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INDIA TAX

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In this edition of our thought leadership publication, we have tracked the progress of some significant cases decided by the appellate forums across the country along with important press releases issued by the Central Board of Direct Taxes.

TRANSFER PRICING

CASE LAW 1:

HDFC Bank Ltd. Vs. Assistant Commissioner of Income-tax [2018] 100 taxmann.com 438 [Bombay]

The assessee needs to have a transaction (not being an international transaction) with the person referred to in Sec 40(A)(2)(b)of the Income Tax Act, 1961 ('the Act') in respect of payment of expenditure for which payment had been made or was to be made to such a person, to fall within the ambit of Specified Domestic Transaction ('SDT').

Facts of the case:

HDFC Bank Ltd. ('the company' or 'the assessee') was a company registered under the Companies Act, 1956. It was company engaged primarily in the business of banking and registered as a banking company with the Reserve Bank of India ('RBI'). HDFC Ltd. held 16.39% shares and HDFC Investment Limited (which is a wholly owned subsidiary of HDFC Ltd.) held 6.25% shares in the assessee.

The assessee received a show cause notice for alleged non-reporting of related party transactions which included purchase of loans from HDFC Ltd. set out in Sec 40A(2)(b) of the Act. Assessee submitted that the SDTs entered by it were reported in the Form 3CEB before the Assessing Officer ('AO') and also explained that the impugned transactions could not be termed as SDT. AO rejected assessee's claims and made a reference to the Transfer Pricing Officer ('TPO'). On being aggrieved, the assessee filed a writ petition before the Hon'ble High Court.

Decision of the Hon'ble High Court:

The Hon'ble High Court stated that a transaction could be termed as SDT only if it was entered between a assessee and a person referred to in Sec 40A(2)(b) of the Act.

The Hon'ble High Court observed that the assessee had purchased a loan from HDFC Ltd. Further, Sec 40A(2)(b)(iv) read with explanation (a) of the Act states that for one to have a substantial interest, it should be the beneficial owner of shares carrying not less than 20% of the voting power and therefore, it was held that HDFC Ltd. did not have a substantial interest in the assessee.

The revenue contended that on clubbing of both the investments of HDFC Ltd. and HDFC Investment limited (the threshold of 20% would be crossed.

The Hon'ble High Court stated that as per the explanation (a), two conditions are to be fulfilled:

1. The person should be the beneficial owner; and
2. These shares (of which the person is the beneficial owner) should carry not less than 20% of the voting power.

The Hon'ble High Court stated that clubbing the investments of both the companies is not permissible as it would effectively mean that HDFC Ltd., being a shareholder of HDFC Investments Ltd., is the beneficial owner of the shares which HDFC Investments Ltd. holds in the assessee. A shareholder of a company can never be construed as a legal or beneficial owner of the properties and assets of the company. Therefore, the Hon'ble High Court stated that even though HDFC Ltd. indirectly held 20% of the voting power in the assessee, it did not have a substantial interest in the assessee.

The Hon'ble High Court also stated that the transaction was with regards to purchase of loans which is an asset and not an expenditure and therefore, would not fall within the ambit of sec 92BA(i) of the Act.

Therefore, the Hon'ble High Court ruled in favour of assessee and held that HDFC Ltd. did not have any substantial interest in the assessee and thus not a person referred in sec 40A(2)(b) of the Act. Consequently, the transaction of purchase of loans could not be treated as SDT.

CASE LAW 1:

EPRSS Prepaid Recharge Services India Pvt Ltd Vs. ITO [ITA No.828/PUN/2016] (TPUN)

A well settled Latin principle 'generalia specialibus non derogant' has inferred that a general provision would not be applicable when specific provision exists.

Facts of the case:

The assessee was engaged in providing grouting and precast solutions for subsea off-shore construction industry. The company provided products and solutions to support and protect subsea pipelines, cables and structures. The main contention of the Assessing Officer ('AO') was that the grouting activities carried out in India would squarely fall within the purview of Article 5(1) of the Indo-UAE Double Taxation Avoidance Agreement '('DTAA').

Against this, the assessee contended that the grouting activities carried out in India would fall within the construction activity contemplated in specific provision of Article 5(2)(h) of the Indo-UAE DTAA.

The number of days spent in India were lesser than the stipulated period of 9 months i.e. duration test in India as per Article 5(2)(h) India-UAE DTAA. The AO relying on the decision rendered by the Hon'ble Delhi Tribunal in the case of Fugro Engineers BV, held that the company did not carry out any installation work and therefore, it would not be covered by the specific provision of Article 5(2)(i) of the relevant DTAA but as per the general provision of PE under Article 5(1) of the DTAA.

On appeal, the Hon'ble Dispute Resolution Panel ('DRP') upheld the order of the AO and held that by keeping the number of days less than nine months, the assessee had circumvented the provision of the Act by manipulating the stay of number of days in India. The Hon'ble DRP further, opined that the equipment of the assessee was in India for at least 264 days on which work for execution of construction was carried on. Thus, the assessee has equipment PE in India.

Aggrieved by the decision of the Hon'ble DRP, the assessee preferred an appeal before the Hon'ble Tribunal.

Decision of the Hon'ble Tribunal:

The Hon'ble Tribunal distinguished the decision of the Tribunal relied on by the revenue authorities on factual basis. Further, the Hon'ble Tribunal held that the concept of equipment PE has not found any place in the Indo-UAE DTAA.

Further, it held that a special provision would always override the general provision and that the revenue authorities were not permitted to rewrite the provisions of DTAA.

On a plain reading of the provisions of the Article 5(2)(h), the grouting activities carried out would squarely fall within the purview of the provisions and it did not form a PE on the basis of of number of days.

Reliance was also placed on the Circular No. 7/2016 wherein the conditions were mentioned for the consortium to be treated as an Association of Person ('AOP'). Since the assessee's consortium did not fulfil the said conditions, the consortium was not treated as AOP i.e. separate entity. Therefore, all the members of the consortium were independently responsible for execution of work and the foreign parties were required to supply the equipment's only along with the warranty and eventually the appeal was allowed.

In addition to this, it was submitted that the title in the goods were passed from the suppliers to the assessee outside India at the port of shipment. Thus, no income had accrued to those parties in India in terms of provisions of section 5 and section 9 of the Act and therefore, the provisions of section 195 of the Act would not apply to these payments.

Therefore, the Hon'ble Tribunal set aside the order of the DRP and allowed the appeal of the assessee.

DOMESTIC TAX

CASE LAW 1:

Ramprasad Agarwal v. Income Tax Officer ('ITO') [2018] 100 taxmann.com 172 (TMum)

If the assessee was able to prove that the payment of consideration as well as the allotment of shares thereof, were genuine and the Assessing Officer was unable to bring any material on record to show that the consideration was inadequate, then it could not be concluded that the assessee introduced his unaccounted money by way of bogus capital gains.

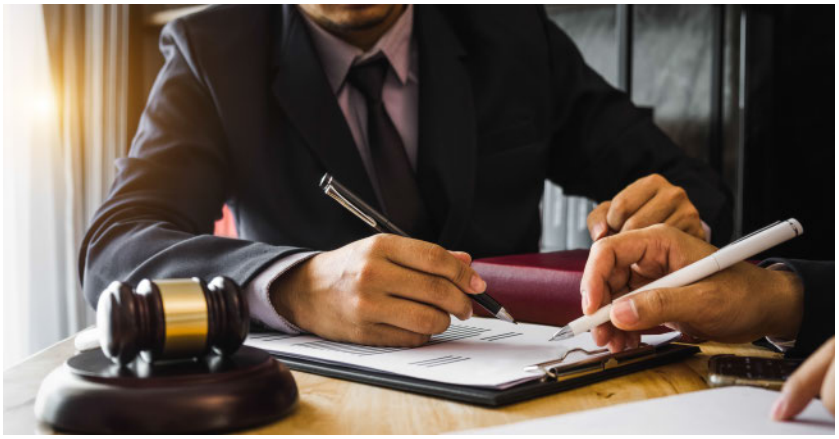
Facts of the case:

The assessee had filed his return of income for the Assessment Year ('AY') 2014-15 showing income under the head salary, house property, other sources and long-term capital gains ('LTCG') which was duly processed u/s 143(1) of the Act.

The assessee during the year had earned LTCG amounting to INR 83,45,689/- from sale of shares of Rutron International Ltd. ('the company'). The AO received information from Director General Income Tax ('DGIT') Inv., Kolkata that there were some companies engaged in the business of providing bogus long-term gains to the customers for commission. On the said basis, the case of the assessee was reopened as the assessee had sold shares of one of those alleged shell companies. The AO issued a show cause notice demanding explanation for the genuineness and correctness of the assessee's share transactions and the claim of LTCG, thereon. The AO after receiving the submissions of the assessee had disallowed the assessee's claim for exempt LTCG u/s 10(38) of the Act on the grounds that the assessee was involved in the trading of shares of penny stocks and share of shell companies.

Aggrieved by the decision of the AO, the assessee filed an appeal before the Hon'ble Commissioner of Income Tax (Appeals) ['CIT(A)']. The CIT(A) upheld the decision of the AO.

Aggrieved by the decision of the CIT(A) the assessee preferred an appeal before the Hon'ble Mumbai Tribunal.



Decision of the Hon'ble Tribunal:

The assessee had replied to the notice issued by the AO wherein, the assessee stated that he had made the payment as well as received the sale proceeds through the banking channel and the same was reflected in the bank statement of the assessee. Thus, the question of introducing the unaccounted money is ruled out as the payment and receipt was through the bank account of the assessee. The assessee had also provided a copy of letter of allotment as issued by the company and his demat statement. Thus, the share allotment cannot be considered as bogus since, the holding of shares was clearly reflected on the face of the documents. Therefore, it can be concluded that, since the transaction was directly between the company and the assessee, the presence of an intermediary providing any bogus capital gain for commission was not acceptable. Thus, the question of existence of any commissioned agent was also ruled out, thereby carving the assessee's transactions out of the bogus transaction racket. Since, the revenue was unable to provide any significant facts on record to prove, that the consideration paid by the assessee was inadequate, the assessee could not be held guilty of introducing unaccounted money through his claim for LTCG.

Therefore, the Hon'ble Tribunal held that the revenue had failed in proving that the consideration paid by the assessee was inadequate and on the other hand, the assessee provided all the necessary facts and figures on the record to substantiate the genuineness and correctness of the transaction and thus, ruled the decision in the favour of assessee.

CASE LAW 2:

ACIT Vs. Karam Chand Rubber Industries Pvt Ltd, ITA No.6599/DEL/2014

No additions can be made on account of bogus purchase merely on the ground that parties could not be traced, when payments are made to parties through banking channels and assessee has substantiated the purchase by way of various documentary evidences such as C form and VAT returns.

Facts of the case:

The assessee, a company was engaged in the business of manufacturing of cycle/rickshaw rims. A search u/s 132 of the Act was carried out at M/s Dhirani Group during which the business premises of assessee was also covered. The assessee case was selected for assessment and notice was issued u/s 153A of the Act. In response to the said notice, the assessee company filed its return of income. During the course of assessment proceedings, the Assessing officer observed that assessee has purchased nickel from four parties. The AO issued summons u/s 131 of the Act to the four parties. However, the summons were returned unserved by the postal Authorities. The AO therefore asked the director of the assessee company to produce the above four parties for his examination. Since the director of the assessee company failed to produce the above four parties, the AO conducted enquiry through inspector of the unit. The inspector reported that such concerns/firms could not be located and never existed at the address provided by the assessee. The AO issued questionnaire to the assessee asking him to furnish the complete details in respect of four parties from whom purchases were made. The assessee provided Form C and VAT return, however the AO rejected the same on the ground that these details do not prove the existence of the parties nor about their genuineness. The AO held that the assessee failed to prove the identity and genuineness of the parties from whom the purchases were made and added the amount of purchases to the Income of the assessee.

The Hon'ble CIT(A) deleted the additions, by observing that the AO has not referred to any seized documents on the basis of which any adverse conclusion could have been arrived in respect of purchase from the said four suppliers. The Hon'ble CIT(A) further held that there was no finding on part of the AO that the payments were made by assessee otherwise than through banking channel and that there was no movement of goods and that raw material purchased from these four parties were not utilized in manufacturing process.

Decision of the Hon'ble Tribunal:

The Hon'ble Tribunal upheld the order of Hon'ble CIT (A). In its decision, the Hon'ble Tribunal held that the assessee discharged the initial burden on it by substantiating the genuineness and creditworthiness of suppliers by providing C Form issued to the suppliers, VAT returns and form No. XXXVIII of the Department of Commercial Taxes which accompanies details of each consignment of goods that enters Uttar Pradesh from outside the State. None of these documents were proved to be false or untrue. Also, the payment to suppliers were made

through approved banking channel. There was no finding on the part of the AO that raw material purchased from the above parties was not utilized in manufacturing process and sales has been accepted by the revenue. Thus, the AO was not justified in treating purchases as bogus and adding the entire amount to the income of the assessee just because the said suppliers were not found on the address given by the assessee on the ground that the suppliers never existed. The Ld. DR submitted the print out from the website of the government of NCT, Delhi of the bills showing the status of the said concern as 'cancelled'. This indicates that at some point of time, these concerns were very much available in the website of Government of Delhi and therefore it could not be said that these suppliers are bogus. Further, there was no requirement under the law that the buyer of goods should continue to keep track of the sellers.

Thus, the Hon'ble Tribunal did not found infirmity in the order of the Hon'ble CIT (A) deleting the addition on account of purchases and accordingly decided in favour of the assessee.

CASE LAW 3:

ACIT v/s Shri Subodh Menon (ITA No.676/Mum/2015) and ACIT v/s Shri P.N. Ramaswamy (ITA No.2776/ Mum/2015)

The difference between the fair market value and the face value of the additional shares received by the director of the company cannot be merely taxed under section 56 or section 17 of the Income Tax Act, 1961 without having proper explanation for the same.

Facts of the case:

As the facts and circumstances in the case of both the assessees were same, both the appeals were heard together and decided by this consolidated order.

The facts of the case of Mr. Subodh Menon are as follows:

Mr. Subodh Menon ('the assessee') was the director as well as promoter of M/s Dorf Ketal Chemicals India Pvt. Ltd., a closely held company and derives income from salary, income from house property and income from other sources. At the beginning of the year, the assessee was holding 7,28,664 shares in the said company. During the year, the assessee increased his stake to 28,22,696 shares by acquiring 20,94,032 shares at Rs.100/- per share. As per the Assessing Officer the fair market value ('F.M.V') of these shares was Rs. 1438.64 per share and so the difference between the face value and F.M.V was brought to tax u/s 56(2}(vii)(c) of the Act. Alternatively, the AO held that such transaction could be considered u/s 17 of the Act as the assessee was a director of M/s Dorf Ketal India Pvt. Ltd. and received income from salary. The shares allotted to assessee, being a salaried employee, were to be treated either as perquisite or profit in lieu of salary as per the AO.

As a result of the above, an appeal was made by the assessee to the Hon'ble CIT(A), who passed an order deleting such addition.

Aggrieved with Hon'ble CIT(A)'s order, an appeal was made to the Hon'ble Tribunal by the Revenue.

Decision of the Hon'ble Tribunal:

As per the Hon'ble Tribunal, the transaction of issue of shares was carried out to comply with a covenant in the loan agreement with the bank to fund the acquisition of the business by the subsidiary in USA and therefore, such a bonafide business transaction could not be taxed under section 56(2)(vii) of the Act especially when there was not even a whisper about money laundering by the AO in the assessment order. Further, it was observed that the consideration for the shares was received through banking channel. Also, the object behind introduction of section 56(2)(vii) was not to strike at honest and bona fide transactions where the consideration for the transfer was correctly disclosed by the assessee but to bring within the net of taxation those transactions where the consideration in respect of the transfer was shown at a lesser figure than that actually received by the assessee, so that they do not escape the charge of tax on capital gains by understatement of the consideration.

Moreover, the provisions of section 56(2)(vii) are applicable only from 1st October 2009. In the instant case, the offer was made by the company to the shareholders to subscribe for the shares on 7th September 2009 pursuant to resolution passed by board of directors on the same date. Further, on 21st September 2009, the company informed the shareholders about the acceptance of shares offered by the company. Therefore, the offer made by the company was accepted by the shareholders before 1st October 2009 and hence, the contract between the company and the shareholder for issue by the company of shares was completed before 1st October 2009. Accordingly, the provisions of section 56(2)(vii) do not apply to as the contract was executed prior to 1st October 2009.

Hence, the Hon'ble Tribunal dismissed the first contention of the Revenue that the difference should be charged to tax u/s 56(2)(vii) of the Act.

Further, as per the Hon'ble Tribunal the provisions of section 17 would not apply since shares were offered and allotted to the assessee by the company by virtue of the assessee being a shareholder of the company and were not allotted by the company to the assessee in his capacity of being an employee of the company. Also, referring to Circular No. 710 dated 24 July 1995 the Hon'ble Tribunal was of the view that since the shares were offered to the assessee at the same rate as offered to the general public i.e. Rs. 100, the difference between the fair market value and issue price could not be brought to tax as a perquisite under section 17 of the Act in the hand of the assessee.

Thus, the Hon'ble Tribunal dismissed both the appeals filed by the Revenue and decided in favour of the assessee.

CASE LAW 4:

M/s M.K. Agrotech Private Ltd. Vs. Addl.CIT , Mysore [IT Appeal No.83 of 2010]

Payment made by modes other than account payee cheque or account payee bank draft in cases of business exigency shall not be disallowed u/s 40A(3) of the Income Tax Act ('the Act') in case satisfactory evidence supporting the transaction were produced by the assessee before the officer.

Facts of the case:

In the present case, the assessee had filed return of income for assessment year 2005-06 declaring a total income of INR 6,68,16,400/-.

The case was later on selected for scrutiny u/s 143(2) of the Act, whereby the Assessing Officer ('AO') disallowed expense of INR 5,31,09,701/- on the ground that the assessee had contravened the provisions of section 40A(3) of the Act by making payment for its purchases via non-crossed bank drafts and added 20% of the said amount in the assessed income of the assessee.

The assessee had produced all the supporting documents to legitimize the purchases such as the dealer invoice, transit/receipt documents along with a bank report which confirmed that tough the drafts were not crossed but the amounts pertaining to the draft were credited to the respective party's bank account from whom the purchases were made. The assessee contended that the drafts were produced to the sellers only because they needed immediate realization of the funds as per the needs of the industry.

On appeal, the Commissioner (Appeals) ('CIT(A)') as well as the Hon'ble Tribunal upheld the order of the AO. Aggrieved by the order of Hon'ble Tribunal, the assessee filed an appeal before the Hon'ble High Court.

Decision of the Hon'ble High Court:

The Hon'ble High Court held that the facts of the case of Attar Singh Gurmukh Singh Vs. ITO, Ludhiana, were squarely applicable in the present case as well, as it was rightly held by the Hon'ble Supreme Court that the provisions of section 40A(3) of the Act were to be read along with Rule 6DD of the Income Tax Rules, 1962 wherein the payment can be made by means other than those specified in the section 40A(3), however, the assessee is bound to provide satisfactory evidence to the AO in relation to the said transaction. Accordingly, the Hon'ble High Court held that the appeal of the assessee shall be allowed and the orders of the AO, the CIT(A), and the Hon'ble Tribunal shall be set aside, as the assessee provided all satisfactory evidences supporting the said transaction and also provided bank report stating that all the funds pertaining to the uncrossed draft were passed on through recognised bank accounts only.

Thus, the Hon'ble High court decided in the favour of assessee

CASE LAW 5:

Pradeep Kumar Soni Vs. ITO (ITA No. 2739/Del/2015) (Vinod Soni Vs. ITO (ITA No. 2736/Del/2015), Babli Soni Vs. ITO (ITA No. 2737/ Del/2015), Beena Soni Vs. ITO (ITA No. 2738/ Del/2015))

Since the purchase consideration paid by four individual assessees amounting to INR 3,75,000 each did not cross the threshold limit of INR 50,00,000 u/s 194-IA of the Act, the said section would not be applicable, even though the common sale transaction amounted to INR 1,50,00,000.

Facts of the case:

Four assessees of the same family purchased 1/4th undivided equal shares an immovable property. The 1/4th share purchase consideration for each person was only INR 37,50,000 each. However, during the course of assessment proceedings, the AO held that since the value of the property purchased, under a single sale deed was exceeding INR 50,00,000, therefore as per section 194-IA(2) of the Act, the assessee was required to deduct tax at source ('TDS') @1%. The AO thus held that all the four assessees were defaulters u/s 201(1) of the Act and passed a common order u/s 201(1) accordingly. On appeal, the Hon'ble CIT(A) confirmed the findings of the AO.

Aggrieved, the assessees preferred appeal before the Hon'ble Tribunal.

Decision of the Hon'ble Tribunal

The Hon'ble Tribunal noted the following:

- Section 194-IA(1) of the Act is not applicable where the consideration for transfer of immovable property is less than INR 50,00,000;
- Section 194-IA(1) of the Act is applicable on any person being a transferee, so section 194-IA(2) of the Act is also, applicable only with respect to the amount related to each transferee and not with reference to the amount as per the sale deed; and
- In the instant case, there were four separate transferees and the sale consideration with respect to each transferee was INR 37,50,000, and hence, less than Rs. 50,00,000/- each.

Bearing in mind the above provisions and facts, the Hon'ble Tribunal held as under:

- Each transferee was a separate income tax entity and therefore, the law has to be applied with reference to each transferee as an individual transferee / person.
- The law cannot be interpreted and applied differently for the same transaction, if carried out in different ways. The law cannot be read in the following manner, 'In case of four separate purchase deed for four persons separately, section 194-IA of the Act is not applicable, and in case of a single purchase deed for four persons, section 194-IA of the Act is applicable.'
- The action of the AO of passing a common order u/s 201(1) of the Act shows that he was also clear in his mind that with reference to each transferee, section 194-IA of the Act would not be applicable since in each case purchase consideration was only INR 37,50,000.

Thus, the Hon'ble Tribunal held that the addition made by the AO was not sustainable in the eyes of law, and the same would thus be deleted. Further, as far as the issue of charging interest was concerned, the Hon'ble Tribunal stated that the same is consequential in nature, hence, need not be adjudicated.

Thus, each transferee is a separate entity under the Act, and the threshold limit of INR 50,00,000 u/s 194-IA of the Act was to apply to each transferee individually.

RECENT IMPORTANT CIRCULARS, NOTIFICATION AND PRESS RELEASE ISSUED BY THE CENTRAL BOARD OF DIRECT TAXES ('CBDT')

1. PRESS RELEASE DATED DECEMBER 24, 2018: EXCEPTION FROM ONLINE FILING OF APPLICATION UNDER SECTION 197 AND 206C (9) IN THE CASES OF NRIS AND RESIDENT APPLICANTS

The Central Board of Direct Taxes ('CBDT') vide press release dated December 24, 2018 provides an extension in filing a manual application for lower withholding of tax to non-resident Indians (NRIs) till March 31, 2019.

A link for the same is provided herewith:
https://www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/741/Exception _ online _ filing _ application _ under _ section _ 197 _ 206C _ 9 _ cases _ NRIs _ resident _ applicants-PressRelease-24-12-2018.pdf

2. NOTIFICATION NO. 88/2018/ F. NO. 370142/17/2018-TPL DATED DECEMBER 18, 2018

The CBDT vide Notification No. 88/2018/ F. No. 370142/17/2018-TPL dated December 18, 2018 amends Rule 10DB of the Income Tax Rules, 1962 pertaining to

A link for the same is provided herewith:
https://www.incometaxindia.gov.in/communications/notification/notification88 _ 2018.pdf

3. NOTIFICATION NO. 7/2018 DATED DECEMBER 27, 2018

The CBDT vide Notification No. 7/2018 lays down procedures, formats and standards for issue of Permanent account number (PAN).

A link for the same is provided herewith:
https://www.incometaxindia.gov.in/communications/notification/notification _ 7 _ 2018 _ pan.pdf

4. NOTIFICATION NO. 8/2018 DATED DECEMBER 31, 2018

The CBDT vide Notification No. 7/2018 lays down procedures, formats and standards for filing an application for grant of lower/ no TDS certificate under sub-section (1) of Section 197 / collection of the tax at any lower rate under subsection (9) of Section 206C of the Income-tax Act, 1961 through TRACES- reg.

A link for the same is provided herewith:
https://www.incometaxindia.gov.in/communications/notification/notification _ 8 _ 2018 _ tds.pdf

5. CIRCULAR NO.8/2018 DATED DECEMBER 26,2018	The CBDT Vide circular No. 8/2018 clarifies provision of finance Act, 2018 A link for the above circular is provided herewith: **https://www.incometaxindia.gov.in/communications/circular/circular _ 8 _ 2018.pdf**
6. CIRCULAR NO.9/2018 DATED DECEMBER 26,2018	The CBDT vide circular No. 9/2018 extends the date of furnishing report u/s 286(4) of the Act in respect of reporting accounting year up to February 28, 2018 to March 31, 2019 A link for the above circular is provided herewith: **https://www.incometaxindia.gov.in/communications/circular/circular _ 9 _ 2018.pdf**
7. CIRCULAR NO.1/2019 DATED JANUARY 1,2019	The CBDT vide circular No. 1/2019 clarifies for deduction of TDS from salaries u/s 192 of the Act during the financial year 2018-19 A link for the above circular is provided herewith: **https://www.incometaxindia.gov.in/communications/circular/circular _ 1 _ 2019.pdf**

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