Explanation to Indirect Share Transfer Provisions Applicable Retrospectively: ITAT

The Income Tax Appellate Tribunal (ITAT), Delhi has recently held that the **Explanation 7 under section 9(1)(i)** of the [**Income Tax**]() Act 1961, which is related to the **Indirect Share Transfer Provisions**, shall be applicable retrospectively.

In a recent case— "Augustus Capital Pvt Ltd Vs DCIT (ITAT Delhi)", the ITAT has directed that the Explanation 7 under section 9(1)(i) of the Act shall apply. Let us understand first the case in detail.

Case Details:

The Appellant (Augustus) on 27th March 2015, had sold its entire shareholding in Accelyst Pvt Ltd to an Indian company — “Jasper Infotech Pvt Ltd”.

- The shares were sold for **₹41,24,35,969/-**.
- The taxes at source on this entire sale consideration amounted to ₹17,84,19,800/-, which the buyer, Jasper Infotech Pvt Ltd withheld (suspended). The TDS has amounted 43.26% on this whole sales consideration of shares.
- With regard to the amended provisions of the section 9(1)(i) of the Act, *read with Explanations 5, 6 & 7*, the assessee (Jasper) clarified that this entire transaction involving shares transfer of the foreign company Accelyst Pvt Ltd, which also held investment in India, is not taxable.
- However, the ITAT has finally declared that the Explanation 7 under section 9(1)(i) shall be applied retrospectively. Hence, this sales consideration arising out of the share transfer **is taxable**.

Now let us refer to the Explanations 5, 6 & 7 of the section 9(1)(i) of the Act, to understand this case.

Special Provisions of section 9(1)(i) of Income Tax Act

According to the Section 9(1)(i) of the Income Tax Act 1961, the following type of income shall be ***deemed to accrue or arise*** in India :

Income which is accruing or arising, directly or indirectly, by way of—

- Any business connection in India; **OR**
- From any property based in India; **OR**
- Through or from an asset or source of income based in India; **OR**
- Through the direct or indirect transfer of a capital asset (incl. Equity shares) located in India.

Now, there are some explanations added to this section by way of various amendments:

i. ***Explanations 5:*** A capital asset being an equity share or any interest in a company incorporated outside India shall be deemed to be and shall always be deemed to have been located in India, if the share or the interest has derived its value considerably, directly or indirectly, from the assets located in India. This was inserted by the Finance Act 2012 with retrospective from 1st April 1962.
ii. ***Explanations 6:*** A share or interest, as referred to in Explanation 5, shall be deemed to derive its value considerably from the assets that are located in India only if, on a specified date, the value of such assets is—

- ₹10 crore rupees; and
- Representing at least 50% of the total value of entire assets held by the company.

iii. ***Explanations 7:*** Any income shall not be deemed to accrue or arise to any non-resident individual or entity, is the same is derived from the transfer of share or interest in a company or the entity, registered or incorporated outside India. This explanation was inserted by the Finance Act 2015.

Now the assessing officer in this case was of firm belief that since the Explanation 7 was inserted by the Finance Act 2015, and became effective from 1st April 2016, therefore, it is not applicable during the year under this consideration.

- However, the ITAT has given that Explanation 7 begins with the phrase "For the purposes of this clause" [section 9(1)(i)] unlike the Explanation 5 that begins with the phrase "For removal of doubts". Hence, the Explanation 7 has to be read with Explanation 5.
- This is because the Explanation 5 has itself been given a retrospective effect and Explanations 6 & 7, were inserted **in furtherance of the objective of** Explanation 5, these have to be read together.

With this clarification, the ITAT has confirmed that the Explanation 7 under section 9(1)(i) of the Act shall apply with retrospective effect. As a result, the buyer has to consider the TDS on sales consideration from share transfer and specify the same in its **TDS returns** as well.
