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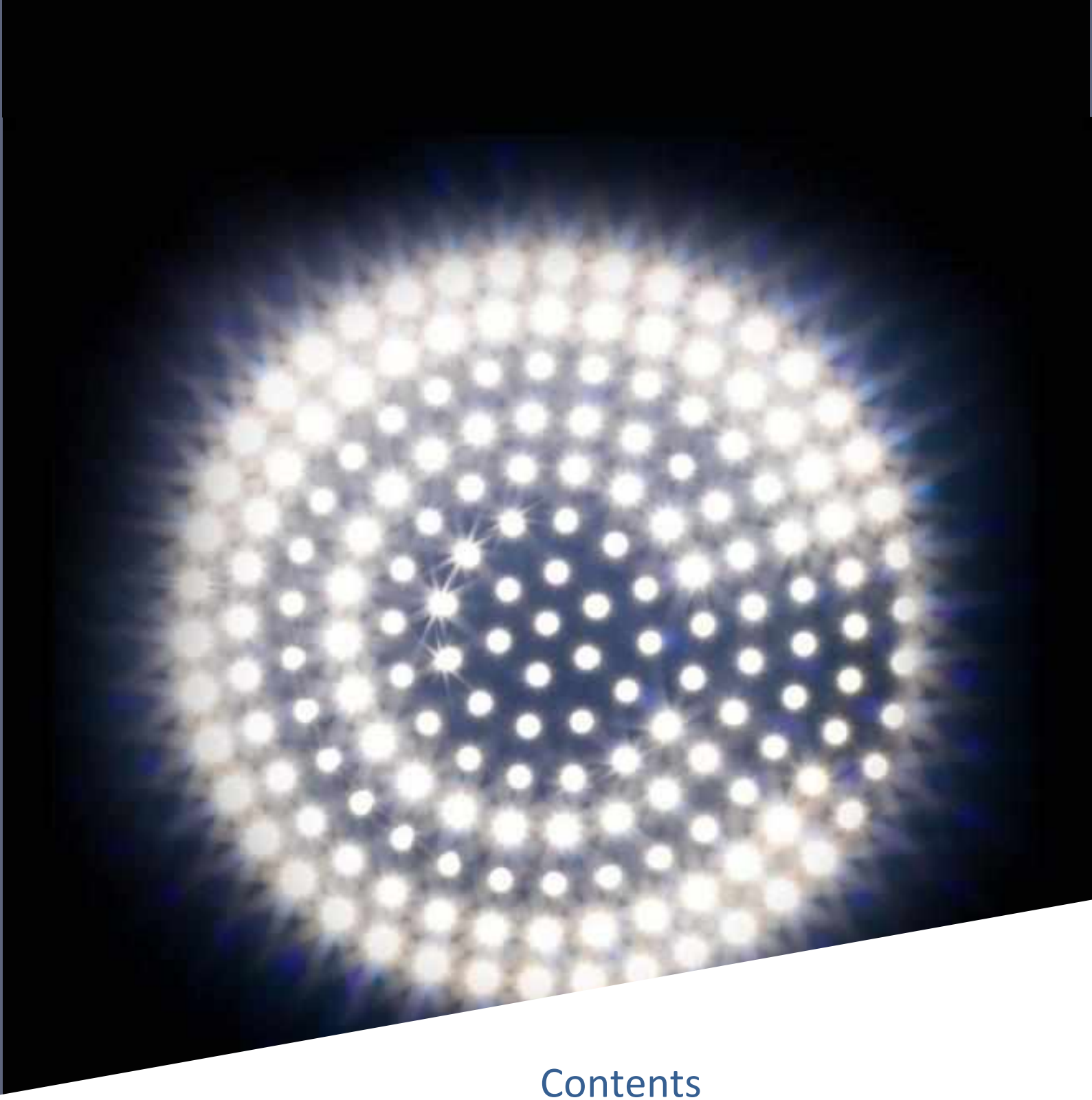
TAXATION TIMES

August 2020

Taxation Times is a monthly newsletter published by UJA specifically with an intent and object to simplify and provide clarity on certain provisions of the Income Tax Act, discuss the implications of various amendments and circulars notified time and again, understand the judicial precedents as decided by various courts and interpret these.

The Taxation Times is an initiative to keep you abreast with the latest development in the realm of the Direct Taxes in India.



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"Our economy is based on spending billions to persuade people that happiness is buying things, and then insisting that the only way to have a viable economy is to make things for people to buy so they'll have jobs and get enough money to buy things."– Philip Slater.

Under the current circumstances, India bears witness to the truth of the above quote. PM Modi is urging the nation to develop an eco-system, which is self - reliant. The primary objective of Make in India was to attract investments from around the world to strengthen India's manufacturing sector and open employment opportunities.

Speaking at the India Global Week 2020, a three day virtual conference, Shri PM Modi said *"We are making the economy more productive, investment friendly and competitive. There are many possibilities and opportunities in various sunrise sectors in India."*

As we look forward to the revival of the Indian economy and world economy at large, it would be interesting to see how the various initiatives which are being undertaken by Government would actually bear fruit to help the economy stand back on it's feet.

Coming back to this month's Taxation Times, here's a look at what's inside:

1. A slump sale is a lucrative business acquisition model. However, before opting for such a transaction, the pros and cons of such a transaction need to be carefully evaluated. Read on to know what a slump sale is and opinions of different courts on structuring of a 'Slump Sale'.

2. Recent decisions by the Delhi Tribunal and Kolkata Tribunal.

3. Circulars, Notifications, Press releases for July 2020 and upcoming compliances for August 2020.

We hope that you find this edition of the Taxation Times useful.

Do you have any inputs to make the forthcoming issues of the Taxation Times more useful & relevant? Please share your feedback on info@uja.in.

We look forward to hearing from you!

Best Wishes,
UJA Tax Team

Slump Sale – Simplified

Slump Sale has been widely used as a business acquisition model in India. A slump sale is typically the transfer of a business undertaking on a going concern basis for a lump sum consideration. Valuation is not done for individual components but for a whole business undertaking.

s. 2(42C) and s. 50B have been introduced by Finance Act 1999 applicable w.e.f AY 2000 – 2001.s. 2(42C) of the Income Tax Act (hereinafter referred to as 'ITA') defines the term 'slump sale' *as* **transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to individual assets & liabilities.**

As per s. 50B in the ITA, the profits & gains arising out of slump sale under s. 2(42C) becomes chargeable under the head 'capital gains'. s. 50B of the ITA lays down the mechanism to compute 'net worth' which is deemed to be the cost of acquisition of the undertaking being transferred for the purpose of s. 48 and 49 of the ITA.

Capital Gain in case of slump sale is computed as under:

Particular	INR
Full Value of Consideration	XXX
Less : Expenditure in relation to transfer	XXX
Less : Net Worth of the undertaking being cost of acquisition & improvement	XXX
Capital Gain/ Loss	XXX

It is to be noted that benefit of indexation is not available in case of slump sale & depending upon the period of holding of the undertaking being transferred, the gain arising from the transfer is classified as long – term or short – term. Also, for the purpose of computing net worth, change in valuation of assets on account of revaluation shall be ignored.

Net Worth is defined in Explanation to s. 50B of the ITA to mean aggregate value of total assets of undertaking or division as reduced by the value of liabilities of such undertaking or division as appearing in it's books of accounts.

Elements of Slump Sale

Based on the definition of s. 2(42C) of the ITA & various judicial precedents from time to time, the following are integral to any slump sale :

1.**There has to be a 'sale' of an undertaking**:

- s. 2(47) of the ITA defines 'transfer' to include sale, exchange, relinquishment, extinguishment of rights. However, it is pertinent to note that for the purpose of slump sale, only 'sale' of an undertaking is regarded as a transfer that is to say – exchange, relinquishment, extinguishment of rights do not fall within the ambit of slump sale and hence provisions of s. 50B do not apply.
- Several business transfers have been structured such that the transferor assessee receives shares of the transferee assessee in exchange of an ongoing business concern. In such cases, such 'exchange' cannot be regarded as 'sale' for the purpose of s. 50B of the ITA.

- The issue relating to the concept of 'Slump Exchange' and its taxability was dealt by Hon'ble Mumbai Tribunal in Bharat Bijlee Limited V. ACIT (ITA No. 6410/Mum/2008) (2011-TIOL-197-ITAT- MUM). In that case, the assessee had transferred its lift division on a going concern basis against allotment of certain number of preference shares and debentures of the transferee company. Such consideration was determined on a lump sum basis and was not allocable to any specific asset of the undertaking transferred. Since, the said transaction is in the nature of 'exchange' and not 'sale', it would not qualify as a 'slump sale' as defined u/s. 2(42C). Consequently, the provisions of s. 50B is not applicable to it and in absence of any specific computation provision.
- Also, it is essential that the assets should be sold against some consideration. If an undertaking is transferred on a going concern basis without any consideration, the same would not be considered as a 'slump sale'. The Hon'ble Mumbai Tribunal in the case of Avaya Global Connect Ltd. V/s ACIT held that if an undertaking has been transferred without any consideration since the liabilities exceeded the assets of the undertaking, the said transaction cannot be regarded as a 'slump sale' in terms of s. 2(42C) of the ITA.
- In another instance, the issue before the Hon'ble Mumbai ITAT in the case of Mahindra Engineering & Chemical Products Ltd. V/s ITO, the transfer of a business by executing 9 separate agreements for transfer of assets & liabilities of the M-Seal division to Pidilite Industries Limited. The Hon'ble ITAT noted that in the commercial world, transactions would have to be considered in totality and that the substance of the transaction is relevant in form. Hence, the transaction of sale of business division by entering into 9 different agreements for transfer of assets & liabilities will qualify as a slump sale for the purpose of the ITA.

2. **The transfer should be on a 'going concern' basis**:

The undertaking should be transferred on a 'going concern' basis. The buyer of the undertaking should purchase the undertaking with all the assets & liabilities and there should be no break or cessation in the business operations of the undertaking being transferred

3. **No individual values to be assigned to the 'assets'**:

The consideration for the slump sale has to be lump – sum without attributing individual values to the assets & liabilities forming a part of the transferred undertaking. The purchaser purchases the entity as a whole & not individual assets & liabilities. Therefore, the business has to be purchased as a whole and the value to individual assets & liabilities need not be assigned. However, here it needs to be noted that for the purpose of determination of an asset or liability for the payment of stamp duty, registration fees or other similar taxes & fees, it can be said to be assignment of values to individual assets & liabilities

Conclusion :

An undertaking transferred on a going concern basis as a result of 'sale' is regarded as 'slump sale'. However, the undertaking is transferred otherwise than by 'sale', the same will not qualify as 'slump sale'.

Whilst 'slump sale' is a preferred arrangement of taking over a business of an entity, there are several practical & commercial challenges, which need to be carefully evaluated before concluding and finalizing such transactions. Needless to say, before entering into such transaction, the tax position can should be critically examined in the light of the facts & circumstances to avoid undue litigation.

Case Law

"In a recent decision, the Hon'ble Delhi ITAT has held that the corporate guarantee fee paid by the taxpayer to it's AE in Netherlands is not liable to tax as 'interest' in India under Article – 11 of the India – Netherlands DTAA. Further, neither can such payments be taxable as 'fees for technical services' under Article – 12 of India – Netherlands DTAA".

Background :

The taxpayer[1] is a company engaged in the business of leasing motor vehicles, financial services and fleet management. The taxpayer had reimbursed actual corporate guarantee fees to it's Associated Enterprise ('AE') – Lease Plan Corporation NV ('LP Corporation'), a Netherland based company. Since the payments were in the nature of reimbursements of actual expenses, no taxes were withheld on such payments.

During the course of the assessment proceedings, the Ld. Assessing Officer ('AO') held that such payments were made to the non – residents and therefore these fall within the purview of s. 9(1)(vii) of the Income Tax Act 1961 ('ITA') and taxable in India as 'fees for technical services'. However, in the assessment order, the Ld. AO merely referred to the fact that taxes should be withheld on reimbursements made under s. 195 of the ITA and disallowed the reimbursements paid.

Before the Ld. CIT(A), the taxpayer submitted that the payments made are not in the nature of 'fees for technical services' as it does not involve any element of technical, consultancy or advisory services. The Ld. CIT(A) noted the facts of the case and confirmed the disallowance made by the Ld. AO. He further held that the reimbursements of expenses can be taxable in India as 'interest' under Article 11 of India – Netherlands DTAA or 'fees for technical services' as per Article – 12 of India – Netherlands DTAA.

Aggrieved, the taxpayer has preferred an appeal before the Hon'ble ITAT.

Issues for Consideration:

Are the payments made towards reimbursement of corporate guarantee fees chargeable to tax in India as 'interest' as per Article 11 of the India – Netherlands DTAA or 'fees for technical services' as per Article 12 of the India – Netherlands DTAA.

Revenue Contention :

The taxpayer has credit facilities with banks in India and LP Corporation agreed to stand in as a surety in favour of the bank by way of security for the proper discharge by the taxpayer of all obligations paid to the bank. The corporate guarantee given by LP Corporation is maintained until the repayment of the entire loan to the bank.

The Ld. CIT(A) in his appellate order held that no extended meaning can be given to the words '*income deemed to accrue or arise in India'* as per s. 9 of the ITA. Whatever is payable by a resident to a non – resident doesn't always come under the purview of s. 9(1)(vii) of the ITA. Services of a non – resident are taxable in India only if there is sufficient territorial nexus with India so as to furnish a basis for imposition of tax. It must have a direct link with services rendered in India. When such a link is established, the same may be again subject to relief under provisions of the DTAA. The guarantee commission has been paid to the holding company

[1] Lease Plan India (P) Ltd V/s DCIT [2020] 117 taxmann.com 343 (Delhi – Trib)

Pursuant to the agreement extended by it to various banks in India and incase of any default by the taxpayer in India. Thus, the situs of the services have been rendered in India and is the income of the non – resident in as per s. 9 of the ITA. This corporate guarantee fee partakes the nature of 'interest' as per clause 6 of Article 11 of the DTAA.

Alternatively, the Ld. CIT(A) also stated guarantee commission paid could fall within the ambit of 'fees for technical services' since the guarantee fees paid is for enjoying unrestricted and easy access to credit in India. The fees are payable in respect of services utilized in the business carried on in India for earning income in India.

To support this view, reliance was placed on decision of the Hon'ble Madras high Court in Skycell Communications Limited[2] wherein 'technical services' for the use of mobile communications was interpreted, however, 'managerial consultancy' was not dealt with. Reference was also made to the decision of Bharti Cellular[3] Ltd and GVK Industries Pvt. Ltd[4].

Drawing inference from these case laws, It was concluded that certain managerial and consultancy services have been offered by the holding company by way of executing the guarantee agreement in which it has undertaken to bind itself as a surety and in favour of the bank for proper discharge of the subsidiary company's obligation to the bank. Therefore, these can be classified as 'fees for technical services'. In accordance with s. 5(2) and s. 9(1)(i) and s. 90(2), the payments to LP Corporation represent income of non – resident which has accrued or arisen in India on which taxes need to be deducted at source.

Taxpayer Contention:

Before the Tribunal, the Ld. AR placed reliance on the definition of 'interest' as per clause 6 of Article 11 of India – Netherlands DTAA and the guarantee fees paid to LP Corporation does not fall within into the definition of 'interest'. Thereafter, attention was invited to Clause 5(b) of Article 12 of the DTAA wherein it is clearly held that to satisfy the condition of chargeability of fees for technical services, such services should have been 'made available' to the taxpayer. Accordingly, the corporate guarantee fees is neither 'interest' nor 'fees for technical services'. Therefore, since the income of the non – resident is not taxable in India and therefore no taxes to be withheld'.

He placed reliance on the decision of the Hon'ble SC in GE India Technology P Limited[5] and Kotak Securities Limited[6] to define the scope of fees for technical services. Several other case laws were referred to wherein it was held that when services are not made available to the taxpayer, the payments cannot be construed as fees for technical services. Attention was also invited to the decision of the co-ordinate bench in the case of Idea Cellular Limited, Capgemini SA, Neo Sports Broadcast Private Limited[7]and circular No. 202 dtd. 5th July 1976 to submit that guarantee commission is neither interest nor fees for technical services.

To further support his contention, the AR relied on the decision of the Delhi Tribunal in the case of Johnson Matthey Public Ltd Company[8] where the co-ordinate bench after holding that Guarantee Commission Fee is not interest, nor fees for technical services, not even business income but classified the same as 'Other income' as per Clause 23 of India – UK DTAA. However, since the Other Income clause is not present in the India – Netherlands DTAA, the corporate guarantee fee cannot be charged as 'other income' either.

Decision:

The Hon'ble Tribunal has considered the contentions of both the parties and examined the transaction in light of Article 11 and Article 12 of India – Netherlands DTAA.

As per Article 11, to consider income as 'interest', two criteria need to be satisfied :

i. Provision of capital and

ii. It should be in the form of a debt claim

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[2]Skycell Communications Limited 251 ITR 53 – Madras High Court
[3]CIT V/s Bharti Cellular Ltd. 319 ITR 139 – Delhi High Court
[4]GVK Industries Pvt Ltd – Supreme Court (371 ITR 453)
[5]GE India Technology (P) Ltd V/s CIT (327 ITR 456) (Supreme Court)
[6]CIT V/s Kotak Securities Ltd (383 ITR 1)(Supreme Court)
[7]Idea Cellular Ltd V/s ADIT (Intl. Taxation), Capgemeni SA V/s ACIT (Intl. Taxation), Neo Sports Broadcast Private Limited V/s CIT (TDS) Mumbai 159 ITD
[8] Johnson Mathey Public Limited Company V/s DCIT (International Taxation) New Delhi.

In the present case, the taxpayer has reimbursed the corporate guarantee fees to it's AE. The AE has not provided any capital to the taxpayer on which income is earned. Further, there should be 'debt' and there should be a 'claim' on that debt and 'form' which income should arise to qualify as 'interest'. The word 'debt claim' predicate the existence of debtor – creditor relationship and this relationship arises only when there is a provision of capital. In the instant case, there is no provision of capital & therefore the corporate guarantee fee cannot be cannot be classified as 'interest' as per Article 11.

As per Article 12(5) of India – Netherlands DTAA, 'fees for technical services' means payments of any kind to any person in consideration for rendering technical or consultancy services. Looking at the nature of 'service' provided by LP Corporation in providing guarantee, it is a financial service can cannot by any stretch of imagination be considered as 'consultancy services'. Even otherwise, it does not cross the threshold of 'make available' in Article 12(5)(b) of India – Netherlands DTAA. Hence, corporate guarantee fee cannot be held to be 'fees for technical services'.

In view of the aforesaid contentions, the reimbursement of corporate guarantee fees is neither 'interest' nor 'fees for technical services' and therefore not taxable in India. Hence, deleted the disallowance made by the AO.

"In a recent decision, the Hon'ble Kolkata ITAT has held that s. 68 of the ITA cannot be invoked when shares are allotted in exchange of investment in shares and the taxpayer has not received any sum of money for such allotment of shares".

Case Walkthrough:

The taxpayer[9] is a company engaged in the business of manufacturing of MS Ingots and has filed its return of income declaring a loss. During the Assessment Year (AY) under consideration, the taxpayer had received INR 6,00,00,000/- on account of share capital & share premium. The Assessing Officer ('AO') during the course of the assessment proceedings disallowed and added back to the total income of the taxpayer the aforesaid sum as unexplained cash credit under s. 68 of the Income Tax Act 1961 ('ITA'). Aggrieved, the taxpayer preferred an appeal before the Hon'ble CIT(A). Before the CIT(A), the taxpayer contended that s. 68 of the ITA could not be invoked since no money was received against the allotment of shares. The shares were issued against the purchase of their investment in shares of Zest Marcom Private Limited. The issue of shares was recorded by way of a book entry. The taxpayer relied on the decision of the Hon'ble Calcutta High Court[10].

The submission of the taxpayer was remanded back to the AO who in turn confirmed the aforesaid facts. The CIT(A) deleted the disallowance made by the AO citing that s. 68 has no applicability when shares were allotted by the taxpayer under a barter system.

The revenue has preferred the appeal before the ITAT.

Matters before the Authority:

Can the said amount of INR 6,00,00,000/- be treated as unexplained cash credits under s. 68 of the ITA?

Decision :

The Tribunal perused the material on record. The case of the taxpayer was clearly covered in in the case of M/s Bhagwat Marom Pvt. Ltd[11]which was in favour of the taxpayer. In the said case, it was observed that shares were issued to the assessee company during the year under consideration at premium to certain companies in lieu of shares held by the said companies and thus there was no inflow of cash involved in these transactions. The said transactions were covered into the books of accounts of the assessee by way of journal entries and this did not involve any credit to the cash amount. Reliance was also placed on M/s Jatia Investment Co. (supra).

Conclusively, the decision of the CIT (A) was upheld by the ITAT and the deletion of the said amount was confirmed.

[9] DCIT V/s Alishan Steels Pvt. Ltd (Kolkata Tribunal – I.T.A No. 2246/KOL/2017)
[10] Jatia Investment Co V/s CIT [206 ITR 718][11]
[11] ITO V/s Bhagwat Marom Pvt. Ltd (Kolkata Tribunal)

Due dates for Compliance under Income tax

- Due date for deposit of Tax deducted/collected for the month of July, 2020. However, all sum deducted/collected by an office of the government shall be paid to the credit of the Central Government on the same day where tax is paid without production of an Income-tax Challan

- Due date for issue of TDS Certificate for tax deducted under section 194-IA in the month of June, 2020*
- Due date for issue of TDS Certificate for tax deducted under Section 194-IB in the month of June, 2020*
- Due date for issue of TDS Certificate for tax deducted under Section 194M in the month of June, 2020*

- Quarterly TDS certificate (in respect of tax deducted for payments other than salary) for the quarter ending June 30, 2020*
- Certificate of tax deducted at source to employees in respect of salary paid and tax deducted during Financial Year 2019-20

  The due date for issuing certificate has been extended from June 15, 2020 to August 15, 2020 vide the Taxation and Other Laws (Relaxation of Certain Provisions) Ordinance, 2020 read with Notification No.35 /2020, dated 24-06-2020.

- Due date for furnishing of challan-cum-statement in respect of tax deducted under section 194-IA for the month of July, 2020*
- Due date for furnishing of challan-cum-statement in respect of tax deducted under Section 194-IB in the month of July, 2020*
- Due date for furnishing of challan-cum-statement in respect of tax deducted under Section 194M in the month of July, 2020*

Notifications & Circulars

Circulars :

1. A circular was issued by the CBDT giving One-time relaxation for Verification of tax-returns for the Assessment years 2015-16, 2016-17, 2017-18, 2018-19 and 2019-20 which are pending due to non-filing of ITRV form and processing of such returns.

   https://www.incometaxindia.gov.in/communications/circular/circular_13_2020.pdf

2. A clarification was issued in relation to notification issued under clause (v) of proviso to section 194N of the Income-tax Act, 1961 (the Act) prior to its amendment by Finance Act, 2020 (FA, 2020)-Reg.

   https://www.incometaxindia.gov.in/communications/circular/circular_14_2020.pdf

Notification :

1. CBDT notified the National Pension Scheme – Tier II – Tax Saver Scheme.

   https://www.incometaxindia.gov.in/communications/notification/notification_45_2020.pdf

2. Amendment to rule 31A, in sub-rule 4 was also notified by the CBDT.

   https://www.incometaxindia.gov.in/communications/notification/notification_43_2020.pdf

Press Releases :

1. CBIC and CBDT sign MoU to facilitate smoother bilateral exchange of data
   https://pib.gov.in/PressReleasePage.aspx?PRID=1640147

2. MoU between CBDT and MoMSME signed
   https://pib.gov.in/PressReleasePage.aspx?PRID=1639978

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