Legal Decisions[1]

Income Tax

LD/66/139

Multi Commodity Exchange of India Ltd.
vs.
Dy. Commissioner of Income Tax
23rd February, 2018

Reassessment initiated beyond 4 years period upheld based on special audit report

The assessee is electronic spot exchange for commodities. Regular assessment proceedings were completed in case of assessee for AY 10-11 under Section 143(3). A special audit was directed by the Forward Market Commission (FMC) in the affairs of the assessee-company from inception till 30th September 2013. Subsequently, based on the special audit report of Price Water House Coopers Private Ltd. (PWC), AO issued notice under Section 148 to re-open the assessment for AY 2010-11, recording his reasons. The assessee contended that the AO was without jurisdiction to reopen the assessment beyond 4 years' time particularly when regular assessment was also made. Aggrieved, assessee filed this writ petition before the High Court.

High Court observed that the special audit report was not available during the regular assessment order. As per High Court, special audit report was the fresh tangible material available with the AO and on examination of the same, AO found that claims made by the assessee for deduction and expenditures were excessive and to that extent the claims made were *prima facie* bogus. High Court relied on ruling in *Phool Chand Bajrang Lal & Anr* [2013 ITR 456], wherein it was held that, "*Where the transaction itself, on the basis of subsequent information was found to be a bogus transaction, the mere disclosure of that transaction at the time of the original proceedings could not be said to be a disclosure of "true" and "full" facts and the Officer would have jurisdiction to reopen the concluded assessment in such a case".* High Court stated that assessee could not take shelter of the first proviso to Section 147. Further, the reasons recorded do indicate that the special audit report dated 21st April 2014 was the basis of the reopening notice and thus it cannot be said that the Assessing Officer did not have reasonable belief that prima facie income chargeable to tax has escaped assessment.

Further, on the issue of whether there was a borrowed satisfaction by the AO from the special audit report, High Court stated that the special audit report was the tangible material which formed the basis of the AO's reasonable belief and thus there was an appropriate application of mind by the AO.

The assessee further contended that the special audit report of April 2014 was for purposes other than to detect tax evasion, because of which it could not be relied upon for purpose of issuing impugned notice. High Court stated that power of the AO to reopen an assessment under Section 147/148 on the basis of reasonable belief was not fettled or circumscribed, to be formed only on material found during a tax audit or with material found during examining a case of tax evasion. In fact the basis of fresh tangible material is unqualified i.e. the source of the material could be from any place, however, the only pre-condition is that on the basis of the material so found/obtained by the Assessing Officer, he himself must form a reasonable belief that income chargeable to tax has escaped assessment before issuing a notice for reopening.

Separately, High Court observed that the fact that criminal proceedings initiated on the basis of special audit report were quashed was irrelevant. High Court further observed that the AO had disposed the objections raised by assessee against reopening of the case in some detail only after which he had found them to be unacceptable. Thus, there was no non-application of mind while disposing of objections.

While concluding the matter, High Court stated that though the orders of assessment passed under Section 143(3) had sanctity attached, it did not grant immunity to an assessee from proceedings for reopening of assessment of Section 147/148, provided the jurisdictional requirements therein were satisfied, at the time when the reopening notice was issued.

High Court thus ruled in favour of Revenue.

[1] *Contributed by CA. Sahil Garud, CA. Mandar Telang, Indirect Taxes Committee, Committee on International Taxation, Insolvency and Bankruptcy Laws Group, Disciplinary Directorate and ICAI's Editorial Board Secretariat.*
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LD/66/140

Commissioner of Income Tax
vs.
Dr. Vandana Gupta
20th February, 2018

Concealment penalty under Section 271(1)(c) upheld though assessee declared additional income voluntarily, since assessee failed to offer any explanation as to the nature of income or its source

The assessee filed her return of income for declaring a total income of ₹9.18 lakhs. A survey was conducted under Section 133A at the business premises of assessee and the assessee surrendered ₹2 crores and filed a revised return declaring this amount as an additional income. The AO initiated penalty proceedings for concealment of income which was affirmed by the CIT(A). ITAT ruled in favour of assessee holding that assessee disclosed this income in the revised return based on voluntary statement made by her. Aggrieved, Revenue filed an appeal before the High Court.

High Court referred to SC ruling in *MAK Data Pvt. Ltd.* [(2014) 1 SCC 674] and noted that the facts of that case had a close bearing with facts of this case. The SC had held that *"The AO, in our view, shall not be carried away by the plea of the assessee like "voluntary disclosure", "buy peace", "avoid litigation", "amicable settlement", etc. to explain away its conduct.... We are of the view that the surrender of income in this case is not voluntary in the sense that the offer of surrender was made in view of detection made by the AO in the search conducted".*

High Court observed the assessee merely made a voluntary surrender and had not offered any explanation as to the nature of income or its source. There was complete failure to furnish any details with respect to the nature of income, and had the assessee given the same, that could have become a reasonable basis for deletion of penalty. High Court thus upheld the stand of Revenue that the revised return was an afterthought, based on the subsequent event of disclosure of ₹2 crores.

High Court analysed Explanation 1 to Section 271(1)(c) and observed that an assessee was not absolved of penalty, if he *"offers an explanation which he is not able to substantiate and fails to prove that such explanation is bona fide and that all the facts relating to the same and material to the computation of his total income have been disclosed by him".* Thus, mere offer of the amount during the search in the absence of any explanation for the source of income rendered the assessee's argument insubstantial.

Thus, High Court delivered the ruling in Revenue's favour.

LD/66/141

Salora International Ltd.
vs.
Commissioner of Income Tax, New Delhi
20th February, 2018

Penalty order levying concealment penalty under Section 271(1)(c) quashed by High Court since pass penalty order within 6 months from the date of receipt of CIT(A) order

The assessee had declared loss of ₹4.61 Lakhs for AY 1989-90 whereas the AO made a computation of the book profits of ₹4.73 lakhs and determined its liability at ₹1.42 Lakhs. The assessee preferred an appeal to the CIT(A) which was partly allowed, and the order of the CIT(A) was accepted by the assessee. The order of CIT(A) was served on the assessee on 21/01/1994. The Revenue had appealed before the ITAT against CIT(A)'s deletion of certain additions, however the appeal was later withdrawn by the Revenue. The order of ITAT permitting the withdrawal was made on 31/03/1997. In the meantime, penalty proceedings under Section 271(1)(c) were intiated.

The assessee contended that penalty proceedings were time-barred as per Section 275(1)(a) since penalty cannot be imposed after six months from the end of the month in which the order of the CIT (A) was received, which ended on 31/01/1994. The AO passed penalty order on 25/11/1997. CIT(A) ruled in favour of assessee holding wherein he noted that if an appeal is filed and not effectively pursued and the same is withdrawn thereafter, then it will cancel the effect of having been an appeal, which is the same as not preferring an appeal. Therefore, CIT(A) deleted the penalty. ITAT however ruled in favour of Revenue stating that the period of limitation available to the AO under Section 275(1)(a) is a period of six months from the date on which the order of the Tribunal permitting the withdrawal was received by the department.

High Court perused Section 275 and observed that the expiry of six months period is to be considered from the date of completion of proceedings or from the end of the month in which the 'order' of the CIT(A)/ITAT is received. Going by the intent of the provision, the order must be an adjudicatory

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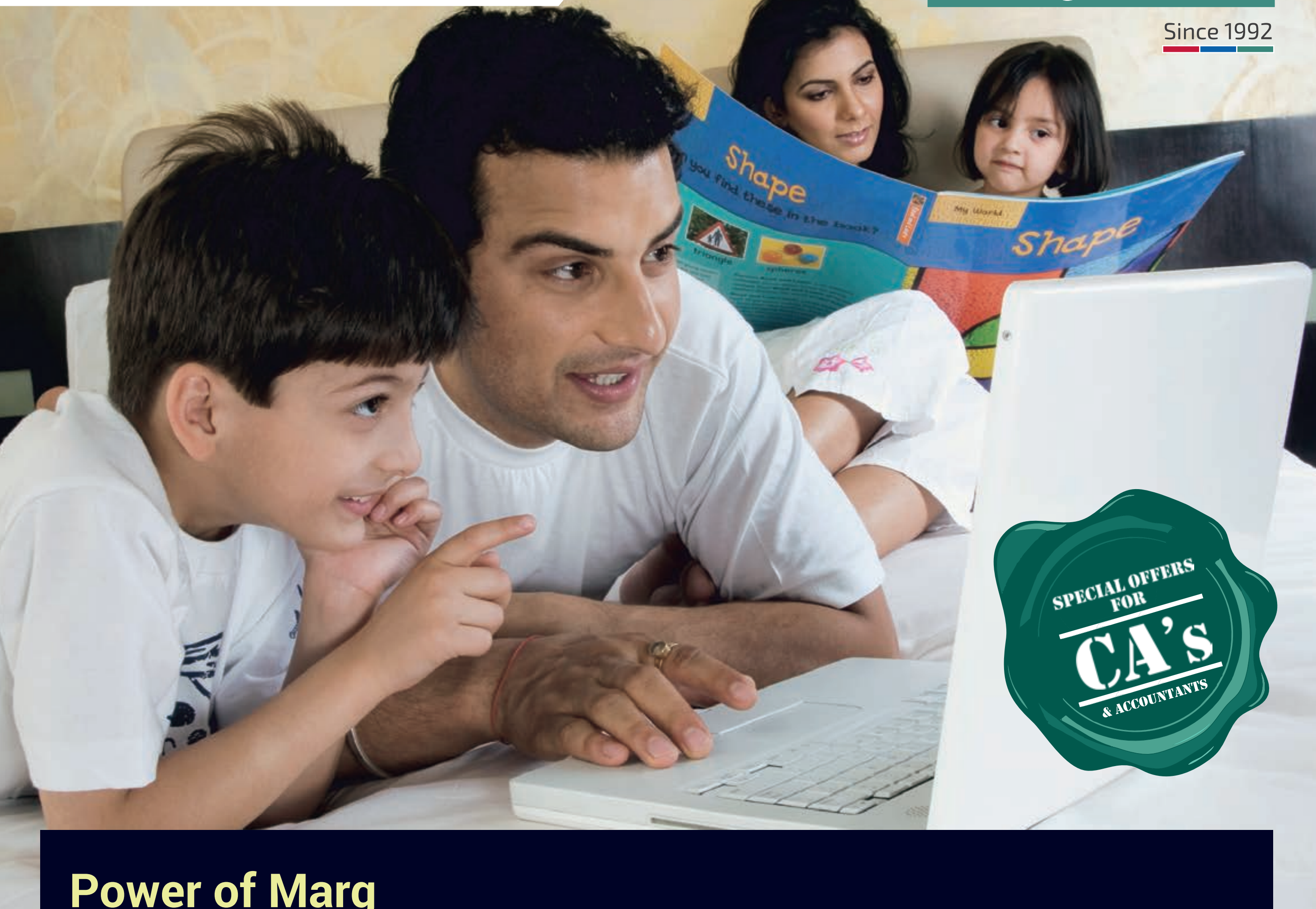

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order that culminates in "the proceedings" that is to be deemed a terminus quo for the completion of penalty proceedings. As per High Court , any other interpretation of the 'order' would inject a great deal of uncertainty because in either case of maintainability of an appeal preferred by either the revenue or the assessee, in the eventuality of withdrawal of that appeal, without an adjudicatory order, the period of limitation would be deemed to subsist. High Court remarked that an interpretation of the 'order' that permits certainty should be adopted rather than an interpretation that makes the legal position inchoate and unsatisfactory.

Absence of an appeal by the assessee against the CIT(A)'s order meant that at least with respect to the amount of addition that it had accepted, the penalty proceedings survived, and it was incumbent upon the Revenue to complete the penalty proceedings and pass order within the six months period.

High Court thus rejected the Revenue's contentions and ruled in favour of assessee.

LD/66/142
Kantibhai Naranbhai Prajapati.
vs.
Income Tax Officer
15th February, 2018

When original basis of imposition of penalty were altered in appeal, the basis for sustaining penalty is rendered non-existent; Section 271(1)(c) penalty deleted.

During the course of assessment proceedings, the A.O. found that the assessee had failed to provide explanation/to prove the sources of cash deposits to the extent of ₹25 Lakh, and thus the A.O. made an addition thereof as unexplained cash credit, and penalty proceedings were also simultaneously initiated. Applying the peak credit theory on such deposits, the CIT(A) restricted the addition to ₹12 Lakh. CIT(A) confirmed the penalty on the ground of 'furnishing inaccurate particulars of income' rather than on the ground of 'concealment of income'.

ITAT noted that the basis and foundation for imposition of penalty was altered by the CIT(A) since penalty was confirmed on a different premise. The original satisfaction for imposition of penalty has been altered in a significant way by the appellate authority and thus the very basis for sustaining the penalty is rendered non-existent. The ground for action by AO was allegation of 'concealment', which was substituted by CIT(A) to 'furnishing inaccurate particulars of income'.

Thus, ITAT held that in the absence of continuity in the findings of the AO and the CIT(A), the order of the penalty passed by the AO is liable to be struck down on this ground alone. ITAT relied on Gujarat High Court's rulings in *New Sorathia Engineering Company* [(2006) 282 ITR 642(Guj.)] & *Manu Engineering Works* [(1980) 122 ITR 306 (Guj.)] to hold that where concurrent Income Tax authorities were not sure about nature of default, the penal action under Section 271(1)(c) was not sustainable in law.

Thus, ruling in favour of the assessee, ITAT deleted the penalty action under Section 271(1)(c).

LD/66/143
Pavankumar Sanghvi.
vs.
Income Tax Officer
12th February, 2018

Addition under Section 68 confirmed despite confirmation from lender.

The assessee had received unsecured loans of ₹10 lakhs each from two lenders. Doubting the genuineness of the transaction, AO made an addition of ₹20 lakhs as unexplained credits under Section 68 of the Act. The assessee had also made interest payments against these loans which were also disallowed resultantly by the AO. The CIT(A) as well as ITAT ruled in favour of Revenue.

With respect to a lender, ITAT observed that the Bank statement of that was showing a credit of ₹10,00,000/- just before the cheque to assessee was paid. The bank balance before these two transactions, and after these two transactions, was only ₹13,000. As per ITAT, this kind of the state of bank account does not inspire any faith in the proposition that the entity in question is a genuine business concern. ITAT noted that the lender had shown a turnover of ₹122.92 crore but there was no closing stock, and with equivalent amount of purchases, there was a profit of only 0.09% and a tax payment of ₹1.96 lakhs by that lender. ITAT observed that at such a scale of operations of the lender, there were no travelling or telephone expense, and entire expenses of the business, except on brokerage and assortment of diamonds, were less than ₹5 lakhs in a year. The level of turnover and the expenditure incurred on achieving such high turnover did not match at all. For the other lender also, the ITAT noted that there was a similar trend of high transactions during the day and a consistently minimal balance at the end of the working day. As per ITAT, it was not a representative of what a genuine business would be. Thus, the ITAT had confirmed the addition, aggrieved by which, the assessee had filed an appeal before High Court.

High Court rejected assessee's contention that since the amount came through banking channel and the audited accounts of lenders were filed before the AO, the genuineness of the transaction, the capacity of the lender and the factum of lending were established. High Court stated that since the Tribunal had minutely examined the position of the lenders, the circumstances under which, the amounts were allegedly loaned to come to the conclusion that the transactions were not genuine, the High court had no reason to interfere.

High Court thus dismissed assessee's writ and ruled in favour of Revenue.

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LD/66/144

Asst. Commissioner of Income Tax

vs.

Agra Development Authority

07th December, 2017

Amended Section 12AA(3) does not authorise Commissioner to cancel charitable trust's registration from retrospective effect.

The assessee trust was granted registration under Section 12A with effect from 01/04/2003 and since then assessee claimed exemption for many years thereafter. As per Revenue, assessee's activity was clearly in the nature of trade and business activities, and it did not fall within the meaning of the term "charitable purpose" as defined under Section 2(15). Thus, by order dated 04/02/2012, the CIT cancelled registration of assessee w.e.f. AY 2009-10, holding that amendment made to Section 12AA(3) w.e.f. June 1, 2010 gave the power to cancel assessee's registration with effect from an earlier year. ITAT ruled in favour of assessee, aggrieved by which the Revenue filed appeal before the Allahabad High Court.

Revenue relied on Bombay High Court ruling in *Sinhagad Technical Education Society* [(2012) 343 ITR 23] which was rejected by High Court noting that Bombay High Court had not decided the issue whether CIT could issue a notice under Section 12AA(3) to cancel a registration under Section 12A or 12AA with retrospective effect.

High Court observed that assessee was granted registration under Section 12A by assessing authority in accordance with law for all past assessment years from 01.04.2003. Further, nowhere it was alleged that assessee had obtained registration by practicing fraud or collusion or concealment of any material fact. Registration was granted to the assessee much prior to the introduction of the first proviso to Section 2(15) and hence on the date of grant of registration, the assessee was fully eligible for the registration.

High Court observed that registration order cannot be allowed to be cancelled with retrospective effect so as to affect past transactions that too in absence of any express legislative intent and without any adverse inference being first drawn against the assessee. In view of the above, High Court relied on co-ordinate bench case in *Shivalik Cellulose Ltd.* [1992 U.P.T.C.-1], wherein cancellation of registration was upheld but retrospective cancellation was categorically struck down.

High Court observed that nowhere in the language of Section 12AA(3) it was suggested that registration of the assessee may be cancelled with retrospective effect. High Court held that the use of the words, *'or have obtained registration at any time under Section 12-A of the Act'* added by amendment w.e.f. June 1, 2010 only indicated that CIT was vested with the power to cancel a registration that may have been granted to an assessee at any time prior to the aforesaid amendment itself. As per High Court, CIT is however not empowered to cancel the registration with retrospective effect from a date prior to the date of issuance of the order/notice to cancel the registration. High Court held that cancellation of the assessee's registration under Section 12-A of the Act, if at all, could be done only prospectively and not retrospectively.

High Court held that ITAT should have examined whether the assessee was engaged in a charitable activity covered under Section 2(15) and ITAT should not have set aside the entire order as it did.

High Court observed that the law neither contemplates an inviolable right to claim exemption solely on the strength of a registration certificate nor does the Act appear to contemplate that in case of an opinion being formed by the Commissioner that an assessee is engaged in an activity specified in the first proviso to Section 2(15) of the Act, he must necessarily seek to cancel the registration granted by him earlier. In fact, the Act carves out a middle path by allowing the registration to stand but it's benefit to be deprived in assessment proceedings in certain specified circumstances.

High Court thus ruled in favour of assessee on the aspect of cancelling the registration with retrospective effect.

On the issue of validity of notice proposing cancellation of registration and subsequent order of cancellation being invalid, High Court held that it did not suffer from any jurisdictional error. Merely because the Commissioner had wrongly given effect to such cancellation w.e.f. A.Y. 2009-10, it did not vitiate the entire order. High Court however remitted back the matter to ITAT to decide the issue on merits. High Court thus ruled in favour of Revenue on this aspect.

Transfer pricing

LD/66/145

Prin. Commissioner of Income Tax

vs.

M/s Oracle (OFSS) VPO Services Pvt. Ltd.

05th February, 2018

Related Party filter is relevant and fits in with the overall scheme of a transfer pricing study; If a particular entity predominantly has transactions with its AE in excess of a certain threshold percentage its profit making capacity may result in a distorted picture; Comparables suggested by Revenue rejected.

The assessee in its return for Assessment Year 2007-08 reported three categories of international transactions with its Associated Enterprise ("AE") namely 'provision of services', 'recovery of expenses', and 'sale of call manager phones'. The assessee chose to benchmark the transactions using Transactional Net Margin Method ('TNMM') to be the most appropriate method for the determination of arm's length price ('ALP'). TPO agreed with this method but excluded 13 of the 22 comparable companies selected by assessee on the basis that they were not premised upon the relevant single year data but rather based upon multiple years' data. The OP/TC yielded an operating margin to the AE at 11.61% (within the tolerable range of +/-5% of the three years weighted average of OP/TC), which was computed at 12.51%. The average margin considered by the TPO of comparables was 22.09%. Accordingly the TPO made an upward adjustment of ₹3,25,93,468/-.

DRP, in its fresh exercise excluded 4 comparables to arrive at an average margin of comparables at

23.62% and thus increased the adjustment to ₹7.32 crores.

ITAT deleted the adjustments made by DRP. ITAT took into account the RPT and excluded certain comparables by applying a broad ballpark threshold of taking into account the functioning and profits of comparable entities, whose unrelated transactions were in equal to or in excess to 75% of their business.

Before High Court, Revenue argued that the deletion directed by ITAT, based upon its application of the RPT filter and the exclusion of the comparable Wipro Limited was an error of law.

As per High Court, the RPT filter, is relevant and fits in with the overall scheme of a transfer pricing study which is premised primarily on comparing light entities having similar if not identical functions. Therefore, if a particular entity predominantly has transactions with its associate enterprise – in excess of a certain threshold percentage, its profit making capacity may result in a distorted picture, either way. High Court noted that ITAT was of the opinion that a broad threshold figure of 25% RPT in the case of comparables was essential. Applying that rationale, the ITAT excluded some comparables listed in the TPO's report. As per High Court, there is no error of law per se in this approach.

With respect to the exclusion of Wipro Limited as a comparable, High Court noted that ITAT had excluded the company for having high brand value. High Court stated that brand value of an entity has a significant role in its ability to garner profits and negotiate contracts. While considering the comparables, the likelihood of profits derived or attributable to the brand having regard to the consistency of the quality of services that an entity is able to offer would be relevant; although functionally, the two entities may be similar in terms of the services or products they offer, brand does play its own role in price or cost determination. High Court thus affirmed ITAT's ruling on this aspect.

Ruling in favour of assessee, High Court thus dismissed Revenue's petition.

LD/66/146

Daimler India Commercial Vehicles Private Limited
vs.
Dy. Commissioner of Income Tax
30th January, 2018

Reassessment proceedings under Section 147 *quashed since assessee had made full disclosure in form 3CEB filed by it and thus onus had shifted on the AO.*

During the assessment proceedings for AY 2009-10, assessee's case was referred to the TPO under Section 92CA(1) for determination of the arm's length price (ALP) of assessee's international transaction with its associated enterprises (AEs). The TPO, vide order dated 27/12/2012 accepted ALP of the international transactions. Thereafter, AO completed the assessment vide order dated 25/02/2013 under Section 143(3) and assessed the total loss of the assessee after making certain disallowances. Subsequently, AO sought to reopen the assessment under Section 147 stating that he had reasons to believe that the assessee's income chargeable to tax had escaped. The AO dismissed objections filed by the assessee against such reopening, aggrieved by which the assessee filed the instant writ petition before the High Court.

Revenue submitted that the assessee proposed to start commercial production of vehicles in the year 2012 and noted that assessee was approaching the ICICI bank for obtaining a loan of ₹2,200/- crore for it. The AO observed that during instant AY 09-10 which was the pre-production period, the expenditure incurred by the assessee such as interest on loans, commitment charges, project appraisal fee, loan processing fees in whatever name it is called, formed part of capital employed in industrial undertaking. The Revenue submitted that the assessee had not fully and truly disclosed the material fact that they had not commenced its business during the year and mere production of the account books or other evidence before the AO would not necessarily amount to disclosure within the meaning of the explanation (1) of Section 147 of the Act. Revenue rejected assessee's stand that the required information was mentioned in Form 3CEB submitted before the TPO, stating that it was TPO's scope to go into Form 3CEB, and not the AO's.

As per High Court, mere escape of income is insufficient to justify the initiation of action after the expiry of four years. Such escapement must be by reason of the failure on the part of the assessee to truly and fully disclose the material facts necessary for the assessment. High Court remarked that the duty of assessee was only limited to fully and truly disclosing all the material facts and is not required to prepare a draft assessment order. High Court rejected Revenue's reliance on decision in *A.L.A Firm* case [1991 (55) taxmann 497 (SC)] stating that it was as per pre-existing law. High Court further rejected Revenue's contention that it was not necessary that the information based on which reopening was made, must be extraneous to the record. Further, High Court acknowledged that declaration of law in *A.L.A. Firm* was of the pre-existing law and the law as existed was dealt with in *Kelvinator of India*.

High Court noted that TPO considered this issue and while passing the order specifically recorded that the commercial production proposes to start in the year 2012. Assessee had argued that this material was available and considered by the AO as could be seen from the scrutiny assessment order of AO. High Court rejected Revenue's stand that it was not AO's duty to look into Form No. 3CEB and it is for the TPO, to take note of the same. High Court stated that even assuming that the Assessing Officer did not look into the Form No. 3CEB, he is bound to look into the order passed by the TPO, since he is required to see whether any other additions have been made, and further since order of TPO is binding on the AO.

High Court observed that Revenue had initiated the re-assessment proceedings purely based on existing information provided by the assessee in the course of original assessment and based on the return of income and documents filed for the subject year. Thus in the absence of any new material in the hands of the Assessing Officer or discovery of some materials or a new insight after the completion of the original assessment, the question of reopening does not arise. The impugned reopening proceedings was a clear case of change of opinion as there was full and true disclosure by the assessee at the time of scrutiny assessment/original assessment.

High Court thus ruled in favour of assessee.

Customs

LD/66/147

Royaloak Furniture India LLP
vs.
Additional Director General Directorate Revenue Intelligence
30th January, 2018

Tax payers have no right to choose their adjudicating authority

The assessee filed instant writ petition on the twin grounds of validity of provisions of Section

28(1) of Customs Act, 1962 and on the issue of lack of jurisdiction of Revenue to issue the said show-cause notice in that regard.

Assessee placed its reliance on SC ruling in case of *Commissioner of Customs vs. Sayed Ali* [2011 (265) E.L.T.17 (S.C.)] wherein it was laid down that it is only the officers of customs who have the jurisdiction to issue notice under Section 28, therefore the authorities belonging to the Intelligence Wing, who are the authorities assigned the function of preventing evasion of duty do not have the power of assessment under the Customs Act. Assessee submitted that Section 28(11) inserted w.e.f. 16/09/2011, does not remove this defect, and therefore as per the assessee, said provision of Section 28(11) of the Act itself is ultra vires and liable to be struck down by this Court.

High Court observed that the provisions of Section 28(11) of the Act were illegal or ultra vires, and the same were issued as per the well-settled legislation practice of undoing the effect of the judgments of the Constitutional Courts by removing the defects pointed out by the Courts of law in consonance with legislative objects sought to be achieved.

High Court referred to SC ruling in *Sayed Ali* case [supra] wherein it was held that if the Revenue's contentions that once territorial jurisdiction is conferred, the Collector of Customs (Preventive) becomes a "proper officer" in terms of Section 28 of the Act is accepted, it would lead to a situation of utter chaos and confusion, in as much as all officers of customs, in a particular area, be it under the Collectorate of Customs (Imports) or the Preventive Collectorate, would be "proper officers". High Court stated that since the Court found that the Revenue's contention that once the territorial jurisdiction is conferred, the Collector of Customs (Preventive) becomes a 'proper officer' in terms of Section 28 is not acceptable, the Parliament had no option, but to declare even these Anti-evasion Wing officials to be 'proper officers' to legally vest them with the jurisdiction to undertake the proceedings for assessment. Accordingly, provisions of Section 28(11) were inserted on 16/09/2011, soon after a decision of SC in *Sayed Ali's* case, otherwise, it would have resulted in quashing proceedings based on lack of jurisdiction and would have rendered several SCNs and proceedings liable to be quashed on the technical and narrow ground of lack of jurisdiction.

High Court stated that deeming of all designated officers to be 'proper officers' for undertaking the assessment proceedings, cannot be said to be unguided power conferred upon the authorities of concerned Revenue Department. It is left to the concerned Revenue Department itself to bifurcate, assign and divide its jurisdiction amongst its several designated officials. Nobody can deny that these authorities work for the ultimate object of implementation of the Customs Act, 1962. The tax payers have no right to choose their adjudicating authority. High Court noted that in view of multiple imports by the same assessee which may be in the different territories of India, the conferment of jurisdiction on all the authorities on pan India basis for the smooth functioning and discharge of their duties is not only necessary and essential but also appropriate.

High Court thus rejected striking down of Section 28(11) of the Act and left it to the concerned Commissioner to adjudicate the show-cause notice in accordance with law. Further, since the assessee had not filed any reply or objections to said show cause notice before Principal Commissioner/Commissioner of Customs, the challenge to such notice by the assessee was 'premature'.

VAT

LD/66/148
M/s J.C. Industries
vs.
State of Karnataka
16th January, 2018

Writ petitions challenging reassessment order under Section 39(1) quashed by High Court holding that there was no breach of natural justice principles.

The assessee had filed writ petition under Article 226 and 227 challenging the impugned re-assessment order under Section 39(1) of Karnataka VAT Act for the period of April 2012 to March 2013. The only ground raised before this Court is the alleged breach of principles of natural justice in as much as the adverse material was not confronted to the petitioner and merely on the basis of a Investigation Report, the disallowance of 'Input Tax Credit' was made by the Assessing Authority. Also, no opportunity had been given to controvert the issue whether the alleged selling dealer was bogus or not.

As per Revenue, there was a selling dealer which was bogus and non-existent and was indulging in only giving "sales invoices" and there was no actual movement of goods and sales to the assessee, who was engaged in the sale of Aluminium False Ceiling, Wall Cladding etc. and who had claimed ITC inter alia on the alleged purchases of PVC laminates, Fire rated door plain glass, pre-laminated sheets and Mineral Fiber Tiles etc. Hence, the reassessment order was passed by the assessing authority raising the demand.

Having heard the parties, High Court was of the view that the writ jurisdiction could not be invoked by the assessee in the current circumstances.

High Court observed that on a perusal of the Proposition Notice itself it is clear that the Respondent-authority has specifically mentioned the purported disallowance of Input Tax Credit in respect of the purchase invoices. It was noted that seller had not filed any returns with the Dept. and therefore construing the same to be a bogus dealer, the ITC was proposed to be disallowed in the hands of the assessee. From the investigation by the Revenue, the assessing authority had come to the conclusion that the seller existed only on papers and there were no actual sales of goods to the assessee. Thus, the Revenue had sufficiently discharged their burden while disallowing concerned ITC in respect of sales invoices and the onus entirely shifted on the assessee to remove such suspicion, by producing the said dealer during the assessment proceedings. The burden in such cases could not be assumed to be lying upon the Assessing Authority in this regard, since the enquiry conducted by them resulted in the conclusion that such a dealer did not even exist. There could not be said to be any breach of principles of natural justice in the course of such assessment proceedings resulting in the disallowance of the ITC in the hands of the assessee, if the selling dealer himself was shown to be non-existing.

High Court observed that the State cannot be expected to give credit of Input Tax Credit unless on a verification that the selling dealer is not only shown to be existing but such actual sales attracting such liability is established in the hands of the selling dealer and such tax has been deposited by the selling dealers with the State in due discharge of his obligations under the provisions of the KVAT Act, 2003 or at least he exists to undertake the discharge of such tax obligation on his part. Such false Input Tax Credit given in the hands of the purchasing dealer like the present assessee cannot only result in false credits to be allowed in the hands of the dealers which causes loss to the public revenue to the State, but in such cases, the Revenue Authorities are of course empowered to undertake such verification process to its logical end and the petitioner-assessee cannot be held entitled to cut short such process of investigation particularly by invoking the writ jurisdiction of this Court.

Ruling in favour of Revenue, High Court held that the instant petitions of the assessee were misconceived, and thus dismissed the same.

Service Tax

LD/66/149

Union of India
vs.
M/s Intercontinental Consultants and Technocrats Pvt. Ltd.

7th March, 2018

Hon'ble Apex court held that prior to 14.05.2015, 'reimbursement of expenditure' would not form part of 'gross amount charged' as envisaged u/s. 67 and thus, not includible in value of service, chargeable to service tax.

Facts:

The present appeal was filed by revenue against the decision of Hon'ble Delhi High Court in writ petition decided vide 2012-TIOL-966-HC-DEL-ST. Said writ petition was filed by respondent assessee challenging vires of Rule 5 of Service Tax (Determination of Value) Rules, 2006. Hon'ble HC noted that the charge of service tax under Section 66 has to be on the value of taxable services rendered by service provider to the service recipient, that can be brought to charge and nothing more; the quantification of value of services can, therefore, never exceed the gross amount charged by service provider, for the services provided by him. Accordingly, High Court held that the scope of Rule 5 goes beyond Section 67. In the process, the High Court observed that the expenditure or cost incurred by the service provider in the course of providing the taxable service can never be considered as the gross amount charged by the service provider 'for such service' provided by him, and illustration 3 given below Rule 5 which included the value of such services was a clear example of breaching the boundaries of Section 67.

Aggrieved by decision of HC, in present appeal, revenue contended that the expression 'gross amount charged' would clearly include all the amounts which were charged by the service provider and would not be limited to the remuneration received from the customer; the very connotation 'gross amount charged' denotes the total amount which is received in rendering those services and would include the other amounts like transportation, office rent, office appliances, furniture and equipments etc.; this expenditure cost would be part of consideration for taxable services, hence, that essential input cost had to be included in arriving at gross amount charged by a service provider. Revenue further submitted that since Section 67 specifically lays down the principle of gross amount charged by a service provider for the services provided or to be provided, Rule 5 cannot be said to be contrary to Section 67 as it only mentions what is the meaning of gross amount charged.

The respondent-assessee pointed out that in terms of amendment to Section 67 w.e.f. 14.05.2015, explanation has been added which lays down that consideration includes the reimbursement of expenditure or cost incurred by the services provider. It was therefore submitted that, for period prior to amendment, the term 'consideration' was having limited sphere, viz, it was only in respect of taxable services provided or to be provided. Further, respondent assessee also relied on para 2.4 of Circular/Instructions F. No. B-43/5/97-TRU dated June 6, 1997 wherein it is clarified that *"...various other reimbursable expenses incurred are not to be included for computing the service tax"*.

Thus, the core issue before Hon'ble SC in present appeal was as to whether Section 67 of the Act permits the subordinate legislation to be enacted in the said manner, as done by Rule 5 of Valuation Rules, 2006 i.e. whether reimbursable expenditure also forms part of 'gross amount charged' as referred in Section 67.

Held:

Hon'ble SC held that for valuation of taxable services for charging service tax, the authorities are to find what is the gross amount charged for providing 'such' taxable services, and hence, any other amount which is calculated not for providing such taxable service cannot be a part of that valuation as that amount is not calculated for providing 'such' taxable service. That is the plain meaning which is to be attached to Section 67. Thus, on this interpretation to be given to Section 67, Hon'ble SC held that High Court was right in interpreting Sections 66 and 67 to say that in the valuation of taxable service, the value of taxable service shall be the gross amount charged by the service provider 'for such service' and the valuation of taxable service cannot be anything more or less than the consideration paid as quid pro qua for rendering such a service . The decision of High Court that Rule 5 went much beyond the mandate of Section 67, was upheld by Hon'ble Supreme Court.

Hon'ble Supreme Court further held that the aforesaid view gets strengthened from the manner in which the Legislature itself acted; realising that Section 67, dealing with valuation of taxable services, does not include reimbursable expenses for providing such service, the Legislature amended by Finance Act, 2015 with effect from May 14, 2015, whereby clause (a) of explanation to Section 67 which deals with 'consideration' is suitably amended to include reimbursable expenditure or cost incurred by the service provider and charged, in the course of providing or agreeing to provide a taxable service, thus, only with effect from May 14, 2015, by virtue of provisions of Section 67 itself, such reimbursable expenditure or cost would also form part of value of taxable services for charging service tax. Hon'ble Apex Court also held that such substantive change brought about with amendment to Section 67 has to be prospective in nature. Accordingly, revenue's appeal was dismissed.

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LD/66/150

Commissioner of Service Tax

vs.

M/s Bhayana Builders (P) Ltd. ETC

19th February, 2018

Apex court held that value of goods/materials, supplied free of cost, by recipient of service to the service provider, is not includible in "gross amount charged" u/s. 67, being neither monetary or non-monetary consideration paid by or flowing from service recipient accruing to the benefit of service provider.

Facts:

Respondent assessee, being engaged in the business of construction, duly discharged service tax liability on 33% of the gross amount charged to service recipients for whom the construction was carried out. Some of the goods/materials were supplied by the service recipient. Since these materials were to be utilised in the projects meant for service recipients themselves, obviously, no cost thereof was charged from respondent assessee. Department alleged that the value of such goods or materials even when supplied or provided free should be included, while calculating the "gross value" u/s. 67 and 33% thereof be treated as value for the purpose of levying service tax. Vide decision dated 06.09.2013, the larger bench of Hon'ble Delhi Tribunal decided the issue in favour of assessee, correctness whereof was challenged before Apex Court in this appeal. The issue before Hon'ble SC was as to whether the value of goods/materials supplied or provided free of cost by a service recipient and used by service provider for providing the taxable services of construction of commercial or industrial complex, is to be included in the computation of gross amount charged by the service provider, for the valuation of taxable services.

Held:

Hon'ble SC noted that in terms of Section 67 unless an amount is charged by the service provider to the service recipient, it does not enter into the equation for determining the value on which service tax is payable. Any amount charged which has no nexus with the taxable service and is not a consideration for the service, does not become part of the value which is taxable under Section 67. The cost of free supply goods provided by the service recipient to the service provider is neither an amount "charged" by the service provider nor can it be regarded as a consideration for the service provided by the service provider. In fact, it has no nexus whatsoever with the taxable services for which value is sought to be determined. Thus, SC held that a plain meaning of the expression *'the gross amount charged by the service provider for such service provided or to be provided by him'* would lead to the obvious conclusion that the value of goods/material that is provided by the service recipient free of charge is not to be included while arriving at the 'gross amount' simply because of the reason that no price is charged by the assessee/service provider from the service recipient in respect of such goods/materials.

As regards revenue's contention that in terms of Explanation to Section 67, payment received in any form and any amount credited or debited, is to be included for the purpose of arriving at gross amount charged and is leviable to service tax, Hon'ble Supreme Court noted that the definition of "gross amount charged" given in clause (c) of Explanation to Section 67 only provides for the modes of the payment or book adjustments by which the consideration can be discharged by the service recipient to the service provider. It does not expand the meaning of the term "gross amount charged" to enable the Department to ignore the contract value or the amount actually charged by the service provider to the service recipient for the service rendered. The fact that it is an inclusive definition and may not be exhaustive also does not lead to the conclusion that the contract value can be ignored, and the value of free supply goods can be added over and above the contract value to arrive at the value of taxable services. The value of taxable services cannot be dependent on the value of goods supplied free of cost by the service recipient. The service recipient can use any quality of goods and the value of such goods can vary significantly. Such a value, has no bearing on the value of services provided by the service recipient. Thus, Hon'ble Supreme Court held that, a value which is not part of the contract between the service provider and the service recipient, has no relevance in the determination of the value of taxable services provided by the service provider. Further, Hon'ble Supreme Court noted that the explanation contained in the erstwhile notification, which prescribed 33% of the value to be attributable to provision of service in case of construction contracts, only explained that gross amount charged shall include the value of goods and materials supplied or provided or used by the provider of construction service. Thus, though it took care of the value of goods and materials supplied by the service provider/assessee by including value of such goods and materials for the purpose of arriving at gross amount charged, it did not deal with any eventuality whereby value of goods and materials supplied or provided by the service recipient were also to be included in arriving at "gross amount charged".

Accordingly, upholding decision of larger bench of Tribunal, present appeal by revenue was dismissed by the Supreme Court.

LD/66/151

Concord India Pvt. Ltd.

vs.

Commissioner of Service Tax

11th January, 2018

Tribunal held that once an activity is exempted by virtue of its inclusion in exemption notification, *no service tax can be demanded from service recipient in respect of such activity by resorting to reverse charge mechanism prescribed u/s. 68(2) of FA, 1994.*

Facts:

The appellant, a business entity with 'nil' turnover, paid service tax on inward legal services rendered by advocates during 'March 2012 to March 2013' under reverse charge mechanism in terms of Notification No. 30/2012-ST dated 20.06.2012 (i.e. RCM Notification). On realising that said services were exempted from service tax in terms of Sr. no. (6) of Notification No. 25/2012-ST dated 20.06.2012 (i.e. Exemption Notification), appellant filed refund claim for service tax paid by them under RCM, which was rejected by the lower authorities on the ground of non-submission of challans for payment of service tax liability/ST-3 returns and also on principles of unjust enrichment. Aggrieved by said order, appellant filed appeal before Commissioner (Appeals) which was rejected on the ground that refund claim is barred by limitation. Consequently, appellant filed present appeal.

Held:

Tribunal held that once an activity is exempted under Section 66B in terms of Mega Exemption Notification No. 25/2012-ST, the question of invoking Notification No. 30/2012-ST issued u/s. 68(2), for fastening service tax liability on service recipient under reverse charge mechanism does not arise at all. Further, relying on decision of Hon'ble Bombay HC in case of *P.C. Joshi vs. UOI 2015 (37) STR 6 (Bom)* holding that Notification No. 30/2012 does not override Notification No. 25/2012 and that the exemption from levy of service tax is very much available to small entities with turnover of less than Rs. 10 lakhs in respect of the advocate services, Tribunal held that appellant would be entitled to refund of service tax mistakenly paid by them under RCM in respect of exempted services.

As regards rejection of appeal by Commissioner (Appeals), Tribunal held that findings of Commissioner (Appeals) that claim is barred by limitation is not sustainable as the lower authority has categorically held that refund claim is not barred by limitation and also, even the revenue has not challenged the findings of the authority that refund is not barred by limitation, by filing appeal.

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LD/66/152

M/s Compucom Software Ltd.

vs.

Commissioner of Central Excise

29th November, 2017

Tribunal held that the input services rendered by foreign vendors outside India would be chargeable to service tax under reverse charge mechanism because though such services are used by Indian person while rendering output services abroad, place of consumption would be India as such services are used by Indian entity while providing its output services.

Facts:

Appellant provided software services to their clients located in USA i.e. outside India. It engaged various other vendors in USA in order to help them in rendering software services to their main client in USA. Revenue contended that in respect of payments made to such vendors, appellant is liable to pay service tax under reverse charge mechanism being importer of such services. While rebutting the same, appellant submitted that onsite service provided by the appellant outside India were facilitated by these vendors, who are also located outside India, as these services are fully rendered outside India, there is no liability on the appellant to pay tax on reverse charge basis as no service is received by appellant in India.

Held:

Tribunal noted that admittedly the appellant engaged various vendors as service providers, which facilitated them to provide onsite service to their clients based outside India. However, even if the vendors are located outside India, the appellants, located in India, did benefit and consumed the services of the vendors, which in turn helped them to provide the services to the clients based aboard. Thus, it was held that the appellant's services to the main client, which is not being taxed being exported service, is facilitated and supported by services of these vendors and thus, covered under the tax entry "Business Auxiliary Service". Further, Tribunal also concurred with revenue's contention that present case is a reverse case of the ratio laid down in *Microsoft Corporation (I) Pvt. Ltd. 2014-TIOL-1964-CESTAT-DEL* and *Paul Merchants Limited 2013 (29) STR 267 (Tri. Del)* and as affirmed by the Hon'ble Delhi High

Court in *Verizon Communication India Pvt. Ltd. -2017-TIOL-1863-HC-DEL-ST*. Tribunal held that since the destination has to be decided on the basis of the place of consumption, not the place of performance of service, as such, service tax liability on appellant was upheld in respect of services received by them abroad from various vendors located outside India.

International Tax

LD/66/153

Production Resource Group (401 ITR 256)

Authority for advance ruling (AAR) rules on fixed permanent establishment (PE) and disposal test in a service arrangement and held that Applicant had a fixed PE in terms of the on-site space provided to store its equipments

Facts:

The Applicant is a company incorporated in Belgium and is engaged in the business of providing technical equipment and services for events, including lighting, sound, video and LED technologies.

The Applicant entered into an agreement to furnish lighting and searchlight services during the opening and closing ceremonies of the Commonwealth Games in India in 2010, on a turnkey basis.

The technical scope of work included installation, maintenance, dismantling and removal. It required an ongoing presence available on call, to service, rectify or repair any equipment supplied by the Applicant.

For provision of the services, the Applicant undertook all related activities, such as obtaining all authorisations, permits and licenses, engaging personnel with the requisite skills, ensuring their availability, procuring and/or supplying all necessary equipment for its business, subcontracting, shipping and loading, insurance etc.

For carrying on the above activities, the Applicant was provided with an office space, as well as an on-site space for storing its tools and equipment inside the stadium where the Games were held, under a lock.

The Applicant's employees and equipment were present in India for a period of 66 days for preparatory, installation and dismantling of the equipment.

The Applicant was of the view that its income was not taxable in India.

Income did not amount to FTS since the services provided were standard in nature and there was no "rendering" of services, which implied a continued provision of specified, identified services, and not merely an end result. Also, by invoking the MFN clause, the restricted scope of the make available condition under the India-Portgual DTAA can be applied in the present case. Since the make available condition was not met, the income did not qualify as FTS. There was no transfer of any IP or right to use any IP by the Applicant to the OCCG. Hence, the royalty definition was not triggered.

The Applicant did not have a PE in India in the absence of any fixed place of business in India to which it could enter or make use as a matter of right.

The Applicant's presence was only transient; it didn't satisfy the characteristics of a PE of continuity, regularity and stability.

The Tax Authority alleged that the Applicant had a fixed PE in India at the premises of the OCCG, since it had a comprehensive physical presence, through its key personnel on the ground, throughout the period of the Games. Furthermore, Tax Department contended that applicant's income also qualified as Fees for Technical Services (FTS) and Royalty as per Indian Tax Laws (ITL) as well as under the DTAA.

Aggrieved by the above, the Applicant sought an advance ruling on the issue of taxability of its income from the OCCG, under the DTAA.

Issue:

Whether, in the facts of the case, applicant is having fixed place PE in India?

Held:

In view of the overall facts and the terms of the Agreement, the AAR held that the Applicant had a fixed permanent establishment (PE) in terms of the on-site space provided to store its equipment under a lock. AAR observed as follows:

The provision of a lockable space for storing its tools and equipment inside the stadium implies that the Applicant had access to and control over this space to the exclusion of other service providers engaged by the OCCG, including the OCCG itself. This space was not merely for storage alone but, looking into the nature of the business, for carrying out the business itself.

Given the expensive equipment, time lines, precision and the highly technical nature of the work involved, it is inconceivable that the space provided to the Applicant, along with the required security, would not be at the Applicant's disposal, with the exclusive right to access and control.

Provision of an empty workspace to the Applicant implies that such workspace was placed at the disposal and under access and control of the Applicant. Also, in the facts, the business had to be carried out on-site.

Reliance was placed on Klaus Vogel to hold that it is immaterial that the place of business is located in the business facilities of another enterprise which may be the owner.

Further, AAR observed that subcontracting of some activities by the Applicant is indicative of the fact that the Applicant had an address, an office from which it could call for and award subcontracts.

The Applicant entered into various contracts for the purpose of its business in a contracting state, and was employing technical and other manpower for use at its site. The site was, thus, an extension of the foreign entity on Indian soil, as referred to in the case of *Vishakhapatnam Port Trust* (supra).

Undertaking comprehensive insurance of its equipment is also indicative of having a fixed place of business, since that is the place where it kept, assembled and created the end products required for rendering the services. No insurance company would insure any equipment, structures etc., against any risk of fire, damage or theft, unless the place was safe and in the exclusive custody and at the disposal of the customer, and in a well-defined address or physical care. Goods are not ordinarily insured when lying at a third person's premises.

It was mandatory for the Applicant to acquire all authorisations, permits and licenses. This indicates that the Applicant had a definite place at its disposal, as it could, otherwise, not be made liable for any default in the absence of the same.

For a PE to emerge, the fixed place need not be enduring or permanent, in the sense that it should be in its control forever. The context in which a business is undertaken is relevant. Relying on the SC decision in the FOWC case, the duration for which the fixed place was at the disposal of the Applicant was sufficient for the business required.

Furthermore, it was held that the Applicant's income did not qualify as royalty under the DTAA in the absence of provision of any intellectual property (IP) by the Applicant. By applying the most favored nation (MFN) clause of the DTAA, read with the India-Portugal DTAA, income did not qualify as fees for technical services (FTS), since the make available condition was not met though, in the facts, services were held to be technical in nature.

LD/66/154
Danisco India Private Limited
vs.
Union of India
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Delhi HC

Hon. Delhi High Court holds that in case of conflict between the tax rate prescribed in Section 206AA of the Income Tax Act and in a tax treaty, the tax treaty rate would apply

Facts

The petitioner is an Indian resident taxpayer, who, in the normal course of its business remits payments to M/s DuPont Singapore, a non-resident company, located in Singapore. DuPont is not a tax assessee in India. Tax relationship between the two countries is regulated in terms of Indo-Singapore Double Taxation Avoidance Agreement (DTAA). Article 12 of DTAA mandates a cap of 10% upon the recovery of amounts, in respect of tax incidence that occurs in the concerned host country.

Petitioner raised a contention that Supreme Court in its decision in case of *Azadi Bacho Andolan* (2003) 263 ITR 706 (SC), held that even if the tax rate for the activity which would form part of the expression FTS is higher, not more than 10 per cent could be recovered by the tax authorities.

Petitioner contended that Section 206AA has the effect of undoing the provisions of DTAA, besides being in violation of Article 265 of Constitution of India.

The petitioner in support of its contention that the levy of 20% rate is unconstitutional also relied upon the recommendations of Justice Easwar's Committee's Report of 2016 made to the Central Government.

Held

Hon. High Court observed that issue urged has been rendered largely academic on account of corrective amendment made by the Parliament- which substituted pre-existing sub-Section (7) with the present Section 206AA (7).

The amendment is mitigating to a large extent, the rigors of the pre- existing laws. The law, as it existed, went beyond the provisions of DTAA which in most cases mandates a 10% cap on the rate of tax applicable to the state parties. Section 206AA (prior to its amendment) resulted in a situation, where, over and above the mandated 10%, a recovery of an additional 10%, in the event, the non- resident payee, did not possess PAN.

ITAT relied upon the decision of Hon. ITAT in case of *Serum Institute of India* (ITA 792/ PN/2013) and *Azadi Bachao Andolan* (SC) and held that DTAA acquires primacy in such cases, where reciprocating states mutually agree upon acceptable principles for tax treatment and the provision in Section 206AA (as it existed) has to be read down to mean that where the deductee i.e the overseas resident business concern conducts its operation from a territory, whose Government has entered into a Double Taxation Avoidance Agreement with India, the rate of taxation would be as dictated by the provisions of the treaty.

LD/66/155
DCIT
vs.
Credit Suisse AG
90 taxmann.com 181
Mumbai ITAT

Fees received by a Dubai branch of taxpayer (a swiss company) from an Indian company for referring an Indian resident client is in nature of commission to be taxed as business income and not as fees for technical services

Facts

The taxpayer (assessee) is a tax resident of Switzerland and a part of Credit Suisse group. It has a bank branch office in Dubai (CSDB) and India. Its Dubai branch received referral fee from the Indian company, which was an associate enterprise, for referring an Indian resident client to such Indian Company for bringing out issue of convertible bonds.

Assessee contended that such referral fee received by CSDB was a 'business income' not liable to tax in India because CSDB did not have a 'permanent establishment' in India as recognised in Article 5 of the Indo-Swiss DTAA.

The Assessing Officer, however, held that impugned fee was in the nature of 'fee for technical services' and not 'business income' and brought to tax said fee in hand of the assessee as 'fee for technical services'.

As per the Assessing Officer, 'referral fee' is deemed to accrue or arise in India and therefore, the same is taxable in India. This has been inferred on the strength of the fact that the fee has been paid by the Indian Company after execution of the work of the referred client based in India and therefore, the source of the fee is located in India

On appeal, the DRP upheld the plea of the assessee and deleted the addition made by the Assessing Officer.

Issue

Whether the referral fees received by CSDB from an Indian resident entity liable to tax in India as FTS?

Held

Hon. Mumbai ITAT relying upon the decision of Hon. AAR in case of *Cushman & Wakefield (S) Pte. Ltd.* [2008] 305 ITR 208/172 Taxman 179 (AAR) and Hon. Mumbai ITAT in case of *CLSA Ltd vs. ITO* (International Taxation) [2013] 56 SOT 254/31 taxmann.com 5 (Mum.-Trib). wherein referral fee earned by a non-resident assessee from an India based entity for referring certain international clients was held not to be in the nature of 'fees for technical services', upheld the order passed by DRP.

Hon. ITAT noted that merely because the fee was payable by the Indian Company to CSDB after

execution of the work of the referred client is no ground to determine the nature of the payment. CSDB has no PE in India and also the fact that assessee's PE in India i.e., Mumbai bank branch had no role to play in the performance of the referral activity in question.

Thus, considering that the referral activity was undertaken outside India and assessee's Mumbai branch (PE) had no role to play in the performance of the referral activity, the referral fee of ₹18,27,90,578/- earned by CSDB could not be construed to be attributable to assessee's PE in India.

LD/66/156

AB Holdings, Mauritius – II, In re
90 taxmann.com 177
AAR

Transfer of Indian company's shares by Mauritian company to its subsidiary company in Singapore not liable to tax

Facts

The applicant is a company incorporated in Mauritius in the year 2008, having its registered office at Mauritius with a valid tax residency certificate granted by the Mauritius tax authorities (hereinafter called as M1 Company).

It was a part of C Group ('C' Equity Portfolio II LP and 'C' Affiliates Fund LP'), which cumulatively holds 87.56 per cent shares of the applicant and the balance 12.44 per cent shares are held by other individual investors. The sole purpose of its incorporation was to invest in 'S' sector in India and other Asian markets.

In the same year, the M1 Company acquired the business of an Indian Company ('AB International'). The share purchase agreement for the acquisition of the shares of AB International was signed by the director of the Applicant.

M1 Company's business was managed by 3 directors out of which 2 were residents of Mauritius at the time of making the investments. The initial and subsequent investment were made through banking channels. Details of the investments were provided to the RBI under FEMA, 1999. FIRC was obtained from the RBI which shows that remittances were for the acquisition of shares and the money had come from the M1 Company.

As part of the corporate strategy of the Group, to support its business in the Asia-Pacific region in the medium to long-term, and to obtain operational and cost benefits from centralising the ownership of investments and operations in Asia-Pacific region, a regional headquarters in Singapore was proposed. Pursuant to filing the application, 'AB' Singapore was incorporated.

Thereupon, in order to achieve aforesaid objectives, the M1 Company transferred the shares held in 'AB' International to 'AB' Singapore, a Group company. The shares of other Group companies were also transferred to 'AB' Singapore in exchange of shares to achieve the objective.

Issues

On the above facts, the advance ruling is sought on following questions by M1 Company:

1. Whether the M1 Company will be entitled to the benefits of India-Mauritius DTAA with respect to taxes on income and capital gains?
2. If the treaty benefits are available, whether the gains arising to the M1 Company from the proposed sale of shares in 'AB' India Private Limited ('AB India') to a Group Company would not be liable to tax in India having regard to the provisions of Article 13 of the India-Mauritius tax treaty?
3. If the gains arising from the proposed sale of shares by Mauritian company are not chargeable to tax in India, whether there will be any obligation to withhold tax under Section 195 of the Act?
4. If the gains arising from the proposed sale of shares by Mauritian company are not

chargeable to tax in India, whether the transfer pricing provisions of Section 92 to Section 92F of the Act will apply?

5. Whether on the facts and circumstances of the case the applicant will be liable to tax under the provisions of Section 115JB of the Act in relation to income earned from the proposed transaction?

Held

The AAR held that M1 Company is a tax resident of Mauritius and would ordinarily be covered under the India-Mauritius DTAC. It was incorporated in Mauritius on 07-10-2008 and possesses a valid Tax Residency Certificate granted by the Mauritius tax authorities, and holds a Category 1 Global Business License. Further, M1 Company also placed reliance on the Circular 789 issued by CBDT. As per the Circular, all the entities who are incorporated in Mauritius and liable to tax as per the Mauritius tax laws would be considered as a resident of Mauritius for the India Mauritius DTAA. M1 Company was of the view that the conditions in this circular India – Mauritius DTAA would be applicable in the present case also.

M1 Company was set up to act as an investment holding company, to invest in 'S' sector in India and other Asian markets. The transfer of shares from 'AB' International to 'AB' Singapore, a group company, in 2012 was done along with shares of other Group companies also, as part of a reorganisation, which indicates a long-term business and commercial purpose.

The AAR further observed that the transfer was done as a part of the business reorganisation. Further, the spread from the date of investment to the date of transfer was over almost 7 years, and not short-term or overnight transactions for avoiding tax. There is nothing that invites any curious investigation on this issue also.

Further the AAR was of the view that though 'C' Group being the Holding Company, would not be involved in any important decision making, be it the funding of the subsidiary company, deciding its objectives, its target markets, and making investments and disinvestments, etc. It can be no one's case that the holding company would have no role at all to play in the affairs of its subsidiary, whose activities have to be necessarily in consonance with the overall goals of the holding company.

Viewed in the above context, setting up a subsidiary for purposes of investment cannot be questioned. Further, as regards role of the holding company, and its control and management, it is seen that the principal investor and MD in the holding company, 'S' was also a Director in the M1 Company, as also in many other companies of the group. Being in investment business and having identified the 'S' sector in India, and elsewhere, as an investment destination, it is only logical that he would have a persuasive influence on the investment decisions of the company, irrespective of where he was located. Further, the directors of M1 Company were well qualified and engaged in meaningful discussions with reference to the business of M1 Company. In the totality of circumstances, 'S' and the other Directors' movements in and out of Mauritius at different times, alone cannot lead to the conclusion that the control and management of the company was not in Mauritius, or that it was with the holding company.

Further for the office/place of management, Mauritian tax authorities have certified that the place of business of the applicant is at the given address in Mauritius, the returns filed show this address and Board meetings also take place at this address, as mentioned in the Resolutions. Further, in the case of Investment companies, investment decisions do not require huge offices and staff. In this case, the auxiliary services have been outsourced to International Management (Mauritius), which provides all secretarial assistance.

In view of the foregoing factual position, and keeping the context of an Investment holding company in mind, where its only business is of making investments and gaining from capital appreciation, no adverse inference can be drawn as to the applicant's independent status, its investment decisions as also the control and management of its business. The signature of the directors on the documents pertaining to the additional investment and restructuring etc. indicates key decisions were taken by them.

The department was of the view that M1 Company is a benami shareholder/a name lender and the actual owner of shares of 'AB' International is the 'C' Group. Reliance was placed on the decision of the Supreme Court in the case of *Jaya Dayal Poddar vs. Mst Bibi Hazra AIR 1974 SC 171*, which laid down key principles and basis on which a transaction could be held as benami. These are:

(i) the source from which the money came;
(ii) the nature and possession of the property after the purchase;
(iii) the motive in giving the transaction a benami colour;
(iv) the position and relationship of the parties;
(v) the custody of the title deeds; and
(vi) the conduct of the parties after the sale of the property. Of these, the source from which the money came is considered the most important.

Based on the analysis of various facts and circumstances, the AAR was of the view that M1 Company fulfilled all the criterion laid out above, and its investments in the Indian company cannot be questioned, when no other peculiarity or illegality is noticed, especially with regard to the flow of actual funds for investment in 'AB' International. Accordingly M1 Company was the legal and beneficial owner of shares and fully competent to transfer the same.

Based on the above facts, the AAR was of the view that the benefit under the India- Mauritius DTAC shall be available to the applicant, in the spirit of Circular no. 789, and on the principle *Pacta Sunt Servanda*, that the treaty should be honoured in good faith and hence the India–Mauritius DTAA would be applicable in the present case and the present transaction.

Further, based on paragraph 4 of Article 13 of the India–Mauritius DTAA, the capital gains

arising to M1 Company on the transfer of the shares would not be subject to capital gains and hence not taxable in India.

Further, AAR relied upon the Supreme Court judgment in the case of *GE Technology Centre (P.) Ltd. vs. CIT* 327 ITR 456, in cases where there is no chargeability to tax under the provisions of the Act, as per expressions used in the Section 195 itself, there will be no obligation to withhold tax. Based on this it was held that there is no obligation on M1 Company to withhold tax in this case, as the capital gains arising in the hands of the applicant was not chargeable to tax in view of paragraph 4 of Article 13 of the India - Mauritius DTAA.

In respect of the applicability of the transfer pricing provisions as per Section 92, the Department was of the view that Chapter X of the Act does not contain any such requirement of taxability of income as the one laid under Section 195. The AAR agreed with the view of the Department that any income arising from an international transaction has to be computed having regard to arm's length price, if the same is between two or more 'associated enterprises'. Hence this transaction of sale of shares in the Indian company should be subjected to and benchmarked as per the transfer pricing provisions contained in Chapter X of the Act.

The AAR was of the view that Section 115JB of the Act is not applicable to Foreign Companies as per the retrospective amendment to Section 1 15JB by Finance Act, 2016, and the clarification issued by the CBDT dated 24th September, 2015. Accordingly, the AAR held that Section 115JB would not apply in present case.

Legal Update

Disciplinary Case

Summary of a disciplinary case, in the matter of:

ABC Bank of India vs. CA. XYZ

Facts of the case

A Complaint in Form I dated 22nd March, 2010 was received from Chief Manager, ABC Bank of India, Mumbai (hereinafter referred to as the "Complainant"), against CA. XYZ (hereinafter referred to as the "Respondent"). The charges alleged in the Complaint are as under:

- The Respondent certified the financial statements of M/s. XXX (hereinafter referred to as "Firm") for the financial years 1999-2000, 2000-2001 and 2001-2002, so as to make the said firm eligible for bank finance.
- The Respondent has submitted bogus/fabricated sale agreement and Society's NOC of flat owned by him. The Respondent in the instant case is seller of the property financed by the Bank. Further the Respondent stood as guarantor for the home loan for which documents have been fabricated by him.

The matter was enquired into by the Board of Discipline, which *inter-alia* gave its findings as under:

- The Board noted that the Respondent had audited the Balance Sheet of the Company for Financial Years 1999-2000, 2000-2001 and 2001-2002 and issued his tax audit report(s) for the same.
- The Board further noted that the Respondent entered into an agreement for sale dated 19th March, 2013 with the proprietor of the firm i.e. his client V.L. Bhat for his flat at Brindavan Co-operative Housing Society Ltd.
- The Board also perused the legal opinion of Advocate Alikhan G. Mahawla dated 03/02/2006 stating:-

  "Upon comparing Certified copy obtained from Office of Sub-Registrar of Assurances of Document registered under serial No. BDR4-6985/2003, with the Agreement deposited at your branch purported to be registered with Sub-Registrar under the said Serial Number. It is apparent that the document at your Branch is Fake. For under the said Serial Number document registered at Office of Sub-Registrar is a Deed of Grant entered into between One Shri Satyanarayan Ramdev Singh Thakur as Grantor M/s Virendra Kumar & Brothers as Grantee".

Thus the Board opined that as per legal opinion of Advocate Alikhan G. Mahawla dated 03/02/2006, sale agreement dated 09/03/2003 between the Respondent and his client Mr. V. L. Bhat, submitted to the Complainant -Bank was fake.

The Board keeping in view the documents on record and oral submissions made by the Complainant opined that it is clearly evident that the Respondent himself availed and helped his client to avail loans from different banks on the security of the same flat. Further, no NOC had been taken from the Secretary of the society before the loans were sanctioned to the Respondent or his clients on the basis of documents forged by the Respondent. Further, the Board also noted the fact that several cases had been filed by the Complainant Bank/others against the Respondent in various Courts which are still pending and further recovery proceedings have also been initiated against the Respondent. The Board also noted the fact that the Respondent is not residing at the latest address available in the Institute's records and the emails to the mail–id of the Respondent available in the Institute's records are also being bounced back, meaning thereby, that the whereabouts of the Respondent are not known.

The Board clearly opined that the manner in which the Respondent has acted in the dual capacity i.e. as an auditor of his client and also entering into bogus agreements for sale with his clients to secure either directly or through his clients loans on the same flat, is unwarranted and unbecoming of a Chartered Accountant. A chartered accountant, as a professional, is expected to maintain high standards of integrity, not only at the professional level, but also at the personal level. Accordingly, Board held the Respondent "Guilty" of "Other Misconduct" falling within the meaning of Clause (2) Part IV of the First Schedule of the Chartered Accountants Act, 1949. Thereafter, the Board afforded an opportunity of hearing to the Respondent and after considering all the material on record, ordered that the name of the Respondent be removed from the Register of Members for a period of 3 (three) months which shall run concurrently with the punishment awarded to him in another case. ■