordinance Factory. We believe that inputs which are used in any manufacturing process loses its identity and can be said to be used in manufacturing process, irrespective whether some portion of them are lost during the said process. The inherent nature of such goods or manufacturing process should not result in declaration of such goods as lost. **It is rather a loss in identity than a loss of inputs**.

**Will decision bring peace of mind for taxpayers?**

The modern era beings (including artificial beings i.e. corporates) crave for peace of mind. While this should be a settled position of no ITC reversal on inputs lost in manufacturing / testing process under GST regime as well, yet the issue is reaching the doors of Courts to provide relief. The decision of High Court brings some relief to the industry regarding ITC on inputs lost during manufacturing process; but also brings forth a concerning fact that department is prepared to interpret 'lost' or 'destroyed' in widest sense. The interpretation adopted by department in this case leads to distrust against the whole idea of GST being the law created for seamless flow of ITC.

Taxpayers will be concerned that questions may now commence on ITC reversal in other situations as well including abnormal loss during manufacturing activity in exceptional cases, inputs or finished goods destroyed during testing or Research & Development, control samples which are destroyed when their useful life is over. In all these cases, the goods were used for intended purposes and such activities are actually part and parcel of business processed itself and thus not lost.

The High Court did not shed light on ITC eligibility in such cases, and the Authors are concerned that department may now target any kind of loss or destruction without considering the nature / cause / circumstance in which such loss or destruction takes place. Authors feel that taxpayers should be provided clarity on intent and coverage of ITC restriction under this clause. Taxpayers may consider filing representations for seeking clarity on these points.

*The article was first published on Taxsutra.*

**Deepak Suneja**
*Partner*
**NITYA Tax Associates**

**Neha Jain**
*Managing Associate*
**NITYA Tax Associates**

**Swati Goyal**
*Associate*
**NITYA Tax Associates**

## Take Away Food from Restaurants

# A Move Away From Service Tax and GST

Service tax law initially levied a tax on purest form of services such as telecommunication services, banking services etc. where no element of supply of goods was involved. This situation drastically changed when more complex forms of services were introduced to taxation such as works contract services, restaurant service etc. which involved a substantial supply of goods. Taxation of goods, when supplied as part of service, has always been a disputed matter. Levy of service tax on restaurant service is one such classic example that would take few more years to resolve.

Restaurant service was brought within the ambit of service tax in the year 2011. TRU document of 2011 explained the scope of restaurant service. It stated that restaurant provides multiple services along with foods & beverages such as use of restaurant space & furniture, air-conditioning, well-trained waiters, linen, cutlery & crockery, music, dance floor etc. A customer can get personalised services by indicating his preference of ingredients in meals such as salts, chilies, onions, oil etc. The fundamental pillar to tax restaurant service was involvement of predominant service element in such a supply. Even the honorable Supreme Court of India gave its assent to this theory when it held that a restaurant can sell goods above MRP since a customer is paying for services not for goods.

Everything is ok when we take a classic 'Dine-in' example. However, things are little different when we take up home-delivery models, pick-up counter models, online app purchases. Let us analyse the reason.

The fundamental pillar of 'service element' is missing in all such models. In a classic takeaway model, orders are received either over telephone, by e-mail, online booking or through a food delivery service such as swiggy or zomato. Prepared meals are brought to

a separate counter and are picked up either by the customer or a delivery agent. These takeaway counters are generally positioned away from the main dining area. A customer does not get any experience of services which are available in fine-dining. Thus, supply of meals under a take-away model is a simplicator sale of goods which should not attract service tax. This subject became hotdog in 2015 and the Deputy Commission of Central Excise & Service Tax Division, Chandigarh issued a clarification confirming that service was not applicable on food sold by way of pick-up and home deliveries. The recent judgment by Madras High Court in the case of Anjappar Chettinad **A/C Restaurant**[1] upheld this view and pronounced that sale of foods under a takeaway model is not covered under the declared service of supply of food or any other article of human consumption or any drink.

Is the above situation better in GST? In view of the Author, taxing takeaway model under GST is similar to 'old wine in a new bottle' story. The GST law earnestly attempted to simplify taxation of restaurant service including takeaway but somehow failed! The main reason for this is use of many conditions & situations in taxing entry. Imagine a dish that has all vegetables from the kitchen as an ingredient. The result is obvious that it is likely to become a healthy meal rather than a chef's special dish of the day!

Entry 6(b) of Schedule II of the CGST Act treats "supply, by way of or as part of any service or in any other manner whatsoever of goods, being food or any article for human consumption or any drink for a consideration" as a composite supply of service. Service Rate Notification went a step ahead to define restaurant service to include a situation where food is taken from a restaurant and consumed away from the premises (let say at home). Thus, it targeted to cover takeaway model under restaurant service so that single GST rate can be applied on food supplied by a restaurant for consumption on its premise or away from its premises.

The use of the expression "by way of or as part of any service" created complete chaos! To qualify as service, the food needs to be supplied by way of service (such as restaurant, outdoor catering) or as part of any service (such as free food in airlines,). Thus, as a first step there has to be a service and next step would be such service includes supply of food. Wherever a service element is missing in the transaction then it can neither be a composite supply of service under Schedule II of the CGST Act nor

[1]2021-VIL-422-MAD-ST

restaurant service as per Rate Notification. This takes us back to same old situation. In takeaway model, there is no element of service. Thus, even under GST, supply of food under takeaway model needs to be taxed as simplicitor sale of food instead of restaurant service. The advance rulings in case of **Sri Venkateshwara Agencies**[2]**, Kundan Mishthan Bhandar**[3]**, Deepak & Co.**[4] **and Manoj Mittal**[5] also took the same view. On the other side, advance ruling in the case of R**ajeev Kumar Garg**[6] took a contrary view and held takeaway as supply of service. So all in all, generation changed but the dish remained same!

The above tax position is going to have a far reaching implication on restaurant services. At ground level, most of the restaurants are considering takeaway model as part of restaurant service and charging 5 percent GST. Now, this position might be challenged by the department in light of recent Madras High Court judgment (cited supra). In case restaurant wishes to adopt correct tax position then it has to maintain separate booking keeping for dine-in sales and takeaway sales. Further, as no ITC is available in 5 percent restaurant scheme, the restaurant would be required to keep a track of procurements used for preparation of meal served in dine-in and takeaway model which seems to be a big challenge as well. Furthermore, there will remain dispute on service classification in hybrid models like drive thru, takeaway establishment where the intention is supply of food as takeaway but there is a facility of air-conditioning and limited sitting space. We have to wait and watch how much masala tax authorities adds to this dispute!!

*The article was first published on Taxsutra.*


**Gaurav Narula**
*Associate Director*
**NITYA Tax Associates**

**Shubham Agarwal**
*Senior Associate*
**NITYA Tax Associates**

**Tushar Kapoor**
*Research Associate*
**NITYA Tax Associates**


*[2]2020-VIL-128-AAR*
*[3]2019-VIL-24-AAAR*
*[4]2018-VIL-29-AAR*
*[5]2021-VIL-185-AAR*
*[6]2021-VIL-18-AAR*


## Mitigating Risk and Fraud in Procurement

Digital Training on Mitigating Risk and Fraud in Procurement scheduled on 18th, 19th, 20th & 21st May, 2021 presented by Achromic Point. In this session Understanding the Context and Motivations behind Procurement Fraud and Bribery was discussed by Ajay Upadhyay , Partner- Forensic Services, Risk Consulting at KPMG, Srinivasa Rao, Partner & Leader – Risk Advisory Services at Nangia Andersen LLP shared his insights on Implementing Effective Anti-Fraud Controls. Building Effective Barriers to Procurement Fraud was taken by Varun Wadhwa, Country Compliance Officer – India at CBRE South Asia Pvt. Ltd. Vinay Garodiya, Partner at EY Forensic & Integrity Services & Pooja Roy, Director at EY Forensic & Integrity Services jointly present their thoughts on Bribery Proofing the Organisation – Tools, Techniques and Approaches.


## Data Analytics for Internal Auditors

Webinar on Data Analytics for Internal Auditors conducted on 24th, 27th, 29th May & 7th June, 2021, where it aims to give the participants an understanding of the types of data analytics, its benefits and the various standards of data analytics along with their respective limitations.
In this Vetrivelan A B, Associate Director at Deloitte Risk Advisory & Siddharth Sundararajan, Assistant Manager at Deloitte Risk Advisory shared their insights on The Data Analytics Rationale, Standard Data Analytics in Risk, Control and Internal Audit was taken by Swapna Choudhury, Associate Director at Deloitte Risk Advisory. Karthik Ramachandran, Associate Director at Deloitte Risk Advisory & Harish Venkatraman, Assistant Manager at Deloitte Risk Advisory discussed about the Use of Data through the Audit Lifecycle, whereas, Vetrivelan A B, Associate Director at Deloitte Risk Advisory & Puja Vaid, Director at Deloitte Risk Advisory spoken on Technology Trends in Data and Analytics.


# Digital Training on FEMA- Legal & Compliance

In this Digital Training on FEMA- Legal & Compliance conducted on 24th, 25th, 27th, 28th & 29th May, 2021. Here, Foreign Direct Investments was discussed by Arti Narsana, Principal Associate at Vaish Associates Advocates. was taken by Narasimhan P G, Chartered Accountant shared his views on Overseas Direct Investments by a person resident in India. Shashishekhar Chaugule, Partner, Tax & Regulatory services at Desai Haribhakti & Co shared his insights on External Commercial Borrowings (ECB), Anup Vijay Kulkarni, Principal Associate at J Sagar & Associates spoke upon Investigations by Enforcement Directorate / Compounding by RBI and the last session on Export and import of Goods and Services was taken by Manish Tyagi, Partner at MHA Legal.


# Direct Tax Summit & Awards 2021

In this Direct Tax Summit & Awards 2021 on 28th May, 2021, where the Faceless assessment, faceless CIT(A) and faceless ITAT – a case of overkill was discussed by Sachit Jolly, Partner at DMD Advocates, TDS & TCS - Compliance nightmare for companies was taken by Maulik Doshi, Senior Executive Director at Nexdigm (Formerly SKP). Naveen Aggarwal, Partner – Corporate and International Tax, India-US Corridor Leader at PMG in India & Debojit Mahanta, Associate Director at BSR & Co LLP shared their insights on Equalization Levy – Paradox in intent and scope and the USTR Investigation. Dilip Gupta, Founder & Advisor at Wecore Advisors LLP spoke upon Interplay of Transfer Pricing with GAAR and POEM. Amit Singhania, Partner at Shardul Amarchand Mangaldas & Co was gracious enough to moderate the panel discussion on Stay before ITAT, Abolition of AAR and Settlement Commission – Effect on pending litigation where his co-panelists Haroon Qureshi, Vice President – Taxes at Genpact, Alok Pareek, [CA, CS, LLB], International Tax and GST Professional & Salil Goel, Chartered Accountant also shared their insights on the same which received a lot of attention from the audience.


## Certificate Course on Practical Knowledge of Arbitration and Dispute Resolution

In this Certificate Course on Practical Knowledge of Arbitration and Dispute Resolution scheduled on 8th, 9th, 10th & 11th June, 2021, where Fundamentals of Arbitration as Dispute Resolution, Drafting and Understanding Arbitration Clauses Practical Aspect of Arbitration Law and Claiming and Proving Damages was discussed by Sujoy Datta at Vaish Associates Advocates, Surekh Kant Baxy, Associate at Vaish Associates Advocates & Sakshi Singh, Associate at Vaish Associates Advocates.


## Hands on Digital Training on Drafting Commercial Contracts

In this Hands on Digital Training on Drafting Commercial Contracts scheduled on 14th, 16th, 18th, 21st, 23rd & 25th June, 2021. Formation of a Contract, Ancillary Agreements & Payments and Interest were discussed by Isha Sinha, General Manager | Group Head – Legal at Medicover Hospitals, Saurya Bhattacharya, Partner at HSA Advocates shared his insights on Breach Remedies/Damages/Indemnities. Session on Implied & Express Terms in Contracts was taken by Ekta Bahl, Partner at Samvad Partners, Aastha Abhya, General Counsel at M2P Fintech & Adwaita Sharma, Advocate and Secretary at UNCITRAL National Coordination Committee India (UNCCI) shared insights on Welding Boilerplate. Last session on Term and Termination; Entire Agreement Clauses; Governing Law, Jurisdiction and Dispute Resolution Clauses was taken by Prashant Jain, Co- Founder & Managing Partner at Samisti Legal.


# Certificate Course on Due Diligence and Business Valuation

In this Certificate Course on Due Diligence and Business Valuation scheduled on 8th, 10th, 15th & 17th June, 2021, where the 30 Minutes Presentation on Due Diligence was given by CA Sekkizhar Balasubramanian. Aashish Verma, Director of Achromic point as a moderator along with his panelists CA Sekkizhar Balasubramanian, Yatin Narang, Associate Partner at Vaish Associates Advocates, Manish Tyagi, Partner at MHA Legal and Raghu Babu G, Co-founder at R & A Associates & Samisti Legal had a discussion on Mergers and Acquisitions, Due Diligence, When is Due Diligence Required and The Phases of Due Diligence. Yatin Narang, Associate Partner at Vaish Associates Advocates, Priyanka Jain, Principal Associate at Vaish Associates Advocates, Arnab Roy, Principal Associate at Vaish Associates Advocates. Vijaydeep Singh, Director – Transaction Advisory Services at Morison SCV Consulting Pvt. Ltd., Shashank Karnad, Partner & CEO Forensic Services at Mahajan & Aibara shared their insights on Types of Due Diligence. Last session on Business Valuation was taken by Anand Shah, Director at KNAV.


# Evolving Role of Internal Audit

In this Webinar on Evolving Role of Internal Audit conducted on 28th, 29th, 30th June, 1st, 2nd, 3rd July, 2021. Where, Shashank Karnad, Partner & CEO at Forensic Services Mahajan & Aibara shared his insights on The evolving role and future outlook of internal auditing, Conducting Audit Engagements Remotely was taken by Giridhar Janardana, Partner at BlueRidge Consulting Services. Use of Data Analytics in Internal Audit was explained by Shreyans Dudheriya, Executive Director & Leader - Risk Analytics at PwC India, whereas, CARO (Companies Auditors Report Order) taken by Monish Sharma, Director at Sudit K Parekh & Co LLP. GK Gupta, Vice President- Internal Assurance at Max Life Insurance spoke upon Synergies between the risk function and Internal Audit. Last session on Recent significant Amendments in the Companies Act was discussed by Raghu Babu G, Co-founder at R & A Associates & Samisti Legal.


## Digital Training on Goods and Services Tax (GST) & Customs

In this Digital Training on Goods and Services Tax (GST) & Customs scheduled on 12th, 14th, 17th, 19th, 21st, 24th, 26th & 28th July, 2021. Here, Chargeability and Classification ws discussed by Himanshu Goel, Associate Partner at TR Chadha & Co LLP. Ravikumar Yanamandra, Director at Ernst & Young shared his insights on Analysis and Issues in Place of Supply and Time of Supply & Input Tax Credit ('ITC') and related issued. Abhishek A Rastogi, Partner at Khaitan & Co. spoke upon Writ petitions including anti-profiteering and credits, Refunds under GST explained by Yogesh Gaba, Managing Partner- Indirect Tax and International Trade at GABA & CO., Session on Valuation and contentious issues was taken by Sandeep Chilana, Managing Partner at Chilana & Chilana law offices. Appeal, Revision, Offence, Penalty, Inspection, Search, Seizure, and Arrest in GST was discussed by Ranjeet Mahtani, Partner at Dhruva Advisors LLP & Customs & Foreign Trade Policy by N V Raman, Founder Partner at NOVELLO Advisors LLP.


## Labour Codes - Key Issues and recent Amendments- 2nd Edition

In this Webinar on Labour Codes - Key Issues and recent Amendments- 2nd Edition conducted on 23rd, 24th, 30th & 31st July, 2021. Here, Sessions on Wages, Social Security, Industrial Relations & Health & Working Conditions was discussed by Savitha kesav Jagadeesan, Senior Resident Partner at Kochhar and Co. & Gaurav Chatterjee, Partner at Kochhar and Co.

# Upcoming Events – 2021


## White Collar Crime: A Corporate Perspective
## A Certification Programme

**9th August 2021**– Session 1 **|** **11th August 2021**– Session 2 **|** **13th August 2021**– Session 3 **|** **16th August 2021**– Session 4 **|** **18th August 2021**– Session 5 **|** **20th August 2021**– Session 6

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## Demystify the Ind AS /IFRS –
## A digital training on practical aspects

**23rd August 2021**– Session 1 **|** **24th August 2021**– Session 2 **|** **25th August 2021**– Session 3 **|** **26th August 2021**– Session 4 **|** **27th August 2021**– Session 5

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## Internal Auditing - A Virtual Training Course

**6th September 2021** – Session 1 **|** **7th September 2021** – Session 2 **|** **8th September 2021** – Session 3 **|** **9th September 2021** – Session 4 **|** **10th September 2021** – Session 5

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## Workshop on Data Privacy, Digital Forensics and Cyber Investigations

**14th September 2021** – Session 1 **|** **15th September 2021** – Session 2 **|** **16th September 2021** – Session 3 **|** **17th September 2021** – Session 4

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## Certificate Course on International Tax

**14th September 2021** – Session 1 **|** **16th September 2021** – Session 2 **|** **21st September 2021** – Session 3 **|** **23rd September 2021** – Session 4 | **28th September 2021** – Session 5 **|** **30th September 2021** – Session 6 | **5th October 2021** – Session 7 **|** **7th October 2021** – Session 8

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## Virtual Conference on Insolvency and Bankruptcy Code in India (IBC)

**5th October 2021** – Session 1 **|** **7th October 2021** – Session 2 **|** **12th October 2021** – Session 3 **|** **14th October 2021** – Session 4 | **19th October 2021** – Session 5 **|** **23rd October 2021** – Session 6

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**Achromic Point Consulting Pvt. Ltd.**
F-11, First Floor, Kalkaji,
New Delhi - 110019, India
T: (O) +91-11-2628-1521
E: feedback@achromicpoint.com