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INTERNATIONAL TAXATION
Case Law Update

A. HIGH COURT

1 *CIT vs. M/s Nokia Solutions and Networks - [TS-960- HC - 2022 (Delhi)]*

For computing profits attributable to the Indian PE of the assessee, net profit margins of the foreign assessee were to be applied and if resultant figures resulted in losses then no profit/income would be attributable to PE

Facts

i) The assessee was a company incorporated in Finland and was engaged in the manufacture and supply of telecom equipment to Indian telecom operators. The assessee had an Indian AE, NSNIPL which was engaged in rendering installation and commissioning services in relation to the telecom network equipment supplied by the assessee. The assessee claimed that its income from the supply of equipment to Indian telecom operators would not be taxable in India as the assessee did not have a PE in India.

ii) During relevant assessment years, the assessee made payments to Indian AE on account of provision for software services.

iii) The Assessing Officer held that the assessee had a DAPE in India on the ground that the Indian AE was involved in market survey, market research, consumer survey, marketing promotion, after-sale services and warranty services which created mutual goodwill for each other and dependency on each other. Furthermore, the engagement of the assessee and Indian AE was end to end which included pre-bid discussions, bid discussions,conclusion of the contract, capturing requirements of the client, design as per requirements of the client, supply of equipment and installation and commissioning of equipment.

iv) The Hon'ble Tribunal held that on a plain reading of Article 7(1) of the DTAA, the question of attributing profits to the P.E. would arise only if the foreign enterprise is making a profit. This is the condition precedent. If it is making a loss then no question arises at all of attributing any profit to the P.E., which would be taxable in India

v) It noted that the Assessing Officer had taken the gross profit margins of the assessee company for 2009 and 2010 as per its audited accounts instead

of the net profit margins. The gross profits margins of the assessee company for 2009 and 2010 were positive, and that was how the Assessing Officer could attribute profits to the P.E. In so adopting the gross profit margins of the assessee company, the Assessing Officer has acted in a manner which was directly contrary to article 7(1) of the DTAA. It is the Net Profits margins which are to be considered for attribution as per the DTAA.

vi) It held that the computation made by the Assessing Officer in his assessment order was incorrect as the Assessing Officer had not allowed the payments made by the assessee to NSNIPL for the services rendered by NSNIPL as a deduction from the profit attributable to the alleged PE. If the said payments were allowed as a deduction from the gross profit figures taken by the Assessing Officer then again the resultant figure would be losses. Consequently, even if the method of attribution adopted by the Assessing Officer was considered to be correct, in any event, there would be no profit/ income attributable to the PE.

vii) Consequently, the Hon'ble Tribunal by following its own order in ***Nokia Corporation (Formerly Nokia Networks Oy.) vs. Asst. DIT(IT) [2007] 17 SOT 25/112 TTJ627 (Delhi),*** concluded that even if the assessee had a P.E. in India, no profit or income could in law at all be attributed to the P.E. which would be taxable in India.

viii) Aggrieved, the Revenue filed an appeal before the Hon'ble Delhi High Court.

Decision

i) The Hon'ble Delhi High Court noted that Article 7 of the India-Finland DTAA clarifies that the issue of taxability of Assessee would arise only if profits accrue to the Assessee and that too only to the extent they can be attributed to its PE in India.

ii) The Hon'ble Delhi High Court dismissed Revenue's appeal as devoid of substantial questions of law upholding the Hon'ble Tribunal order holding that no profit could be attributed to the Assessee even if it had a PE in India since the Assessee had recorded a net loss at the global level.

Note - Revenue conceded that two out of four proposed questions i.e. whether i) Research & Development activities carried on by NSNIPL constituted a PE and (ii) software supplies could be taxed as royalty was covered in Assessee's favour by i) coordinate bench ruling in the case of Adobe Systems Inc. [W.P (C) 2384/2016 dated 16.05.2016] ii) the Hon'ble Supreme Court ruling in the case of ***Engineering Analysis [(2022) 3 SCC 321]*** respectively.

B. TRIBUNAL

2 *DCIT vs. Reliance Industrial Holdings (P.) Ltd, [(2022) 144 taxmann.com 180 (Mum- Tribunal]*

A director who holds no share in the company cannot be treated as Associated Enterprise u/s 92A(j) merely because he is described as KMP in its audited accounts since he cannot be regarded as controlling the company merely by reason of being its director and being described as 'Key Managerial Person' in audited annual accounts. [AY 2008-09 and AY 2010-11]

Facts

i) Information was received by the Assessing Officer from the investigation

wing that the Assessee Company had given a guarantee to the ICICI Bank, Singapore in respect of the loan given to Biomatrix Marketing Pvt Ltd. ('Biomatrix'). The AO while recording the reasons for re-opening the assessment, formed the view that the assessee and Biomatrix, on whose behalf the guarantee was said to be given by the assessee, were associated enterprises and that the ALP adjustment in respect of the above transaction has escaped assessment.

ii) The reasons for coming to such a conclusion were as under:

a) The assessee company had provided a bank guarantee to ICICI Bank, Singapore, for sanctioning loan to M/s Biomatrix.

b) The relationship between the assessee company and M/s Biomatrix was examined and the books of accounts of the assessee revealed that Mr Sandeep Tandon (deceased) who was the director in the assessee company was also a 91% shareholder in M/s Biomatrix at the time of the deal.

c) Further, as per para 10 of the Notes and Accounts of the Audit Report of the financial year 2008-09 of the assessee, Mr Sandeep Tandon was shown as the "Key Managerial Person" ('KMP').

d) Section 92A(2)(j) of the Income-tax Act, 1961, relating to the provision of Transfer Pricing provides:-

"92A(2) for the purpose of sub-section (1) two enterprises shall be deemed to be associated enterprises if, at any time during the previous year (j) "Where one enterprise is controlled by an individual, the other enterprise is also controlled by such individual or his relative or jointly by such individual and relative of such individual;"

e) Accordingly, it was evident that Mr Sandeep Tandon was a person controlling the affairs of both the assessee company and M/s Biomatrix Ltd and hence the assessee and M/s Biomatrix were Associated Enterprises within the ambit of Section 92A(2)(j).

iii) Hence, the assessment was re-opened and the assessment was made after an ALP adjustment in respect of the corporate guarantee extended by the assessee to ICICI Bank Singapore in respect of Biomatrix.

iv) Aggrieved, the assessee carried the matter in appeal before the CIT(A), and even though the assessee had succeeded on other grounds, there was no adjudication on the ground w.r.t reasons for re-opening the assessment as the same was treated as infructuous.

v) The assessee was not satisfied despite the relief given to the assessee by CIT(A) and filed a cross objection before the Hon'ble Tribunal.

Decision

i) The Hon'ble Tribunal held that in the case of reopened assessments first and foremost one has to see the reasons recorded for reopening the assessment, as these were the reasons which gave jurisdiction to the Assessing Officer for initiating and proceeding with

the reassessment and the reasons so recorded must meet the judicial scrutiny.

ii) It relied on the judgement of the Hon'ble Bombay High Court in the case of ***Hindustan Lever Ltd. vs. R.B. Wadkar [(2004) 268 ITR 332 (Bom)]***, and held that it was well settled in law that reasons, as recorded for reopening the reassessment, were to be examined on a standalone basis. Nothing could be added to the reasons so recorded, nor anything could be deleted from the reasons so recorded.

iii) It further added that even though the reasons, as recorded, might not necessarily prove escapement of income at the stage of recording the reasons, such reasons must at least point out to an income escaping assessment and not a mere need for an inquiry which might result in detection of an income escaping the assessment.

iv) It noted that the only basis recorded in the reasons for re-opening the assessment was for the assessee being treated as the associated enterprise of Biomatrix (wherein Mr. Sandeep Tandon held 91% equity and who was also a Director in the assessee company) was that as per para 10 of the Notes and Accounts of the Audit Report of the financial year 2008-09 of the assessee, Mr Sandeep Tandon was shown as the "Key Managerial Person" (and that consequent ALP adjustment had escaped assessment.)

v) It added that just because someone was described as a KMP in the annual accounts and was a director of the company, it cannot be said that, "enterprise is controlled by an individual" as was the necessary precondition for invoking Section 92A(2)(j).

vi) It further added that in order to be said to be in control of another company, as stated in section 92A(2)(b) and (f), either such person should hold more than 26% of the voting power of the company or such person appoints more than half of the directors or members of the governing board or one or more of the executive directors or members of the governing board. Clearly, the connotations of 'control' in the scheme of Section 92A(2) were far more cogent than visualized by a simplistic notion of KMP.

vii) It held that it was futile to even suggest that a person can be said to be in control of a company merely because he was a director of the company, or he was described as a 'KMP' of the said company in its own choice of words in the annual accounts.

viii) It held that nothing recorded in the reasons for re-opening even remotely suggested that this person had more than 26% voting rights, or even significant voting rights, in the company, that person had the right to nominate less than half the board of directors, or one or more executive directors or the members of the governing body, or that there was anything cogent to signify control over the company.

ix) The Hon'ble Tribunal thus concluded that the reasons recorded by the Assessing Officer did not lead to the conclusion that the assessee and Biomatrix were associated enterprises, and, therefore, it could not be said that any income, on account of ALP

adjustment, had escaped assessment and accordingly, quashed the reassessment proceedings.

3 *Sonakshi Sinha vs. CIT [(2022) 142 taxmann.com 414 (Mumbai- Trib.)]*

Foreign Tax Credit could not be disallowed where the assessee had filed Form No. 67 before the completion of the assessment even though the same was not in accordance with Rule 128(a) of the Income-tax Rules (pre-amended) which required the same to be filed on or before the due date of filing of ITR u/s 139(1). [AY 2018-19]

Facts

i) The assessee, an individual and an actor by profession provides services for the promotion and marketing of brands of goods, services, and events. For the year under consideration, the assessee filed its Return of income declaring a total income of ₹ 18,53,90,330. Further, the case was selected for scrutiny under the limited scrutiny criteria for the issue of double taxation relief u/s 90/91 of the Income-tax Act, 1961 ('Act'). The requisite notice u/s 143(2) of the Act was issued

ii) The learned AO had found that the assessee had claimed a foreign tax credit amounting to ₹ 29,21,327. However, from the filing portal, it was observed that the assessee had uploaded form No 67 for claiming foreign tax credit on January 20, 2020, whereas Assessee had filed her Return of Income on September 22, 2018, which was within the due date as per provisions of Section 139(1) of the act.

iii) The AO was of the opinion that the assessee had failed to comply with the letter and spirit of Rule 128(9) of the Income-tax Rules, 1962 ('Rules') which says that form number 67 was required to be filed for claiming foreign tax credit on or before the date of filing of the return. Further, AO also noted that the assessee uploaded Forn 67 after being served with 2 notices of assessment. Thus, the AO disallowed the foreign tax credit claimed by the assessee.

iv) The assessee filed an appeal before National Faceless Assessment Centre ('NFAC'). The assessee claimed before the NFAC that filing form number 67 was a procedural requirement and not a mandatory requirement for claiming the foreign tax credit. Merely because form number 67 was not filed within the due date prescribed in Section 139 (1) of the act but during the course of assessment proceedings, the assessee should not be denied credit for foreign taxes paid. The Assessee further relied on the judgment of Brinda Ramakrishna versus Income Tax Officer 5(3)(1) Bangalore (2021) ITA No. 454/bang/2021 dated 17/11/2021, along with several other decisions which stated that rule 128 being merely a procedural provision, any default in its compliance should not result in disallowance of the credit eligible to be allowed and claimed.

v) However, the CIT(A) rejected the claim of the assessee that the filing of the form at any time would make the rule absurd and also mentioned that all the beneficial provisions should be interpreted strictly as was held by Honourable Supreme Court in ***Ramnath & Co. vs. CIT [116 taxmann.com 885].*** Thus, the appeal of the Assessee was dismissed.

vi) Aggrieved, the assessee filed an appeal before the Hon'ble Tribunal.

Decision

i) The Hon'ble Tribunal after considering the facts of the case noted that the co-ordinate bench in the case of 42 ***Hertz Software India (P.) Ltd vs. ACIT [2022] 139 taxmann.com 448 (Bangalore - Trib.)*** relied on its earlier decision in the case of ***Ms. Brinda Rama Krishna vs. ITO [2022] 135 taxmann.com 358 (Bang - Trib)*** wherein it was held that "one of the requirements of Rule 128 for claiming FTC is that Form 67 is to be submitted by assessee before the filing of the returns and that this requirement cannot be treated as mandatory, rather it is a directory in nature. This is because Rule 128(9) does not provide for disallowance of FTC in case of delay in filing Form No. 67. Further, the Hon'ble Tribunal noted that the same view was taken by a coordinate division bench in ***Vinodkumar Lakshmipathi vs. CIT(A) NFAC ITA No.680/Bang/2022 dated 06.09.2022.***

ii) It held that it was well settled that while laying down a particular procedure, if no negative or adverse consequences were contemplated for non-adherence to such procedure, the relevant provision was normally not taken to be mandatory and it was considered to be purely directory and that admittedly Rule 128 did not prescribe denial of credit of FTC.

iii) It further added that the Act i.e. section 90 or 91 also did not prescribe a timeline for filing such declaration on or before the due date of filing of ROI. It also added that Rule 128(4) clearly mentioned the situations in which the claim of FTC would not be allowed whereas Rule 128(9) does not say that if the prescribed form would not be filed on or before the due date of filing of the return no such credit would be allowed.

iv) It further noted that by the amendment to the rule with effect from 1 April 2022, the assessee could file such form number 67 on or before the end of the assessment year. Therefore, the legislature in its own wisdom had extended such a date which is beyond the due date of filing of the return of income.

v) It distinguished the case of the assessee with the issue involved in the decision of the Hon'ble Supreme Court in the case of Wipro Ltd by saying that here it was not the case of violation of any of the provisions of the Act but of the rule, which did not provide for any consequence, if not complied with.

vi) Thus, the Hon'ble Tribunal concluded that foreign tax credit should be granted to the assessee after filing Form 67, even if it has filed the same after the due date of filing the Return of Income.

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"Truth can be stated in a thousand different ways, yet each one can be true."

— *Swami Vivekananda*