

TAX FLASH NEWS

7 May 2021

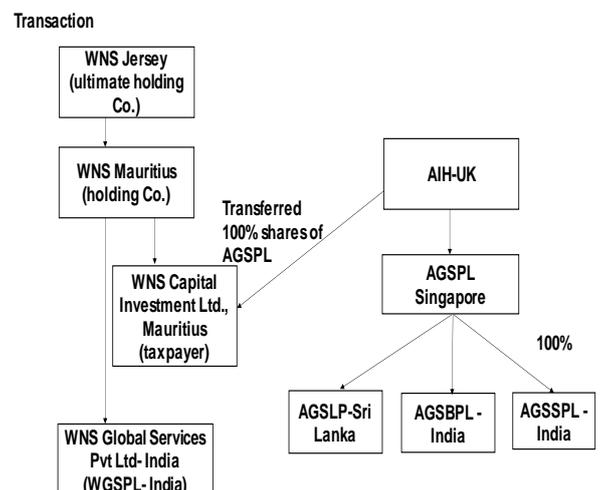
TDS liability cannot be fastened on a transaction of indirect transfer of shares occurred before the retrospective amendment introduced by the Finance Act, 2012

Recently, the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of WNS Capital Investment Ltd, Mauritius¹ (the taxpayer) dealt with the issue of deductibility of tax at source under Section 195 of the Income-tax Act, 1961 (the Act) on transfer of shares of a Singapore company (having subsidiaries in India) by a UK company to a Mauritian company (the taxpayer) when the transaction has occurred prior to the retrospective amendment made by the Finance Act, 2012 in Section 9(1)(i) and Section 195. The Tribunal held that for a person to deduct tax on the basis of an amendment in the Act which was enacted subsequent to the date on which tax deduction obligations were required to be performed, is expecting that person to do the impossible. When a law is nowhere even on the horizon, leave aside the statute, it is wholly impossible for any person to perform the obligations imposed by such a law. Accordingly, the taxpayer was not liable to deduct tax at source under Section 195 at the time of making payment to the UK company.

The Tribunal distinguished the decision of the Supreme Court in the case of Vatika Township Pvt Ltd² (relied on by the tax department) as the same was on a taxability provision and not on a withholding tax provision. The provisions pertaining to withholding tax obligations require to be dealt with in a manner different than the taxability provisions.

The Tribunal held that once the tax is not required to be deducted under Section 195, the tax demands under Section 201 was not sustainable in law. The Tribunal observed that the issue was entirely tax neutral inasmuch as it was a case in which the person selling the shares have already paid taxes on the capital gains.

Facts of the case



On 11 July 2008, the taxpayer is a subsidiary of WNS Mauritius (WNS-M). WNS-M is a company owned by Jersey based entity. The taxpayer purchased 100 per cent equity shares in Singapore based entity (AGSPL) from UK based entity (AIH-UK). AGSPL, in turn, was holding three subsidiaries i.e. AGSBPL-India, AGSSPL-India, and AGSLP-Sri Lanka. The WNS-M also has a fully owned Indian subsidiary (WGSPL India).

With effect from 1 July 2007 and vide amalgamation approved by the Bombay High Court vide order dated 11 August 2009, the two Indian subsidiaries of AGSPL i.e. AGSBL-India and AGSPPL-India were amalgamated with WGSPL India.

The Assessing Officer (AO) observed that the predominant purpose of the taxpayer's purchasing shares of AGSPL was the underlying assets, by way of shareholdings in AGSBPL-India and AGSSPL-India and hence it attracts taxability of gains on sale of these shares in the hands of the seller of these shares. The

¹ DCIT v. WNS Capital Investment Ltd, Mauritius – [ITA No. 3851/Mum/2018]-Taxsutra.com

² CIT v. Vatika Township Pvt Ltd [2014] 367 ITR 466 (SC)

AO observed that this income was embedded in the payment for the shares as made by the taxpayer, and it had the obligation to deduct taxes from such income. The Commissioner of Income-tax (Appeals) [CIT(A)] held the decision in favour of the taxpayer. The tax department filed an appeal before the Tribunal.

Tribunal's decision

This is a case of payment made by one non-resident to another non-resident and the claim of the AO was that the payment so made by the taxpayer had an income taxable in India embedded therein. Explanation 2 to Section 195, imposes the tax withholding obligations on non-residents in respect of payments involving income taxable in India was introduced by the Finance Act 2012 though purportedly with retrospective effect from 1 April 1962. The Explanation states that the obligation to deduct tax shall apply to all persons, resident or non-resident, whether or not the non-resident person has (i) a residence or place of business or business connection in India; or (ii) any other presence in any manner whatsoever in India.

The Supreme Court in the case of *Kanthi Enterprises v. State of Karnataka* observed that there cannot indeed be any question about the powers of legislature for enacting any law, or making amendment in the law, imposing a tax with retrospective effect, as it is well-settled in law that the legislature can impose tax retrospectively though it cannot be arbitrary and unreasonable³. However, so far as tax deduction requirements under Section 195 are concerned, these requirements impose duties and obligations on a person. The nature of this provision is thus of regulating the conduct of a person so far as tax withholding obligations are concerned. The question, therefore, arises whether such a legislative amendment can also be introduced with retrospective effect. The Tribunal distinguished the decision of the Supreme Court in the case of *Vatika Township Pvt Ltd*⁴ relied on by the tax department as the same was on a taxability provision and not on a withholding tax provision. The provisions pertaining to withholding tax obligations require to be dealt with in a manner different than the taxability provisions.

The Supreme Court in the case of *Engineering Analysis Centre of Excellence*⁵, while dealing with a similar situation held that the 'person' mentioned in Section 195 cannot be expected to do the impossible. The expanded definition of 'Royalty' inserted by Explanation 4 to Section 9(1)(vi), effective from a time when such explanation was not actually and factually in the statute. For a person to perform the tax withholding obligations on the basis of an amendment in law which was enacted on a date later than the date on which tax withholding obligations were required to be performed, is expecting that person to do the impossible. When a law is nowhere even on the horizon, leave aside the statute, it is wholly impossible for any person to perform the obligations imposed by such a law.

The taxpayer, therefore, cannot be faulted for not deducting tax at source from payments made to AIH-UK in respect of purchase of shares in AGSPL, which, in turn, are said to derive substantial value from underlying assets in India.

Accordingly, the Tribunal held that the tax was not required to be deducted under Section 195 at the time of making the said payment. Once it has been held that tax deduction at source is not required under Section 195, the demands under Section 201 was not sustainable in law, as the entire case of the revenue authorities hinges on Explanation 2 to Section 195, and its retrospective application.

Further this issue is entirely tax neutral inasmuch as it is a case in which the person selling the shares, i.e. AIH-UK, is said to have already paid taxes on the capital gains.

The Tribunal observed that where the income in the hands of the seller is upheld, the upholding of levy of interest under Section 234B will only be a natural corollary. Whether interest is charged under Section 201(1A) or under Section 234B, it is to be charged at 1 per cent per month and the levy of interest under one of these provisions is to the exclusion of levy of interest under the other provision.

Our comments

This is an important decision of the Mumbai Tribunal as it has applied the principle of impossibility to the TDS provisions under Section 195 on a transaction of indirect transfer of shares pursuant to retrospective amendment by the Finance Act, 2012. The Courts have already laid down / applied this principle in some of the cases⁶.

Since the amendment was not in force when the payment was made, the retrospective amendment cannot fasten obligation to deduct tax at source. The Tribunal in various cases⁷ have held that if the payment is made prior to an amendment made in the TDS related provisions under the Act, there was no obligation to deduct tax where the amount is credited or paid before such amendment.

The Tribunal has made an important observation that where the income in the hands of the seller is upheld, the upholding of levy of interest under Section 234B will only be a natural corollary. Thus, interest under Section 201(1A) would not apply.

⁶ *Engineering Analysis Centre of Excellence v. CIT* [2021] 125 taxmann.com 42 (SC), *CIT v. NGC Networks (India) Pvt. Ltd.* (ITA No. 397/2015) (Bom)

⁷ *Wifi Networks Pvt. Ltd. v. DCIT* [2016] 177 TTJ 767 (Bang), *Channel Guide India Ltd. v. ACIT* [2012] 25 taxmann.com 25 (Mum), *Kerala Vision Ltd v. ACIT* [2014] 35 ITR(T) 81 (Coch), *Metro & Metro v. ACIT* [2014] 29 ITR(T) 772 (Agra), *ACIT v. NGC Networks (I) Pvt. Ltd.* [2014] 150 ITD 772 (Mum), *Sterling Abrasives Ltd. v. ITO* [2010] 3 taxmann.com 757 (Ahm), *ACIT v. BSR & Co.* [2016] 70 taxmann.com 69 (Mum)

³ *Kanthi Enterprises v. State of Karnataka* [2002] 7 SCC 283, 288

⁴ *CIT v. Vatika Township Pvt Ltd* [2014] 367 ITR 466 (SC)

⁵ *Engineering Analysis Centre of Excellence v. CIT* [2021] 125 taxmann.com 42 (SC)

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,
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

home.kpmg/in



home.kpmg/in/socialmedia



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.

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

© 2021 KPMG Assurance and Consulting Services LLP, an Indian Limited Liability Partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

KPMG (Registered) (a partnership firm with Registration No. BA- 62445) converted into KPMG Assurance and Consulting Services LLP (a Limited Liability partnership firm) with LLP Registration No. AAT-0367 with effect from July 23, 2020.

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.

This document is meant for e-communication only.