India Tax Konnect

July 2026

KPMG. Make the Difference.

Direct Tax

a. Decisions – International tax

Tribunal rejects Revenue's re-characterisation of part of share sale consideration as other income on the grounds of alleged valuation inflation: Mumbai Tribunal[1]

Facts of the case

The taxpayer, a tax resident of Mauritius, was engaged in investment holding activities for the Group.

An Indian company ('ICo1') was partly held by the taxpayer and partly by the Indian promoters.

During FY 2021-22, another Indian company ('ICo2') entered into a Share Purchase Agreement ('SPA') to acquire 60 per cent shareholding in ICo1, of which 51 per cent was purchased from the Indian promoters and 9 per cent from the taxpayer, with all shareholders receiving the same price per share.

The taxpayer claimed that the capital gains arising from the sale of ICo1's shares were not taxable in India under the India–Mauritius tax treaty ('the Mauritius Treaty').

The Revenue, however, observed that an affiliate of the taxpayer ('FCo') had entered into a long-term purchase commitment with ICo1 to continue procuring services for five years which led to artificial inflation in the value of ICo1's shares – computed as per the Discounted Cash Flow ('DCF') method – and consequently increased the sale consideration received by the taxpayer.

Accordingly, the Revenue alleged that the entire transaction was a colourable device and concluded that 20.80 per cent of the sale consideration received by the taxpayer represented compensation for the purchase commitment rather than consideration for sale of shares and re-characterised the said amount as income from other sources. Consequently, the portion attributable to the purchase commitment was not eligible for the treaty protection available for capital gains.

Revenue's contentions

The DCF valuation of ICo1 was significantly influenced by the projected revenues, including the assured business committed by FCo under the purchase commitment arrangement.

The purchase commitment by FCo was executed alongside the SPA and formed an integral part of the acquisition transaction.

The only apparent beneficiary of the purchase commitment by FCo was the seller group, including the taxpayer, because it enabled them to realise a substantially higher sale price for the shares.

Relied on the principle of 'substance over form' and argued that mere description of the entire amount as share sale consideration in the SPA did not preclude the Revenue from examining the true character of the receipt.

Taxpayer's contentions

The service transaction between FCo and ICo1 was a genuine and *bona fide* business transaction and not a hoax undertaken to inflate the value of ICo1's shares.

[1] *Fifth Third Mauritius Holdings Ltd.* v. *ACIT* (ITA No. 2010/Mum/2025)

Contd….

FCo was a major customer of ICo1 for several years before the share sale, and the purchase commitment merely provided assurance to ICo2 regarding the continuation of this longstanding business relationship after the transaction. Even after the transfer of shares, FCo not only continued to procure services from ICo1 but procured services in excess of the purchase commitment provided by it.

ICo2 acquired ICo1's shares from both the taxpayer and the Indian promoters at the same price. If the purchase commitment had artificially increased the value of the shares, it would have also benefited the Indian promoters which sold a substantially larger stake.

Market precedents exist where strategic buyers acquired captive or carve-out technology units of large enterprises and, as part of the transaction, secured long-term revenue streams through master services agreements.[2]

The Revenue had no power to re-characterise a receipt in the absence of a statutory provision to that effect.[3] Reliance was also placed on the decisions in the cases of *Arun Dua*,[4] and *D.S. Bist & Sons.*[5]

Tribunal's decision

The Mumbai Bench of the Tribunal concurred with the taxpayer's position and rejected the Revenue's re-characterisation of 20.80 per cent of the sale consideration as income from other sources.

Key observations of the Tribunal included:

No material was brought on record to establish that the transaction was a sham, colourable device, or a make-believe arrangement. On the contrary, the material on record demonstrated that FCo had been a longstanding and significant customer of ICo1, even prior to the transfer of shares and that the purchase commitment was merely a commercial assurance provided to the purchaser as part of the acquisition transaction.

All shareholders, including the taxpayer and the Indian promoters, sold their shares to ICo2 at the same agreed price per share. While accepting the consideration received by the Indian promoter shareholders, the Revenue sought to re-characterise only the taxpayer's consideration – such selective approach was inherently inconsistent and unsupported by any statutory provision.[6]

The statute does not empower the Revenue to bifurcate the agreed sale consideration of shares between independent parties and treat a part thereof as income from other sources merely based on conjectures regarding valuation.

Foreign-source income exclusion under the domestic FTS provisions not applicable merely because the payment is routed through foreign branch: Bangalore Tribunal[7]

Facts of the case [8]

The Indian company provided software services to overseas clients under an onsite-offshore delivery model, under which onsite services were rendered through the foreign branches, including its branch office located in the United States of America ('the US branch'). For providing these services, certain processes were subcontracted to other US-based companies.

---

[2] Press releases relating to various other transactions such as TCS-Citi, HCL-Volvo, Wipro-ATCO

[3] *DIT* v. *Besix Kier Dabhol SA [2012] 26 Taxmann.com 169 (Bombay); PCIT* v. *Aegis Ltd. [2019] 102 taxmann.com 495 (Bombay)*

[4] *CIT* v. *Arun Dua [1990] 186 ITR 494 (Calcutta)*

[5] *D.S. Bist & Sons* v. *CIT [1984] 149 ITR 276 (Delhi)*

[6] *Chryscapital Investment Advisors (India) Private Limited* v. *DCIT* [2015] 376 ITR 183 (Delhi); *PCIT* v. *New Silk Route Advisors P Ltd* [2018] SCC ONLINE BOM 9057

[7] *Sasken Technologies Ltd.* v. *ACIT* (ITA No. 2057 & 2058/Bang/2025)

[8] This note covers issue relating to withholding tax implications on payments to US-based sub-contractors. Other grounds of appeal have not been covered in this note.

Contd….

The Indian company made payments to the US-based subcontractors for rendering onsite software development services. However, these payments were routed through the US branch, and no tax was deducted at source ('TDS') on such remittances.

The Indian company contended that the expenses were incurred by its US branch for earning onsite revenue. Since the corresponding customer revenues were initially booked by the US branch, the payments made to the US branch were for earning income from sources outside India. The payment to the sub-contractor though qualified as fees for technical services ('FTS') under the Income-tax Act, 1961 ('the 1961 Act),[9] it fell within the exclusion provided therein and thus, was not taxable under the 1961 Act. In addition, the services provided by the subcontractors did not 'make available' any technical knowledge, experience, skill, know-how, or process and therefore, could not be characterised as fees for included services ('FIS') under the India-USA tax treaty ('the US Treaty').[10] Since these payments were not taxable in India, there was no TDS obligation.

The Revenue, however, alleged that the US branch was merely a payment conduit and the source of income was in India. Accordingly, the payments did not qualify for the exclusion and were taxable as FTS under the 1961 Act. Further, as the 'make available' condition under the US Treaty was satisfied, these payments were chargeable to tax in India as FIS. Accordingly, the Indian company failed to discharge its TDS obligation.

Relevant provisions

As per section 9(1)(vii)(b) of the 1961 Act, FTS payable by an Indian resident to a non-resident is deemed to accrue in India, except where the fee is payable in respect of services utilised in a business carried on by such Indian resident outside India or for the purposes of making or earning any income from any source outside India ('exclusion clause').

Article 12(4)(b) of the US Treaty provides that FIS includes consideration for rendering of any technical or consultancy services if such services make available technical knowledge, experience, skill, know-how, or processes.

Revenue's contentions

FTS exclusion under the 1961 Act not available

As per the master service outsourcing agreements between the Indian company and the sub-contractors, the services were directed by the Indian company and not by the US branch. The responsibilities of those sub-contractors, as well as the deliverables, were owed to the Indian company. The Indian company retained control over the performance and remained responsible for any acts of omission or commission. The sub-contractor had no independent contractual relationship with the customers and acted only as the Indian company's affiliate or sub-contractor.

Thus, the income was sourced in India and the work performed by the non-resident sub-contractors could not be regarded as services utilised for business carried on outside India.

Relied on the orders passed by the Authority for Advance Rulings in *Infosys Technologies Ltd*[11] and *Wallace Pharmaceuticals (P.) Ltd.*[12] to support its contention that the payments to the US branch did not qualify for the exclusion clause.

[9] Section 9(1)(vii)(b)
[10] Article 12

[11] *Infosys Technologies Ltd.*, In re [2013] 350 ITR 178 (AAR)
[12] *Wallace Pharmaceuticals (P.) Ltd.*, In re [2005] 278 ITR 97 (AAR)

Contd.…

Direct Tax

<u>Payments qualified as FIS under the US Treaty</u>

For the ‘make available’ condition to be satisfied, the services must be aimed at transmitting technical knowledge so that the payer derives an enduring benefit and can use the knowledge or know-how independently in future without the service provider’s assistance.

In the instant case, technical knowledge and know-how were transferred to the Indian company and ‘make available’ condition was satisfied on account of the following:

- The non-resident subcontractors directly interacted with clients, gathered business requirements, and provided technical inputs to the Indian company for software development, which was a highly specialised technical field.
- The confidentiality and intellectual property clauses in the sub-contract agreements indicated that technical and confidential information was made available to the Indian company by the sub-contractors. Further, the ownership of the intellectual property rights vested with the Indian company.
- Inclusion of non-compete and non-disclosure obligations in the sub-contract agreements showed that technical knowledge, skill, experience or know-how was made available to the Indian company; otherwise, there would have been no reason to incorporate such protective provisions.

Tribunal’s decision

The Bangalore Bench of the Tribunal held that since the ‘make available’ condition under the US Treaty was not satisfied, the payments made to the US branch were not chargeable to tax in India and there was no TDS obligation on the Indian company.

Key observations of the Tribunal included:

<u>FTS exclusion under the 1961 Act not available</u>

Routing payments through the US branch did not establish that the services were utilised for a business carried on outside India or for earning income from a source outside India.

Since the business was carried on in India and the payments were connected with income earned from India, the Indian company was not entitled to the benefit of the FTS exclusion.

<u>Payments did not qualify as FIS under the US Treaty</u>

The payments to US branch could not be characterised as FIS under the US Treaty since the ‘make available’ condition was not satisfied. Though the services were rendered and information generated from the sub-contractors’ work was shared with the Indian company, the Revenue failed to establish that the Indian company was thereby enabled to perform the same functions on its own.

Applying the principles laid down in *De Beers India Minerals,*[13] the Tribunal reiterated that mere provision of services, or transfer of information or work product, is insufficient to constitute FTS/ FIS unless the recipient is equipped to use the underlying technical knowledge or expertise independently in future without further assistance from the service provider.

[13] *CIT* v. *De Beers India Minerals Pvt. Ltd*. [2012] 346 ITR 467 (Karnataka)

Contd….

Direct Tax

Specialised customer-specific professional services provided along with software subscription taxable as fees for technical services: Delhi Tribunal [14]

Facts of the case

The taxpayer, a tax resident of the USA, was engaged in providing data software solutions.

During FY 2021-22, the taxpayer *inter alia* received the payment for supply of software subscriptions which included receipts for professional services.

The issue arose whether receipts from software subscription and from professional services were taxable in India by way of royalty or FTS under the 1961 Act and FIS under the US Treaty.

Taxpayer's contentions

Considering the following terms of the Enterprise Subscription Master Agreement ('ESMA') the receipts from supply of software subscription were not in the nature of royalty or FTS/FIS:

- The customer was given a non-transferable and limited access of software on subscription basis and only for its own business purposes. The recipient had no right to modify, alter, sub-license, transfer etc., the taxpayer's software.
- While the software was modified / customised by the taxpayer to suit the individual customer's requirements, however, there was no transfer of technology to the customers.

The receipts for professional services were mainly for migration from old to new version of the taxpayer's software and to assist the customers in deriving maximum value from implementation and use of the software subscriptions.

Relied upon the Supreme Court ruling in *Engineering Analysis*[15] and other judicial precedents[16] to contend that the receipts from software subscriptions and related services could not be characterised as royalty or FIS under the US Treaty.

Revenue's contentions

Distinguished *Engineering Analysis* ruling on the ground that the taxpayer's software was not a shrink-wrap software involving mere transfer of object code; rather, it was a customised software modified and configured to meet the specific operational needs of customers. Unlike the shrink-wrap software considered in *Engineering Analysis* (where no source code was transferred), the taxpayer's data platform operated through programming languages such as Java, Python, C++ etc. which required transfer of source code.

Referred to the relevant clauses of ESMA and argued that the taxpayer did not supply a standard software product to its customers but offered a subscription-based package that included software access, technical support services (providing remote help in resolving software issues faced by the customers), training, consulting, etc.

The taxpayer's software package enabled the customers to undertake and perform various business functions. The customers were recipients of specialised skills,

[14] *Cloudera Inc* v. *ACIT* (ITA No. 1185/Del/2025) – Multiple appeals with common issues; appeal filed for FY 2021-22 was taken as the lead case

[15] *Engineering Analysis Centre of Excellence (P.) Ltd.* v. *CIT* [2021] 432 ITR 471 (SC)

[16] *CIT(IT)* v. *Salesforce. Com Singapore Pte. Ltd.* [2024] 165 taxmann.com 580 (Delhi); *Aecom Technical Services INC.* v. *ITO* [2026] 485 ITR 357 (Delhi); *CIT* v. *Amazon Web Services Inc.* [2025] 174 taxmann.com 1188 (Delhi)

Contd….

knowledge, know-how and the same was augmented through continuous support service provided by the taxpayer. Hence, the 'make available' condition under the US Treaty was satisfied in the instant case and the entire receipts from software subscription were taxable in India.

Tribunal's decision

After examining the ESMA terms, including the restrictions on the use, transfer, and modification of the software, and considering the judicial precedents cited by the taxpayer, including *Engineering Analysis*, the Delhi Bench of the Tribunal held that there was no transfer of technology to customers. The subscription receipts (excluding the receipts for professional services) did not constitute royalty or FTS/ FIS.

With respect to receipts for professional services, the Delhi Tribunal held that these receipts were taxable as FTS/ FIS under the Act and the US Treaty.

Only 6 out of 12 customers had availed professional services, while the remaining customers purchased only software subscriptions. This indicated that professional services were separate from, and not automatically bundled with, the software subscription offerings.

The amount charged for professional services varied significantly across customers, with some paying substantial amounts in addition to subscription fees. This suggested that the services were specialised customer specific consultations rather than for providing assistance for migration from old to new version of the software application.

Commercial support services not taxable as Royalty in the absence of imparting of technical knowledge or expertise: Mumbai Tribunal [17]

Facts of the case

The taxpayer, a tax resident of the Netherlands, was engaged in providing corporate travel management services.

It entered into a Global Framework Network Agreement with group companies, including the Indian group entity ('ICo') for rendering centralised support services. These services included global account management, marketing, supplier relationship management, procurement, pricing support etc. and were rendered from outside India.

The taxpayer claimed that the services fee received from ICo was neither taxable in India as royalty nor as FTS under the 1961 Act, read with the India–Netherlands tax treaty ('the Dutch Treaty').

The Revenue, however, alleged that the services rendered by the taxpayer related to core business functions of ICo and enabled ICo to access the group's commercial knowledge, experience and skill developed over the years by the group. It involved imparting of information concerning technical, industrial, commercial knowledge and experience/ skill. The software required by ICo for performing its core operations was supplied by the taxpayer. The service fees constituted royalty under section 9(1)(vi) of the 1961 Act, read with Article 12 of the Dutch Treaty, and were thus taxable in India. Alternatively, the payment is taxable as FTS.

[17] *ACIT* v. *BCD Travel Services BV* (ITA No. 7451/Mum/2025)

Contd.…

Relevant provisions

Explanation 2 to section 9(1)(vi) of the 1961 Act provides that royalty includes consideration for the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill.

As per Article 12(4) of the Dutch Treaty, the term "royalties" includes consideration for information concerning industrial, commercial or scientific experience.

Article 12(5) of the Dutch Treaty defines FTS as consideration for the rendering of any technical or consultancy services if such services are ancillary and subsidiary to the application or enjoyment of the right, property or information for which royalty is received; or ‘make available’ technical knowledge, experience, skill.

Taxpayer’s contentions

The service fees represented consideration for commercial services. Mere application of the knowledge/ experience to render services did not result in imparting of information concerning industrial, commercial or scientific experience to be construed as royalty.

Referred to the OECD Commentary 2017 on Article 12 of the OECD Model Tax Convention, which distinguishes between the payment for supply of know-how and payment for provision of services.

The Commentary clarifies that payments are treated as royalty when they are made for the transfer of ‘know-how’—that is, for confidential industrial, commercial, or scientific knowledge developed through prior experience and capable of providing economic value to the recipient. In contrast, where a service provider merely applies its own expertise, skills, and experience to perform services without transferring that knowledge, skill or expertise enabling the recipient to use it independently, the payment constitutes consideration for services rather than for transfer of know-how.

Relied on judicial precedents,[18] including the Tribunal’s favourable orders in its own cases for earlier years, to contend that service fee received was neither royalty nor FTS under the 1961 Act, read with the Dutch Treaty.

Tribunal’s decision

Following its earlier orders, the Mumbai Bench of the Tribunal held that the service fee received by the taxpayer was not taxable as royalty or FTS under the 1961 Act, read with the Dutch Treaty.

Key findings from the Tribunal’s order for the earlier year included:

The services rendered included services in the field of finance, account management, and human resources and did not involve the transfer of rights, imparting of any information concerning the working of, or the use of, a patent, invention, model, design, etc.

Services rendered by the taxpayer were not technical in nature but commercial services with no intellectual property or any other right provided to the service recipient (i.e. ICo).

[18] *GECF Asia limited* v. *DIT* [2014] 34 ITR(T) 303 (Mumbai); *Marck Bioscience Ltd* v. *ITO*(IT) [2017] 164 ITD 205 Ahmedabad Tribunal); *Koninklijke Philips Electronics N.V.* v. *DCIT* [2018] 99 taxmann.com 23 (Kolkata Tribunal); *Diamond Services International Private Limited* v. UoI [2008] 169 taxmann.com 201 (Bombay)

Contd….

Further, ICo could not have performed similar services without continued support from the taxpayer and therefore, the requirement of 'make available' technical knowledge, skills etc., for the services to be characterised as FTS under the Dutch Treaty remained unfulfilled. Accordingly, the receipts could not be treated as FTS under the Dutch Treaty.

b. Decisions – Domestic tax

Advance received for stock-in-trade not taxable absent capital asset transfer negotiations; no virtual forfeiture merely due to lapse of time: Karnataka High Court [19]

Facts of the case

The taxpayer, an individual, was engaged in the business of procuring and facilitating the acquisition of land for real estate projects.

In February 2006, he received certain advances from the Indian promoter entities to identify, procure and facilitate the acquisition of land for their business projects.

These advances continued to be reflected as outstanding liabilities in the financial statements for the year ended 31 March 2015.

The Revenue contended that the advances remained outstanding for nearly eight years without any claim from the promoters, amounting to virtual forfeiture. It argued that the taxpayer had utilised the funds to acquire assets in its own name rather than procure land on behalf of the promoters. Accordingly, the advances assumed the character of income in the taxpayer's hands and were taxable as income from other sources under section 56(2)(ix) of the 1961 Act.

The taxpayer argued that advances were received in the course of business. Since there was neither negotiation for transfer of a capital asset, nor forfeiture of advances, the provisions of section 56(2)(ix) were not applicable.

[19] *PCIT/ ACIT* v. *Ravi Shankar Shetty* (ITA No. 225 of 2021)

Contd.…

Relevant provisions

As per section 56(2)(ix) of the 1961 Act, any sum of money received as an advance or otherwise in the course of negotiations for transfer of capital asset will be taxable as income from other sources, if such sum is forfeited and the negotiations do not result in the transfer of such capital asset.

High Court's decision

Section 56(2)(ix) can be applied where the twin conditions – failed negotiation for the transfer of a capital asset and actual forfeiture of advance received in the course of negotiation for such transfer – are satisfied. Since these conditions were not fulfilled in the instant case, the Karnataka High Court ruled in favour of the taxpayer.

No forfeiture of advance

The Court rejected the Revenue's plea of virtual forfeiture, holding that mere lapse of time does not amount to forfeiture unless there is material to demonstrate that the recipient has become entitled to retain the advance absolutely. Since the advances continued to be reflected as liabilities in the taxpayer's books and were acknowledged by the promoters, they could not be treated as forfeited merely because eight years had elapsed without any refund claim.

Relied upon its earlier decision in *Alvares & Thomas*,[20] wherein it was held that merely because a creditor could not be traced, it could not be concluded that there was a cessation of liability for the purposes of section 41 of the 1961 Act.

[20] *CIT* v. *Alvares & Thomas* [2017] 394 ITR 647 (Karnataka)

No negotiation for transfer of a capital asset

Considering the purpose for which the advance was given to the taxpayer, the relationship between the taxpayer and the promoters was not that of a transferor and transferee negotiating the transfer of a capital asset, but the one where funds were made available to the taxpayer for carrying out a business activity.

In the ordinary course of the taxpayer's business, the land proposed to be acquired would partake the character of 'stock-in-trade' and not capital asset.[21]

Dividend stripping implications not applicable unless the statutory conditions are met: Mumbai Tribunal[22]

Facts of the case

The taxpayer, an individual, had invested in certain mutual fund ('MF') units on 19 March 2018. He received tax-exempt dividend on these units in two tranches – on 22 March 2018 and 7 March 2019. The units were ultimately redeemed on 18 March 2019, and short-term capital loss ('STCL') was claimed in the tax return filed for FY 2018-19.

Based on the information gathered during a survey conducted on the asset management company managing the MF, the Revenue alleged that the MF had manipulated its accounting methodology by treating part of the unit premium reserve as distributable surplus and declaring dividends out of capital rather than realised profits, which was in violation of SEBI guidelines. Thus, the dividend received by the taxpayer represented a return of capital rather than genuine dividend income.

[21] The definition of "capital asset" under section 2(14) of the 1961 Act expressly excludes stock-in-trade

[22]. *Colvyn James Harris* v. *DCIT* (ITA No. 8925/Mum/2025)

Contd….

Direct Tax

The Revenue further contended that the entire arrangement was a colourable device as the taxpayer entered into a pre-planned arrangement with the MF to receive tax-exempt dividend and generate artificial STCL for set-off against other capital gains.

Though the specific provisions under the 1961 Act relating to dividend stripping were not applicable, the Revenue still alleged dividend stripping and reduced the amount of aggregate dividend from the cost of acquisition and computed short-term capital gain (‘STCG’) on redemption of the MF units.

Relevant provisions

Section 94(7) of the 1961 Act is an anti-avoidance provision dealing with ‘dividend stripping.’

It provides that the loss arising from the sale of securities or units will be ignored to the extent of the dividend received on such securities or units for computing taxable income, if the following conditions are cumulatively satisfied:

- Securities or units are acquired within 3 months prior to the record date;[23]
- Such securities are sold/ transferred within 3 months after the record date, or the units are sold/ transferred within 9 months after the record date; and
- Tax-exempt dividend or income is received or receivable on such securities or units.

[23] As per the Explanation to section 94, “record date" means such date as may be fixed by a Mutual Fund for the purposes of entitlement of the holder of the units to receive income.

Taxpayer’s contentions

The Revenue's allegation that the transaction was fictitious, pre-planned or a sham transaction was not supported by any evidence. The transactions were carried out through recognised banking channels, the investment was made in an approved MF, Securities Transaction Tax had been duly paid on redemption of the units and Dividend Distribution Tax had been paid by the MF.[24]

The allegation of manipulation of SEBI regulations by the MF was founded only on conjectures and surmises, without any material establishing that the taxpayer had participated in or was even aware of any such alleged violation.

Even assuming the transaction was pre-planned, the ‘dividend stripping’ provisions could be invoked only if the prescribed statutory conditions were cumulatively satisfied. In the instant case, these conditions were not satisfied:

- For the first tranche of dividend received, the record date was 22 March 2018. The units were sold on 18 March 2019, i.e., after approximately eleven months and twenty-five days, which was beyond the prescribed nine-month period.
- For the second tranche of dividend received, the record date was 7 March 2019, whereas the units had been acquired on 19 March 2018, which was much beyond the period of three months preceding the record date.

The recomputation of capital gains cannot be sustained without identifying the charging or disallowance provision authorising such adjustment. The Revenue could not disregard the STCL computed by the taxpayer by resorting to general allegations of dividend stripping or colourable device.

[24] Section 115R

Contd.…

Judicial precedents relied upon by the taxpayer

- The Supreme Court's decision in *Walfort Share & Stock Brokers*[25] wherein it was held that even if the transaction is pre-planned, the genuineness of the transaction cannot be doubted, and the loss cannot be ignored unless the transaction falls within the four corners of section 94(7).
- The Bombay High Court's decision in *Karan Maheshwari*,[26] wherein reassessment proceedings initiated on almost identical allegations involving the same MF (as in the instant case) were quashed. The principles laid down in this decision continued to hold good as the Special Leave Petition preferred by the Revenue against the High Court's decision was dismissed by the Supreme Court.
- The Mumbai Bench of the Tribunal's decision in *Subhkam Ventures*,[27] wherein similar additions arising from the survey of the same MF (as in the instant case) were deleted.

Tribunal's decision

The Mumbai Bench of the Tribunal concurred with the taxpayer's position and held that since the statutory conditions were not cumulatively fulfilled, dividend stripping provisions were not applicable. The Revenue was not justified in treating the dividend as return of capital and reducing the same from the cost of acquisition in the absence of satisfaction of the conditions prescribed under the dividend stripping provisions.

The Revenue proceeded substantially on the basis of general allegations arising out of survey proceedings with no material brought on record to show that the taxpayer was a party to any alleged manipulation by the MF or that the taxpayer knowingly participated in any sham arrangement.

Relying upon the Supreme Court's decision in *Walfort Share & Stock Brokers*, the Tribunal reiterated that dividend stripping transactions cannot be treated as sham or bogus *per se* merely because they involve the receipt of exempt dividend and a subsequent loss on sale of units. Any adverse tax consequence can arise only if the prescribed conditions under section 94(7) are satisfied; otherwise, the loss cannot be disallowed on that basis.

[25] *CIT* v. *Walfort Share & Stock Brokers (P.) Ltd.* [2010] 326 ITR 1 (SC)
[26] *Karan Maheshwari* v. *ACIT* [2025] 176 taxmann.com 700 (Bombay)
[27] *ACIT* v. *Subhkam Ventures (I) Pvt. Ltd.* (ITA Nos. 5657/Mum/2024, 5620/Mum/2024 & 5622/Mum/2024)

c. Circulars/ Notifications/ Guidelines

CBDT notifies TDS exemption on specified payments to specified IFSC units

The Central Board of Direct Taxes ('CBDT') issued two notifications under the Income-tax Act, 2025 ('the 2025 Act') providing relief from tax deduction at source ('TDS') on specified payments made to eligible units located in an International Financial Services Centre ('the payee').

Both the notifications are deemed to have come into force from 1 April 2026.

IFSC units are eligible for a profit-linked deduction for twenty consecutive tax years out of twenty-five years, at the option of the IFSC unit.[28] While the payee was entitled to the deduction, the payers were nevertheless required to deduct tax on certain payments to such IFSC units, requiring the payee to claim the refund of tax withheld. These notifications seek to eliminate this hassle.

[28] Section 147 of the 2025 Act

Contd.…

Direct Tax

TDS exemption on ship lease rental payment[29]

No TDS is required to be deducted on lease rent or supplemental lease rent payments by a lessee to an IFSC unit (being the lessor) for lease of a ship.

For the purposes of this notification, the terms “ship”, “International Financial Services Centre” and “unit” have been defined in the notification itself.

TDS exemption on other specified payments[30]

No TDS is required to be deducted on specified payments to IFSC units, *inter alia*, including interest on external commercial borrowings/ loans, professional fees, referral fees, brokerage, commission on factoring and forfaiting services, insurance commission, and dividend income.

The exemption covers specific IFSC units, including banking unit, insurance intermediary office, finance company, finance unit, fund management entity, investment advisor, and FinTech entity.

For the purposes of this notification, definition of the specified IFSC units has been provided in the notification itself and is aligned with the respective regulations and registration requirements under the relevant International Financial Services Centres Authority Regulations.

Key compliances under both notifications

Compliance obligations of the payee

The payee (i.e. the specified IFSC unit) is required to furnish a statement-cum-declaration in the newly prescribed form[31] to the payer giving details of twenty consecutive tax years for which the payee opts for claiming profit-linked deduction.

This form is required to be furnished for each tax year for which the deduction option is exercised.

Compliance obligations of the payer

The payer is not required to deduct tax on payments made or credited to the payee after the date of receipt of the said form.

The payer is required to report particulars of all the payments made to the payee, on which tax has not been deducted, in the prescribed TDS statement.[32]

The TDS exemption is available only for the tax holiday period for which the prescribed form is furnished. The payer remains liable to deduct tax on payments relating to any other year.

India-Sri Lanka tax treaty amended to incorporate ant-abuse provisions

The Ministry of Finance has issued a notification[33] to give effect to the Protocol amending the existing India–Sri Lanka tax treaty (‘the SL Treaty’). The Protocol, signed on 16 December 2024, entered into force on 19 June 2026 and is effective in India in respect of income derived on or after 1 April 2027.

Since the SL Treaty is not a Covered Tax Agreement under the Multilateral Instruments (‘MLI’), the two countries adopted a bilateral approach to amend the SL Treaty to incorporate anti-abuse provisions aligned with the MLI framework.

[29] Notification No. 75/2026/F.No. 275/18/2026-IT(B)] dated 3 July 2026
[30] Notification No. 80/2026/F.No. 275/19/2026-IT(B)] dated 10 July 2026
[31] Form No. 1(N)

[32] Section 397(3)(b) read with Rule 219 of the Income-tax Rules, 2026
[33] Notification No. 88/2026 dated 16 July 2026

Contd….

Direct Tax

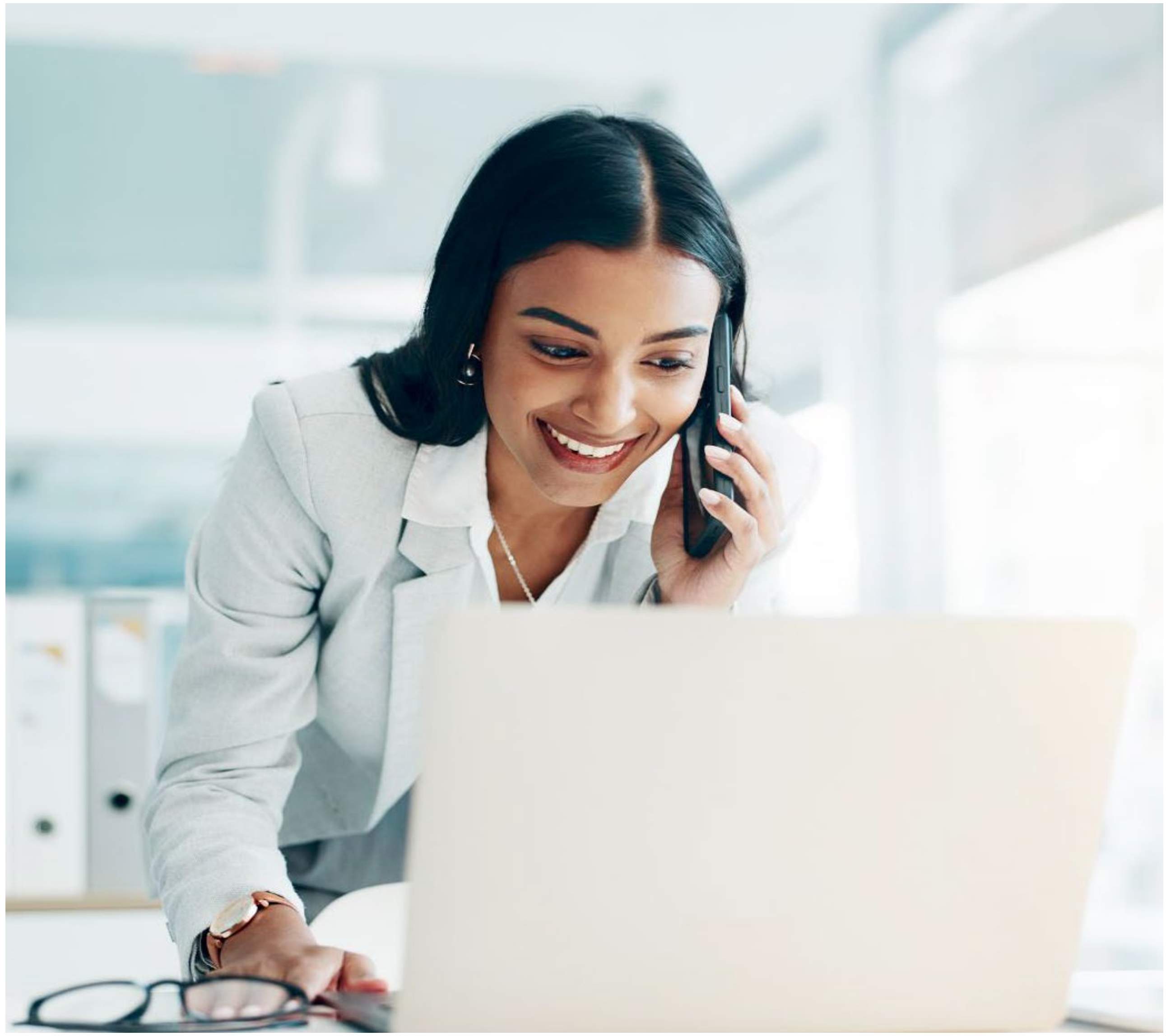
Key amendments

Revision of the Preamble

The revised preamble provides that the amended SL Treaty aims to eliminate double taxation, without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty shopping arrangements) aimed at indirectly benefiting residents of third States.

Introduction of Principal Purpose Test (‘PPT’)

PPT provisions have been introduced to deny Treaty benefits in respect of an item of income if obtaining that benefit was one of the principal purposes of entering into an arrangement or transaction, unless it is established that granting that benefit was in accordance with the object and purpose of the relevant provisions of the Treaty.[34]



[34] Para 6 of Article 28

High Court cases

Minimum average balance is not consideration for banking services and not liable to service tax[35]

Show Cause Notices (‘SCNs’) were issued to Canara Bank, Bank of Baroda, and Karnataka Bank (collectively referred to as ‘the petitioners’) demanding service tax. The SCNs proceeded on the premise that the Minimum Average Balance (‘MAB’) required to be maintained by customers constituted non-monetary consideration for the bouquet of banking services rendered by the petitioners. The authorities sought to assign a notional value equivalent to the penalty charged by the petitioners to customers in the event of failure to maintain the prescribed MAB and demanded service tax, along with interest and penalties. Aggrieved by the SCNs, the petitioners challenged them before the Karnataka High Court by way of writ petitions.

The petitioners contended that they had not charged any consideration for the services provided to customers who maintained the prescribed MAB. According to the petitioners, the requirement to maintain the MAB was merely one of the conditions of the contract entered into between the petitioners and their customers. The petitioners further submitted that the SCNs were contrary to Circular No. 178/10/2022-GST dated 3 August 2022, Circular No. 214/1/2023-ST dated 28 February 2023, and CBEC Circular No. 62/11/2003-ST dated 21 August 2003, as well as the provisions of sections 66B, 65B(44), 65B(51), 66E(e), and 67 of the Finance Act, 1994 (‘the Finance Act’).

The revenue contended that the prescribed MAB constituted non-monetary consideration for the bouquet of banking services rendered by the petitioners.

[35] *Canara Bank* – 2026-TIOL-757-HC-KAR-ST

It was argued that the collection of penal charges when customers failed to maintain the prescribed MAB indicated that the petitioners provided additional services to customers who maintained the required balance.

According to the revenue, the nature and extent of the services extended by the petitioners to their customers were contingent upon the MAB undertaken to be maintained by them. Even where the prescribed MAB was not maintained, the services continued to be provided, albeit subject to the levy of the prescribed penalty. The revenue further contended that the petitioners had agreed to an obligation to render services and, in return, the customers’ act of maintaining the prescribed MAB constituted the consideration for such obligation. It was also argued that the promise to maintain the prescribed MAB qualified as “consideration” under section 2(d) of the Indian Contract Act, 1872 and could be assigned a notional monetary value for the purposes of service tax.

The Court held that maintenance of the prescribed MAB was merely a contractual condition and could not be construed or treated as ‘consideration’ under the Finance Act or the rules made thereunder. The Court further held that the circulars issued by the Board were binding on the revenue. The Court observed that a ‘declared service’ must be supported by consideration and constitute an independent service rendered under a separate contractual arrangement. In the present case, the MAB was only a contractual stipulation, and the penalty for its breach could not be regarded as consideration, particularly when no monetary accrual or pecuniary benefit accrued to the petitioners.

The Court also observed that the choice of opening an account with a prescribed MAB rested entirely with the customer, and the petitioners neither compelled customers to opt for such accounts nor derived any corresponding benefit or

Contd.…

consideration from the MAB requirement. The Court further noted that a GST SCN in case of South Indian Bank on identical grounds was dropped by the adjudicating authority, and the order was accepted by the Government as disclosed in the RTI information sought by the respondents. Since the relevant provisions under the service tax and GST laws are materially identical, the issuance of similar SCNs was also liable to be quashed on that ground. Accordingly, The High Court allowed the writ petitions and quashed the SCNs.

Address on invoice of foreign company not relevant in RCM transaction but one who paid the consideration and issued self-invoice is entitled for ITC[36]

The petitioner company, had six GST registrations across India, including the Kerala unit, which was the petitioner in the present case. Foreign parent of the petitioner provided various services, including email, virus protection, IT management and infrastructure services, and other IT support services to the petitioner company. For these services, the foreign parent company issued an invoice in the name of the Delhi corporate office. However, the consideration for the said invoice was paid by the Kerala unit. The Kerala unit also issued a self-invoice under the reverse charge mechanism (‘RCM’), discharged the applicable GST liability, and subsequently availed input tax credit (‘ITC’) on the basis of the self-invoice. Thereafter, the Kerala unit distributed the ITC to its other units located in Delhi, Haryana, Karnataka, Maharashtra, and Tamil Nadu by way of cross-charging, i.e., by raising tax invoices on such units. The revenue-initiated proceedings alleging wrongful availment of ITC by the Kerala unit and contended that the Kerala unit had violated the provisions of the GST law by distributing ITC without obtaining registration as an Input Service Distributor (‘ISD’).

The petitioner contended that the Kerala unit was the actual recipient of the services since it had paid the consideration to the foreign parent company and, in terms of section 2(93) of the CGST Act, 2017, the recipient includes the person liable to pay the consideration. It was further submitted that the self-invoice issued under section 31(3)(f) of the CGST Act, 2017 constituted a valid document for availing ITC and that all the conditions prescribed under section 16 of the CGST Act, 2017 were satisfied, as the services had been received, tax had been paid, and the requisite documentation was available.

The petitioner also argued that, at the relevant time, the ISD mechanism was not mandatory and, therefore, distribution of ITC without obtaining ISD registration was permissible.

The revenue contended that the ITC had been wrongly availed because the invoice issued by the foreign parent company was in the name of the Delhi unit and not the Kerala unit. Accordingly, the Kerala unit could not avail ITC in respect of supplies received by another distinct person. It was further argued that the company could have distributed the ITC only through the ISD mechanism and that distribution of ITC without obtaining ISD registration was contrary to the statutory provisions. In support of this contention, reliance was placed on section 24(viii) of the CGST Act, 2017 to argue that registration as an ISD was mandatory.

The Court observed that the Kerala unit qualified as the recipient of the services since it had paid the consideration to the foreign parent company and had also discharged the applicable tax by issuing a self-invoice. The Court further held that the invoice issued by the foreign company could not be treated as the relevant document for the purpose of availing ITC, as it had not been issued by a registered supplier. Accordingly, the self-invoice issued by the Kerala unit was the relevant

[36] *Intertek India Private Limited* – 2026-VIL-573-KER

Contd.…

document for claiming ITC, and the Kerala unit was therefore entitled to avail ITC on that basis.

The Court further observed that a careful reading of the unamended section 20 of the CGST Act, 2017 showed that it was merely an enabling provision facilitating the distribution of ITC through an ISD mechanism and did not mandate that such distribution must be carried out exclusively through an ISD. It was further observed that the transaction was revenue neutral and involved no tax evasion and therefore imposing liability on technical reasons cannot be justified under any circumstances and is against the spirit and purpose of the CGST Act, 2017.

Tribunal cases

Uninvoiced shareholder allocations not liable to service tax under RCM[37]

Dana India Private Limited (‘the taxpayer’), an Indian subsidiary of Dana Corporation, USA (‘Dana USA’), was engaged in the manufacture of axles and axle components. Dana USA incurred Selling, General and Administrative (‘SG&A’) expenses for various activities. These expenses were classified into two categories. The first category comprised invoiced allocations relating to strategic administration, human resources, finance, tax, legal, engineering, purchasing, and business development services. Dana USA raised invoices for these amounts, and the taxpayer discharged service tax under the RCM. The second category comprised uninvoiced allocations relating to shareholder/stewardship activities, including maintaining investor relations and external audit compliance. These amounts were neither invoiced to the taxpayer nor accounted for in its books of accounts.

The revenue alleged that the uninvoiced allocations also represented consideration for services received by the taxpayer from Dana USA and issued an SCN demanding service tax under RCM, along with interest and penalties. The Commissioner (Appeals) set aside the demand. Aggrieved by the order, the revenue filed appeals before the Tribunal.

The taxpayer contended that the Master Service Agreement and the Transfer Pricing Report clearly distinguished between chargeable services (invoiced allocations) and shareholder/stewardship activities (uninvoiced allocations). It was further submitted that the uninvoiced allocations represented costs incurred by Dana USA for shareholder/stewardship functions and not for any services rendered to the taxpayer.

It was further contended that the disputed allocations were neither invoiced to nor paid by the taxpayer and were not recorded in its books of account. According to the taxpayer, there was no contractual understanding or agreed consideration in respect of the uninvoiced allocations and, therefore, no taxable service could be said to exist.

The revenue, on the other hand, contended that although Dana USA had allocated SG&A expenses to the taxpayer, service tax had been discharged only on the invoiced portion. According to the revenue, the uninvoiced allocations also represented the value of services received by the taxpayer and formed part of the taxable value. It was further alleged that the taxpayer had wilfully suppressed the facts from the revenue with the intent to evade payment of service tax.

[37] *Dana India Private Limited* – 2026 (5) TMI 1098 CESTAT NEW DELHI

Contd.…

Indirect Tax

The Tribunal held that the uninvoiced SG&A allocations were not liable to service tax under the RCM and upheld the order of the Commissioner (Appeals) setting aside the demand. The Tribunal further held that the uninvoiced allocations were not linked to the rendition of any service or to any consideration payable by the taxpayer. Accordingly, service tax could not be levied on such allocations. The Tribunal further observed that service tax is a contractual levy and that there was no contractual understanding or agreed consideration between Dana USA and the taxpayer in respect of the uninvoiced allocations. The Tribunal rejected the revenue's reliance on debit entries in Dana USA's accounting system, holding that the disputed allocations were not reflected in the taxpayer's books of account and, therefore, could not attract service tax on that basis. The Tribunal also noted that the uninvoiced allocations related to shareholder/stewardship activities undertaken by Dana USA for its own purposes and not for consumption by the taxpayer. Consequently, the Tribunal found no infirmity in the order of the Commissioner (Appeals), dismissed the revenue's appeals, and upheld the dropping of the demand, interest, and penalties.

Foreign Exchange Management Act, 1999

RBI simplifies SNRR account framework through Foreign Exchange Management (Deposit) Regulations, 2026

The Reserve Bank of India ('the RBI') has notified the Foreign Exchange Management (Deposit) (Sixth Amendment) Regulations 2026[38] introducing significant changes to the framework governing Special Non-Resident Rupee ('SNRR') Accounts. The key highlights are as under:

- Non-residents can now open SNRR accounts with an AD bank in India, its overseas branch, or its branch in an International Financial Services Centre ('IFSC').
- SNRR accounts may be used for the purpose of permissible current and capital account transactions with a person resident in India in accordance with the rules and regulations framed under the Act, and for putting through any bona fide transaction with a person resident outside India.
- The amendment permits transfers from NRO accounts to NRE or SNRR accounts, subject to FEMA remittance limits.
- Several operational conditions under Schedule 4 relating to SNRR accounts have been removed, simplifying the framework.

RBI has updated its Frequently Asked Questions in relation to the annual return on foreign liabilities and assets

The RBI on 1 July 2026 has updated its Frequently Asked Questions ('FAQs') in relation to the Annual Return on Foreign Liabilities and Assets ('FLA') under FEMA, 1999.[39]

[38] Gazette ID: CG-MH-E-22062026-273715 notified in FEMA 5(R)(6)/2026-RB dated 18 June 2026
[39] FAQs on FLA return

RBI releases draft Foreign Exchange Management (Foreign Investment) Rules, 2026 for public comments

The RBI has placed on its website the Draft Foreign Exchange Management (Foreign Investment) Rules, 2026 for public comments. The draft rules will supersede the existing Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.[40]

Please click here to access our detailed Flash News on the draft foreign investment rules.

The Government of India notifies amendment to the Foreign Direct Investment policy for the e-commerce sector

The Department For Promotion of Industry & Internal Trade ('DPIIT'),[41] has amended the Foreign Direct Investment ('FDI') Policy *via* Press Note 3 easing the FDI norms for e-commerce exports. DPIIT has allowed foreign-funded e-commerce entities to operate an inventory-based model exclusively for exports of goods manufactured or produced in India, while the existing restriction on inventory led B2C e-commerce for domestic sales remains unchanged. The amendment aims to boost India's e-commerce exports and improve global market access for Indian sellers.

The amendment will come into effect upon notification under FEMA.

[40] RBI Press Release dated 21 July 2026
[41] Press Note No. 3 (2026 Series) DPIIT F. No. P-15015/9/2025-FDI Policy dated 23 July 2026

KPMG in India addresses:

Ahmedabad
Commerce House V, 9th Floor, 902,
Near Vodafone House, Corporate
Road, Prahlad Nagar,
Ahmedabad – 380 051.
Tel: +91 79 4040 2200

Bengaluru
Embassy Golf Links Business Park,
Pebble Beach, 13/02,
'B' Block, 1st & 2nd Floor,
Off Intermediate Ring Road,
Bengaluru – 560 071.
Tel: +91 80 6833 5000

Chandigarh
Elante Offices,
Unit No. A505, 5th Floor, Plot No.178-178A,
Industrial Area Phase-1,
Chandigarh – 160 002.
Tel: +91 172 664 4000

Chennai
KRM Towers, Ground,
1st, 2nd, & 3rd Floor, No. 1,
Harrington Road, Chetpet,
Chennai – 600 031.
Tel: +91 44 3914 5000

Gurugram
Building No.10, 8th Floor,
DLF Cyber City, Phase II,
Gurugram,
Haryana – 122 002.
Tel: +91 124 307 4000

Hyderabad
Salarpuria Knowledge City, Orwell
6th Floor, Unit-3, Survey No 83/1,
Plot No 2, Raidurg, Hyderabad –
500 081.
Tel: +91 40 6111 6000

Jaipur
Signature Towers, Office No. 402,
Fourth Floor,
S Plot No. DC-II, Lal Kothi District
Shopping Center, Tonk Road,
Jaipur – 302 001.
Tel: +91 141 – 672 1000

Kochi
Syama Business Centre, 49/179, 3rd Floor,
NH 47, Bypass Road, Vytilla,
Kochi – 682 019.
Tel: +91 484 302 5600

Kolkata
Unit No. 604,
6th Floor, Tower – 1, Godrej
Waterside, Sector – V, Salt Lake,
Kolkata – 700 091.
Tel: +91 33 4403 4000

Mumbai
Lodha Excelus, Apollo Mills
Compound, 2nd Floor,
N M Joshi Marg, Lower Parel,
Mumbai- 400 011.
Tel: +91 22 3989 6000

Noida
Unit No. 501, 5th Floor,
Advant Navis Business Park, Tower-A, Plot# 7,
Sector 142, Expressway Noida,
Gautam Budh Nagar,
Noida – 201 305.
Tel: +91 0120 386 8000

Pune
9th floor, Business Plaza,
Westin Hotel Campus, 36/3-B,
Koregaon Park Annex, Mundhwa
Road, Ghorpadi,
Pune – 411 001.
Tel: +91 20 6747 7000

Vadodara
Ocean Building, 303, 3rd Floor,
Beside Center Square Mall,
Opp. Vadodara Central Mall, Dr. Vikram
Sarabhai Marg, Vadodara – 390 023.
Tel: +91 265 619 4200

Vijayawada
PR heights, 4th Floor,
NH 16 Service Rd, Opp. Manipal
Hospital Road, Tadepalle,
Andhra Pradesh – 522 501.
Tel: +91 0864 536 2000

kpmg.com/in

Follow us on:
kpmg.com/in/socialmedia