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Direct Tax Alert

November 11, 2021

Mumbai Tribunal rules on scope of Black Money Act in respect of undisclosed foreign bank accounts held in the past

The Income Tax Appellate Tribunal, Mumbai bench ('ITAT') in case of resident individuals[1], has ruled on the scope of the Black Money Act[2] ('BMA'). The ITAT held that undisclosed foreign bank accounts (which existed prior to the enactment of the law) are covered under the purview of BMA and any unexplained credits in such bank accounts would be taxable as undisclosed foreign income.

I. Background of the case

- The assessee, RMB and his wife, ARB, were directors and shareholders in a company incorporated in the British Virgin Islands ('BVI'). This information was not disclosed in the Return of Income ('ROI') filed in India.
- The Investigation-wing of the Income Tax department learnt of information regarding two accounts held in UBS Bank, Singapore branch by the BVI company. Upon further probe, it was learnt that RMB and ARB were the beneficiaries and operators of such accounts which reflected gross credit entries of INR 999.74 crores over a period of time (which also included intra-bank and contra entries).
- The KYC documents related to these bank accounts revealed that passport copies of RMB and ARB were submitted along with hand-written instructions for operating the bank accounts. One of these bank accounts was closed in 2008 and the other in 2011.
- The series of events are briefly given below:

[1] BMA Nos. 02 and 04/Mum/2021 and BMA Nos. 03 and 05/Mum/2021

[2] The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015

Year	Particulars
2013 and 2014	Summons sent by the Investigation-wing of the Income Tax Department. Details of foreign assets, beneficial ownership, etc. were sought from the assessee
2016	Search operations carried out at the premises of the assessee
2017	BMA proceedings initiated by the Assessing Officer ('AO')

- At all the above stages, the assessee denied having any knowledge of these foreign bank accounts.
- On 28 March 2019 (i.e. 3 days before the due date for completion of BMA proceedings), RMB admitted that these accounts were opened in his and his wife's name by his late father by taking their signatures on papers in the past. He submitted that the credit entries in the accounts were loans taken from UBS Bank which were repaid with interest.
- The AO rejected various explanations offered by the assessee and held that the assessee is the beneficial owner of the undisclosed foreign bank accounts. After analysing entries in such bank accounts and considering the explanations offered by the assessee, the AO treated certain unexplained credit entries as "undisclosed foreign income" and computed the total income from these two bank accounts at USD 8.33 million (~INR 56 crores).
- On appeal, the Commissioner (Appeals) ['CIT(A)'] gave partial relief of USD 3.21 million on account of credits in respect of redemption of investments held earlier.
- Thereafter, cross-appeals were filed before the ITAT by the assessee and the AO.

II. ITAT ruling

- Post considering the provisions of the BMA and intent of the legislature, the ITAT reversed the partial relief granted by the CIT(A) to the assessee and upheld the order of the AO completely.

Key principles emerging from the ITAT ruling

(i) Applicability of BMA to undisclosed assets held and income earned prior to the enactment of law (i.e. 1 July 2015)

- The two foreign bank accounts were closed in 2008 and 2011. The assessee contended that an asset which did not exist at the time when the BMA came into force cannot be assessed under the said Act.
- The ITAT held that the BMA[3] specifically provides that an undisclosed asset located outside India shall be charged to tax in the year in which it comes to the notice of the AO.

  The ITAT referred to the decision of the Supreme Court[4] and held that it is immaterial whether the asset existed at the point of taxation or even at the time when provisions of BMA came into existence. The only relevant date for levying tax is when the undisclosed asset comes to the notice of the AO.
- The assessee further argued that BMA cannot be invoked in respect of a foreign asset which was already in the knowledge of the Revenue authorities (i.e. Investigation-wing of the Income Tax department) when the said Act came into force.

  The assessee even relied on the CBDT Circular[5] which prohibited assessees from

[3] Section 3(1) of BMA

[4] UOI v. Gautam Khaitan [2020] 420 ITR 140 (SC)

[5] CBDT Circular no. 13 of 2015

making a one-time voluntary declaration of foreign assets in respect of which Government has prior information on the specified date.

The ITAT held that reliance on the said Circular is to be confined to the compliance window for voluntary declaration under BMA and the same should not apply for making assessments under BMA.

- Regarding undisclosed foreign income, the ITAT held that what is relevant for levying tax is that either such foreign income is not disclosed in the ROI filed or that the ROI is not filed at all by the assessee in India.

- ITAT further rejected the reliance placed by the assessee on the decision of the Supreme Court[6] to contend that the words "***is*** a beneficial owner" in section 2(11)[7] of BMA although normally refers to the "present", often has a "future" meaning. The ITAT noted that the decision does not support the assessee since in the same decision, the Supreme Court has also observed that the word "is" may also have a "past" significance.

(ii) Bank account is an asset under BMA

- The assessee contended that an undisclosed foreign bank account is not an asset under section 2(11) of BMA.
- The assessee argued that though Black Money Rules[8] provides for valuation of undisclosed bank accounts, section 2(11) of BMA does not cover a foreign bank account which does not exist. Therefore, the Rules must be struck down as they go beyond the scope of BMA.
- It was also contended that since section 2(11) of the BMA refers only to such assets having a "cost of acquisition" (i.e. source of investment), a bank account cannot be treated as an undisclosed foreign asset.
- The ITAT rejected the above arguments and held that the amount receivable from bank in respect of a bank account is certainly an asset of the person holding that account.

  It held that a bank account is an asset which gives ownership of the credit balance in that account.

  If the owner of a bank account can substantiate the source of investment which is duly disclosed to Revenue authorities, to that extent, the source of investment is explained, and the requirements of section 2(11) can be satisfied even in respect of a bank account.
- The valuation mechanism provided in Rule 3(1)(e) of the Black Money Rules in respect of a bank account confirms the intent of legislature to include bank accounts within the scope of undisclosed foreign assets.
- The assessee tried to explain that the credit entries in the bank accounts were loans given by the bank itself. The ITAT noted that the assessee had no explanation as to why any bank would commercially give loans without any collateral security or margin money. It is further observed that the assessee could not produce any documentary evidence to substantiate his explanation.
- After considering the above, the Hon'ble ITAT upheld the position taken by the AO in respect of unexplained credit entries in the two bank accounts and held the same to be undisclosed foreign income.

[6] FS Gandhi Vs CWT (1990) 184 ITR 34 (SC)

[7] Section 2(11) of BMA provides that an undisclosed asset located outside India means an asset (including financial interest in any entity) located outside India, held by the assessee in his name or in respect of which he is a beneficial owner, and he has no explanation about the source of investment in such asset or the explanation given by him is in the opinion of the Assessing Officer unsatisfactory

[8] The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Rules, 2015

(iii) No deduction to be allowed while computing undisclosed foreign income/asset

- The ITAT referred to section 5(1)(i) of the BMA which provides that in computing undisclosed foreign income and asset, no deduction in respect of any expenditure/allowance/set-off shall be allowed.
- Therefore, the ITAT rejected the contention of the assessee that debit entries in the bank accounts reflecting expenditure, i.e. receipts net of expenses incurred, must be considered while framing the assessment.

(iv) Beneficial owner of an asset

- The assessee contended that section 2(11) of BMA defines an undisclosed asset as one in which the assessee is a "beneficial owner". Since this term is not defined under the BMA, it must derive its meaning from section 139(1) of the Income-tax Act, 1961[9]. Therefore, unless it is proven that the assessee has directly/indirectly provided consideration for such asset, he cannot be held to be the beneficial owner thereof.
- The Hon'ble ITAT held that merely since the expression "beneficial owner" is defined under the Income-tax Act, 1961, it cannot automatically apply to the BMA as well.

  The context of the definition under the two Acts must meet to invoke the meaning for the purpose of BMA.
- The Mumbai ITAT noted that a similar view has been taken by the Delhi ITAT[10], although by adopting a different reasoning.
- Based thereon, the ITAT rejected the above arguments and held the assessee to be the beneficial owner of the foreign bank accounts under the BMA.

Dhruva Comments

This ITAT ruling is important in the context of BMA since many of the above discussed aspects have been adjudicated at the Tribunal level for the first time.

The ruling has affirmed that BMA will apply to undisclosed assets held even prior to the introduction of BMA if the source of investment in such assets remains unexplained.

The "peak credit theory" often cited by assessees under Income-tax law to contend that only the highest credit balance ought to be taxable as unexplained credit, may not find acceptance under BMA given the express provisions regarding non-deduction of expenditure.

The BMA provides that an undisclosed foreign asset shall be taxable in the year in which it comes to the notice of the AO while there is no such specific provision in respect of undisclosed foreign income. The ITAT has held that unexplained credits in bank account are taxable as undisclosed foreign income. This aspect could be subject to dispute at higher forums as to whether undisclosed foreign income pertaining to past years can be taxed under BMA in a subsequent year.

Further, since Article 20 of the Constitution of India provides that a person cannot be convicted of an offence under a law which did not exist when such offence was committed, there could be dispute on the constitutional validity of the aforesaid provisions under BMA.

[9] Explanation 4 to section 139(1) provides that a "beneficial owner" in respect of an asset is someone who has directly/ indirectly provided for consideration for the asset.

[10] ACIT v. Jitendra Mehra (BMA No. 1/Del/2020)

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