[2021] 436 ITR 474 (AAR)

[BEFORE THE AUTHORITY FOR ADVANCE RULINGS — MUMBAI BENCH(INCOME-TAX)]

PSIT PTY. LTD., IN RE

G. CHOCKALINGAM *J. (Vice-Chairman)* , KISHORE KUMAR VYAWAHARE *Member Revenue* and INDER KUMAR *Member Law*

July 29, 2019.

Section(s): Income-tax Act, 1961, ss. 50D, 55A, 56(2)(viia), 112(1)(c)(iii)
Favouring: Assessee, person

NON-RESIDENT — CAPITAL GAINS — FOREIGN COMPANY HOLDING ALL BUT ONE SHARES IN INDIAN COMPANY — SALE OF ENTIRE SHAREHOLDING IN INDIAN SUBSIDIARY BY FOREIGN HOLDING COMPANY — NOT A CASE OF SLUMP SALE BUT OF SALE OF SHARES — VALUE OF SHARES ASCERTAINED — CAPITAL GAINS CHARGEABLE AT TEN PER CENT. — INCOME-TAX ACT, 1961, ss. 50D , 55A , 56(2)(viia) , 112(1)(c)(iii)

The applicant-company incorporated in and a tax resident of Australia, held all but one of the equity shares in IEE, an Indian company, the one share being held by a nominee of the group. The IEE shares were not listed on any recognized stock exchange in India. In September, 2012 the applicant entered into a share purchase agreement with R, a wholly owned subsidiary of APXL, for sale of its equity shareholding in IEE for a consideration of AUD 5.34 per share, totalling AUD 3,49,99,994.66. The shares E were transferred to the buyer by the applicant on October 15, 2012. The applicant sought a ruling on the question whether the capital gains on transfer of equity shares in IEE would be taxable in the hands of the applicant at the rate of 10 per cent. in accordance with section 112(1)(c)(iii) of the Income-tax Act, 1961 (as against the Department's contention that it was a case of slump sale). The Authority, on the stated facts, ruled :

(i) That the applicant, an Australian company, had sold its entire shareholding in its wholly owned Indian subsidiary to an entity of the APXL group. The Department's contention that the transaction was more than a share transfer was not correct. This was not a case of slump sale. All the assets and liabilities of IEE remained with IEE after the transfer. The share purchase agreement revealed that all strategic agreements automatically stood terminated with effect from the closing of the share purchase agreement. What was transferred was the shares in IEE and neither the subsidiary itself nor its undertaking was the subject matter of sale.

PR. CIT v. UTV SOFTWARE COMMUNICATION LTD. [2019] 103 taxmann.com 12 (Bom) *followed*.

(ii) That the capital gains on transfer of equity shares in IEE would be taxable in the hands of the applicant at the rate of 10 per cent. in accordance with section 112(1)(c) (iii) of the Income-tax Act, 1961.

(iii) That the applicant had provided a valuation report prepared by B & Co. The valuation report listed out various projections and assumptions and after employing the discounted cash flow method, the value of share was arrived at AUD 5.34 (Rs. 372) per share. The actual share transfer had happened at Rs. 182 per share owing to hard bargaining by the buyer. Thus, the value of the shares was ascertained. Thus the fair market value of the capital assets on the date of transfer could not be deemed to be the full value of the consideration received in terms of section 50D nor was reference to the valuation officer under section 55A to ascertain the fair market value called for.

(iv) That the difference between the ascertained price and the actual sale price would be income of the buyer under section 56(2)(viia) and was not pertinent to the case of the applicant, the seller of the shares. The Department was at liberty to proceed against the buyer on the differential between the fair market value and actual sale price in terms of section 56(2)(viia) .

Cases referred to :

Bacha F. Guzdar (Mrs.) v. CIT [1955] 27 ITR 1 (SC) (para 12)
CIT v. Gauranginiben S. Shodhan [2014] 367 ITR 238 (Guj) (para 12)
CIT v. Nilofer I. Singh (Smt.) [2009] 309 ITR 233 (Delhi) (para 12)
CIT (Pr.) v. Quark Media House India (P.) Ltd. [2017] 391 ITR 145 (P&H) (para 12)
CIT (Pr.) v. UTV Software Communication Ltd. [2019] 103 taxmann.com 12 (Bom) (para 12)
Vodafone International Holdings BV v. Union of India [2012] 341 ITR 1 (SC) (paras 12, 15, 16)

A. A. R. No. 1459 of 2013 .

Pranay Kothari, authorised representative, for the applicant.

S. Anbuselvam, Joint Commissioner of Income-tax, for the Department.

RULING

1. The applicant is a company incorporated in Australia and also a tax resi dent of Australia. The applicant is inter alia engaged in the business of wholesale trading of consumer electronics and domestic appliances in Aus-

tralia and New Zealand. The applicant held equity shares of IEE Pvt. Ltd. (earlier known as "PW(I) Pvt. Ltd.") an Indian company. The details with respect to acquisition of equity shares by the applicant in IEE Pvt. Ltd. are as follows :

Sl. No.	Date of acquisition	Number of equity shares	Total cost in INR	Total cost in AUS $
1	April 18, 2006	10,000	100,000	2,999.40
2	July 12, 2006	1,89,000	162,540,000	4,665,996.84
3	June 4, 2007	1,974,353	169,794,358	5,040,651.86
4	March 27, 2009	2,674,420	230,000,120	6,479,789.27

2. The applicant was holding all 65,48,772 but one equity share of IEE Pvt. Ltd. The other one share was held by PMIT Pty. Ltd., a company from PSIT Group, as nominee shareholder for the benefit of the assessee in whom the beneficial ownership of the shares resided. The IEE Pvt. Ltd. is a wholly owned subsidiary of the applicant. The IEE Pvt. Ltd. is a private limited company engaged in the business of wholesale trading of electronic appliances/equipment in India. The shares of IEE Pvt. Ltd. are not listed on any recognized stock exchange in India. In September 2012 the applicant entered into a share purchase agreement with RAIL Ltd. ("the buyer") for sale of equity shares of IEE Pvt. Ltd. The buyer is a wholly owned subsidiary of APXL Sons and is engaged in the business of retailing consumer electronics and domestic appliance goods in India. As per the share purchase agreement 65,48,772 equity shares of IEE Pvt. Ltd. were sold to the buyer for a consideration of AUD 3,49,99,994.66. The consideration agreed to be paid by the buyer to the assessee was AUD 5.34 per share. The equity shares of IEE Pvt. Ltd. were transferred to the buyer by the applicant on October 15, 2012.

3. The applicant in its application filed with the authority on February 21, 2013 and has formulated the following question :

"Based on the facts and circumstances of the case and in law, whether the capital gains on transfer of equity shares of IEE Pvt.Ltd. will be taxable in the hands of the applicant at the rate of 10 per cent. in accordance with section 112(1)(c)(iii) of the Income-tax Act, 1961 ("the Act") ?"

4. The applicant contends that it is a tax resident of Australia and as per article 13(5) of the India-Australia Tax Treaty on "Alienation of property", the sale of equity shares of IEE Pvt. Ltd. may be taxed in India. Accord-

ingly, the sale of equity shares of IEE Pvt. Ltd. will be subject to tax in India as per the provisions of section 45 of the Income-tax Act, 1961. As per section 45 of the Act, any profits or gains arising from the transfer of a capital asset shall be chargeable to tax under the head "Capital Gains" and shall be the income of the transferor in the year in which the transfer occurs. Given the fact that the applicant has held the equity shares of IEE Pvt. Ltd., for a period in excess of 12 months, the gains of sale of equity shares would qualify as long-term capital gains. Since the shares of IEE Pvt. Ltd. have been sold by the applicant on October 15, 2012, the provisions of the Act as applicable to the financial year 2012-13, i. e., the assessment year 2013-14. The tax rate for long-term capital gains to non-resident with effect from the assessment year 2013-14 is 10 per cent. under section 112 of the Act so the gains be taxed at 10 per cent.

5. The Department argues that on perusal of the material on record, the applicant has not transferred the shares of the Indian subsidiary but the Indian business unit to the buyer. In this regard, the Departmental representative refers to the title of the agreement that has been entered into by the applicant, it is called strategic alliance agreement. It is not simple share purchase agreement, but it is strategic transferring of the assets and liabilities of the Indian subsidiary to the buyer.

6. The strategic alliance agreement speaks about the transfer of not only the shares but also the transfer of the assets and liabilities that give intrinsic value to the shares of the Indian company. Therefore, it is submitted that it is not a simple share transfer but transfer of all the assets and liabilities underlying the shares. It is strategic sale and not the sale of shares alone as per recitals 5.2(i) and 5.2(j) of the strategic alliance agreement dated September 2012. The recitals 5.2(i) and 5.2(j) are reproduced herewith—

> 5.2 The following activities shall occur on the closing date simultaneously—
>
> (i) The AS 400 agreement shall come into effect ;
>
> (j) The HK supply agreement shall come into effect ;

> As per recital 1.1 the above terms AS 400 agreement, HK supply agreement, wholesale company has been defined as following :
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> "AS 400 agreement" means an agreement between PSIT Pty. Ltd. Australia and the wholesale company to be executed pursuant to which PSIT Pty. Ltd. Australia will provide to the wholesale, with

effect from closing, use of AS 400 merchandising, inventory control, warehouse management, and accounting systems along with related support services upon terms and conditions specified therein.

"HK supply agreement" means an agreement between PSIT(HK) Sales Limited and the wholesale company in relation to PSIT(HK) Sales Limited providing with effect from closing, buying services to the wholesale company through its Hong Kong buying office upon terms and conditions specified therein.

"Wholesale company" is PW(I) Pvt. Ltd.

7. It is added that as soon as the shares have been transferred to the buyer, the buyer is entitled to the above privileges like use of the accounting systems, warehouse management, inventory control and AS 400 merchandising and also buying services through Hong Kong based company. These agreements have been entered into by the Indian subsidiary, i. e., PW(I) Pvt. Ltd. prior to the closing date of the transaction and thereby there is a sale of these benefits as well to the buyer. Therefore, the above facts clearly show that the transaction is not only for the sale of the shares but other benefits as well. Therefore, after the transaction, the privileges like knowledge of the local vendors, access to the warehouses, access to the foreign suppliers (through HK supply agreement), access to local vendors, the full functional team are being transferred to the buyer. Hence the case of the assessee does not fall under the category of section 112(1)(c)(iii) of the Income-tax Act, 1961 as it is not a simple share transfer agreement but strategic.

8. Further it is submitted that the applicant has sold one of its undertakings and therefore, the transaction falls under the category of slump sale. Slump sale has been defined in section 2(42C) of the Income-tax Act, 1961 which is reproduced herewith - (42C) "slump sale" means the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales.

9. The facts of the case are akin to the definition of slump sale. Here, the applicant has transferred one of the undertakings, i. e., Indian subsidiary PW(I) Pvt. Ltd. to the buyer for a consideration without assigning any value to the assets and liabilities in the sale. The sale consideration has

been paid by the buyer to the applicant based on the strategic alliance agreement which is not a simple share purchase agreement. The agree-

ment speaks about not only transfer of shares but also the benefits, access to the inventory control, warehouse management techniques, access to foreign and local suppliers, manpower of the Indian subsidiary to the buyer and no separate value has been assigned to these assets or liability. Therefore, it can be stated that the transaction is a slump sale and therefore, section 50B of the Income-tax Act, 1961 is attracted and not section 112(1)(c)(iii) and tax rate has to be 40 per cent. and not 10 per cent. as claimed by the applicant.

10. It is argued that the applicant was controlling the affairs of the Indian subsidiary through its key managerial personnel (KMP), i. e., Mr. AS (A Fiji National), who was acting as the chairman and managing director of the Indian subsidiary, i. e., PW(I) Pvt. Ltd. and thus, it can be stated that the applicant was having branch and thereby have permanent establishment in India.

11. The Revenue has stated that since the sale consideration is not ascertainable, the provisions of section 50D are also applicable. Further, it is contended that the reference to the Valuation Officer should be made under section 55A of the Act to determine the fair market value of the capital asset.

12. In response to the Department's contentions, the applicant has made the following submissions :

Sl. No.	Points for consideration	Submission of the applicant
1	Capital gains of the applicant is chargeable to tax under section 112(1)(c)(iii)	(a) The applicant is a non-resident company incorporated in Australia has held equity shares in IEE Pvt. Ltd. (b) Given that IEE Pvt. Ltd. is a private company, IEE Pvt. Ltd. is a company in which public are not substantially interested. (c) The applicant has transferred shares on October 15, 2012 (i.e. the assessment year 2013-14) (d) The provisions of section 112(1)(c)(iii) of the Act introduced with effect from AY 2013-14, provides that the capital gains arising to

		a non-resident would be subject to tax at the rate of 10 per cent. (e) The Finance Act, 2016 and 2017 amended section 112(1)(c)(iii) to extend the benefits to “shares held in a company in which public are not substantially interested” on a retrospective basis from assessment year 2013-14.
		(f) Given that equity shares held by the applicant in IEE Pvt. Ltd. are long-term capital asset, the capital gain would be subject to tax @ 10 per cent. under section 112(1)(c)(iii) of the Act.

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2	Non applicability of slump sale provisions	(a) As per section 2(42C) of the Act, in order for a transaction to be a slump sale it is essential that there is a transfer of an undertaking for a lump sum consideration without assigning values to the individual assets and liabilities. (b) As per section 2(19AA) of the Act, undertaking includes part of undertaking taken as a whole but does not include individual assets or liabilities. (c) From the share purchase agreement, it is clearly evident that the applicant has only transferred equity shares held in IEE Pvt. Ltd. (d) Reliance is placed on the decision of the Bombay High Court in the case of

		Pr. CIT v. UTV Software Communication Ltd. [2019] 103 taxmann.com 12 (Bom) which held that where there is a mere transfer of shares held in a company then there is no transfer of an undertaking and accordingly the provisions of section 50B of the Act cannot be invoked to such a transfer of shares. Reliance is also placed on the below two decisions of the Supreme Court (a) Mrs. Bacha F. Guzdar v. CIT [1955] 27 ITR 1 (SC) (b) Vodafone International Holdings BV v. Union of India [2012] 341 ITR 1 (SC) ; [2012] 17 taxmann.com 202 (f) The Bombay High Court has approved the merger of IEE Pvt. Ltd. with the buyer. (g) Further, the business assets, liabilities, etc. of IEE Pvt. Ltd. continued to be owned and run by IEE Pvt. Ltd.
3	Non-applicability of section 50D of the Act	(a) The provisions of section 50D would be applicable only in case where the consideration accruing as a result of transfer of a capital asset is not ascertainable or cannot be determined. (b) In the present case, the applicant has received a consideration of AUD 34,999,994,66 (c) Given the consideration is ascertained and determined, the provisions of section 50D are not applicable. (d) Reliance is placed on the

		decision of the Bombay High Court in the case of Morarjee Textiles Ltd (ITA No. 738 of 2014)
4	Non-applicability of section 55A of the Act	(a) The provisions of section 55A of the Act can only be triggered where the fair market value of the capital is required to be ascertained. (b) As mentioned in point 4 in the said table, the provisions of section 50D of the Act are not applicable, the provisions of section 55A cannot be triggered. The following judicial precedents support this proposition. CIT v. Smt. Nilofer I. Singh [2009] 309 ITR 233 (Delhi) ; [2009] 176 Taxman 252 (Delhi High Court) Pr. CIT v. Quark Media House India (P.) Ltd. [2017] 391 ITR 145 (P&H) ; [2017] 77 taxmann.com 301 (P&H), CIT v. Gauranginiben S. Shodhan [2014] 367 ITR 238 (Guj) ; [2014] 45 taxmann.com 356 (Guj)

5	Non-constitution of a permanent establishment of the applicant	(a) As per para 7 of article 5(2) of the India-Australia Double Tax Avoidance Agreement, the mere existence of having a wholly owned subsidiary (IEE Pvt. Ltd.) does not constitute a permanent establishment in India. Further it is submitted that Mr. AS is an employee of IEE Pvt. Ltd. and the applicant is not controlling

		the affairs of IEE Pvt. Ltd. through Mr. AS.
6	Provisions of section 56(2) (viia) of the Act.	(a) The Revenue vide its report dated May 16, 2019 has stated that the difference between the fair market value of the shares of IEE Pvt. Ltd. purchased by the buyer vis-a-vis its purchase price, is the income of the buyer. Given that this contention by the Revenue authorities are seeking taxation of the buyer and not the applicant the same has no bearing on the question raised on the taxability of the applicant before the Authority for Advance Ruling.

13. We are carefully considered the rival contentions and perused the docu ments on record. The applicant is an Australian company and has sold the entire shareholding in its wholly owned Indian subsidiary to an entity of APXL group. The question begging attention is determination of tax rate on said transaction. The applicant has insisted that it is a case of share transfer squarely covered under section 112(1)(c)(iii) of the Income-tax Act. The Department on the other hand has raised the following objections :

(i) That the transaction is not of share transfer but also involves trans- fer of entire business operations including HK supply agreement and man- agement and accounting software systems etc.

(ii) The transactions amounts to slump sale and as the subsidiary con- stitute permanent establishment in India in terms of article 13(5) of the India Australia DTAA the income derived from alienation of property other than referred in article 6 becomes taxable in India and would be charged at 20 per cent. or 30 per cent. depending upon whether the assets were short term or long term.

(iii) The provisions of section 50D of the Income-tax Act are appli- cable as there is no clear basis of share price of 5.34 AUD. The provisions of section 55A are applicable as the market value of the capital assets is to be ascertained.

(iv) The difference between fair market value of shares of subsidiary and the stated purchase price is income of the buyer under section 56(2)(viia).

14. From records it is seen that the applicant is operating in India through wholly owned subsidiary (IEE Pvt. Ltd.) and on account of the world wide operations of applicant group, it has established supply agreements and the developed warehouse management, inventory control software and accounting system and the same practices were employed in running

operations in India. It is also noticed that as part of business strategy the applicant group entered into strategic alliance with APXL group in 2006 (much before the impugned sale in 2012), sharing part of its supply chain and other practices. Along with the application what was submitted was share purchase agreement and clause 5.4 of the said agreement mentions that all strategic arrangements would cease with effect from the closing date of share purchase agreement. The Department's contention that the transaction is more than share transfer is thus not correct.

15. The next argument of the Revenue that it is a case of slump sale is not borne out by facts. All the assets and liabilities IEE Pvt. Ltd. remain with IEE Pvt. Ltd. after the transfer and what has changed is the shareholding pattern. Further a perusal of the share purchase agreement, clause 5.4 reveals that all strategic agreement will automatically stand terminated with effect from closing of the share purchase agreement. Furthermore, there is a direct decision of the Mumbai High Court in the case of UTV Software Communication Ltd. [2019] 103 taxmann.com 12 (Bom) on identical issue. There three shareholders accounting for 100 per cent. shareholding in UHEL sold their share to third party and against the stand of the Revenue that the transfer resulted in slump sale, the High Court held that what has been transferred are mere shares and there has been only change in the pattern of holding and there is no transfer of undertaking of UHEL.

16. The facts of the present case are on all fours with the decision of the Mumbai High Court in the case of UTV Software Communication Ltd. [2019] 103 taxmann.com 12 (Bom). As in that case what is transferred here is the shares of IEE Pvt. Ltd. and the subsidiary itself or its undertaking is not subject matter of sale. The Revenue has not presented any contra decision to the above mentioned one.

17. The next contention of the Revenue that the value of share of IEE Pvt. Ltd. is not ascertainable thus the fair market value of the capital assets on

the date of transfer shall be deemed to be full value of the consideration received as per section 50D and also to ascertain the fair market value reference to valuation officer under section 55A is called for. The plea of the Department is not tenable as during the course of hearing the applicant has provided the valuation report prepared by BSR & Co. and the same was shared with the Department and their letter dated May 16, 2019 comments were also offered on the said valuation. The valuation report lists out various projections and assumptions and after employing the discounted cash flow method, the value of share was arrived at 5.34 AUD per share (Rs. 372 per share). The actual share transfer has happened at Rs. 182 per

share owing to hard bargaining by the buyer. Thus, the value of share was ascertained and pleas of the Department are rejected.

18. The next objection is that the difference between ascertained price and the actual sale price is income of buyer as per section 56(2)(viia). The said argument is really not pertinent to the case of the applicant as it is the seller of the shares. The referred section affects the buyer and the Department is at liberty to proceed against the buyer on the differential between fair market value and actual sale price.

19. The last objection is that the wholly owned subsidiary is the permanent establishment of the applicant. Since it is held in preceding paras 14-16 that it is the case of share transfer and undisputably capital gains tax is attracted in the hands of the applicant, the plea is redundant.

20. In the event the question raised in the application is answered in the affirmative, i. e., the capital gains on transfer of equity shares of IEE Pvt. Ltd. will be taxable in the hands of the applicant at the rate of 10 per cent. in accordance with section 112(1)(c)(iii) of the Income-tax Act, 1961.

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