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TAX FLASH NEWS

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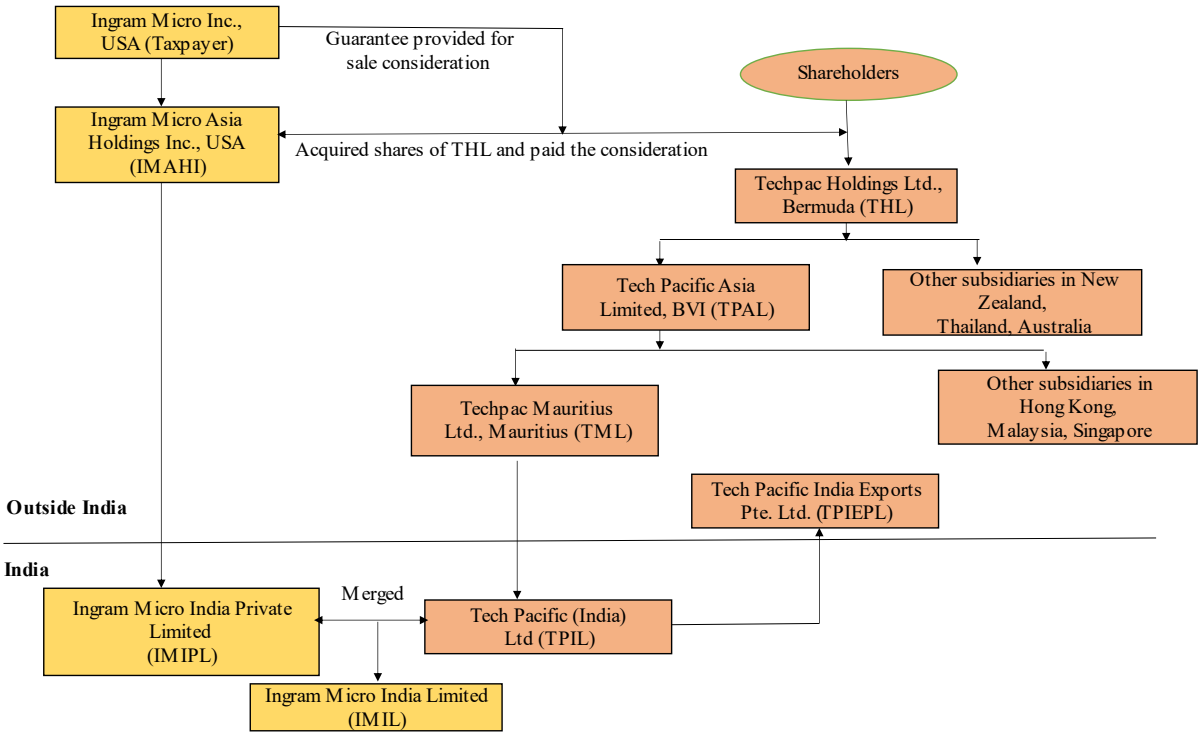
A foreign holding company is not required to deduct tax at source since the shares were purchased by its wholly owned subsidiary company

Recently, the Bombay High Court in the case Ingram Micro Inc.[1] (the taxpayer) dealt with the issue of deduction of tax at source in the hands of a foreign holding company even though the transaction of purchase of shares was undertaken by its wholly owned subsidiary company (WOS). The High Court observed that the taxpayer was not the purchaser of shares. The taxpayer was the guarantor of the payment for the share purchase transaction undertaken by its WOS. Further, the taxpayer had not made any payment with respect to the transaction. The High Court observed that a subsidiary company is an independent entity different from the parent company. The actions and transactions of the subsidiary were not transactions of the holding company. Therefore, the taxpayer was not liable to deduct tax at source under Section 195 of the Income-tax Act, 1961 (the Act).

Facts of the case



The taxpayer, a U.S. based company, is engaged in the business of distribution of technology products. The taxpayer has several companies throughout North America, Europe, the Middle East, Africa, Latin America and the Asia Pacific regions, which supported global operations through an extensive sales and distribution network. Ingram Micro Asia Holdings Inc. (IMAHI), a US based company, and a subsidiary of the taxpayer, held indirectly a subsidiary in India by the name Ingram Micro India Private Ltd. (IMIPL).

[1] Ingram Micro Inc. v. ITO (ITA.No.160/2022) – Taxsutra.com

The Techpac Group is a technology distributor and a leading technology sales, marketing and logistics group in the Asia Pacific region having an extensive spread over countries such as Australia, New Zealand, Singapore, Malaysia, Thailand, India and Hong Kong. Various non-resident shareholders, including private equity funds2, held shares in Techpac Holdings Ltd. (THL), registered in Bermuda. There were a few resident shareholders as well. THL, under its fold, held several operating and non-operating companies in Australia, New Zealand and Thailand and a holding company, Tech Pacific Asia Ltd. (TPAL), in the British Virgin Islands.

TPAL, in turn, held operating and non-operating companies in Mauritius, Hong Kong, Malaysia and Singapore. TPAL had a subsidiary in Mauritius, Techpac Mauritius Ltd. (TML). TML had a wholly-owned operating subsidiary in India by the name Tech Pacific (India) Ltd. (TPIL). TPIL had a WOS in Singapore called Tech Pacific India Exports Pte. Ltd. (TPIEPL).

In 2004, IMAHI acquired the shares of THL, Bermuda, from its existing shareholders. The taxpayer's role in this transaction was that it had guaranteed the payment of the sale consideration by IMAHI under the Share Purchase Agreement (SPA) to the shareholders of THL. The guarantee was never invoked because IMAHI discharged its obligation under the SPA to the sellers and accordingly, the taxpayer stood discharged of its obligations as a guarantor under the said SPA.

Pursuant to the acquisition, the Indian entity of Ingram Group, i.e., IMIPL, was merged into the Indian entity of the Techpac Group, viz., TPIL. Subsequent to the merger, the name of TPIL was changed to Ingram Micro India Ltd. (IMIL).

The Assessing Officer (AO) initiated proceedings under Section 201 against the taxpayer for non-deduction of tax at source. Aggrieved, the taxpayer filed a writ petition challenging AOs order contending that it was not liable to deduct any tax at source because it did not make any payment to anyone. Therefore, it was not in breach of the obligation under Section 195.

High Court decision

The tax department's contention was that the taxpayer made payment through IMAHI. However, the taxpayer had not made any payment to anyone. The AO relied on the annual reports of the taxpayer group where it had been mentioned that the group had acquired Techpac Group. However, the AO's reliance on the annual report of 2005 to conclude that it was the taxpayer who acquired THL was misplaced.

If AO's logic has to be applied, then the ultimate beneficiary were the shareholders of the taxpayer and not the taxpayer and hence, no liability can be fastened on the taxpayer. The tax department failed to appreciate that the comments on the annual accounts were with respect to the Ingram Group and not restricted to the activity of the taxpayer. The taxpayer was not the purchaser of shares of THL. The shares have been purchased by IMAHI, a WOS of the taxpayer and not by the taxpayer. Therefore, Section 195 does not apply to the taxpayer.

A subsidiary company is an independent entity different from the parent company. The actions and transactions of the subsidiary were not transactions of the holding company through the subsidiary. The shares have been acquired by IMAHI and not by the taxpayer through its subsidiary. The SPA has been entered into by IMAHI as the purchaser and not on behalf of the taxpayer. On reference to SPA, it indicates that the taxpayer was the guarantor of the payment to be made by IMAHI and not the purchaser. The tax department had failed to appreciate that the purchaser himself cannot be a guarantor also and that itself indicates that the taxpayer is not the purchaser of the shares of THL.

The obligation under Section 195 is at the time of credit of income to the account of the payee or at the time of payment, whichever is earlier. Since the taxpayer had not made any payment, it cannot be the person responsible for deduction of tax at source.

The tax department's assumption that the taxpayer being the ultimate beneficiary of the acquisition of the shares and ought to have deducted the tax at source on the payments made for the acquisition of shares of THL is not correct. Even if the taxpayer is the ultimate beneficiary of the transaction, it was required to deduct tax at the time of acquisition of shares of THL by IMAHI.

The show cause notice and the TDS order issued by the AO were quashed and set aside.

[2] CVC Capital Partners Asia Pacific LP, Asia Investors LLC, Hagemeyer Caribbean Holding NV

Our comments

In the present case, the Bombay High Court has held that the holding company of a foreign subsidiary was not liable to deduct tax at source because the transaction was of the WOS and not the taxpayer company. The taxpayer was merely a guarantor of the payment for the purchase of shares and it had not made any payment with respect to this transaction. The High Court emphasised on a well-settled principle that a subsidiary company is an independent entity different from the parent company. The actions and transactions of the subsidiary were not transactions of the holding company through the subsidiary. Further the High Court rejected the tax department's assumption that the holding company is the ultimate beneficiary of the acquisition of the shares and ought to have deducted the tax at source.

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