

FIRST LOOK

Vodafone Saga

The Supreme Court Verdict

January 20, 2012





Vodafone International Holdings B.V. vs. Union of India & Anr.

The afternoon of January 20, 2012 would be etched in golden words in the history of the Indian Judiciary; as this date marked the pronouncement of the landmark decision in the case of Vodafone International Holdings by the Hon'ble Supreme Court. The billion dollar question before the Supreme Court was the taxability of transfer of shares of a Foreign Company by a Non-Resident to a Non-Resident.

As tax professionals across the nation and various foreign investors try to read the fine print of the judgement and brainstorm on the far reaching impact it would have, BDO brings to you a short and crisp 'First Look' of this much awaited verdict.

The issues considered by the three member bench of the Supreme Court and the ruling thereon in brief are outlined here forth:

Jurisdiction to tax transactions between Non-Residents

- The transaction under the scanner is a transaction between two Non-Residents, where the subject matter are the shares of a company incorporated outside India.
- The Supreme Court established that the Indian tax authorities have no territorial tax jurisdiction to tax the said offshore transaction.

Applicability of Section 195 & Section 163

- The Supreme Court laid down that the provisions of Section 195 can only be applicable when such payments have an element of income embedded in it which is chargeable to tax.
- Section 163 relates to treatment of a purchaser of an asset as a 'representative assessee', which can be applicable only when income is deemed to accrue or arise in India to the seller.
- Since, there is no transfer of capital asset situated in India, no income is taxable in India and hence provisions of the above sections are not applicable in such offshore transactions.

Whether Section 9 is a 'look through' provision?

'Look through' vs. 'Look at'

- The Supreme Court laid down that 'look through' has to be expressly provided for in the statute or in the treaty and that such clauses cannot be read into the Section by interpretation.
- The implication of charging the transaction under Section 9(1)(i) of the Income Tax Act does not give the Tax Department to "Look Through" and to Lift the Corporate Veil and pierce the transaction but only gives the right to "Look At", key terms that has been established by the Supreme Court.

Discussion on Azadi Bachao Andolan & McDowell

Tax Planning vs. Tax Evasion

- The Supreme Court pronounced that there is no need to distinguish between both the cases as both judgments are in agreement insofar as treaty shopping is concerned.
- It also laid down that a genuine corporate business purpose of a transaction is an evidence that the transaction is not a colorable or artificial device.

Discussion on Intermediary Company led structures

- The court has based its decision on the duration of the holding, timing of exit and continuity of business as important factors in its ultimate view that the Hutch-Vodafone structure is not a sham.
- Offshore transactions evidencing ‘participative investment’ and not sham or tax avoidance preordained transactions, are outside the tax jurisdiction of Indian tax authorities.

Certainty in Tax Laws

- Certainty is integral to rule of law. Certainty and stability form the basic foundation of any fiscal system. Tax policy certainty is crucial for tax payers (including foreign investors) to make rational economic choices in the most efficient manner.

It needs to be now seen whether the Government will uphold this decision and what they propose in the forthcoming Budget. Experts await any introduction of LOB clauses / look through clauses on lines as seen in other countries as well as what is in the proposed DTC in the forthcoming budget. The Industry is hoping that retrospective amendments are not brought to Section 9(1)(i) and to Section 195 amongst others.

While Vodafone rejoices its emphatic victory, do look forward to a detailed BDO Tax Update on this landmark judgement!



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