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Tax Alert

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CASE LAW 1: ITAT Rejects AO's change of share valuation method u/s 56(2)(viib): follows Bombay HC over Kerala HC

VBHC Value Homes Private Limited, Bengaluru vs Income Tax Officer, Ward-7(1)(3), Bengaluru and The Assistant Commissioner of Income Tax, Ward -7(1)(2), Benagluru (Bangalore Tribunal)

Facts

- The assessee obtained a valuation report for determining the value of shares for the purpose of Section 56(2)(viib) of the Income Tax Act,1961 by adopting DCF method.
- However, the Assessing Officer (AO) rejected the DCF method and adopted Net Asset Value (NAV) method and made addition.
- The CIT (Appeals) upheld the action of the AO in rejecting the DCF method and adopting NAV Method and stating that the value of the shares issued exceeds the fair market value per share.
- Aggrieved, the assessee preferred an appeal before the Hon'ble Bangalore Tribunal.

Issue

- Whether AO can change the method of valuation of shares as adopted by the assessee?

Decision of the Hon'ble Bangalore Tribunal

- The Tribunal followed the coordinated bench ruling in the case of Innoviti Payment Solutions Pvt. Ltd., Vs. ITO which in turn followed Bombay HC ruling in the case of Vodafone M-Pesa wherein it was held that AO can scrutinize the valuation report and he can determine a fresh valuation either by himself or by calling a determination from an independent valuer to confront the assessee.
- However, the basis has to be DCF method and he cannot change the method of valuation which has been opted by the assessee.
- The Tribunal declines to follow Kerala HC ruling in case of Sunrise Academy of Medical Specialities and prefer to follow Bombay HC ruling stating that "if two views are possible then the view favourable to the assessee should be adopted."
- It is not open to the AO to change the method of valuation which the assessee has duly opted and the matter was restored back to the AO for a fresh decision.

Conclusion

- The Mumbai Tribunal in the case of Narang Access Pvt. Ltd [TS-608-ITAT-2019(Mum)] had remitted the matter holding that the method of valuation i.e. NAV method or DCF method to determine the FMV of shares has to be adopted at assessee's option and the AO cannot change the method of valuation opted by the assessee.

CASE LAW 2: Seconded employees salary reimbursements, in the absence of agreement, constitutes Permanent Establishment (PE)

Teradata Operations Inc. v. DCIT – ITA Nos. 7805/Del/2017 & 2580/Del/2018 (Delhi Tribunal)

Facts

- The assessee company, incorporated in and tax resident of USA, seconded certain employees to its Associated Enterprise ('AE') in India.
- In this regard, the assessee received reimbursement of cost pertaining to these seconded employees along with reimbursement of relocation expenses.
- During the course of scrutiny, the AO after analysing the secondment arrangement, considered that the seconded employees constituted a service PE. Accordingly, the AO proceeded to tax the profits attributable to such PE.

- Aggrieved, the assessee filed objection before the Hon'ble Dispute Resolution Panel ('DRP') stating that since, Indian AE had the right to control, supervise, take disciplinary action against these employees along with the obligation to pay salary to the seconded employees, they did not constitute a service PE.
- However, the Hon'ble DRP, rejected the contention of the assessee and directed the AO to tax the profits attributable to the service PE.
- Aggrieved, the assessee preferred an appeal before the Hon'ble Delhi Tribunal.

Issue

- Whether employees of assesse company who are seconded to its Indian entity to provide technical expertise and there still exists an employer-employee relationship between the seconded employees and the assesse company, such employees shall constitute a service PE in Indian entity?

Decision of the Hon'ble Delhi Tribunal

- The seconded employees of the assessee has been deputed to manage the affairs of the Indian entity and provide technical knowledge for a shorter period of time.
- During the period of secondment, the employees continued to make their social security contributions in USA and their salaries were also distributed to their bank accounts in USA.
- Further, the seconded employees still had an employer-employee relationship with the assessee (the employer in the home country i.e. USA) and the mere reimbursement of salary did not constitute an obligation to pay salary.
- The Tribunal relying on the decision of the Hon'ble Delhi High Court in the case of Centrica India Offshore Private Limited [2014] - 44 taxmann.com 300, held that in the case of Centrica there was agreement between the Indian entity and expatriate. In the instant case there was no such agreement.
- Thus, the Tribunal upheld the findings of the lower authorities on the issue of existence of PE of the assessee in India in terms of the DTAA
- With regard to attribution of profit to PE, the Tribunal held that the assessee has rendered services to the India through the PE and therefore the income which accrued to the PE is the market value of the services which has been provided by the seconded employees reduced by the cost of the services.
- The market value of the services to PE can also be deduced from the sale value or revenue fetched by India on those services reduced by the average profit margin of India.
- Thus, the Hon'ble Delhi Tribunal restored the file to the Assessing Officer for a fresh consideration for estimation of the profit in accordance with Article 7 of the India USA DTAA.

Conclusion

- Therefore, based on the above observation, the seconded employees were considered as employees transferred from the assessee company to Indian entity, only for a specified duration, to provide technical services.
- Further, it was held that, though the seconded employees worked at the premises of the Indian AE, for all practical purposes they still remained employees of the assessee and therefore, constituted a service PE.

Thank You

Please get in touch with us at:

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