Delhi HC upheld reassessment as Samsung failed to disclose royalty income

Summary – The High Court of Delhi in a recent case of Samsung Electronics Co. Ltd., (the Assessee) held that where pursuant to issuance of re-assessment notice, assessee itself accepted that original return filed by it was incorrect for reason that assessee had failed to disclose income earned by way of royalty and fee for technical service and, accordingly, declared additional income, impugned reassessment was justified

Facts

- A survey was conducted in the premises of the Indian subsidiary, SIEL of the assessee foreign company, SECL(SK). During the course of survey, it was found that SIEL was in the business of manufacturing and trading of consumer electronics. These items were manufactured under the technical assistance of the present (sic. parent) company for which the parent company received fees for technical services. The parent company SECL(SK) was not paid any royalty for use of its brand name 'SAMSUNG' by the subsidiary company. Thus, income of assessee foreign company in the form of royalty had escaped assessment. Further, during post survey proceedings, statements of JSS President & CEO of the Indian company was recorded. It was observed that he was also head of South West Asia operations of the parent company. Thus, he was representing not only SIEL but also SECL(SK) in his capacity as South West Asia head. A close analysis of these statements further revealed that the Indian company's office was being used as place of management for South Asia operations by SECL(SK), therefore, the Indian company would constitute Permanent Establishment of the assessee parent company under article 5(2)(a) of the DTAA and a part of income from sales in South Asian countries should be attributed to SECL(SK). A perusal of records showed that the assessee had not filed its return of income in India for assessment year 2008-09.
- In view of the above, income chargeable to tax had escaped assessment by reason of failure on the part of the assessee to disclose fully & truly all material facts necessary for its assessment. Thus, a reopening notice was issued against the assessee.
- On appeal, the Tribunal observed that the manufacturing royalty/FTS received by the assessee from the Indian subsidiary as reflected in the tax returns filed by the SIEL was not reported by the assessee, and it was only in the returns filed in response to the notices issued under section 148, such an income was reported. The assessee admitted the fact that it did not declare this income in the original return of income. Thus, reassessment was justified.
- On appeal to the High Court :

Held

- The appellant accepts that the "reasons to believe" correctly record that a survey was conducted in the premises of the Indian subsidiary of the appellant company in June, 2010. The appellant also accepts that the Indian subsidiary had manufactured consumer products like washing machines,

refrigerators, air-conditioners, televisions, mobile phones etc. under technical assistance from the appellant and on which fee for technical services was payable. Use of the brand name "Samsung" by the Indian subsidiary in trading and sales on which royalty was payable to the appellant is not denied. The Indian subsidiary had substantial turnover of more than Rs.9,000 crores and royalty payable at the rate of 2 per cent of sales would approximately be Rs.180 crores. Turnover as recorded is not disputed and challenged. Another aspect recorded in the "reasons to believe" had emerged from the statements of officers of the Indian subsidiary recorded during the survey operations and inquiries made thereafter. The statements had revealed that the Indian subsidiary had also covered operations in Bangladesh, Sri Lanka, Nepal, Bhutan and Maldives for which no extra or additional payment was made. "Facts" as then ascertained and known were highlighted in the reasons and grounds to hold that the appellant had permanent establishment in India.

- It was submitted that the "reasons to believe" had erroneously recorded that the appellant had failed to file their return of income, whereas the returns had been duly filed. At the same time, it is accepted that the returns were filed by the branch office of the appellant under the name of 'SECL - India Software Operations'. The returns had included income earned by the branch office from the software operations, as is accepted in the grounds of appeal. Income earned by the appellant from the Indian subsidiary by way of fee for technical services and royalty was not disclosed and included in these returns. Thus, the returns were in a name with prefix "India Software Operations" and were in respect of taxable income earned by the branch office in the said operations as a distinct and separate assessee. Pertinently, the appellant-assessee in response to the notices under section 147/148 had filed returns of income for the assessment years *i.e.* 2004-05 to 2006-07, 2008-09 and 2009-10 including and accounting for fee from technical services and royalty received from the Indian subsidiary. This income though earned and taxable in India, had not been disclosed and accounted for in the returns filed by the branch office in relation to their operations and earnings. Thus, even if it is assumed that the returns filed by the branch office at Bangalore were returns filed by the appellant, the appellant had disclosed new and additional source of income and also the income earned from the said sources in the returns filed in response to notice under section 147 read with section 148. This was true for assessment years from 2004-05 to 2006-07, 2008-09 and 2009-10.
- Aspect and question of permanent establishment and attribution of income to the permanent establishment were issues examined by the Assessing Officer and adverse findings against the assessee were recorded. No doubt, the said findings have been overturned by the Tribunal, but when one examines the question of initiation of re-assessment proceedings under section 147/148 in the present case, one would hold that the appellant has accepted that the "original returns" filed by "them" were incorrect for they had failed to disclose income earned by way of royalty and fee for technical service. This is material and relevant.
- The appellant themselves, pursuant to notice for re-assessment, had declared additional income and accepted their failure to disclose earned income by way of royalty and fee for technical services.

- The contention that "Tax at Source" had been deducted on royalty and fee for technical services would not matter, as the returns filed were wrong and required a correction and modification. Failure to disclose fully and truly all material facts, without debate is correct and established. Deduction of tax at source would not matter, as "the return of income" by "the branch office" was not filed in terms of the provisions of the Act to include income of the appellant and, therefore, the revenue did not have any opportunity to examine and consider the taxable income of the appellant. Deduction of tax at source and failure to disclose taxable income are different and distinct aspects. Escapement and short levy of tax has to be objectively and reasonably estimated by the Assessing Officer at the stage of recording of reasons. This was done and objectively ascertained as is clear from the "reasons to believe" recorded which refer to the turnover and sales of the Indian subsidiary. At the stage of issue of notice/recording of reasons the only question is whether there was relevant material on which a reasonable person could have formed a requisite belief conclusive proof and finding on escapement is neither mandated nor required.
- For reasons recorded stated by the Tribunal are agreed with. Accordingly, there is no any merit in the present appeals and the same are dismissed.