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By

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CONTENTS

Dear Readers,

Greetings for the season!

In this edition, we bring you, Part III of various shades of draft assessment orders and issue surrounding them. In this piece, we have dealt on the issues arising of the e-assessment and faceless assessment schemes.

The next article is on the recent judgment of Honourable Supreme Court in the matter of Bharati Airtel Limited, wherein the judgment of Delhi High Court was struck down. The Supreme Court has asked right questions which the Delhi High Court failed to ask and stated that GSTR-2A is only a facilitator and non-availability of the same cannot be used at a later point of time to swap the entries. The Supreme Court upheld the Para 4 of Circular 26/26/2017 – CT since the same is within the ambit of Section 39(9) of Central Goods and Services Tax Act, 2017. The Supreme Court has distinguished the various High Court judgments which have held that GSTR-3B is a stop-gap arrangement and not a return under Section 39 by relying on the amendment made to Section 39 and finally giving a sanctity to GSTR-3B as return.

The final article is on the recent judgement of Bombay High Court in the matter of Abu Dhabi Investment Authority, wherein the later challenged the veracity of the pronouncement by the Authority of Advance Ruling. The Bombay High Court in a detailed analysis has cleared many issues and settling down certain not-so-spoken matters namely, whether foreign trusts are covered under Indian tax laws, whether a trust whose settlor is sole beneficiary is a valid trust, whether there is a mandatory requirement that trust should also be in revocable terms in order to attract provisions of Section 61 and Section 63 of Income Tax Act, the interplay of DTAA qua the settlor and beneficiary vis-à-vis trustee in different jurisdictions and others is worth reading.

I hope that you will have good time reading this edition and please do share your feedback. I will also urge clients to mail us topics or issues on which you want us to deliberate in our future editions, so that we can contribute to the same.

Thanking You,

Suresh Babu S
Founder & Chairman

GST

RECTIFICATION OF GSTR-3B - SUPREME COURT IN BHARATI AIRTEL LIMITED

Contributed by CA Sri Harsha

The recent judgment of Honourable Supreme Court in the matter of Union of India vs. Bharati Airtel Limited[1] deals with a special circumstance of rectification of Form GSTR-3B. As all of us are aware that Form GSTR-3B is a monthly/quarterly return in which the tax payer assesses his liability and discharge the same by using the cash and credit. The matter before the Honourable Supreme Court is pertaining to the rectification of such return. Though the rectification of the said return is possible in a different methodology as proposed by Circular 26/26/2017-CT dated 29.12.17 by making changes in a different return, the respondent in the subject matter (Bharati Airtel Limited) wanted to carry such rectification in the same return, where the error has occurred. We shall proceed to examine as to how the matter was finally settled by the Honourable Supreme Court.

The Issue:

Form GSTR-3B is a return to be filed in terms of Section 39 of CT Act[2] read with Rule 61 of CT Rules[3]. This is a periodical return, in which the taxpayer is expected to assess his output tax liability and discharge the same using the balances in electronic cash ledger and electronic credit ledger. Any mistakes committed by the taxpayer while filing and realised after filing the return, the same can be carried in the subsequent returns. Let us say, a taxpayer instead of paying tax on INR 10 Crores has paid tax on INR 15 Crores and declared the later turnover in his monthly GSTR-3B and paid the tax and he realises the error after off-setting the liability while filing the return, then he can reduce his turnover to the extent of INR 5 Crores in the subsequent return and adjust the tax paid earlier to the subsequent month's liability. This is guided by the Circular 26/26/2017- CT dated 29.12.17. However, the taxpayer cannot revise/rectify that month's GSTR-3B and claim refund of tax paid on excess turnover paid that is INR 5 Crores. This is what precisely the writ petitioner (the respondent before the Honourable Supreme Court) tried to do. Accordingly, the issue, before the Honourable Supreme Court is, whether rectification of GSTR-3B is possible in the month in which the error was committed or should be done only in accordance with Circular 26/26/2017-CT?

The History:

Bharati Airtel Limited has filed a writ petition under Article 226 of Constitution before Delhi High Court seeking among other things, that Rule 61, GSTR-3B and Circular 26/26/2017 – CT are ultra-vires the provisions of CT Act to the extent that they do not provide for modification of information in the return of tax period to which such information relates and are arbitrary, in violation of Article 14, Article 19(1)(g), Article 265 and 300A of Constitution of India. The main contention before the Delhi High Court was that the writ petitioner has filed the returns for the period July 17 to September 17 without taking the input tax credit into consideration. The reason for which the input tax credit was not taken into consideration was that the Government has failed to operationalise the Form GSTR-2A, which would indicate the possible input tax credit that was available to the taxpayer. Since, the said Form GSTR-2A was made

[1] 2021 (9) TMI 626 – Supreme Court
[2] Central Goods and Services Tax Act, 2017
[3] Central Goods and Services Tax Rules, 2017

available only with effective from September 2018, the writ petitioner after seeing the input tax credit available in GSTR-2A, understood that they have paid extra tax amounting to Rs 923 Crores in cash. The writ petitioner stated that if the Form GSTR-2A was made available with effective from July 17 (as promised by Government), he would not have made such excess payment in cash and accordingly pleaded the Delhi High Court that the rectification of GSTR-3B for July 17 to September 17 should be allowed and by debiting the electronic credit ledger, it is prayed that the amounts paid in cash should be re-credited to electronic cash ledger.

The Delhi High Court after listening to the writ petitioner and the Union of India has stated that since the said Form GSTR-2A was not made available with effective from July 17, as promised by the Government, the writ petitioner could not be put in a disadvantageous position, since making available the data in GSTR-2A was a right and not merely a facility held that the writ petitioner can rectify the return in respect of which the error occurred and not as suggested by Circular 26/26/2017-CT. Accordingly, the Delhi High Court has directed the Government to look into the matter within two weeks of rectification done by write petitioner and give effect to the same. Aggrieved by this, the Union of India has appealed before the Honourable Supreme Court.

Before Honourable Supreme Court:

Submissions by Union of India:

The Government stated that eligibility and utilisation of credit, is a statutory duty fastened on the taxpayer and he can exercise the same subject to satisfaction of the conditions mentioned. It was stated that though the Form GSTR-2A was not available during the period in dispute, the taxpayer is not in a situation to understand his entitlement to credit, since he has all the access to the books of accounts. The records so maintained by the taxpayer would put him in a position to understand the quantum of credit that was eligible and available to set off against the output tax liability. It was stated that the electronic portal was only an enabler and a facilitator in bringing on board all the registered persons which include the supplier, recipient, registered person and other recipients and efficacy of common electronic portal or malfunctioning thereof, does not extricate the registered person from the primary obligation of self-assessment of output tax liability. It is further stated that Section 37 and Section 38 do not provide for right relating to eligibility of credit. The obligation to do self-assessment of credit and output tax liability and to pay tax by using cash or credit, is a matter of exercising option for electing the mode of discharge of output tax liability and reconciliation predicated under Section 37 and 38, does not impact the rights and obligations of the taxpayer regarding the self-assessment of tax.

The Government concluded stating that any rectification regarding omission or incorrect particulars referred to therein, could be furnished in the month or quarter during which such omission or incorrect particulars came to be noticed and taking any other view would result in ushering inconsistency and uncertainty not only to the concerned registered person, but also to his recipient and supplier and others not directly connected with registered person and hence allowing correction/rectification of Form GSTR-3B of the concerned period is not permissible.

Submissions by Assessees:

The respondent, Bharti Airtel Limited, supported the judgment of Delhi High Court and pleaded that the reading down of Circular 26/26/2017 – CT is to be upheld in so far as it restricts the rectification of Form GSTR-3B in the concerned period. It was stated that it is known to everyone that due to non-operability of the forms, Form GSTR-3B was conceived as a stop gap arrangement and now the Government cannot deny the taxpayers their dues, in particular, right to revise their returns and avail credits. It was argued that the provisions in Circular not permitting the rectification of return is conceptually flawed and not consistent with the legislative intent and provisions of CT Act, since it denies the statutory right of the taxpayer to utilise his credits, due to technical problems in not putting the electronic platform in place. It is also pleaded that by not permitting to avail credit in the electronic credit ledger would result in collection of double tax, an unfair advantage to the Government. It is further stated that Government cannot take advantage of its own failure of not being operationalise Forms GSTR-2 and GSTR-3 right at the inception when the provisions of the act came into force. Accordingly, it was pleaded that the judgment of Delhi High Court has to be upheld.

Analysis by Supreme Court:

The Supreme Court after dealing with the jurisdictional issues pertaining to writ petition, jumped right on to the precise question, as to, the failure of Delhi High Court to inquire into the cardinal question as to whether Bharati Airtel Limited was required to be fully or wholly dependent on the auto generated information in Form GSTR-2A for discharging its output tax liability for the period in dispute. The Supreme Court stated that the answer to the above question is an emphatic 'No'. The Court stated that the registered person is obliged to adopt the same mechanism as was adopted by them prior to GST laws to discharge the obligation of output tax liability, which was by making reference to the books of accounts, which are very well under the control of taxpayer. The Court stated that the common electronic portal is only a facilitator to feed or retrieve such information and need not be the primary source for doing self-assessment, pointing out the primary source would be the agreements, invoices, challans, receipt of goods, receipt of services and books of accounts, which are very well in the control of taxpayer and not the tax authorities. The court stated this would be sufficient to arrive at the output tax liability and decide the quantum to be paid in cash and credit. The Court stated that factum of non-operability of Form GSTR-2A, is a flimsy plea taken by Bharati Airtel Limited.

Dealing with the question of reading down of Paragraph 4 of the Circular, the Court stated that same would have arisen only if that para is in contradiction to the express provisions of CT Act or rules made thereunder. Section 39(9) has clearly stated that omission or incorrect particulars furnished in GSTR-3B can be corrected in the subsequent months during which the same were noticed and the circular provides a mechanism for doing so and accordingly the Court stated, that the circular cannot be read down.

The Supreme Court has not accepted the view taken by the Delhi High Court in as much as, since there is no possibility of getting refund of excess or surplus credit, the only remedy available to the taxpayer is to utilise the credit by allowing the rectification of Form GSTR-3B. The Supreme Court stated that the view taken by High Court is not logical, since, there was no obligation cast upon by the taxpayer to pay the liability only in cash and failing to chose the payment of tax liability in credit (for no good reason) cannot be a ground for the taxpayer to later on ask for swapping of entries, so as to show the corresponding output tax liability in the electronic cash ledger from which he can take refund. The Supreme Court stated

that the taxpayer with full knowledge and information derived from its books of accounts had done self-assessment and assessed the output tax liability for the relevant period and chose to pay the same in cash and having so opted, it is not open to now resile from the legal option already exercised on the feeble reason that GSTR-2A was not operational.

The Supreme Court rejected the plea that the provisions of Section 39(9) cannot be applied to the instant facts for the reason that GSTR-3B is only a stop-gap arrangement and not a return under Section 39 read with Rule 61. The Court stated that thought GSTR-3B is not comparable to GSTR-3, nevertheless, GSTR-3B is prescribed as a 'return' and by subsequent amendment of Rule 61(5), wherein it was clarified that taxpayer need not file GSTR-3. Accordingly, the Court held that efficacy of Form GSTR-3B being a stop gap arrangement for furnishing of return, as was required under Section 39 read with Rule 61, would not stand whittled down in any manner. The Supreme Court also stated that it has not subscribed the view of Gujarat High Court in the matter of AAP & Co, Chartered Accountants vs Union of India[4] , wherein it was held that Form GSTR-3B was only a stop-gap arrangement.

Conclusion:

We do not know the exact reason as to why Bharati Airtel Limited has taken such a plea before Delhi High Court, but when we read the decision of Delhi High Court, we were sure that it was not in accordance with the law, and it is highly possible that the same would be reversed by the Supreme Court. Eventually, it happened and the question that the Supreme Court asked, and Delhi High Court failed is, whether the taxpayer is completely dependent on GSTR-2A for finalisation of the credit available to decide on the mode of discharge of output tax liability. For which the response would be no, since from ages, the availment of credit is based on the self-assessment of taxpayer and asking for re-credit of cash paid to cash ledger since the GSTR-2A was not available was completely out of place. We can understand if the matter is pertaining to the period post October 2019, wherein the restriction of credit is based on the availability in GSTR-2A, but this being the matter prior to October 2019, the plea taken, as in the words of Supreme Court, flimsy. Incidentally, this judgment also brings more clarity on the nature of GSTR-3B, the stop-gap arrangement vs the return, where in the Court concluded that it would definitely be a 'return'.

[4]2019-TIOL-1422-HC-AHM-GST

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INCOME TAX

VARIOUS HUES OF DRAFT ASSESSMENT ORDERS – SECTION 144B AND SECTION 144C - PART III

Contributed by CA Sri Harsha & CA Narendra

In the earlier parts of Article, the concept of draft assessment orders viz. its applicability, powers of AO to pass such draft assessment order, procedure for passing such order and, the recourse, subsequent to passing of such draft assessment order under Section 144C, available to the assessee and/or AO is covered. In this article, we intend to cover the faceless assessment scheme.

In order to remove the interface between assessing officer and the assessee, a new procedure of 'Faceless Assessment Scheme' has been introduced and the provisions governing Faceless Assessment Scheme has been provided under Section 144B of the Act. Under the new Faceless Assessment Scheme, a new concept of 'draft assessment order', 'final draft assessment order' and 'revised draft assessment order' has been provided which has come up for a litigation at various judicial fora. In this part, let us discuss the concept of 'draft assessment order', 'final draft assessment order' and 'revised draft assessment order'.

Background of Faceless Assessment:

In order to eliminate the interface between the taxpayer and the income tax department for better transparency and accountability, the Central Government has introduced e-assessment on a pilot basis in 2016. With a view to implement such scheme across the country, through Finance Act, 2018, Section 143 has been amended to insert sub section 3A to 3C for the purpose of e-assessment scheme. By utilizing the powers conferred in Section 143(3A), 'E – Assessment Scheme' has been vide Notification No 61/2019 dated September 12,2019.

In order to make e- assessment procedure more efficient, a new Section 144B has been inserted through the Taxation and Other Laws (Relaxation and Amendment of Certain Provisions) Act, 2020 and same has been named as 'Faceless Assessment Scheme'. As new Section 144B has been inserted, the provisions of Section 143(3A) to (3C) are made effective from 01.04.2021. CBDT[1] vide its Notification ___ dated March 31, 2021 clarified that the provisions of Section 144B are applicable to assessments pending as on 31.03.2021 and assessments initiated on or after 01.4.2021.

The 'Faceless Assessment Scheme' is similar to that of E-Assessment Scheme with some minor modifications. In simple terms, Faceless Assessment means conducting of the assessment without having one to one conversation between the assessee and the income tax department. The primary objective of Faceless Assessment is to achieve better transparency and accountability during the assessment. However, the Faceless Assessment should not be completed by one sided approach and assessee should be given sufficient and required opportunity of being heard. Hence, many checks and balances have been sewn into the Faceless Assessment Scheme thereby which the concept of draft assessment order, final draft assessment order and revised draft assessment order have come up and let us proceed to discuss each of them.

[1]Central Board of Direct Taxes

Draft Assessment Order ('DAO') and Final Draft Assessment Order ('FDAO') under Section 144B:

As discussed above, many checks and balances have been incorporated in Section 144B in order to provide sufficient opportunity to the assessee to represent his matter before the assessing officer. Under the old provisions, once the information/documents have been submitted to the assessing officer, assessment order under Section 143(3) would be passed.

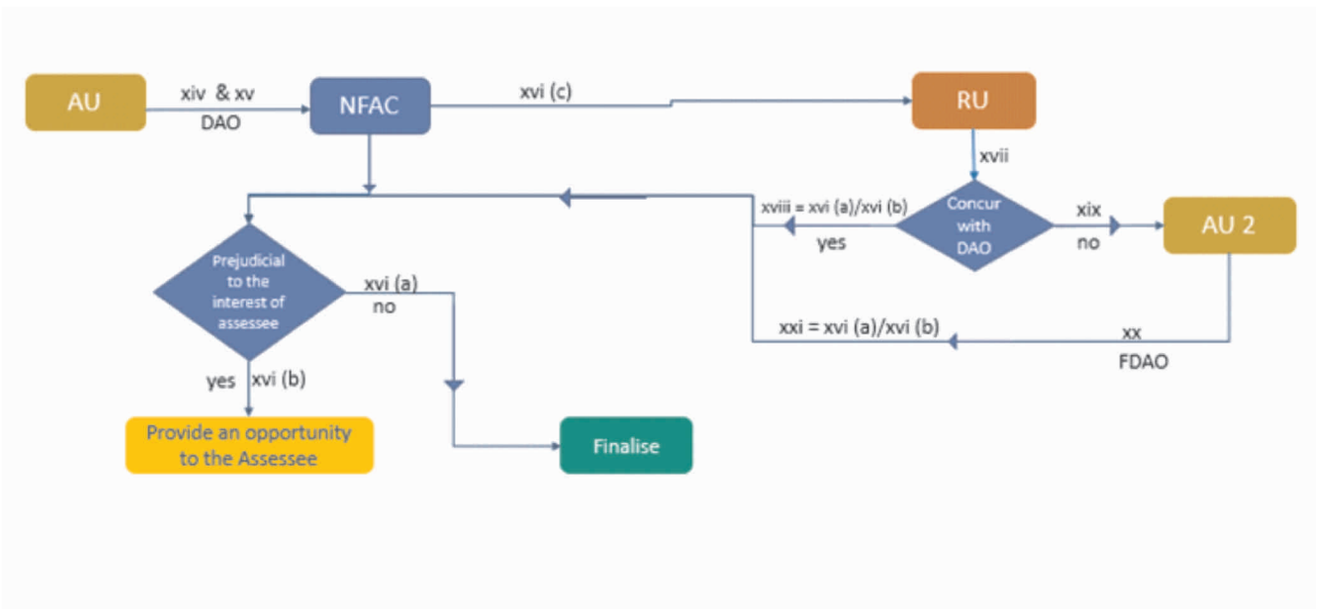
However, new Section 144B states that once the information or documents are submitted or no information is submitted by the assessee, assessing officer namely assessment unit ('AU') has to make a draft assessment order and forward the same to National Faceless Assessment Centre ('NFAC'). Upon receipt of draft assessment order from the AU, NFAC shall examine the order and may:

i. Finalize the assessment if such order is not prejudicial to the interest of the assessee.

ii. Provide an opportunity of being heard to assessee if such order is prejudicial to the interest of assessee.

iii. Alternately, forward such draft assessment order to the Review unit (RU') for review of the draft assessment order.

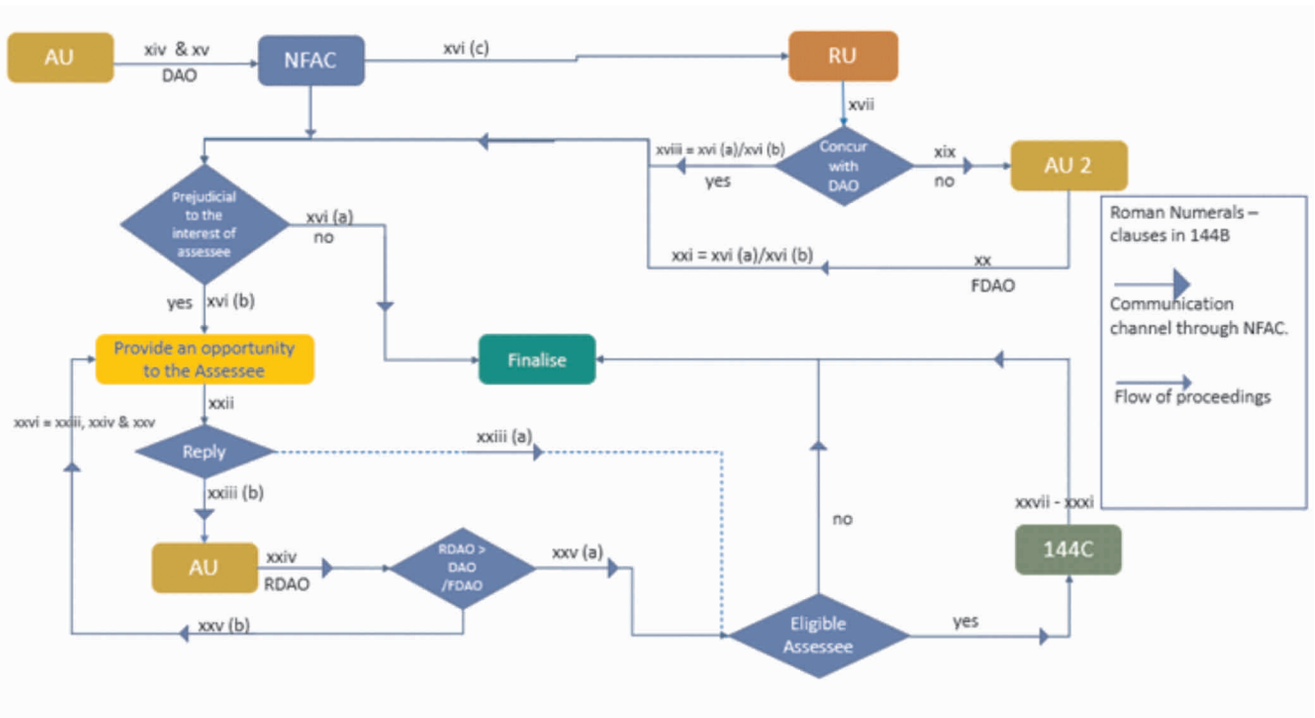
In the case where the DAO is forwarded to the RU, it may concur with the DAO or suggest variations to the same. If RU suggest variations to DAO, NFAC would forward such DAO to another assessment unit ('AU 2') for reconsideration. The AU2 considering the variation suggested, send the FDAO to the NFAC. Upon receipt of FDAO, NFAC may finalize the assessment if it not prejudicial to the interest of the assessee otherwise provide an opportunity of being heard.



Revised Draft Assessment Order ('RDAO') under Section 144B:

Upon receipt of opportunity of being heard from the NFAC, assessee may submit reply to the draft assessment order and same may be forwarded by the NFAC to AU. Upon receipt of reply from the assessee, AU may consider the same and send the revised draft assessment order to the NFAC.If such RDAO is prejudicial to the interest of the assessee than the DAO or FDAO, NFAC shall again give the opportunity of being heard to the assessee and this cycle continues.

If such RDAO is not prejudicial to the interest of the assessee than the DAO or FDAO, NFAC may finalize the assessment subject to the provisions of Section 144C. Further, if assessee fails to utilize the opportunity of being heard, NFAC may proceed to finalize the assessment subject to the provisions of Section 144C. Under the faceless assessment scheme, the proceedings of the assessment would be completed without the involvement of the assessee however such involvement or interaction has to be conducted majorly through exchange of communications in writings.



Opportunity of Being Heard:

Section 144B specifically provides that in the case where the DAO is prejudicial to the interest of the assessee, he shall be provided an opportunity of being heard for representing his matter before the assessing officer. E-Assessment scheme provides that when the DAO is prejudicial to the interest of assessee, he shall be given an opportunity of being heard by giving a notice. However, provisions of faceless assessment scheme by way of Section 144B (7)(vii) states that assessee shall also be given an option of personal hearing so as to make oral submissions before the income tax authority.

The provision of Section 144B(7)(vii) provides special privileges to the assessee to appear personally before the income tax authority for making oral submission. However, the interaction between the assessee and income tax authority has to be made through electronic mode. In the recent times, many cases have reached High Courts in relation to completion of assessments under Faceless Assessment Scheme with an argument that the assessment has not been completed as per the procedure.

Passing of Assessment Order without passing the DAO under Section 144B:

As discussed above, AU shall in first instance send DAO to the NFAC. Upon receipt of such DAO, NFAC shall give an opportunity of being heard to the assessee by forwarding such DAO. Section 144B(9) states that assessment shall be non-est if such assessment is not completed in accordance with the Faceless Assessment Scheme.

In the case of YCD Industries[2] , Delhi High Court has held that the provisions of Section 144B provides for issuance of a show cause notice-cum-draft assessment order, and an opportunity to the assessee to respond to the same where income of the assessee is varied by the revenue. As such procedure is not followed by the revenue, assessment order along with the notice of demand has been set aside to complete the assessment as per the provisions of Section 144B.

The Bombay High Court in the case of Trendsutra Client Services (P.) Ltd[3]. has held that for the first time, the principle of natural justice has been embodied in the piece of legislation itself. The objectives of the faceless assessment scheme provides for imparting greater efficiency, transparency and accountability. However, one of the features of the scheme is stated to be passing of objective, fair and just orders. The High Court held that the provisions of giving an opportunity of being heard would be equally applicable in case variation is proposed in a revised draft assessment order which is prejudicial to the interest of the assessee in comparison to the draft assessment order or the final draft assessment order. Accordingly, the High Court has set aside the assessment order with a direction to complete the assessment in accordance with the provisions of Section 144B.

The Bombay High Court in the case of Golden Tobacco Ltd[4]. has held that it is well settled insofar as mandatory provisions are concerned; it nullifies the Act if not complied with. The object of the Faceless Assessment Scheme is to impart 'greater efficiency, transparency and accountability'. It is also for 'improvement in quality of assessment'. Thus, these provisions' beneficial purpose and importance are for the efficacious implementation of the Faceless Assessment Scheme, unerringly leading to the conclusion that the procedure prescribed under Section 144B is intended to be mandatory and neglect of any procedural safeguard would render the assessment non-est.

[2][2021] 127 taxmann.com 606 (Delhi)
[3][2021] 132 taxmann.com 104 (Bombay)
[4][2021] 132 taxmann.com 296 (Bombay)

The above principle has been upheld by various High Courts. Some of the judicial precedents on the same has been listed below:

- Bhabani Pigments (P.) Ltd. [5]
- Carlsberg India (P.) Ltd.[7]
- Floral Realcon (P.) Ltd.[9]
- Globe Capital Foundation[11]
- Ramtech Consulting[6]
- Smart Vishwas Society [8]
- Toplight Corporate Management (P.) Ltd. [10]

However, the Calcutta High Court in the case of Unisource Hydro Carbon Services (P.) Ltd.[12] has dismissed the writ petition filed by the assessee stating that it is established from record that series of adjournments were granted on the prayer of the petitioner from time to time and the petitioner did not comply with many notices and sometime in response to some of the notices on some occasion replied to the show-cause notice in detail and furnished material evidence and documents in support of its case before the Assessing Officer in course of impugned assessment proceeding. The High Court has rejected the various case laws relied upon by the assessee as the facts of the present case are different from other cases.

Further, the Delhi High Court in the case of Gurgaon Realtech Ltd.[13] has held that the Faceless Assessment Scheme is applicable also to cases where the assessment proceedings are initiated before 31.03.2021 and same are pending on 31.03.2021. The same view has been upheld by the CBDT through its Circular dated 31.03.2021. Accordingly, High Court has set aside the assessment order. The same view has been held in case of Sams Facilities Management (P.) Ltd. [14]

The Delhi High Court in the case of Rmsi P. Ltd[15]. has held that even under E-Assessment Scheme, passing of assessment order without providing an opportunity of being heard shall be treated as non-est. The High Court has pointed that absence of a provision akin to Section 144B(9) in the E-Assessment Scheme, 2019 would not make any difference to such legal outcome in as much as violation of principles of natural justice renders such decision void. Even otherwise, the Income-tax authorities have to remain bound by the statutory scheme of assessment.

Given the above, it can be understood that forwarding of draft assessment order to the assessee is mandatory failing to forward such draft assessment order vitiate the objective and purpose of faceless assessment proceedings. However, it is also the responsibility of the assessee to make timely submission of information or documentation in order to complete the assessment as per the procedure prescribed.

[5][2021] 128 taxmann.com 313 (Delhi)
[6][2021] 129 taxmann.com 201 (Delhi)
[7][2021] 127 taxmann.com 725 (Delhi)
[8][2021] 128 taxmann.com 278 (Delhi)
[9][2021] 132 taxmann.com 8 (Delhi)
[10][2021] 128 taxmann.com 221 (Delhi)
[11][2021] 131 taxmann.com 262 (Delhi)
[12][2021] 131 taxmann.com 175 (Calcutta)
[13][2021] 127 taxmann.com 726 (Delhi)
[14][2021] 130 taxmann.com 376 (Delhi)
[15][2021] 129 taxmann.com 170 (Delhi)

Failing to provide an opportunity for personal hearing:

Another check that has been provided in the faceless assessment scheme is the assessee be given an opportunity of personal hearing for making oral submission. This facility is not specifically provided in the E-Assessment Scheme but incorporated in the Faceless Assessment Scheme under Section 144B (7)(vii). The intention behind the Faceless Assessment Scheme is to remove the interaction between the assessee and the income tax authority but not conduct the assessments one sided. Hence, such option of representing the matter before the income tax authority has been provided in the Faceless Assessment Scheme. In this aspect, many High Courts have allowed the writ petition filed by the assessees.

The Delhi High Court in the case of Sanjay Aggarwal[16] has held that liberty has been given to the assessee, if his income is varied, to seek a personal hearing in the matter. The use of word 'may' cannot absolve the responsibility cast on the revenue. Accordingly, the High Court has set aside the order passed by the revenue without proving such opportunity for personal hearing.

The Bombay High Court in the case of Piramal Enterprises Ltd[17]. has held that principles of natural justice firmly run through fabric of Section 144B(1) of IT Act. Whenever DAO, FDAO is prejudicial to the interest of assessee or RDAO is prejudicial to the interest of assessee in comparison to DAO or FDAO, upon a response to show- cause notice, personal hearing for oral submissions or to present its case before income tax authority is strongly entwined in the provisions on a request from an assessee unless it is absurd, strategized and/or intended to protract assessment etc. It would also emerge from various decisions, ordinarily, such a request would not be declined.

The above principle has been upheld by various High Courts. Some of the judicial precedents on the same has been listed below.

- Balraj Hire Purchase (P.) Ltd.[18]
- Civitech Developers (P.) Ltd. [20]
- Dar Housing Ltd.[22]
- KRS Home Developers (P.) Ltd. [24]
- Lemon Tree Hotels Ltd.[26]
- Religare Enterprises Ltd.[19]
- RitnandBalved Education Foundation [21]
- Satia Industries Ltd. [23]
- Umkal Healthcare (P.) Ltd.[25]

[16][2021] 127 taxmann.com 637 (Delhi)
[17][2021] 129 taxmann.com 18 (Bombay)
[18][2021] 128 taxmann.com 190 (Delhi)
[19][2021] 131 taxmann.com 266 (Delhi)
[20][2021] 130 taxmann.com 56 (Delhi)
[21][2021] 127 taxmann.com 627 (Delhi)
[22][2021] 132 taxmann.com 29 (Delhi)
[23][2021] 131 taxmann.com 134 (Delhi)
[24][2021] 131 taxmann.com 261 (Delhi)
[25][2021] 131 taxmann.com 325 (Delhi)
[26][2021] 128 taxmann.com 409 (Delhi)

As stated above, the provisions of Section 144B are self-driven in the context of providing an opportunity of being heard and providing opportunity of personal hearing. Even such provisions are not provided in Section 144B, income tax authority is bound to adhere to the principles of natural justice and provide an opportunity of being heard. There are many instances under the Income Tax Act where in the Courts have set aside the assessment proceedings to the file of the assessing officer as there was a violation of principles of natural justice by not providing a sufficient opportunity of being heard.

Draft Assessment Order under Section 144B vs. Draft Assessment Order under Section 144C:

Upon reading of provisions of Section 144B and Section 144C, there arises many questions with respect to applicability, difference, legal consequences of draft assessment order under Section 144B and Section 144C. The object and purpose of draft assessment order under Section 144B is to provide an opportunity to the assessee to make submission before the assessing officer if there is any variation which prejudicial to the interest of the assessee. Hence, provisions of Section 144B states that failing to provide an opportunity result in setting aside of the assessment order.

However, the provision of Section 144C provides a special appeal forum for filing of objections against action of the assessing officer. In this regard, many High Courts have held that non-passing of draft assessment order under Section 144C is treated as null and void ab initio (for detailed discussion, please refer Part I).

Which means that failing to forward assessment order under Section 144B results in restarting of the assessment whereas failing to forward draft assessment order under Section 144C results in end to the assessment proceedings.

The question which may come to judicial fora is in a case where there is only a transfer pricing adjustment under Section 92Cand same has been communicated to the assessee through Transfer Pricing Officer (TPO)'s order, whether there is any requirement to pass draft assessment order under section 144B or NFAC can proceed to pass draft assessment order under section 144C?

If it is argued that assessee shall be first given an opportunity under Section 144B by forwarding the draft assessment order, the question arises is whether assessee shall submit reply to such draft assessment order under Section 144B and whether NFAC shall send reply given by the assessee to the AU which is meaning less as AU has not proposed any variation to the income returned to consider the reply given by the assessee except incorporating the TPO's adjustments in the draft assessment order. In this scenario, the viable approach may be that NFAC may pass draft assessment order under Section 144C directly if there is only transfer pricing adjustment.

However, if there are both transfer pricing and other adjustments, it is required to forward draft assessment order under Section 144B first and complete the procedure relating to other than transfer pricing adjustment. Upon receipt of submission by the assessee relating to other adjustments, NFAC may proceed to forward draft assessment order under Section 144C against which the assessee may approach the DRP.

This article is contributed by CA Sri Harsha & CA Narendra, Chartered Accountants. The author can be reached at harsha@sbsandco.com

INTERNATIONAL TAXATION

BENEFICIARY IN REVOCABLE TRANSFER VIS-À-VIS RESIDENT IN DTAA & OTHERS – BOMBAY HIGH COURT IN ADIA

Contributed by CA Sri Harsha

The recent judgment of Bombay High Court in the matter of Abu Dhabi Investment Authority[1] is a judgment for many firsts. The judgment is a result of challenge of AAR[2] ruling in Abu Dhabi Investment Authority (for brevity 'ADIA').

Issue:

ADIA is a public institution owned by and subject to the supervision of Emirate of Abu Dhabi. ADIA has challenged the ruling passed by AAR, wherein the later denied inter-alia the benefit of India-UAE[3] DTAA[4] in respect of the income accruing to the investments made or proposed to be made by Green Maiden A 2013 Trust ('Trust'), which was established by ADIA as settlor and Equity Trust (Jersey) Limited as the trustee (ETL/Trustee).ADIA has invested USD[5] 200 million in India on revocable basis through the above trust, wherein ETL acted as trustee with sole beneficiary as ADIA.

Ruling of AAR:

AAR held since the trust is not in revocable terms and only the corpus is in revocable terms, the provisions of Section 61 and Section 63 shall not be applicable and accordingly the income will be taxable in the hands of trust. Since the trust is registered in Jersey, it cannot access the India-UAE DTAA and the income earned by trust is taxable in India. Further, AAR also held that the provisions of Section 61 and Section 63 does not apply to Foreign Trusts. The AAR also held that since ADIA was the sole beneficiary, the same cannot be called as trust. The Bombay High Court rejected the view taken by AAR. In this article, we try to analyse the views taken by AAR and the rejection by High Court in detail to drive home certain points.

Analysis by High Court:

The trust is settled by ADIA in Jersey and under the deed of settlement dated 22nd July 2013, the trust is being set up and for the benefit of ADIA who is, apart from the settlor, also the beneficiary of the trust. The trust is revocable and determinable. By virtue of provisions of deed of settlement, ADIA made a capital commitment of USD 200 million in the trust in its capacity as settlor. At the time when ADIA was making decision to invest in India, there was no legal framework inUAE under which a trust could be formed, and it is not possible for ADIA to establish a sole shareholder subsidiary company in UAE. ADIA for commercial and administrative reasons has made its all-illiquid investments through separate legal entities to ensure it does not have to directly deal with various portfolio companies. ADIA has been using the Jersey jurisdiction for establishing companies and trusts for making several investments around the world, since Jersey's regulatory regime is compliant with international standards and generally not considered as opaque jurisdiction. The trust was also registered with SEBI[Z] as Foreign Institutional Investor (FII) and later on as Foreign Portfolio Investor (FPI) under the relevant regulations of SEBI.

[1] 2021 (10) TMI 1270 –Bombay High Court
[2] Authority for Advance Ruling
[3] United Arab Emirates
[4] Double Taxation Avoidance Arrangement
[5] United States Dollar
[6] Securities and Exchange Board of India

ETL as trustee has entered into an investment management agreement with Kotak Mahindra (International) Limited (KMIL) and one of the obligations cast on KMIL is that a KMIL group subsidiary will invest in each and every portfolio company alongside the trust. The Deed of Settlement provides that the capital contributions made or proposed to be made by ADIA to trust would be revocable transfer. ADIA's contention was that the income derived from making investment and debt securities in India was not assessable to tax in India having regard to the provisions of Article 24 of India – UAE DTAA read with Section 60 and Section 161 of Act. To obtain a tax certainty, ADIA has approached the AAR on the following questions and the responses of AAR were tabulated as under:

Queries raised by ADIA	Responses by AAR(in the words of High Court)
• Whether capital contribution made/proposed to be made/transferred by ADIA to Green Maiden A Trust be treated as revocable transfer for purposes of Section 63 of Act? • If the answer to the above is affirmative then, whether the entire income which may arise from the investments made by Trust in Indian Portfolio Companies be chargeable to income-tax in hands of ADIA as per Section 61 or be chargeable in the hands of any other person?	• The income from investments in debt portfolios in India is received and accrued to the Trust in India and it is taxable under Section 5 read with Section 9(1)(i) of Act. • Since there is no treaty between India and Jersey, income received or accruing or arising in India to the Trust registered in Jersey is taxable in India. • India – UAE Treaty is not applicable to Trust or Trustee. • Since India has not ratified the Hague Convention on the Law Applicable to Trust and on their recognition, trust laws of a foreign jurisdiction are not applicable in India. • Bifurcate the accrual and receipt of income of trust and the beneficiary in three stages – Stage 1 is the accrual/receipt of mainly interest income to the trust as sub-account of FII. Stage 2 is transfer of income to the trustee of the trust and Stage 3 is receipt of income by ADIA as and when transferred by virtue of deed of settlement between ADIA and Trustee.
• If the answers to the above are affirmative, whether the entire income in hands of ADIA which may accrue or arise from investments made by Trust in the Indian Portfolio Companies be exempted from tax in India based on provisions of Article 24 of India – UAE DTAA? • If the answer to the above is affirmative, whether Indian Portfolio Companies or any other person responsible for paying any sum, to the Trust, are required to deduct tax at source under provisions of the Act, on any sum payable to the trust, the income/assets of Trust being subject to provisions of Section 61 and Section 63 of Act?	

	• Bifurcate the accrual and receipt of income of trust and the beneficiary in three stages – Stage 1 is the accrual/receipt of mainly interest income to the trust as sub-account of FII. Stage 2 is transfer of income to the trustee of the trust and Stage 3 is receipt of income by ADIA as and when transferred by virtue of deed of settlement between ADIA and Trustee. • In Stage 1, the income is taxable in India as there is no treaty between India and Jersey. Even if it is presumed that the income accrues or arises to the trustee, it is still taxable in India as the income has arisen in India and the trustee being a private limited company is registered in Jersey with whom there is no treaty. • The Trust is not a trust registered under Indian Trust Act, 1882 and therefore, does not fall under Section 160(1)(iv). The income has accrued to the sub-account, i.e., the Trust. No income has accrued directly to the trustee and, hence, it cannot be taxed in like manner and to the same extent as ADIA would have been taxable. • Rejected the argument of ADIA that even if the trust is to be ignored, the income would still accrue to ADIA and would be exempt under India – UAE DTAA. Piercing the veil or lifting of veil of an arrangement is for the benefit of Revenue to check if conception is used for tax evasion or not and in present scenario, piercing the veil is not warranted. • Accrual of income to trust is not income derived by ADIA. Hence, said income does not fall under Article 24 of India – UAE Treaty.

	• Had ADIA routed the funds through an entity or structure based in UAE and ADIA being the beneficial owner, then interest income would have been exempt under Article 11(3) of India-UAE Treaty. The said view is fortified by the amendment proposed in Finance Bill, 2020 (exemption for certain income of wholly owned subsidiaries of ADIA). • Section 115AD, applicable to FIIs, is a code in itself. Hence, the income earned by Trust is taxable in India as per Section 115AD of Act.

Submissions by ADIA:

ADIA before the High Court stated that as per Section 61, the taxability of income arising by virtue of revocable transfer of assets shall be chargeable as the income of transferor and shall be included in his total income. Since the transfer to trust is on revocable terms, as per Section 61, the income earned should be taxable in the hands of the ADIA and not in the hands of trust. Alternatively, ADIA also stated that if for any reason, if the provisions of Section 61 are not applicable to the facts, in such case, in terms of Section 161(1)(iv), the trustee can only be taxable on representative capacity. Since the trustee is entitled to receive income on behalf of sole beneficiary, it should be considered as representative assessee of the sole beneficiary. Accordingly, it is pleaded that the income assessed in the hands of Trustee will take colour of the ADIA's income and thereby, the benefit of India – UAE must be granted. ADIA further stated that under Section 166, in case of representative assessee, the revenue has an option embodied in Section 166 to assess the beneficiaries instead of trustees or having assessed the trustee it may proceed to recover tax from beneficiaries. ADIA stated that since it is beneficial interests which are taxable in the hands of trustee in representative capacity, the liability of trustee cannot be greater than the aggregate liability of the beneficiaries and no part of the corpus of trust properties can be assessed in the hands of trustee. ADIA relied on the judgment of Bhavana Nalinkant Nanavati[7] to submit that there is no bar in the settlor being the sole beneficiary and Estate of Late HMM Vikramsinjhi of Gondal[8] to submit that even foreign trusts are recognised under the Indian Tax Laws. ADIA further stated that as per Article 24 of India – UAE DTAA, ADIA is covered under the meaning of term 'Government' of UAE and any income derived by ADIA from India will be exempt from tax.

[7](2002) 255 ITR 0529
[8](2014) 363 ITR 0679

Submissions by Union:

The revenue submitted that there was no treaty between India and Jersey and therefore, the trust was taxable as a non-resident under Section 5(2) and accordingly the income earned by trust is taxable in India. Sine the trust is settled in Jersey, there cannot be applicability of India – UAE DTAA treaty to determine the taxation of income in the hands of trust. The Revenue further submitted that the Indian Trusts Act, 1882 is applicable to only to India and hence the said act cannot be applied to Foreign Trust and for the trust, the liability of trust prevalent will be applicable and as there is no treaty between India and Jersey, Section 63 or Section 161 or Section 164 are not applicable. The Revenue further submitted that ADIA received income through a device and not from direct or immediate receipt or transfer of income by trust and therefore, income received from Indian debt investments is not derived by ADIA and as Article 24 only exempts from tax derived by one government from the other contracting state, the treaty is not applicable.

Observations by High Court:

On Revocable Transfers – Section 61 and Section 63:

The High Court after listening to both the parties has stated that they are not in agreement with view pronounced by AAR. The High Court stated that the provisions of Section 61 and Section 63 would apply only to trusts which fall under the Indian Trust Act, 1882 is not in accordance with the law and Revenue itself has not vehemently put this out. The Court stated that nothing in Section 61 states that it requires involvement of a trust in revocable transfer. All that Section 61 states is that the income in case of revocable transfer is subjected to tax in the hands of transferor. The Court also said that Section 61 and Section 63 are independent. A transfer can be revocable transfer on its own merits without referring to the provisions of Section 63 and the role of Section 63 is to extend the provisions of Section 61 to cases which might not otherwise covered by Section 61 by extending the meaning of word revocable. A settlement or trust are merely instances what could amount to transfer for the purposes of Section 61 and the Court held that Section 63(b) includes in the definition of transfer any settlement or trust or covenant or agreement or arrangement. The Court stated that Section 63 is not only restricted to trust, as long as the conditions specified in Section 63(a) are satisfied, any transfer, whether connected with trust or not will be a revocable transfer. In any event, it was held that there is no requirement that a trust covered under Section 63 should necessarily be an Indian trust falling under Indian Trust Act. The Court concluded that such restriction which was not there in Act cannot be imported in Section 61 and Section 63.

On Hague Convention and Recognition of Foreign Trust under Indian Tax Laws:

The Court further rejected that the stand taken by AAR that India has not ratified the Hague Convention on Law Applicable to Trust and on their recognition, trust laws of foreign jurisdiction are not applicable in India. The Court stated that the word 'trust' is not defined under the IT Act or General Clauses Act and hence it has to be interpreted in its normal meaning. The Court stated that, even if the definition of trust under the Indian Trust Act can be held to say that it does not cover the foreign trust, still the word 'trust' in Section 63 still covers all trust within its ambit. The High Court referred to judgment of Late HMM Vikramsinjhi of Gondal (supra) to drive home the point that even foreign trusts are recognized in tax laws. Accordingly, it was concluded that foreign trusts are covered under the tax laws and accordingly the provisions of Section 61 and Section 63 are applicable.

On Settlor vis-à-vis Sole Beneficiary:

The High Court then proceeded to take up the next issues, as to whether the settlor can be the sole beneficiary. The Court referred to the judgment of Gujarat High Court in Bhavana Nalinkant Nanavati (supra), wherein it was held that settlor cannot be trustee and beneficiary, but settlor can be the sole beneficiary. Since, in the instant case, the settlor and trustee are different, the Court rejected the conclusion of AAR. The High Court has found fault with the approach of AAR in not understanding the reason as to why ADIA chose to invest through trust. The Court stated that when ADIA invests directly, it is clearly eligible for exemption under Article 24 of India-UAE DTAA and this was also accepted by AAR and the creation of trust is not to avoid any tax but for the purposes of commercial expediency.

On Taxation of Representative Capacity – *In the like manner and to the same extent:*

The Court then proceeded to examine the AAR's view on the taxation of representative capacity. The view of AAR that the trustee can be representative assessee but in the instant case, trustee being a resident of Jersey cannot be agent of ADIA and accordingly the trustee cannot be assessed in terms of Section 160 was rejected by the High Court. The High Court stated that there is nothing provided in the Act that the trustee should only be a resident for the purposes of Section 160.

The Court finally concluded that since ADIA has settled the trust on the terms mentioned in Deed of Settlement, the contribution made by it to the trust would be transfer as defined in Section 63 of Act. The Court stated that Section 63 does not anywhere specify that a trust covered by it must necessarily be falling under Indian Trusts Act. As the 'trust' is not defined under Section 63 or Section 2, then it has to be understood as per common parlance and accordingly struck the view of AAR that the provisions of Section 61 and Section 63 are applicable only to Indian Trusts and not to Foreign Trusts. The Court also stated that on perusal of returns to be filed under IT Act, the ITR-5 requires to disclose the details of trusts created under the laws of country outside India, indicating that foreign trusts are recognised for the purposes of tax laws. The Court further stated that, even if, the trust is based out of Jersey and trust is settled in Jersey, ADIA being the settlor and sole beneficiary of trust and resident of UAE, as per Article 24 of India – UAE DTAA, the income which arises to it by virtue of investment in Indian Portfolio companies will be governed by beneficial provisions of treaty. The Court further held that even for a moment, the trust structure is discarded, the income would arise in the hands of ADIA and accordingly covered under Article 24 and ADIA has not attempted to reduce the tax by using the subject structure. The Court stated that even if for a moment, if it is held that the provisions of Section 61 are not applicable, then as per provisions of Section 160, the trustee can be assessed in like manner and to the same extent of beneficiary and since ADIA is the sole beneficiary, the income would be exempted in the hands of trustee in terms of Section 160. The Court accordingly rejected the view of AAR.

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