

Direct Tax Alert

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Mumbai Tribunal grants relief to deductor from withholding tax obligation on account of impossibility of performance, on transaction involving indirect transfer of shares

The Mumbai Bench of the Income-tax Appellate Tribunal has upheld the non-applicability of withholding tax obligation (and consequential interest liability) in the hands of a non-resident deductor, on transaction involving indirect transfer of shares, where such obligation has arisen only on account of the retrospective amendment introduced in section 195 of the Income-tax Act, 1961. The Tribunal placed reliance on the Supreme Court decision in the case of *Engineering Analysis*¹ which has upheld the principle of *impossibility of performance*.

This case involved a transaction concerning acquisition of shares of a Singapore company by a non-resident Mauritius company from a non-resident UK seller on July 11, 2008. In this regard, a question arose as to whether the buyer was liable to withhold tax on the consideration paid to the seller considering that the transaction was

undertaken in 2008 i.e. prior to the retrospective amendment introduced in section 9(1)(i) of the Income-tax Act, 1961 ('the Act') read with section 195 of the Act by Finance Act 2012. The Mumbai Tribunal² has held that, as on the date of performing the withholding tax obligation (i.e. in July 2008), when a law is nowhere even on the

¹ *Engineering Analysis Centre of Excellence v. CIT* [2021] 125 taxmann.com 42 (SC)

² *DCIT v. WNS Capital Investment Limited, Mauritius* [ITA No. 3851 / Mum / 18], *WNS Capital Investment Limited, Mauritius v. DCIT* [C.O. No. 147 / Mum / 2019]

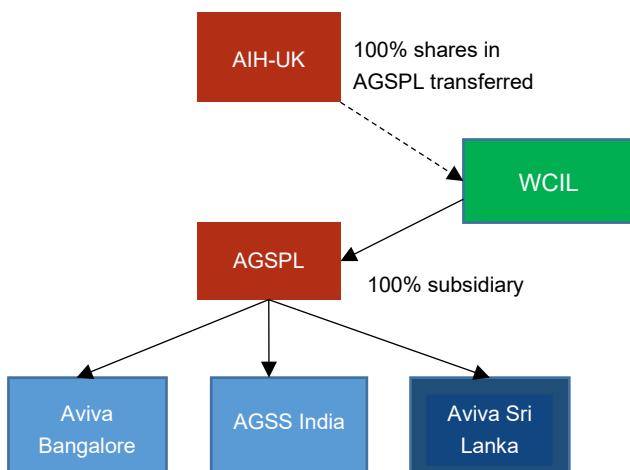


horizon, leave aside the statute, it is wholly impossible for any person to perform the obligations which arise retrospectively imposed by such law. The Tribunal accordingly ruled in favour of the deductor/buyer by affirming that there was no obligation to withhold tax on the consideration paid to the seller and also quashed the levy of consequential interest under section 201(1A) of the Act.

This alert attempt to summarise the decision of the Mumbai Tribunal.

Facts of the case

- WNS Capital Investment Limited ('WCIL' or 'the buyer/deductor'), a Mauritius company, acquired 100% equity shares of Aviva Global Services Singapore Pte Ltd. Singapore ('AGSPL Singapore') from Aviva International Holdings Ltd., UK ('AIH-UK' or 'the seller/deductee') on July 11, 2008 ('the transaction'). At the time of acquisition, AGSPL Singapore was a holding company of three subsidiaries (i) Aviva Global Services (Bangalore) Pvt. Ltd. India ('Aviva Bangalore') (ii) Aviva Global Shared Services Pvt. Ltd., India ('AGSS India') and (iii) Aviva Global Services Lanka (Pvt.) Ltd. Sri Lanka. For ease of understanding, a diagrammatic representation of the aforesaid transaction is as under:



- The Assessing Officer contended that the predominant purpose of the buyer to purchase shares of AGSPL Singapore was to gain control of the underlying assets, by way of shareholdings in Aviva Bangalore and AGSS India. Though the transfer was of AGSPL Singapore's shares, it derived substantial value, directly or indirectly, from assets in India in view of Explanation 5 to section 9(1)(i) of the Act, which was introduced retrospectively by Finance Act 2012. Thus, capital gains on transfer of AGSPL Singapore's shares was taxable in India. Accordingly, it is the sale of these shares which attracts the tax liability in the hands of the seller and income in respect of these shares was embedded in the consideration paid by WCIL to AIH-UK.
- As per the domestic law provisions, even non-residents were obligated to withhold tax from any payment made by such non-resident to other non-residents and hence WCIL had defaulted in not withholding tax from payment made to AIH-UK and accordingly, demand for principal tax on capital gains was raised under section 201(1) along with interest for delay in realisation of tax.
- The CIT(A) noted that AIH-UK had discharged / paid the tax to the extent of principal tax demand, and on verification of this fact, the demand under section 201(1) was deleted. In respect of interest levied under section 201(1A) of the Act, the CIT(A), *inter-alia*, relied on the decision of the Bombay High



Court in the case of NGC Networks³ and deleted the same.

- The Department was thus in appeal before the Tribunal against the relief so granted. The Assessee had also filed Cross Objections before the Tribunal taking various grounds including on non-taxability of capital gains arising from the transaction.

Ruling of the Tribunal

- The Tribunal observed that a statutory provision which imposes the tax withholding obligation on non-resident was introduced by the Finance Act, 2012 – though purportedly with retrospective effect from April 1, 1962.
- The Tribunal referred to the recent Supreme Court decision in the case of *Engineering Analysis (supra)* and held that for a person to perform the withholding obligations on the basis of an amendment in law, which was enacted subsequent to the date on which withholding tax obligations were required to be performed, is expecting that person to do the impossible.
- The Revenue's reliance on the decision of Supreme Court in the case of *Vatika Township*⁴ on validity of retrospective amendment is also not relevant as it dealt with a taxability provision and not with a withholding tax provision. The provisions pertaining to withholding tax obligations require to be dealt with in a manner different than the taxability provisions and, thus, the said decision was distinguished.

- Basis the above, the Tribunal held that WCIL cannot be faulted for not deducting tax from the payment made to AIH-UK.
- Separately, the Tribunal observed that the entire transaction was anyway tax neutral since the seller had already paid taxes on the capital gains and independent proceedings in the seller's case are in progress.
- The Tribunal further observed that if the taxability in the hands of the seller is upheld, interest under section 234B of the Act would be a natural corollary and thus levy of interest either under section 201(1A) or section 234B is to the exclusion of interest under the other provision.
- Alternatively, where no income is held to be taxable in India, no demand under section 201 read with section 195 would subsist given that such demand is a vicarious liability.

Dhruva Comments

This is a first of its kind ruling providing relief in respect of non-applicability of withholding tax obligation on a past transaction involving indirect transfer of shares, where such withholding tax obligation is arising on account of retrospective amendment. The principle of impossibility of performance as applied by the Courts in context of non-applicability of withholding tax obligation on royalty payments pursuant to retrospective amendment in the definition by Finance Act 2012, is now also extended to the provisions governing indirect transfer of shares. Further, even though

³ CIT v. NGC Networks (India) Pvt Ltd [ITA No. 397 of 2015]. In this case, the High Court was dealing with disallowance under section 40(a)(ia) of the Act which had arisen due to short deduction of tax on royalty payment. The definition of royalty being expanded retrospectively vide Finance Act,

2012 entailed deduction of tax under section 194J at a higher rate. The assessee being unable to undertake the same for a transaction prior to amendment, was granted relief on account of impossibility of performance.

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



the Delhi Tribunal⁵ deleted the interest levied under section 234B of the Act on account of retrospective amendment in respect of an indirect transfer transaction, there was no judicial precedent till date which exempted the interest levy in the hands of the deductor. This is a welcome decision which will go a long way in providing relief to non-resident payer who have been facing the brunt of the Revenue pursuant to the introduction of the retrospective amendments in section 9(1)(i) read with section 195 of the Act. Further, this decision will also provide relief to

taxpayers, in general, in cases where taxpayers would have been expected to withhold taxes on the basis of subsequent amendments in law.

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⁵ Cairn India Holdings Ltd v. DCIT [ITA No. 1669/Del/ 2016]



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