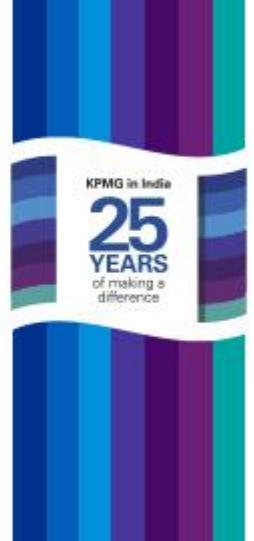


# TAX FLASH NEWS

24 September 2018



## Assured return received by a non-resident on advance payment to a developer is taxable as interest under the India-U.K. tax treaty

### Background

Recently, the Chandigarh Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Sh. Mohinder Singh Sanghera<sup>1</sup> (the taxpayer) held that the assured return received by a non-resident on advance payment to a developer is taxable as interest under the Article 11<sup>2</sup> of the India-U.K. tax treaty (tax treaty). The Tribunal observed that the assured return was not any return from the property in respect of which the taxpayer had paid the amount. The taxpayer had a debt claim against the developer till the proposed property was constructed, possession was handed over and the conveyance deed was executed and registered. Therefore, the developer rightly deducted the tax at 15 per cent of the assured return paid to the taxpayer under the tax treaty.

### Facts of the case

- The taxpayer, a non-resident, invested in the project of the developer along with four other investors during Financial Year (FY) 2007-08. The taxpayer made an advance payment of 95 per cent of the sale price and was provisionally allotted commercial floors in a proposed commercial complex. On such advance payment, the developer was to pay assured return on a monthly basis to the taxpayer till the possession of the commercial space.
- Such payment was made by the developer<sup>3</sup> after withholding of tax under Section 195 of the Income-tax Act, 1961 (the Act) at 15 per cent under the tax treaty.

- The Assessing Officer (AO) reopened the assessment and asked the taxpayer to file its tax return. Consequently, the taxpayer filed a tax return offering tax at 15 per cent on such assured return treating the same as interest income. Consequently, the AO held that the assured return received by the taxpayer was not the interest income, rather the same was a return from investment and assessed the same as 'income from other sources' and addition was made to the total income of the taxpayer.
- The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO.

### Taxpayer's contentions

- As per the provisions of Section 115A(5)<sup>4</sup> of the Act, the non-resident was not required to furnish a tax return if his income consisted only of income referred to Section 115A(1)(a) of the Act, which includes interest income and the tax has been deducted from such income.
- The taxpayer did not have any other income except interest income received from the developer. Further, the taxpayer deducted tax at source at 15 per cent as per the tax treaty. Therefore, the taxpayer was not required to file a tax return.

<sup>1</sup> Sh. Mohinder Singh Sanghera and Jatinder Singh Chatta v. ADIT (ITA Nos. 372 to 374/Chd/2016) – Taxutra.com

<sup>2</sup> Article dealing with interest

<sup>3</sup> From Assessment Year (AY) 2008-09 to 2012-13

<sup>4</sup> It shall not be necessary for the taxpayer (a non-resident or a foreign company whose income by way of dividend or interest of specified nature) to furnish tax return if his or its total income in respect of which he or it is assessable under the Act consisted only of the specified income (referred to in Section 115A(1)(a) of the Act) and tax deductible at source under the provisions of Chapter XVII-B has been deducted from such income

## Tribunal's decision

### Re-opening of assessment

- A perusal of the copy of the reasons recorded revealed that the AO has not used the word 'interest income' rather the AO revealed that he had the information that the taxpayer had been receiving assured returns on the investment made in commercial properties of the developer. Accordingly, the AO reopened the assessment and determined the nature of income as 'income from other sources' and computed the income of the taxpayer accordingly.
- It cannot be said that the AO was supposed to assume that the taxpayer was not required to file the tax return as per the provisions of Section 115A(5) of the Act or the AO was of the view that the taxpayer has been receiving interest income only. Accordingly, the reopening of the assessment was held to be valid.

### Taxability of assured return

- A perusal of the allotment letter issued by the developer revealed that unless and until the conveyance deed was executed and registered, the developer would continue to have full authority over the proposed unit and all the amounts paid by the taxpayer shall merely be a token payment and shall not give any lien or interest in the said unit.
- The property for which the taxpayer had paid the money was not in existence at the time of making payment and even subsequently it was not capable of yielding any income in the shape of rent, lease money, etc. Even otherwise it was not capable of being commercially exploited.
- It cannot be said that the assured return was any return from the property in respect of which the taxpayer had paid the amount. The taxpayer had a debt claim against the developer which means the taxpayer had advanced money to the developer which was nothing but a debt claim till the proposed property was constructed, possession handed over to the taxpayer and the conveyance deed executed and registered.
- It was a financial transaction and the assured return received by the taxpayer was nothing else than the interest received by the taxpayer on the finances provided to the developer to be used for the construction of the property. Therefore, the developer had rightly deducted the tax at 15 per cent of the assured return paid to the taxpayer.
- Accordingly, it has been held that the assured return received by the taxpayer was in the nature of interest and the taxpayer has rightly offered the same as interest income under the tax treaty.

## Our comments

In the instant case, the Chandigarh Tribunal has dealt with the taxability of assured return received on advance payment to the developer. The Gujarat High Court in the case of Nathalal Dayabhai<sup>5</sup> held that interest on earnest money was not taxable as business income but it was taxable as income from other source. It was observed that the taxpayer was not a dealer in land and this was a finding of fact. The Tribunal in the present case has held that the assured return received by the taxpayer on advance payment for the property is in the nature of interest and it is taxable under the 'interest' article of the tax treaty. The taxpayer had a debt claim against the developer till the proposed property was constructed, possession was handed over and the conveyance deed was executed and registered.

In the past, the Courts have directed the tax department not to harass taxpayers by reopening assessments in a mechanical and casual manner.

The Bombay High Court in the case of Hemant Traders<sup>6</sup> held that the AO can assume jurisdiction for reassessment provisions only if he has sufficient material before him. He cannot form a belief on the basis of his whim and fancy, and the existence of material must be real. Further, there must be a nexus between the material and escapement of income.

However, the Tribunal in the present case held that the reopening of the assessment was valid.

<sup>5</sup> CIT v. Nathalal Dayabhai [1994] 208 ITR 762 (Guj)

<sup>6</sup> Hemant Traders v. ITO [2015] 375 ITR 167 (Bom)

**Ahmedabad**

Commerce House V, 9th Floor,  
902, Near Vodafone House,  
Corporate Road,  
Prahlad Nagar,  
Ahmedabad – 380 051.  
Tel: +91 79 4040 2200

**Bengaluru**

Maruthi Info-Tech Centre,  
11-12/1, Inner Ring Road,  
Koramangala,  
Bengaluru – 560 071.  
Tel: +91 80 3980 6000

**Chandigarh**

SCO 22-23 (1st Floor),  
Sector 8C, Madhya Marg,  
Chandigarh – 160 009.  
Tel: +91 172 664 4000

**Chennai**

KRM Towers,  
Ground Floor, 1, 2 & 3 Floor,  
Harrington Road,  
Chetpet, Chennai – 600 031.  
Tel: +91 44 3914 5000

**Gurugram**

Building No.10, 8th Floor,  
DLF Cyber City, Phase II,  
Gurugram, Haryana – 122 002.  
Tel: +91 124 307 4000

**Hyderabad**

Salarpuria Knowledge City,  
6th Floor, Unit 3, Phase III,  
Sy No. 83/1, Plot No 2,  
Serilingampally Mandal,  
Ranga Reddy District,  
Hyderabad – 500 081.  
Tel: +91 40 6111 6000

**Jaipur**

Regus Radiant Centre Pvt Ltd.,  
Level 6, Jaipur Centre Mall,  
B2 By pass Tonk Road  
Jaipur – 302 018.  
Tel: +91 141 – 7103224

**Kochi**

Syama Business Centre,  
3rd Floor, NH By Pass Road,  
Vytilla, Kochi – 682 019.  
Tel: +91 484 302 5600

**Kolkata**

Unit No. 604,  
6th Floor, Tower – 1,  
Godrej Waterside,  
Sector – V, Salt Lake,  
Kolkata – 700 091.  
Tel: +91 33 4403 4000

**Mumbai**

1st Floor, Lodha Excelus,  
Apollo Mills,  
N. M. Joshi Marg,  
Mahalaxmi, Mumbai – 400 011.  
Tel: +91 22 3989 6000

**Noida**

Unit No. 501, 5th Floor,  
Advant Navis Business Park,  
Tower-A, Plot# 7, Sector 142,  
Expressway Noida,  
Gautam Budh Nagar,  
Noida – 201 305.  
Tel: +91 0120 386 8000

**Pune**

9th floor, Business Plaza,  
Westin Hotel Campus,  
36/3-B, Koregaon Park Annex,  
Mundhwa Road, Ghorpadi,  
Pune – 411 001.  
Tel: +91 20 6747 7000

**Vadodara**

Ocean Building, 303, 3rd Floor,  
Beside Center Square Mall,  
Opp. Vadodara Central Mall,  
Dr. Vikram Sarabhai Marg,  
Vadodara – 390 023.  
Tel: +91 265 619 4200

**Vijayawada**

Door No. 54-15-18E, Sai Odyssey,  
Gurunanak Nagar Road, NH 5,  
Opp. Executive Club, Vijayawada,  
Krishna District,  
Andhra Pradesh – 520 008.  
Tel: +91 0866 669 1000

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2018 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.

This document is meant for e-communication only