

HC sets aside tax demand of Rs 3,200 crore on Vodafone India

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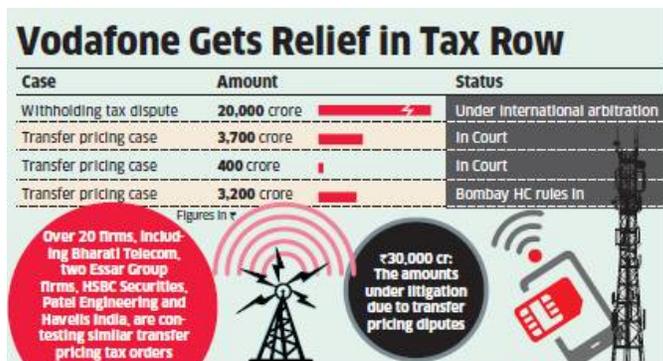
MUMBAI: The [Bombay High Court](#) on Friday set aside a tax demand of Rs 3,200 crore on [Vodafone India](#) handing India's secondlargest telecom operator by number of subscribers a victory, at least for now, in one of its various disputes with Indian tax authorities.

The taxman has accused Vodafone India of violating transfer pricing regulations by under-pricing shares it had issued to its parent, Vodafone Plc, in a rights issue. The alleged under-pricing meant [Vodafone Plc](#) paid less to get a higher stake in Vodafone India, entitling the authority to collect more tax.

"Vodafone has maintained consistently throughout the legal proceedings that this transaction was not taxable," Vodafone said in a statement. This episode and a similar tax demand on [Shell India](#) had caused consternation among foreign investors as this was the first time transfer pricing rules had been applied in this manner. Lawyers dealing with these tax cases said this order may mean that similar tax demands may also be set aside.

Transfer price refers to the actual price at which a transaction takes place between two related parties, usually belonging to the same group. According to law, all cross-border deals between group companies need to be at arms length, that is, as if it was with an unrelated company.

Shreya Rao of Nishith Desai Associates, a law firm that specialises in tax consulting, said that the case had created confusion, because the tax department took the view that share subscription was taxable either if the value was too high or too low.



The judgement, however, explains that since income by way of share premium is not taxable, a shortfall in premium cannot be either, said Anuradha Dutt, counsel for Vodafone. "I hope the decision will not be challenged (in Supreme Court) because this is an opportunity for the government to show the investors that it is not upholding what is called tax terrorism." Premium refers to the difference between the par value of a share, usually Rs 10, and its actual value.

Government lawyers were unavailable for comment on whether they will challenge the judgement or not. ET Now reported, citing finance ministry sources, that the government was considering appealing to the [Supreme Court](#).

In the case of Vodafone India, the tax authorities disputed the valuation at which the Indian subsidiary had issued shares to its UK-based parent. While Vodafone used a method approved by RBI, the tax department used a methodology called discounted tax flow to arrive at a higher value per share.

It then went on to characterise this difference as additional income accruing to Vodafone India and sought to tax it. Vodafone's lawyers, led by Harish Salve, argued that the extra income did not exist and could not be taxed. Further, inflows by way of capital infusion had never been taxed, Vodafone's lawyers contended.

Vodafone's long-standing Rs 20,000-crore withholding tax dispute with the Indian government, which has hurt the country's image as an investment destination, is currently under international arbitration.

The company is also fighting two separate transfer pricing cases in the same court. Shell India Markets, which is facing aRs 10,000-crore

tax demand, and Leighton India Contractors companies have also approached the court against orders of the income-tax department. All the cases have been bunched together. An order in the case of Shell India may be pronounced on Monday.

Rakesh Nangia, a chartered accountant who runs a firm by the same name, said this still leaves a large number of cases involving Indian companies, where third party purchasers have bought shares, in limbo.

While the fine print of the judgement will be examined over the next few days, Nangia said the ruling holds for parent companies buying into their Indian arms. But the question is, will it also apply to third party share purchases?

Rao of Nishith Desai said, "Once the HC has given a verdict, although it is not binding, other high courts will look to it for the reasoning in similar cases."

Tax experts said over 20 firms, including [Bharati Telecom](#), two [Essar Group](#) firms, [HSBC Securities](#), Patel Engineering and [Havells India](#), are contesting similar transfer pricing tax orders. The amounts at stake exceed Rs 30,000 crore.