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TAX FLASH NEWS

28 April 2021

Carry forward of capital loss on sale of shares is allowed to a Singapore entity under the Income-tax Act even though such capital gains are not taxable in India under the tax treaty

Executive Summary

The Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Goldman Sachs India Investments (Singapore) Pte Ltd[1] (the taxpayer) dealt with the issue of allowability of carry forward of short term capital loss on sale of shares vis-à-vis the India-Singapore tax treaty. The Tribunal held that the capital losses incurred from transactions in the Indian capital markets should be construed as income accruing or arising in India falling within the scope of Section 5 of the Income-tax Act, 1961 (the Act). Therefore, such short term capital losses would be eligible to be carried forward to subsequent years. The Tribunal observed that while determining taxability of the income of the taxpayer, if provisions of the Act are more beneficial as compared to the India-Singapore tax treaty (tax treaty) then the beneficial provisions of the Act will apply in determining the taxability of such income. The Tribunal rejected the tax department's argument that since the capital gains earned by the taxpayer is exempt under the provisions of the tax treaty, capital losses are to be ignored.

Facts of the case

The The taxpayer is a Singapore based entity and registered with the Securities and Exchange Board of India (SEBI) as a sub-account of Goldman Sachs & Co. The Goldman Sachs & Co. is registered with the Securities and Exchange Board of India (SEBI) as a Foreign Institutional Investor (FII). During the Assessment Year (AY) 2012-13, the taxpayer incurred short term capital loss. The taxpayer claimed that the said losses are to be assessed under the provisions of the Act and has claimed carry forward of losses. However, the Assessing Officer (AO) denied the carried forward of such capital losses to subsequent years. The AO observed that since the capital gains earned by the taxpayer is exempt under the provisions of the tax treaty, it follows that capital losses are to be ignored.

The Dispute Resolution Panel (DRP) confirmed the action of the AO. Aggrieved, the taxpayer filed an appeal before the Tribunal.

Tribunal's decision

On a perusal of the decision of Goldman Sachs Investments (Mauritius) Ltd.[2], the Tribunal observed that while determining taxability of the income of the taxpayer, if provisions of the Act are more beneficial as compared to the tax treaty then the beneficial provisions of the Act will apply in determining the taxability of such income. Thus, having regard to the provisions of Section 90(2) of the Act and given that the provisions of Section 74 permit the taxpayer to carry forward capital losses to subsequent assessment years, the provisions of the Act are more beneficial than the provisions of the tax treaty.

During the year under consideration, the taxpayer had filed its return of income in accordance with the provisions of the Act. Based on judicial jurisprudence, the provisions of the tax treaty cannot be thrusted upon the taxpayer simply because the taxpayer is a tax resident of a country with which India has entered into a tax treaty or on account of the mere perception of the AO that the taxpayer may claim benefits under the tax treaty in subsequent years.

Accordingly, the Tribunal held that the capital losses incurred from transactions in the Indian capital markets should be construed as income accruing or arising from transactions undertaken in India falling within the scope of Section 5 and therefore, the same should be eligible to be carried forward to subsequent years in accordance with the provisions of Section 74.

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[1] Goldman Sachs India Investments (Singapore) Pte Limited v. DCIT [ITA No. 6619/Mum/2016] – Taxsutra.com

[2] Goldman Sachs Investments (Mauritius) Ltd. v. DCIT [2020] 120 taxmann.com 23 (Mum)

Our comments

The Tribunal in the present case has observed that the taxpayer is eligible to opt for the provisions of the Act being beneficial provision as against the tax treaty. Thus, it may compute capital losses under the provisions of the Act and carry forward the same to the future years.

As per Section 90(2), in case where India has a tax treaty with another country then, in the case of taxpayer to whom such tax treaty applies, the provisions of the Act shall apply to the extent they are more beneficial to the taxpayer. This principle has been upheld by the Supreme Court in the case of Azadi Bachao Andolan[3].

The effect of the tax treaty pursuant to Section 90 is that if no tax liability is imposed under the Act, the question of resorting to the tax treaty does not arise. No provision of the agreement can fasten a tax liability when the liability is not imposed by the Act[4].

Reference may be made to the decision of Pune Tribunal in the case of Patni Computers Systems Ltd[5] where it was held that merely because India entered into a tax treaty with a foreign country, the taxpayer cannot be denied the taxability under the Act.

Even in the instant case, the Tribunal observed that the provisions of the tax treaty cannot be thrusted upon the taxpayer simply because the taxpayer is a tax resident of a country with which India has entered into a tax treaty or on account of the mere perception of the AO that the taxpayer may claim benefits under the tax treaty in subsequent years.

It is important to note that Article 13(4) of the India-Singapore tax treaty is not an exemption provision. The Mumbai Tribunal in the case of D. B. International (Asia) Ltd.[6] observed that Article 13(4) in clear and unambiguous terms expresses itself as not an exemption provision but it speaks of taxability of a particular income in a particular State by virtue of residence of the taxpayer. The expression ‘exempt’ with reference to the capital gain derived by the taxpayer, has been loosely used. On the contrary, the overriding nature of Article 13(4) makes the capital gain taxable only in the country of residence of the taxpayer.

Further, with respect to carry forward of capital loss by a non-resident, a useful reference may be made to the decision of Mumbai Tribunal in the case of Flagship Indian Investment Co. (Mauritius) Ltd[7]. In this case, the taxpayer had brought forward capital loss (on transfer of securities) from earlier years. The AO in the said cases had held that, since the capital gains were exempted under the India-Mauritius tax treaty, the capital losses would also be exempted and therefore, the taxpayer was not entitled to carry forward the capital losses of earlier years. The Mumbai Tribunal held that the taxpayer was justified in claiming the carry forward of losses of earlier years to subsequent years.

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[3] Union of India v. Azadi Bachao Andolan [2002] 125 Taxman 826 (SC)
[4] CIT v. R M Muthaiah [1993] 202 ITR 508 (Kar)
[5] DCIT v. Patni Computer Systems Ltd. [2008] 114 ITD 159 (Pune)
[6] DCIT v. D. B. International (Asia) Ltd [2018] 96 taxmann.com 75 (Mum)
[7] Flagship Indian Investment Co. (Mauritius) Ltd. v. ADIT [2010] 38 SOT 426 (Mum)

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