

Government reinforces the 'legislative will' and overrules Vodafone and Ericsson AB decisions – (No refund to Vodafone ?) – Mar 16, 2012

By S Sivakumar

IN what could be treated as a major googly, the Government has retrospectively amended Sections 2(14) and 2(47) of the Income tax Act, 1961 by introducing Explanations with effect from April 1, 1962 (the day, Income tax Act, 1961 came into effect)...

In terms of these retrospective amendments, the following explanation is being added to Section 2(14) of the Income tax Act, 1961 which deals with 'capital asset', with effect from April 1, 1962:

'Explanation .-For the removal of doubts, it is hereby clarified that "property" includes and shall be deemed to have always included any rights in or in relation to an Indian company, including rights of management or control or any other rights whatsoever;';

In another amendment, the following explanation is being added with effect from April 1, 1962 to Section 2(47) dealing with 'transfer':

'Explanation 2.-For the removal of doubts, it is hereby clarified that "transfer" includes and shall be deemed to have always included disposing of or parting with an asset or any interest therein, or creating any interest in any asset in any manner whatsoever, directly or indirectly, absolutely or conditionally, voluntarily or involuntarily, by way of an agreement (whether entered into in India or outside India) or otherwise, notwithstanding that such transfer of rights has been characterised as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India;';

The Government has also inserted the following Explanations, with effect from 1st April, 1962 under Section 9(1)(i) of the Income tax Act, 1961 :

'Explanation 4.-For the removal of doubts, it is hereby clarified that the expression "through" shall mean and include and shall be deemed to have always meant and included "by means of", "in consequence of" or "by reason of".

Explanation 5.-For the removal of doubts, it is hereby clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India.';

The implications arising out of these retrospective amendments are that, the law laid down by the Supreme Court in the Vodafone case, would stand statutorily overruled, on a retrospective

basis. It was widely expected that the Government would not go for a retrospective amendment, but only a prospective amendment, if at all. What has now come out from the Government's side is a totally unexpected retrospective tax proposal, aimed at scuttling a decision of the Apex Court.

The story of major retrospective direct tax amendments, to overcome unfavourable decisions does not end here. In another equally important retrospective amendment effective from 1 st June, 1976, the Government has also amended Section 9(1)(vi) of the Income tax Act, 1961 by inserting the following Explanations:

'Explanation 4.-For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.

Explanation 5.-For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not-

- (a) the possession or control of such right, property or information is with the payer;
- (b) such right, property or information is used directly by the payer;
- (c) the location of such right, property or information is in India.

Explanation 6.-For the removal of doubts, it is hereby clarified that the expression "process" includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret;'

The issue involving the taxation of income of non-residents, arising out of the supply of software licenses has been a highly litigated matter. Very recently, the Karnataka High Court had taken the view, in the Samsung case that, payments for import of shrink wrapped software packages are taxable in India and consequently, the Indian importer would have to deduct tax at source. The Delhi High Court however, in the Ericsson AB case, had taken a contrary view that, such payments are not taxable in India. Interestingly, the Bombay ITAT, in the Solid Works Corporation case had taken the view that the Delhi High Court decision would prevail over the decision of the Karnataka High Court. This has clearly been, not to the liking of the Government, which has settled the matter once and for all, by going for a retrospective amendment effective June 1, 1976. The petitioners have already gone to the Supreme Court asking for the Samsung decision of the Karnataka High Court to be quashed, by this now seems to be academic.

Before parting...

I am not against the Government reinforcing the will of the 'legislature' by amending the tax provisions, when it feels that the Courts have not rightly interpreted the law. This is especially so in the Vodafone case, where the Apex Court has clearly expressed its view that, in the absence of clarity (in respect of indirect deemed accrual of income) in the law, it could not interpret the law otherwise. But, to retrospectively amend the law going back to 1962 and 1976 is clearly obnoxious. The tax payer, whether in India or outside India, cannot be made to suffer for lack of clarity in tax provisions created by the Government itself, in the first place.

The retrospective amendment to Section 9(1)(vi) would come as a big blow for software importers, who have been expecting that that the Supreme Court would overrule the decision given in the Samsung case.

There can be little doubt that, these retrospective amendments could do a lot of damage to the so-called stability of the tax regime in India, as perceived by the foreign investors and foreign service providers.

For most of us, tax practitioners, Section 9 has been 'the' Section of the Income tax Act, 1961. This is one Section on which tons and tons of views have been expressed, in respect of which numerous case laws are available and, more importantly, this is one Section which has been feeding most of the big time Consultants and Lawyers. The Government would seem to have the final laugh, after all. Our beloved Section 9 will never be the same.

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