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TAX JURISPRUDENCE

CASE LAW ALERT – SEP 2023
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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		
Cognizant Technology Solutions India Pvt. Ltd Vs. ACIT [ITA No.269/Chny/ 2022] (Chennai Trib.)	Whether consideration paid for buyback of shares can be considered as dividend u/s. 2(22) as distribution of accumulated profits?	The Hon. Tribunal held considering the fact that the purchase of shares through approved scheme before the application of section 115QA was a colourable device and accordingly amounts to distribution of accumulated profits and hence is dividend u/s. 2(22) and hence DDT is payable u/s. 115O.
Indirect Tax		
M/s BOKS BUSINESS SERVICES PVT LTD Vs COMMISSIONER OF CENTRAL GOODS AND SERVICES TAX DELHI SOUTH AND ANR [2023-TIOL-1090-HC-DEL-GST]	Whether the provision of principal service of Book keeping, Payroll and accounts, through the use of cloud technology make the petitioner an intermediary where the agreement uses the word 'agent'?	Hon'ble Delhi High Court set aside the impugned order and directed the authority to process the petitioner's claim for refund.

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

DIRECT TAX

Case 1 – Cognizant Technology Solutions India Pvt Ltd Vs ACIT [ITA No.269/Chny/2022] (Chennai Trib.)

Facts in brief & issues involved:

- The assessee's share capital was owned by four non-resident shareholders, three from the USA and one from Mauritius. The assessee acquired equity shares from all shareholders in compliance with a restructuring scheme approved by the Madras High Court.

- After the acquisition, the Mauritian entity became the majority shareholder with 99.87% shareholding and the remaining 0.13% retained by existing USA-based shareholders. Two USA-based shareholders completely liquidated their shareholding in this scheme.

- The AO held that consideration paid by the assessee to its shareholders for purchase of own shares through a scheme sanctioned by the HC is akin to distribution of accumulated profits if it entails the release by the company to its shareholders all or any part of its assets, and hence is taxable as deemed dividend u/s.2(22)(a) of the Act. Alternatively, the consideration paid represents distribution to shareholders on reduction of its capital and hence is taxable as deemed dividend u/s.2(22)(d).

Contention of the taxpayer:

- The assessee contended that purchase of shares and extinguishment thereof does not amount to reduction of capital as per Companies Act and hence, consideration paid for purchase of own shares by the company which are ultimately extinguished cannot be said to be reduction of capital. Both, the Companies Act and Income Tax Act consciously treat that purchase of own shares and reduction of capital are different concepts from one another.

- Section 2(22)(d) is not applicable as the assessee had under the Scheme made an offer to purchase its own shares from its shareholders and acceptance of such offer by the shareholders is a contract, which comes into existence. The payment to

shareholders was made in pursuance of contract and not on account of extinguishment of shares. Similarly, section 2(22)(a) is also not applicable as payment made to shareholders is towards discharge of consideration payable under contract of purchase of shares and hence, cannot be regarded as distribution

- Section 115QA though enacted by the Finance Act, 2013, its scope was enlarged only vide amendment made by the Finance Act, 2016 w.e.f. 01.06.2016 by amending the definition of buyback. Since, HC had approved the Scheme vide order dated 18.04.2016, the amended provisions of Sec.115QA of the Act are not applicable. Once the Scheme is approved by HC after inviting objections from Government, then it is binding on all stakeholders.

Contention of the Revenue:

- The entire Scheme was moved in a hurried manner which is evident from the fact that on 29.02.2016, amendment to section 115QA was announced and was in the public domain. The assessee implemented the Scheme on 18.05.2016 and on 01.06.2016, amendment to section 115QA had come into force. This resulted in assessee hurriedly distributing accumulated profits to its shareholders without coming into taxation net.

- The term 'buyback' is not used anywhere in the Scheme. The transactions are always described only as purchase of equity shares. Clause 6.7 of the Scheme clearly states that purchase of equity shares shall not be treated as buyback u/s.68 of the Companies Act.

- In order to come within the ambit of section 2(22)(d) of the Act, there must be a distribution to the shareholders on the reduction of capital and further, it must be to the extent of accumulated profits. In the present case, both conditions are satisfied as share capital has been reduced by 54.70% and distribution of money is out of the general reserve and accumulated credit balance in P & L A/c.

- Alternatively, the payment falls within the ambit of section 2(22)(a) as there is distribution of accumulated profits entailing release of assets to the shareholders.

Observation and Decision of Tribunal:

- The Tribunal upheld the order of the AO, and to do so, the Tribunal looked through the transaction to conclude that it was a colourable device which was hastily executed on 18th May 2016 to evade the distribution tax under the amended provisions of Section 115QA that came into force from 1st June 2016.

- Post sanction of Scheme, shareholding percentage of Mauritius entity was increased to 99.87%. Hence, there has been an artificial shifting of shareholding base from USA to Mauritius solely with the aim of claiming DTAA benefits, because, as per India Mauritius DTAA capital gains on transfer of equity shares is not taxable in India.

- The definition of dividend u/s.2(22)(a) is an inclusive definition and it goes beyond the conventional or traditional meaning associated with dividend. Therefore, the object of such an expansive definition provides that the company does not camouflage payments out of accumulated profits to its shareholders through different channels in order to avoid payment of tax. The Bench also concurred with AO that the payment falls within the ambit of section 2(22)(a) as there is distribution of accumulated profits entailing release of assets to the shareholders.

- The order sanctioning the Scheme itself clearly provides that the sanction shall not grant immunity to the assessee from payment of taxes under any law for the time being in force. Further, the role of the High Court in approving the Scheme is very limited. The tax consequences would be for the AO to look into the Scheme. The assessee cannot take shelter on the basis of self-serving provisions of the Scheme and state that certain provisions of the Income Tax Act have been excluded.

- The conditions prescribed u/s.77A are not satisfied as purchase of own shares by the assessee is more than 25% of the total paid up share capital and free reserve, in view of the fact that the post sanction of the Scheme, 54.70% of the capital has been

reduced, which is nothing but distribution of accumulated profits and reduction of capital which falls under the definition of dividend u/s. 2(22)(d).

- Section 46A is only applicable to buyback u/s.77A of Companies Act, 1956 and not to other forms of purchase of own shares. Further, Section 115 O contains a non-obstante clause which would override the provisions of Section 46A.

- Hence, the entire Scheme is a colourable devise to try to avoid payment of tax dues and hence, there is a capital reduction and distribution out of accumulated profits.

NASA Comments: -

- The above case relates to Assessment Year 2017-18. If a company now buyback it's share u/s 68 of Companies Act, provisions of Section 115QA shall be applicable.

INDIRECT TAX

Case 1 – M/s BOKS BUSINESS SERVICES PVT LTD vs COMMISSIONER OF CENTRAL GOODS AND SERVICES TAX [2023-TIOL-1090-HC-DEL-GST]

Facts in brief & issues involved:

- Boks Business Services Pvt Ltd (" the Petitioner") is engaged in the business of providing booking, payroll, and accounting services through the use of cloud technology to its affiliated entity incorporated in UK.

- The petitioner filed refund application of unutilized ITC in respect of export of services (zero rated supplies) which was rejected on the ground that services rendered to foreign clients of the petitioner fall within the category of intermediary services and therefore the place of supply of services falls was within the territory of India.

- Show cause notice (SCN) was served to which the petitioner responded and explained the nature of its services, but the explanation was not accepted and adverse order was passed treating petitioner as an 'intermediary'

- Aggrieved by the said order, the petitioner filed an appeal before the Appellate Authority which was also rejected on the same grounds that as per the agreement the petitioner has agreed to act as agent.

- Aggrieved with the impugned order of Appellate Authority the petitioner filed writ before the Hon'ble Delhi High Court.

Observations & Decision of Hon'ble High Court:

- The Hon'ble High Court held that as per the agreement, it is clear that petitioner is not an intermediary, as the petitioner is neither facilitating the provision of the services by third party nor acting as agent for procuring the services for its affiliate.

- In case of intermediary services, there are three entities - one providing the principal service, one receiving the principal service, and an intermediary who acts as an agent or a broker for facilitating or arranging such services for the service recipient.

- In the aforesaid case although the agreement uses the word "agent" it is clear that the petitioner is not acting as an agent for procurement of services for the service recipient. The fact that such services may be for the clients of the petitioner's affiliate, does not make the petitioner "intermediary "

- The petitioner is contracted to provide the services of book-keeping, payrolls, and accounts using cloud technology and is the principal service provider in the context of the services provided by it.

- Reliance was made on the following case laws:
  - **M/s Ernst And Young Limited v. Additional Commissioner, CGST – 2023 VIL-190-DEL,**
  - **M/s Cube Highways and Transportation Assets Advisor Private Limited v. Assistant Commissioner CGST Division-2023-VIL-547-DEL.**

- Based on aforesaid observations, the impugned order was set aside and adjudicating authority was directed to process the petitioner's claim for refund as expeditiously as possible and preferably within four weeks from the date of the order.

Nasa comments:

- This decision of Hon'ble High court highlight that it is very important to understand the contract so as to determine the exact relation between the contracting parties. The contracts must be read / interpreted in a manner so as to give effect to the intentions of the contracting parties.

- Further this judgement will pave a way forward for jurisprudence where the revenue department rejects the refund application on the ground that services fall under the category of **intermediary services**.

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