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TAX JURISPRUDENCE

CASE LAW ALERT – MAY 2022
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EXECUTIVE SUMMARY OF JUDGEMENTS / ADVANCE RULINGS UNDER DIRECT AND INDIRECT TAXES

We are pleased to draw your attention to following important decisions which might be useful for you to take call on tax position.

Case & Citation	Issue Involved	Decision
Direct Tax		
Blackstone FP Capital Partners Mauritius V Limited [TS-381-ITAT-2022(Mum)]	Whether the concept of 'beneficial ownership' is inbuilt in Article 13 of India - Mauritius Double Taxation Avoidance Agreement ('DTAA')?	It is not at the discretion of the Revenue to decide as to what constitutes beneficial ownership and the Revenue must also examine this fundamental concept and give categorical findings as to how requirements of beneficial ownership are satisfied in each case. ITAT restores the matter with a direction to pass a speaking order after giving a fair and reasonable opportunity of hearing to the Assessee in this regard.
Shri Jigar Jashwantlal Shah Vs. ACIT (ITA No. 1541/ Ahd/2017)	Whether renouncement of rights in shares by taxpayer's (a) wife and father (b) third party shareholders in favour of taxpayer is taxable u/s 56(2)(vii)(c) of the Act?	Since wife/father fall within the definition of "relative", the same are excluded from the purview of operations of section 56(2)(vii)(c) and hence, renunciation of rights in shares in favour of the taxpayer shall not be taxable u/s 56(2)(vii)(c). Renunciation of rights in shares by the third-party shareholders has resulted in disproportionate allocation of rights in shares in favour of the taxpayer and hence, the same shall be taxable u/s 56(2)(vii)(c).

Indirect Tax		
Cosmic Ferro Alloys Ltd [2022-TIOL-50-AAR-GST]	Whether sale of a business unit for lump sum consideration amounts to sale of goods or sale of service or sale of goods and services? Whether the said transaction will be exempted under Entry no. 2 of the Notification No.1 2/2017-Central tax (rate) dated 28.06.17?	The transaction of transfer of business unit of applicant shall be treated as supply of services and will be exempted under Entry no. 2 of the Notification No. 12/2017-Central tax (rate) subject to fulfilment of conditions to qualify as a going concern.
Corbett Nature Reserve, Ramnagar Nainital [2022-TIOL-16-AAAR-GST]	Whether GST is payable on Naturopathy services provided along with the accommodation?	AAAR upheld the order of Uttarakhand AAR that had earlier ruled that these centres are akin to hotels and resorts and their main function is to provide accommodation and food similar to hotels and resorts and therefore are liable to GST.

The brief analysis of above referred decisions and rulings are given below.

DIRECT TAX

Case 1 – Blackstone FP Capital Partners Mauritius V Limited [TS-381-ITAT-2022(Mum)

Facts in brief & Issue Involved

- Assessee, a company domiciled in the Republic of Mauritius, is also registered as a foreign venture capital investor (FVCI) with the Securities and Exchange Board of India.

- During assessment year 2016-17, the assessee has sold 8,31,67,132 equity shares of CMS Info Systems Ltd for a consideration of USD 15,95,02,497 to Sion Investment Holdings Pte. Ltd. giving rise to a capital gain of USD 14,21,80,932 (i.e. approximately INR 904.98 crores)

- The Assessing Officer ('AO') noted that it would be necessary to understand the real owners of the shares under consideration since as per Article 13 of the India-Mauritius DTAA, gains derived by the resident of one of the contracting states from alienation of any property (in the current case the underlying shares), shall be taxed only in the state of which the seller is a resident.

- Upon carrying out an examination of the information obtained from various sources, the AO held that it is a perfect case for lifting the corporate veil and held that the effective and beneficial ownership of the underlying shares was in Caymans Island and not in Mauritius and thus, the benefit under Article 13 of the India-Mauritius DTAA will not be admissible.

Observations & Decision of the ITAT

- The Hon'ble ITAT held that the concept of beneficial ownership being a sine qua non to entitlement to treaty benefits, in the absence of specific provision to that effect, cannot be inferred or assumed.

- It would thus seem possible that reading a beneficial ownership test, when such a test is not embedded in the treaty provision itself, is rather than an impermissible interpretation of the treaty provisions, is a rewriting the treaty provision itself, thereby defeating the purpose of entering a mutually agreed upon tax treaty.

- AO has clearly fallen in error in proceeding on the basis that the concept of beneficial ownership is relevant in the context of Article 13, without assigning any specific and cogent reasons in support of this inference.

- It is not at the whim or fancy of a tax authority to decide as to what constitutes 'beneficial ownership'. It is absolutely fundamental that as what constitutes 'beneficial ownership' must also be examined and categorical findings are given as to how these requirements of beneficial ownership are satisfied.

NASA Comments

- The is a welcome decision as it reverses the interpretation by tax authorities according to their own discretion thus frustrating and negating the certainty and predictability sought to be achieved by the tax treaty partners.

Case 2 – Shri Jigar Jashwantlal Shah Vs. ACIT (ITA No. 1541/ Ahd/2017)

Facts in brief & Issue Involved

- Taxpayer along-with his wife and father were holding 1,03,000 and 82,200 shares of M/s. Kintech Synergy Limited ("Company").

- Company came out with the right issue of shares and offered the right to all shareholder in the same ratio.

- Taxpayer was allotted 1,03,000 shares at a face value of Rs.10 per share as per his proportionate shareholding. The taxpayer's wife and father were also eligible for additional 82,200 shares on a proportionate basis, however they renounced their right of entitlement in favour of the taxpayer.

- Further, the taxpayer was allotted 14,800 shares in pursuant to renunciation of rights by third party shareholders in his favour.

- AO reopened the assessment and concluded that aggregate FMV of 2,00,000 shares (i.e. 1,03,000 + 82,200 + 14,800) allotted to the taxpayer is Rs.5,10,00,000/- which far exceeded the consideration amount of Rs.20,00,000/- paid for the receipt of shares and hence, as per provisions of section 56(2) (vii) of the Act, the same should have been taxable in the hands of the taxpayer.

Contentions of Taxpayer

- The shares were not received by way of "transfer" but were allotted by way of right allotment and hence, the provisions of section 56(2)(vii) cannot be invoked.

- Relied on the decision of Supreme Court in the case of Khoday Distillers 307 ITR 312 (SC) wherein the Hon'ble Supreme Court held that the word 'allotment' indicates creation of shares by appropriation out of the unappropriated share capital to a particular person and such creation would not amount to transfer, and hence provisions of section 56(2)(vii) of the Act cannot be invoked.

- As far as the additional allotment of 82,200 shares are concerned, the same have been renounced in favour of taxpayer by immediate family members, who have been excluded from purview of section 56(2)(vii) of the Act.

Observations & Decision of the Hon' ITAT

- On a plain reading of section 56(2)(vii)(c), the term used is 'receives' and the said term cannot be restricted to receipt by way of 'transfer' alone. Further, section 56(2)(vii)(c) nowhere speaks of the word 'transfer' or 'receives by way of transfer', so as to give a restricted interpretation to section 56(2)(vii)(c) of the Act.

- Once the shares have been issued proportionate to existing shareholding of the petitioner, the provisions of section 56(2)(vii)(c) of the Act cannot be invoked. This is because there is no disproportionate allotment of shares and the gain accruing on allotment of fresh shares will be offset by the loss in value of existing shares.

Therefore, the provision of section 56(2)(vii) shall not apply to 1,03,000 shares allotted to the taxpayer in proportionate to his shareholding.

- Since wife / father are falling within the definition of the term "relative', the same are excluded from the purview of operation of section 56(2)(vii)(c) of the Act. Consequently, such renunciation of rights in shares (i.e. 82,200 shares) in favour of the petitioner would not attract the provisions of section 56(2)(vii)(c) of the Act.

- As regards 14,800 shares allotted to the taxpayer in view of renunciation of rights in shares by third party shareholders, the Honorable ITAT held that taxpayer has gained both quantitatively as well as qualitatively, and due to such renunciation, his shareholding in the Company has increased from 29.90% to 53.22%, thereby giving him the controlling interest in the Company, resulting in disproportionate allotment of rights shares in his favour. Hence, the provisions of section 56(2)(vii)(c) of the Act shall apply and consequently, the income would be taxable in the hands of the taxpayer.

NASA Comments

- This judgement once again re-affirms the position that if the shares are allotted strictly on proportionate to existing shareholding, then though the provisions, per se, are applicable, but the same will not operate adversely. This is because the gain accruing on allotment of fresh shares will be offset by the loss in value of existing shares.

- However, renunciation of rights in shares by third party shareholders results in disproportionate allocation, as the taxpayer's shareholding increases substantially compared to the other shareholders. Hence, the provisions of section 56(2)(vii)(c) of the Act shall apply to such transactions resulting in taxability in the hands of recipient of shares.

INDIRECT TAX

Case 1 – M/s Cosmic Ferro Alloys Ltd [2022-TIOL-50-AAR-GST]

Facts in brief & Issue Involved

- Applicant is engaged in manufacturing of Ferro alloys and Cold Rolled Formed Sections having its factories at Barjora ("FERRO Unit") and Singur ("CRF Unit") respectively functioning and running independently.

- Applicant intended to sell its CRF unit involving transfer of all the assets and liabilities (due and payable) to the purchaser for a lump sum consideration.

- Applicant raised following questions before the AAR –

    - Whether the transaction would amount as supply of goods or supply of services or supply of goods and services?

    - Whether the transaction would be covered under Entry no. 2 of Notification No. 12/2017-Central tax (Rate) dated 28th June 2017?

Contentions of Applicant

- The proposed transaction is transfer of business as a going concern wherein all assets and liabilities have been agreed to be transferred to the purchaser and said unit will continue its business without any hindrances and / or stoppages.

- The transaction contemplated, being sale of an independent unit, is a supply of service as a going concern and in view of Entry No 2 of the Notification No. 12/2017- Central Tax (Rate) dated 28th June 2017, the said transaction is to be charged at 'NIL' rate of tax.

- Applicant submitted the Business Transfer Agreement to prove that CRF unit will continue to do the same business as it was involved in before the proposed takeover/transaction.

Observations & Decision of Advance Ruling Authority

- Such transfer of a business unit cannot be treated as supply of goods since business cannot be said to be a movable property to qualify as 'goods' as defined in u/s 2(52) of the CGST Act. Further, anything other than goods, money and securities falls within the meaning of 'services' as defined u/s 2(102) of the CGST Act.

- The term 'Going Concern' is not defined in the CGST Act, 2017. Relying on the explanation of going concern given in other statutes and rulings, AAR observed that to qualify as a 'Going concern', the parties to transaction should neither have any intention nor the necessity of liquidation or of materially curtailing the scale of the operations.

- Applicant has not furnished any documentary evidence from the auditor with regard to the 'entity's ability to continue its operation for the foreseeable future'. In absence of this, AAR was unable to conclude that the applicant has neither the intention nor the necessity of liquidation or of curtailing materially the scale of the operations.

- AAR held that the impugned transaction shall be treated as supply of services and would be covered under Entry No. 2 of the Notification No. 12/2017 -Central Tax (Rate) dated 28th June 2017 subject to fulfillment of the conditions to qualify as a going concern.

NASA Comments

- AAR speaks of furnishing documentary evidence from the auditor with regard to the 'entity's ability to continue its operation for the foreseeable future'. This appears to be weird as auditors will not be able to issue any such certificate / document at the time of business transfer transaction. Moreover, procurement of such document is not a pre-condition for availing the exemption.

- As ruling of AAR does not have binding precedence, one must take a considered call looking at the facts of the case.

Case 2 – M/s Corbett Nature Reserve, Ramnagar Nainital [2022-TIOL-16-AAAR-GST]

Facts in brief & Issue Involved

- Applicant is running a resort and runs an independent Naturopathy Center (registered under the Clinical Establishment Act, 2010) in the said resort providing various services in the form of nature cure (drugless cure) and yoga therapies (healthcare services). Such services are provided to in-house customers as well as outsiders.

- Applicant had sought an advance ruling as to whether the Naturopathy Center is eligible to claim exemption under Entry No. 74 of Exemption Notification No. 12/2017 – Central Tax (Rate) dated 28th June 2017 i.e. healthcare services provided by a clinical establishment.

- Uttarakhand AAR observed that supply of services provided by applicant, being composite supply, is rightly classifiable as 'Room or Unit Accommodation services provided by hotels, inn, guest house, etc.' and thereby liable to GST.

- Being aggrieved by said ruling, applicant has preferred an appeal to AAAR.

Contentions of Applicant

- Applicant is entitled to claim exemption on following two grounds:

    - The Naturopathy Center is an independent clinical establishment; and

    - Applicant has appointed an authorized medical practitioner to provide healthcare services in its Naturopathy Center.

Observations & Decision of Appellate Advance Ruling Authority

- Applicant has advertised and marketed their accommodation service as their main service and Naturopathy as additional service.

- Thus, accommodation services along with other services including Naturopathy rendered to guest during their stay is a composite supply wherein the accommodation services constitute the predominant element and therefore, is the "principal supply" and other ancillary services including Naturopathy shall form part of said composite supply.

- On true and fair analysis of the aforesaid Notification, the conclusion is compelling that all services provided in relation to or in addition to accommodation service are liable to GST in as much as, all such ancillary / additional activities having a proximal nexus with accommodation service.

NASA Comments

- While the AAAR order is specific to the appellant, the precedent set can be used in similar cases where wellness centers are run as a part of hotel or club facilities.

- Following questions / issues remains open:

    - Whether wellness and yoga services are covered under the definition of health care services as defined in clause 2(zg) of Exemption Notification;

    - Whether same ruling applies to wellness and yoga services provided to walk-in customers not residing in the resort;

    - Whether position will change if wellness and yoga services are charged separately not forming part of the accommodation package;

- Ruling by AAAR is binding only on applicant and its jurisdictional officer.

We will be glad to provide any elaboration or elucidation you may need in this regard.

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