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Quantera Global

TransPrice Times

Edition: 16th January 2018 – 15th February 2018

AB Holdings, Mauritius-II – AAR

Outcome: In favour of applicant
Category: Capital Gains treaty benefit

The Authority for Advance Rulings (AAR) rules on taxability of shares held by the Mauritian applicant in an Indian group company transferred to its group company in Singapore.

As per facts of the case, the applicant operated as an investment holding company as part of its MNE Group with its ultimate holding entity in USA. The applicant carried out business in Mauritius with 2 resident directors and 1 non-resident director who is the MD of the said USA entity. Accordingly, applicant invested in the Indian subsidiary time to time in a targeted sector. To support its business in the Asia-Pacific (APAC) region, a group strategy was developed to open a regional headquarter in Singapore to cater APAC region (including India). To infuse more investment in Singapore, a reorganisation was proposed by way of transfer of shares from the existing Indian group company to Singapore. Accordingly, the applicant indirectly would hold the shares through its subsidiary in Singapore.

The question posed before the AAR was whether the proposed transaction of transfer of shares constituted tax avoidance, and whether applicant was eligible to avail the benefit of capital gains exemption under Article 13(4) of India-Mauritius tax treaty.

Revenue authorities contended that since the ultimate parent was in USA and applicant's management comprised of the MD of the US entity who took decisions with no passport record of presence in Mauritius, the control and management of the applicant would be in US and not Mauritius. This evidence was submitted to prove that the applicant was not a tax resident in Mauritius and disallow treaty benefits to applicant. Further, the authorities constituted the transaction as tax avoidance through a paper company such that it intended to appreciate value of shares of applicant indirectly through Indian assets.

AAR observed that the applicant had a valid Tax Residency Certificate from Mauritius and held that setting up a subsidiary for investment purposes cannot be questioned. In respect of place of control and management, it was ruled that with current digital medium, the MD of ultimate US parent entity would have influence on investment decisions irrespective of his movements at different times during a relevant year. Terming the contentions of Revenue as unrealistic, the AAR accepts applicant's contention that the transaction was not a benami/colourable device and allows treaty benefit on proposed capital gains.

AB Mauritius – AAR

Outcome: Against applicant
Category: Related Party Transactions

The AAR holds the transaction of sale of shares held by Mauritian applicant in India to its subsidiary in Singapore as taxable in India, and denies treaty benefit to the taxpayer under Article 13 of India-Mauritius tax treaty.

As per the details, the applicant acquired shares of an Indian company under a Stock Purchase Agreement (SPA) in 2003. The SPA was executed by the MD of the Promoter group company of the applicant with an authorisation letter from the board of directors of the applicant to allow the MD to sign the SPA. The directors of applicant did not sign the SPA and only the name of the applicant was mentioned in the SPA.

However, the MD was not a director on the board of the applicant. The shares were then taken over from its previous owner of the shares as a payable loan under a loan agreement. After this transaction involving SPA and loan agreement, the Applicant became the owner of the shares of the Indian company and then discharged the liability loan over time. As per a recent corporate plan, the Applicant proposed to invest in its subsidiary in Singapore.

Revenue authorities contended that it was only in 2004 i.e. 1 year after the SPA, that the MD of the Promoter group company informed the Applicant in its board of directors' meetings regarding the investment in the Indian company. It was only at this moment that arrangements to take care of loan liability were made and business reorganisation plan was ratified by the directors of the applicant. Further, the authorities submitted that applicant acquired 99% of the Indian company's shareholding without paying any consideration, whereas the remaining 1% was held by Promoter group which paid consideration by cancellation of debt. It also contended that as per the SPA, the shares were transferred in the name of Promoter group and since no consideration was paid by applicant, the applicant could not be treated as the owner.

AAR ruled that there was no mention of any liability clause in the SPA and held that the applicant's name was superimposed in the agreement as part of some arrangement of which the applicant was not aware at all. Further, the letter of authorisation submitted by the applicant was rejected by the AAR as there were no evidences of decisions or discussions in the Board to show the MD was authorised who was not even in a director in the applicant company. Accordingly, AAR denies treaty benefit and holds sale of shares to Singapore as taxable in India.

Oracle (OFSS) BPO Services Pvt Ltd – HC – Delhi

Outcome: In favour of taxpayer
Category: Related Party Transactions

Hon'ble High Court upholds application of 25% Related Party Transactions (RPT) filter applied for comparability analysis required to benchmark international transactions of taxpayer.

A comparability analysis entails accepting only certain companies which are comparable to the tested party's (party subject to transfer pricing) activity and reach the required arm's length price. In the present case, Tax Court in a fresh assessment of the comparability analysis, had included a RPT filter of 25% which resulted in final set of comparables consisting of unrelated transactions equal to or exceeding 75% of their respective business.

Rejecting Revenue's appeal, Hon'ble High Court held that RPT filter is relevant and opined its necessity to avoid a distorted picture of profitability which would be having excessive transactions with its associated enterprises over and above the threshold percentage. Thus, holds that to compare light entities with similar (if not identical) functions, a RPT filter is relevant and fits in with the overall scheme of a transfer pricing study.

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