

# Tax Flash News

13 April 2023

## The Supreme Court's decision on the determination of place of 'control and management' of the company incorporated in Sikkim when the Income-tax Act was not applicable to Sikkim-based companies

### Executive Summary

Recently, the Supreme Court in the case of Mansarovar Commercial Pvt. Ltd.<sup>1</sup> (the taxpayer) dealt with the issue of determination of place of 'control and management' of a company incorporated in Sikkim. The taxpayer argued that it was a resident of Sikkim, carrying on business in Sikkim and thus, till the applicability of the Income-tax Act, 1961 (the Act) to Sikkim-based companies, it was governed and taxed under the Sikkim Income-tax Manual, 1948. However, the AO held that the control and management of the taxpayer were wholly with its auditor, who had an office in New Delhi. Therefore, the taxpayer was a resident of India under Section 6(3) and its income was taxable under the Act. The Supreme Court observed that it is not *de jure* control and power, but *de facto* control and power actually exercised in the course of the conduct and management of the affairs of the company is important. The domicile or the registration of the company is not at all relevant. The determinate test is where the sole right to manage and control of the company lies. Accordingly, the Supreme Court held that the control and management of the taxpayer company were with the auditor in Delhi.

### Facts of the case

- The taxpayer was engaged in the business of commercial agents in agricultural products and incorporated under the Registration of Companies (Sikkim) Act, 1961. Sikkim became part of India in April 1975.

- All laws in force in the territories comprising the State of Sikkim or any part thereof were to continue to be in force therein until amended or repealed by a competent legislature or other competent authority.
- The Finance Act, 1989 brought amendment and the Act was made applicable to the State of Sikkim from the previous year relevant to the Assessment Year (AY) commencing from 1 April 1990.
- The taxpayer argued that it was a resident of Sikkim, carrying on business in Sikkim and not elsewhere and that till 31 March 1990, it was governed by the Sikkim Income-tax Manual, 1948 and not the Act. Therefore, the income earned by the taxpayer till that date was earned in Sikkim from the business conducted in Sikkim.
- The AO held that the control and management of the taxpayer were wholly with its auditor, who had his office in New Delhi. Therefore, the taxpayer was a resident of India under Section 6(3) and its income was taxable under the Act.

### Supreme Court's decision

- The Supreme Court relied on the observations of the CIT(A) and the High Court where it was concluded that the control and management of affairs were wholly in India for the following reasons:
  - The auditor was not only doing audit work but determining who should be the directors of the taxpayer.

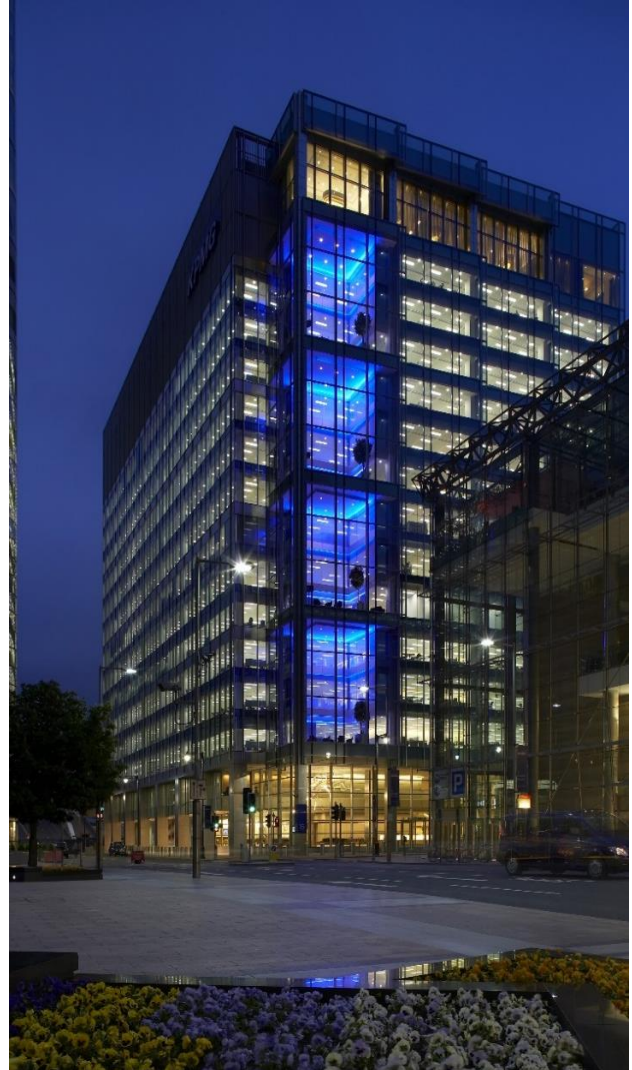
<sup>1</sup> Mansarovar Commercial Pvt. Ltd v. CIT (Civil Appeal No. 5773 of 2022) – Taxsutra.com

Note: The Supreme Court, in this case, has dealt with various issues. However, this flash news only covers the issue of determining the place of 'control and management' of a company incorporated in Sikkim

- The rubber seals, letterheads, blank signed cheques and other records were all found in the auditor's office. The AO's factual determination remained undisputed and fortified that the control and management were in Delhi.
  - There is no presumption in law that control and management are at the registered office.
- The Supreme Court observed that it is not *de jure* control and power, but *de facto* control and power actually exercised in the course of the conduct and management of the affairs of the company is important.
  - The domicile or the registration of the company is not at all relevant. The determinate test is where the sole right to manage and control of the company lies.
  - In view of above and relying on various decisions<sup>2</sup>, the Supreme Court held that the control and management of the affairs of the taxpayer company were with the auditor in Delhi.

### Our comments

The Supreme Court has given important observations to determine the place of control and management of the company for example place of authority where important decisions are taken, the actual place where control and management are exercised, domicile or the registration of the company is not relevant, etc. It would be interesting to see how these observations of the Supreme Court will help to determine the tax residential status of overseas subsidiaries of Indian multinational companies under the provisions of Place of Effective Management (POEM).




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<sup>2</sup> CIT v. Nandlal Gandalal [1960] 40 ITR 1 (SC), V.V.R.N.M. Subbayya Chettiar v. CIT [AIR 1951 SC 101], Erin Estate v. CIT [1959 SCR 573], Narottan and Pereira Ltd. v. CIT [1953] 23 ITR 454 (Bom), B.R. Naik v. CIT (1945) 13 ITR 124

# KPMG in India addresses:

## Ahmedabad

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

## Bengaluru

Embassy Golf Links Business Park,  
Pebble Beach, 'B' Block,  
1st & 2nd Floor,  
Off Intermediate Ring Road, Bengaluru – 560071  
Tel: +91 80 6833 5000

## 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,  
Vytila, 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

2nd Floor, Block T2 (B Wing),  
Lodha Excelus, Apollo Mills Compound, N M  
Joshi Marg, Mahalaxmi, Mumbai- 400011  
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

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KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011 Phone: +91 22 3989 6000, Fax: +91 22 3983 6000

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