Tax Update

March 05, 2020

Dear All,

Taxation of indirect transfer of shares (i.e. shares of a foreign company which derives substantial value from the assets located in India) has been one of the most debated issues under the direct tax laws in India.

With this update, we are delighted to share with you that in a matter involving indirect transfer of shares, we have received the Order of the Hon'ble Income-tax Appellate Tribunal (**ITAT**) Mumbai, in favor of the taxpayer (Sofina S.A, Belgium). The ITAT upheld the contention of the taxpayer allowing the benefit of the Double Taxation Avoidance Agreement (**DTAA**) between India and Belgium. This matter was argued by ELP, Taxand India along with a Senior Counsel.

Brief overview of the facts and ruling of the ITAT is set out below:

Facts:

- The taxpayer is an investment company registered in Belgium and listed on Euronext, Brussels. The taxpayer had acquired shares of a Singapore company to the extent of 11.34%, which in turn held 100% shares in an Indian Company.

- Taxpayer sold its entire shareholding in the Singapore Company to the Buyer, which deducted taxes at the rate of 43.26% on the capital gains. Pursuant to such deduction of taxes, the taxpayer filed its return of income claiming the entire taxes deducted as refund in light of the beneficial provisions under Article 13(6) of the India Belgium DTAA.

- The Tax Officer (**TO**) rejected the contention of the taxpayer and held that the capital gains arising from sale of shares of the Singapore company is taxable in India, as the said company is substantially deriving its value from the assets located in India. The taxpayer filed its rejections before the Dispute Resolution Panel, which upheld the Order of the TO. The taxpayer filed appeal before the ITAT.

Ruling of the ITAT:

- Article 13(5) of the India Belgium DTAA applies only if the shares transferred are of a company which is a resident of India and the same forms part of a participation of at least 10% of the capital stock of the company. Gains arising from alienation of such shares would be taxable in India. As the shares transferred are of a Singapore company, application of Article 13(5) of the India Belgium DTAA stands excluded in the present fact pattern.

- Article 13(4) of the India Belgium DTAA envisages a "see-through" provision, which however, is limited only in relation to immoveable property. On the other hand, Article 13(5) of the India Belgium DTAA does not permit a see-through approach, in the absence of usage of words "directly or indirectly". Accordingly, in the absence of a see-through approach, the transfer of shares of the Singapore company cannot be regarded as transfer of shares of its Indian subsidiary.

- Under the deeming fiction (Explanation 5 to Section 9(1)(i) of the IT Act) a foreign company cannot be treated as a company resident in India, considering no corresponding provision exists under the India Belgium DTAA. Explanation 5 to Section 9(1)(i) of the IT Act does not define residence of a person and only deems shares of a foreign company to be situated in India. Unilateral amendments in the domestic law cannot be allowed to override the provisions of the tax treaties.

- The ITAT accordingly held that as Article 13(5) of the India Belgium DTAA is not applicable to the present fact pattern and gains if any, would be taxable under Article 13(6) of the India Belgium DTAA. The ITAT followed the decision of the Hon'ble Andhra Pradesh High Court in the case of ***Sanofi Pasteur Holding SA vs Department of Revenue, Ministry of Finance, [2013] 30 taxmann.com 222 (Andhra Pradesh)*** in this regard.

We trust you will find this an interesting read. For any queries or comments on this update, please feel free to contact us at insights@elp-in.com

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