THE CHAMBER OF TAX CONSULTANTS

Estd. 1926
ज्ञानं परमं बलम्

Celebrating 50 YEARS OF
THE CHAMBER'S JOURNAL
1975-2025

The Chamber's Journal

YOUR MONTHLY COMPANION ON TAX & ALLIED SUBJECTS

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Special Feature on
Trends in
International Tax Interpretation

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THE CHAMBER OF TAX CONSULTANTS

The Chamber of Tax Consultants

cordially invites you for

Invitation

Celebrating

50 YEARS OF

THE CHAMBER'S JOURNAL

1975-2025

on Friday, 25 April 2025 **from** 5:30 pm to 8:00 pm
at 4th Floor, Walchand Hirachand Hall, IMC, Churchgate, Mumbai

Special Guest

Mr Dakshesh Parikh

Executive Editor, Business India Group



Vijay Bhatt, President
Anish Thacker, Editor
Ameya Kunte, Chairman, Journal Committee

The event will begin with high tea at 5:30 pm.

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3, Rewa Chambers, Ground Floor, 31, New Marine Lines, Mumbai-400 020
Phone : 2200 1787 / 2209 0423 / 2200 2455
E-Mail: office@ctconline.org
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Guest Editorial

Vipul B. Joshi, Advocate

With immense honour and humility, I pen this Guest Editorial to commemorate the 50th anniversary of The Chamber's Journal - a brainchild of Shri. B. C. Joshi, a great visionary much ahead of his time, who set in motion this journey and chartered its course. It was during his presidency of the Chamber in 1975 – the year of the CTC's rebirth and revival – that the mouthpiece of the Chamber was launched, with him penning the first editorial. A brief history of the Journal is narrated in this issue, which depicts the stalwarts of the profession, Shri. Sanat P. Mehta, Shri Y. P. Trivedi, Shri Dinesh Vyas, and Shri V. H. Patil, joining this journey as part of its Editorial Board and blessing this historic venture. Blessings were also showered by the Governor of Maharashtra, the Finance Minister of India, Supreme Court Judges, the Commissioner of Income Tax, Bombay, and, above all, none other than Shri Nani A. Palkhivala. What can be a more momentous beginning?

As we celebrate the 50th anniversary of our Journal, we reflect on its remarkable journey - a journey of growth, adaptation, and constant evolution in tandem with the dynamic world of taxation.

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THE SEED

Fifty years ago, in August 1975, a seed was sown with a very simple but resolute vision: "*to provide for a vehicle of thoughts, which ultimately may turn out to be an exchange of thoughts between practitioners, the taxpayers, and the tax officials to the ultimate benefit of all.*" The seed, over the years, got transformed into a strong large banyan tree, withering storms to give shed to varied opinions, thoughts, and discussions that were allowed to nurture and grow freely without fear or favour. It is a matter of immense satisfaction that the Journal has grown the way the founders had desired and navigated the set course, even in rough waters.

THE JOURNEY

As we look back on this journey spanning five decades, it is indeed remarkable to witness how far we have come. Over the past five decades, the tax landscape has undergone tremendous shifts - a landscape that cannot remain immune to, but in fact reflects, the changes in the economic, social, and political landscapes, locally and globally. From the stagnant and tightly controlled pre-liberalisation economy of the sixties, we are now in the era of a free market and global digital economy with its own unique and varied complexities. Such transition, in turn, has impacted the evolution of tax laws and tax jurisprudence. Being witness to this period of transition, the Journal not only chronicled such developments but also evolved and widened its coverage.

Consequently, from the debates amongst tax professionals during the nascent evolutionary years of direct tax laws of the sixties that focussed on the foundational aspects of taxation and centered around topics like unaccounted income, penalties et al., to the present-day debates cantering around topics

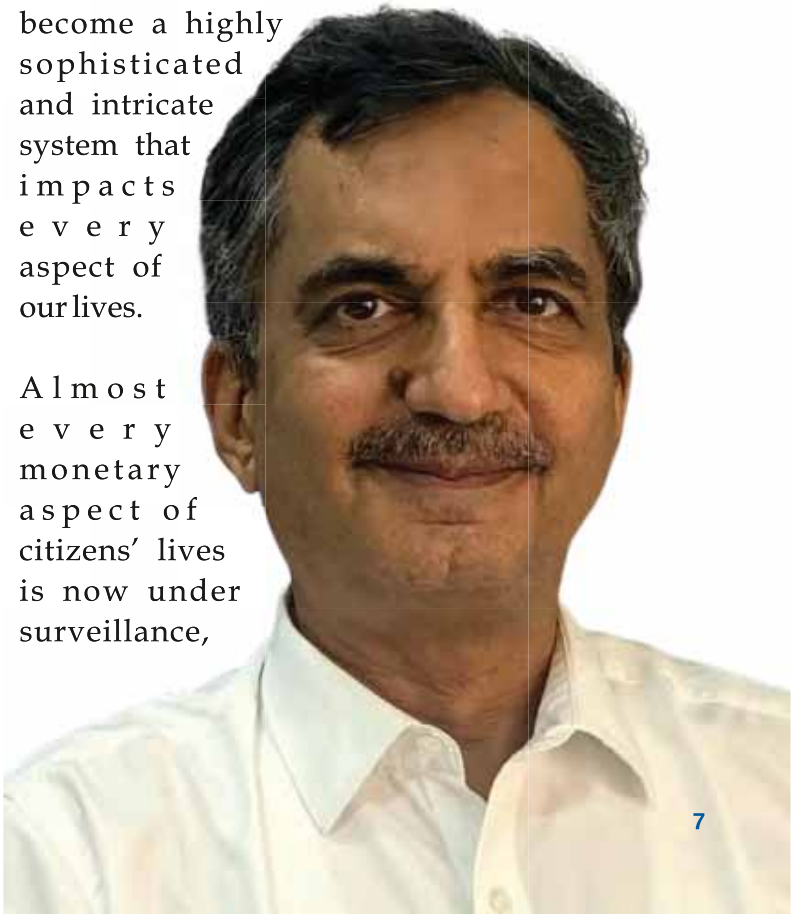
like digital assets and digital taxes, crypto tax, cross - border taxation regimes, etc. - the Journal has captured these transformations covering a wide range of topics, adapting to the tax system getting matured and digitized over the time. Today, the Journal covers not only intricate direct tax and international tax developments but also captures indirect tax, apart from varied allied laws like corporate law, foreign exchange laws, accounting and auditing, securities laws, general law, etc, with innovative features, including its signature feature of Special Stories. Though the issues covered today may be different from those covered 50 years ago, the mission remains unchanged: to provide a platform for advancing understanding of tax laws with thought-provoking articles, insightful analysis, and experts' comments - with contributions from the emerging and best of the established minds in the professions - and shaping the way we understand the intricacies of our tax system.

But beyond the academic discussions, the Journal has maintained a deep sense of purpose and social responsibility. Just as we have always voiced our demand and support for fairness, efficiency, and transparency in tax laws and tax administration, we have been equally vocal about ethical and fair standards of practice by tax professionals. We have also not hesitated to raise grievances and protests against unfairness – within the department or outside. Besides, we have always strived to zealously guard the independence of the judiciary and judicial functioning.

THE CRITICAL PHASE

Today, we are at a critical phase of the transformation of the tax regime – or rather, at a historical phase. After over six decades and a half, the country is on the verge of adopting a new income tax law, ushering in a new era of tax laws and jurisprudence. Even in the field of indirect taxation, though the GST is almost eight years old, it has achieved its stability level just now, overcoming the teething problems. It is now ready for the matured level of deliberations and reforms. At this once-in-a-lifetime opportunity, the need of the hour is to spread awareness and knowledge about the new developments in tax laws and facilitate meaningful discussion and analysis, including constructive criticism and suggestions, to help evolve better tax laws and better tax regimes. Besides, the world of taxation is inherently dynamic, with the constant emergence of new challenges. Adapt & evolve or perish – this is the present-day life mantra.

At the same time, due note must be taken of some tell-tale warning signs as to how the tax laws have been slowly but steadily sneaking into the private lives of citizens. What started as a modest vehicle to merely collect revenue from individuals and businesses has now become a highly sophisticated and intricate system that impacts every aspect of our lives.



Almost every monetary aspect of citizens' lives is now under surveillance,

…the coming years will undoubtedly present even more challenges and test our ability to withstand and tackle them. As we face these challenges, the Journal will remain dynamic and evolved, with a strong and independent voice to be heard by all and mighty.

monitoring, and scrutiny. The line between the right to have privacy & freedom and the overriding right of the State to tax is slowly getting blurred and thinner. This certainly warrants a serious discussion to draw a Lakshman Rekha.

Then, there is this alarming trend of tax laws and tax administration being used ('weaponized'—to borrow the cliché metaphor) for extraneous purposes. This, again, is a perilous trend, having the potential to cross the line of democratic and constitutional values and fall into the arena of autocracy, dictatorship, and anarchy.

This is besides the perennial issue of the tax administration's rigid mindset, which still reeks of inefficiency, insensitivity, corruption, and lack of accountability. Before trying to impose stricter and onerous tax laws in the name of bringing the best of international practices into the country, we should first have the best of international administrations to match and support such practices. Otherwise, the mismatch is sure to bring chaos and confrontations. The digitization of tax administration evolving into quasi-judicial functions like faceless assessment and faceless appeal is one such example. Though the intent and the efforts are indeed laudable, the implementation at the ground level leaves much to be desired and betrays the trust of the policy-makers and the taxpayers.

At the international level, the recent disturbing developments of the rise of far-right nationalist sentiments and ignited economic nationalism resulting in aggressive protectionist measures are real threats that loom large over the world. It is feared that this (trade) war threatens to bring a recession reminiscent of the Great Depression of the 1930s. Apart from the severe impact on the national and international economy, this is going to throw serious challenges to the tax laws and tax policies of the countries worldwide. India is no longer insulated.

THE ROAD AHEAD

On the road ahead, the coming years will undoubtedly present even more challenges and test our ability to withstand and tackle them. As we face these challenges, the Journal will remain dynamic and evolved, with a strong and independent voice to be heard by all and mighty.

This golden anniversary is not just a moment of reflection on the Journal's journey and achievements but also a time of introspection, correction, and improvement. This is also the time to renew our commitment in these crucial and transformative times – the commitment to disburse knowledge with qualitative content, to provide a platform for facilitating healthy debates and discussions, to play a concrete role in shaping a fair and impartial tax regime, and to promote best practices. For, this is not only the aspiration of the hapless taxpayers but is also the mandate left by the founders, who discharged this role without fear or favour, with dignity and grace!

ACKNOWLEDGMENTS
Needless to say, such a long and fulfilling journey would not have been possible without the selfless support of the editors, the members of the Editorial Board, the contributors, and the entire team, who worked tirelessly with dedication. As we cross this milestone, we sincerely thank all of them. Above all, we humbly acknowledge the faith the readers have continued to place in the Journal, which has made the Journal such an influential publication and made this milestone possible.

We look forward to a fascinating and fulfilling journey with you all in this next phase of the Journal's journey! As part of the 50th anniversary year of the journal, we have decided to publish six special issues starting in July. All six issues focus on the fundamental aspects of taxation and are well-designed by senior professionals. These core aspects have somehow been neglected and overlooked over the years in this frenzy of churning out artificial and deeming provisions and the onslaught of judgments that bombard our smartphones every day - nay, almost every hour! We have distanced ourselves from the finer aspects of basic taxation principles and have travelled far away. The new generation perhaps is not even aware that such core principles existed, and still exist, and that they are not merely mirages or theoretical sermons that have no practical application, having simply an ornamental value. They are, in fact, the guiding lampposts that illuminate our understanding of basic taxation philosophy and show the right path.

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The new generation perhaps is not even aware that such core principles existed, and still exist, and that they are not merely mirages or theoretical sermons...

This month's special story issue focuses on an important fundamental aspect of international taxation – **'Trends in International Tax Interpretation'.** A cross-border taxation system carries the inherent feature of conflicting interests between the two states involved, each having its own unique understanding of the principles of interpretation, based also on the understanding adopted by its judiciary – notwithstanding the guiding principles contained in Conventions and Commentaries. Then, even within a country, the judiciary has to navigate such intricate issues by balancing the competing—often diagonally opposite and sometimes contradictory—stand adopted by the two sides. Coupled with the fact that the ordinary rules of interpretation do not necessarily apply while interpreting tax treaties, this aspect poses unique challenges.

In the era of rising cross-border conflicts on trade and taxation fronts, the Special Story is very timely. Senior experts in the field have meticulously planned this Special Story, giving insight into the intricate issues involved in the topic and explaining the latest developments on this aspect. We are sure this will provide a good understanding and clarity on this crucial aspect of international taxation.

Vipul Joshi
Advocate
Guest Editor

From the President

CA Vijay Bhatt

Dear Members,

It is with great pride that we mark a significant milestone – 50 Glorious Years of our Chamber's Journal since its first issue in April 1975.

I extend my heartfelt gratitude and congratulations to all who have contributed to this remarkable journey of Half Century, including all the Past Presidents, Managing Council Members, Editors, Editorial Board Members, Assistant Editors, Chairmen and members of the Journal Committee, Authors, CTC Staff and Esteemed Journal Subscribers. Your dedication and support have been instrumental in shaping the Journal.

A special appreciation is due to our publishers, M/s. Finesse Graphics & Prints Pvt. Ltd. led by CA Rajesh Bhagat, for their long-standing partnership with the Chamber, spanning over 35 years.

To celebrate this landmark occasion, the Chamber has organized an event on April 25, 2025, details of which are also included in this journal.

March was a vibrant month, filled with various festivals and academic activities. I extend my warmest greetings to all members for Holi, Gudi Padva, Ramzan Eid, and Baisakhi followed by Shri Ram Navmi.

On the one hand, the world witnessed massive earthquakes in some parts and on the other, the upheaval caused in the markets partly due to the new Tariff Policy of the USA, has rocked all of us. It is feared that the Global Economy is staring at slower economic growth, disrupted supply chains and heightened inflation. The extent of the impact can only be ascertained with the passage of time, but it appears that India may not be as badly hit as some of the other countries. Be that as it may, the geo political situation is fragile and one will have to continuously keep a watch on the developments that happen, to be able to take appropriate action to the extent possible.

The RRC Committee successfully hosted the 48th Direct Tax RRC in Raipur, Chhattisgarh, with a record-breaking 351 delegates. I commend all the faculty members for sharing their expertise and making our delegates enriched with knowledge. The RRC witnessed a few exciting moments. Firstly, the delegates travelling from Mumbai to Raipur in the early morning Indigo flight were enthralled by the flight announcement welcoming and greeting the undersigned and all the delegates of 48th RRC on board. It was a matter of joy & pride for all the delegates that our Chamber's name was pronounced in the Sky. My thanks to Indigo airline. A special session of Panel Discussion was held for delegates aged under 40 years. One unique feature of the RRC that emerged was visit by Swami Shri Gyanvatsal-ji of Swaminarayan Mandir and his interesting address to our delegates. He also encouraged our delegates for interaction with him. I express my sincere gratitude to Past President CA Hinesh Doshi for organizing his visit within less than one day. For the first time in the history of Chamber, a special group photo of the delegates was captured by the Drone Camera, which will be released in due course of time. The delegates enjoyed over fellowship during popular Antakshari hosted by CA Bhavesh Joshi & CA Ishan Shah. I congratulate Chairman CA Ankit Sanghvi and his team for their exceptional experiments and efforts for the successful RRC.

The Chamber has organized a Full day seminar in hybrid mode on 17th April, 2025 on "TDS &

TCS Provisions – a 360° Perspective" jointly with IMC and BCAS at IMC, Mumbai, which will be addressed by esteemed Tax Officials. I encourage members to attend this interesting seminar in large numbers.

The International Taxation Committee organized a workshop on "Wealth & Succession Planning and Estate" Taxation in physical mode, which was attended by about 180 participants. The workshop was addressed by eminent faculty members on the subject. My congratulations to CA Karishma Phaterphekar and her team for organizing this physical event meticulously. The Committee has also organized 18th RRC on International Taxation at Goa from 12th to 15th June, 2025. I encourage members to enroll for this RRC at the earliest.

The Membership & Public Relations Committee organized Self Awareness Series on 19th March,2025 virtually on the topic "Etiquette and Climbing the Corporate Ladder" by Advocate Shri Deepak Tralshawala, which was very well attended by the members. On 29th March, 2025 after a gap of about 5 years, the committee organized a Musical Evening of togetherness and fellowship for its members "Basera Yehin Hai", wherein CTC Members presented their singing talent. For the first time in the history of the Chamber, the staff members of the Chamber also presented their singing skills. I thank all the members for their active participation. I also thank organizing team of CA. Bhavesh Joshi, Ms.Varsha Galvankar & CA Suresh Subramanian, who designed the program under the able guidance of advisor Shri Kishor Vanjara.

I congratulate the Chairman CA Premal Gandhi and his team for organizing these events.

The Student committee has organized 14th Dassur Essay Competition. I urge the members to encourage their students to participate in this competition of skill for their benefit.

Last month, the Law & Representation Committee has made representations to RBI, GST Council, SEBI & CBDT for various matters affecting stakeholders, the details of which are available on the CTC Website.

This month's Journal features a special story on 'Trends in International Tax Interpretation'. I thank CA Ameya Kunte and his team for selecting this unique topic. I thank the team involving CA Toral Shah & CA Jiger Saiya for their support. On the occasion of Women's Day celebrated last month, all the authors of the special features are experienced women professionals across India.

Before I conclude I wish you all a very Happy New Financial Year 2025-26, which will also mark the Centenary Year of the Chamber beginning on 4th July, 2025.

Jai Hind !

CA Vijay Bhatt
President



Special Message from the Journal's Editor

CA Anish M. Thacker

My Brothers and Sisters,

"Every kind of peaceful cooperation among men is primarily based on mutual trust and only secondarily based on institutions such as Courts of Justice and police"

– Albert Einstein

On the momentous occasion of completion of 50 glorious years of "The Chamber's Journal", a tax journal which indeed is one of its kind, I extend my sincere and warm greetings to each one of you.

The history of the journal is nicely chronicled separately in tis issue by Past President, Shri Kishor Vanjara. Suffice it to say that over the years, The Chamber's Journal has now become one of the most prestigious and sought after tax journals in the country and though, on paper, its subscription may not appear to be very substantial, the adulation and respect its begets, is indeed praiseworthy and noteworthy.

The first editorial of this Journal was penned for the April 1975 issue by the Chamber's beloved and deeply respected Past President Late Shri B.C. Joshi, Advocate. In that editorial, Joshi Saheb expressed concern at "the absence of significant unison to understand the kaleidoscopic complications of the Income Tax Act" (so very aptly and beautifully put by him). The situation today is that these kaleidoscopic complications continue to exist and probably have mushroomed. Today, we are seeing an endeavour to 'simplify' the provisions and make them easy to understand by taxpayers at large, but the atmosphere of watchful apprehension is heightened. What is therefore the cause of the existence of these complications, be they real or perceived? In my humble view, it is the lack of robustness of trust between the taxpayer and the tax department. If we have an atmosphere of openness and fairness on both sides, the refrain by Joshi Saheb in his editorial, half a century ago, will probably be addressed.

Apologies, this message is going to be one of celebration and gratitude rather than one of anguished expectation over many years. The milestone of completion of 50 glorious years of the Journal is a result of combined efforts of several individuals and teams. The Editors over five decades, the Editorial Board Members, the Journal Committee members over the years, so aptly led by dynamic Chairpersons, the Presidents, Office Bearers, Managing Council Members, the staff of the Chamber and the printers and publishers and of course, without any doubt, all of you readers, have contributed to the success and eminence of this journal and I take this opportunity to express my deepest gratitude to each and everyone of you for your patronage and support.

I would like to especially thank two special people o this occasion. One is Advocate Vipul Joshi, Past President, Former Editor and the equally illustrious son of Late Shri B. C. Joshi, who very kindly, immediately consented to being guest editor of this month's issue (and it was only benefitting that the torch bearer of Joshi Saheb's legacy, a tax professional

par excellence and a genuine and warm human being, edits this issue); and the other is

CA Rajesh Bhagat of Finesse Graphics & Prints Pvt. Ltd., our printer and creative partner of the Journal for more than three decades. You will notice that look and feel of the Journal has changed from this issue onwards. Thank you both for your immense support to this Journal.

Vipul will no doubt cover this in his editorial, but let me mention that this issue is a tribute to 'Naari Shakti', being the issue where all the articles on the special story have been contributed by women professionals. I thank each of these professionals for helping us uphold our annual tradition of a special women's issue, every year.

Not taking too much of your time, let me bid you goodbye for now. Please continue to patronize, help and support the Chamber and The Chamber's Journal with all your might. Another glorious occasion of the start of the centenary year is just around the corner.

Jai Hind!

CA Anish M. Thacker
Editor

RECOGNISING OUR PAST EDITORS

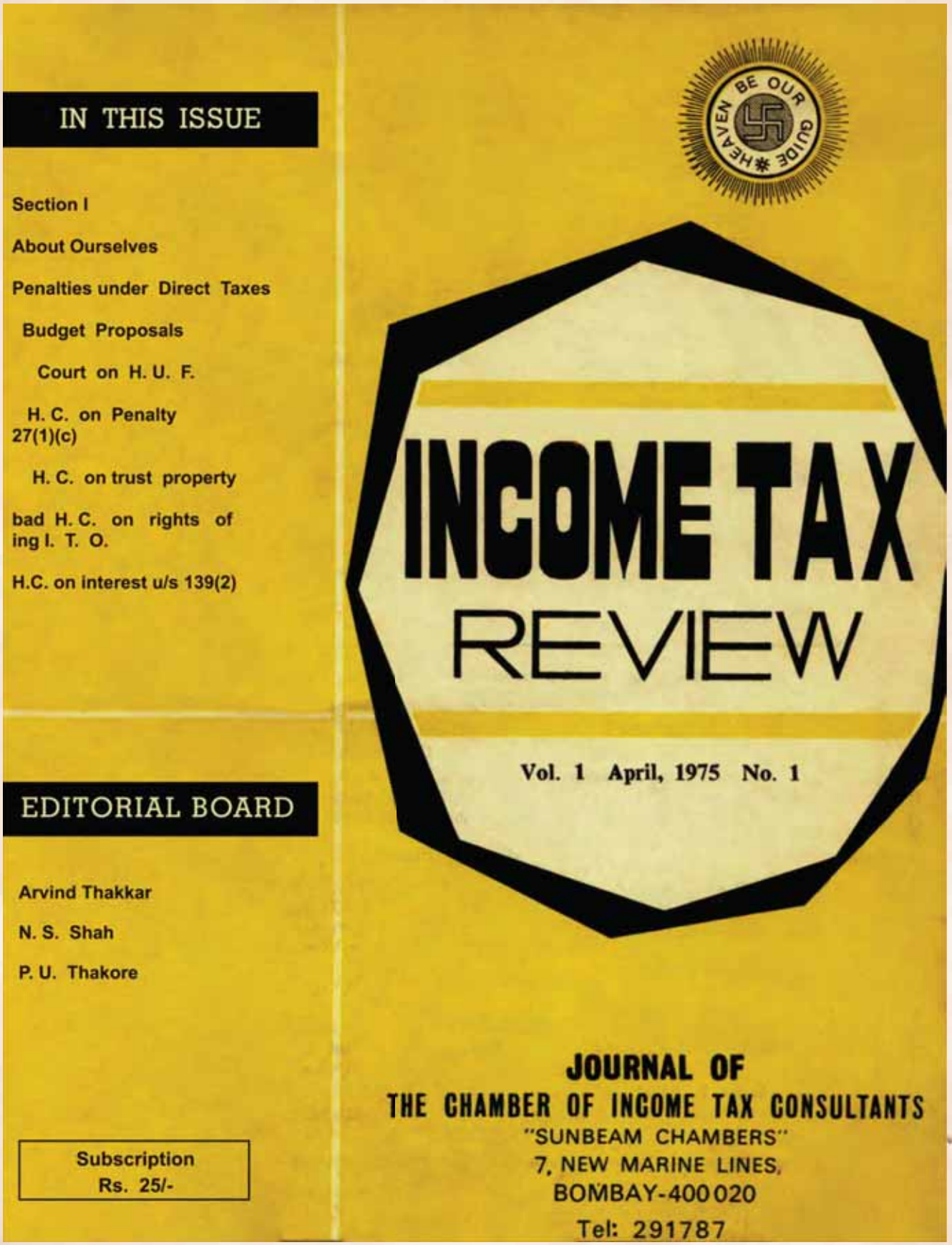
The success of the Chamber's Journal is a testimony of the expertise, experience, equanimity and editorial finesse of our editors, who have over the year, put in their blood, sweat and tears for upholding the quality of this journal. We deeply appreciate their work and thank them for their contribution. They are mentioned in alphabetical order (to the extent records are available) below:

1) Late Shri Arvind Thakkar
2) Late Shri B. C. Joshi, Advocate
3) CA Chetan Karia
4) Late Shri H. K. Sajnani, Advocate
5) Dr. K. Shivaram, Advocate
6) Shri K. Gopal, Advocate
7) Shri K. K. Ramani, Advocate
8) Shri Keshav Bhujle, Advocate
9) Late Shri V. H. Patil, Advocate
10) CA Vipul Choksi
11) Shri Vipul Joshi, Advocate



In Retrospect...

Cover of the First Issue of Income Tax Review



From : Bombay-20, dated 12th March 1975.

Shri O. V. Kuruvilla
The Commissioner of Income Tax, Bombay City I, Bombay.

To.

Shri Balchandra C. Joshi, President,
Chamber of Income Tax Consultants,
Opp. Liberty Cinema, Sunbeam Chambers
7, New Marine Lines, Bombay-400 020.

Sir:

Subject: Publication of "Income Tax Review".

I am very happy to know that the Chamber of Income Tax Consultants, Bombay, is proposing to publish a Journal called "Income Tax Review", to provide a forum for tax payers and tax practitioners for expressing their views in addition to reporting decisions of Courts, Tribunals etc. This is a commendable venture. I am sure such a publication will benefit not only the tax-payers and tax-practitioners, but also the tax-gatherers.

I wish the venture all success.

Yours faithfully,

SD/-
(O. V. Kuruvilla)
Commissioner of Income Tax, Bombay City, Bombay.

Mr. B. C. Joshi,
President
The Chamber of Income Tax Consulants
Bombay.

19th March, 1975.

I have pleasure in sending to the Chamber of Income Tax Constultants a message of good wishes on the publication of their journal, "Income-Tax Review". The journal has set itself a most onerous task — to elucidate the complex laws of the country in order to help both the taxpayer and the tax administrator. I wish the journal all success in achieving this laudable objective.

SD/-
N. A. PALKHIVALA



B. C. JOSHI — Advocate

Even though Income Tax has held the field for last over fifty years and even though the major part of Income-tax is being paid by the erstwhile State of Bombay and now Maharashtra and particularly the citizens of Bombay, there is no significant unison in the effort to understand the kaleidoscopic complications of the Income-tax Act. Periodic efforts by practitioners and conferences by groups do not serve the purpose of a concerted attempt to understand the Income-tax and allied laws and to represent against some of the invidious features in an organised way. Within the last over 50 years, the Income-tax laws have given birth to number of children; to mention a few mischievous children the Expenditure tax, the Estate Duty Act, Wealth Tax Act and the Gift tax. The proliferation is much more complicated with host of allied and subsidiary legislations of Rules and Notifications. While tackling the problems of understanding the law or application of law to a given problem requires expertise and experience which has been the preserve of only a few so far, it is in the interest of the tax-practitioners, tax-payers and the tax-masters alike that these laws should be understood by every tax payer. It is equally important that some of the weak spots are highlighted, some ugly growth here and there recommended to be amputed and, wherever necessary, reform is made in the law not only with a view to deliver to the State the maximum tax with minimum bleeding, but with a view to achieving some of the social objectives which 25 years of Republic Democracy has failed to achieve.

It is indeed a happy moment, that one of the oldest institutions of the tax-practitioners, i.e., the Chamber of Income-tax Consultants has taken up this task and started a periodical publication to deal with Income tax law and the allied laws and their problems, the practice and dealings with some pernicious thorny spots. It is in a sense a pioneering effort by a Chamber of Practitioners, because quite a few Income-tax practitioners' Associations exist, but nonetheless there is none which is dedicated to the problems of tax payers and the tax practitioners alike on a common platform. Indeed, these objectives cannot be achieved except by an organised association, with a band of selfless workers dedicated to these problems even at some personal sacrifice.

It is unfortunate that the Central enactments having far-reaching consequences and affecting citizens throughout the length and breadth of this vast country should still have some of its problems in a state of uncertainty and some in a

state of suspended animation. It is equally unfortunate that by the time a point of law becomes clear, it is further adulterated with hybrid amendments with the result that the tax laws which, in principle should remain crystalised and clear so as to be understood by the common people at large, remain a labyrinth of multiple puzzles some of which still remain to be understood, sorted out and interpreted. It is equally unfortunate that law-reporting in this country has taken roots in quantity and not in quality, because quite a number of decisions binding constitutionally remain un-ravelled, un-noticed and un-reported. When an important judgement is embodied in a printed journal, it is already few months or few years past. The result has been that the people and the practitioners have been kept obliviously ignorant of binding decisions and the direct consequence is that the correct law may not be noticed by the tax-masters (most of whom learn the law by a process of trial and error). The resultant chaos has been responsible for a perennial crop of litigation. The cost in terms of money and waste of time being stupendous to the people, the tax payers and the tax masters is in the final analysis a national waste.

This is our first step, towards our aim to have a common platform for the tax payers and the tax practitioners to come together to discuss laws, exchange notes, to report the gist of recent decisions of the Supreme Court, High Courts and the Tribunals, to give timely information on impending or hurriedly introduced changes in law. I am sure, the tax payer and the tax practitioner well equipped with the latest law will un-ravel and cut the gordian knots. What we have in mind for launching this journal is not merely commercial reporting, but to provide for a vehicle of thoughts, which ultimately may turn out to be an exchange of thoughts between practitioners, the tax payers and the tax officials to the ultimate benefit of all.

It is a proud moment for this Chamber and we dedicate this journal to the tax payers, tax masters and the tax practitioners, aspiring that this vehicle of thoughts will serve useful purpose to one and all.



Chronicling the Journal's Journey over the last Five Decades

Kishor Vanjara, Tax Consultant

The Chamber's Journal (formerly known as the Income-tax Review) is completing 50 glorious years. It as usual started out as quarterly publication. Its objective, as chronicled by Late Shri B.C. Joshi who penned the first editorial as the Chamber's first step towards its aim to have a common platform for the taxpayers and tax practitioners to come together to discuss laws, exchange notes, to report the gist of recent decisions of the Supreme Court, High Courts and the Tribunals and to give timely information on the impending or the hurriedly introduced changes in law.

I am proud to state that the Journal retains many of these attributes even today and has added a feature of insightful special stories in each issue on topics of common interest. For the benefit of the readers, I have chronicled below, the significant milestones of the Journal over its long journey of five decades. This is bulleted as below:

- During the Presidentship of Late Shri B.C Joshi, the first issue of the "Incomer Tax Review" was released on 31st March, 1975 by Shri O. V. Kuruvilla, the then Commissioner of Income Tax, Mumbai.

- Shri Arvind Thakkar was the First Editor of the Income Tax Review. Interestingly, the very first editorial in the April 1975 issue was written by Late Shri B.C. Joshi himself.

- Coincidentally, for this first issue of the 50th year, the Editor is also a Thacker (Anish) and the Ediorial is penned by Vipul Joshi, son of late Shri B.C. Joshi.

- The Journal was initially published quarterly with a subscription of Rs .10/- per year for members and Rs. 25/- for non-members.

- The first advisory board was constituted in 1975-76 comprising of Late Shri B. C. Joshi, Late Shri S. P. Mehta, Shri Y. P. Trivedi and Late Shri V. H. Patil.

- After one year of being a quarterly publication, the Income Tax Review became bi-monthly.

- From April 2001, Income Tax Review became a monthly journal.

- The first editorial board members were Late Shri Arvind Thakkar, Late Shri N. S. Shah and Late Shri P. U. Thakore. After three years two more members, Late Shri B. C. Joshi and Late Shri D. D. Mehta were co-opted on the Editorial Board.

- In the year 1981, the first issue of the Journal which was a special issue on a particular topic was published. This was on the Voluntary Disclosure of Income Scheme (VDIS).

- The year 1987 saw the publication of "special issues" on a regular basis.

- The Income-tax Department, Mumbai started subscribing Journal with 80 copies, increased to 234 copies in the year 2001-2002. The journal continues to be read by Departmental Officials and Tribunal Members even today.

- In 1991, a quarterly digest "March of the Law" was started. Every third issue of the Journal was "March of the Law"

- The Chamber got the certificate of postal registration for the Journal in December 2000. This continues till date and the Journal is sent by post to many of its subscribers.

- From April 2002, in place of special issues, The Chamber started "Special Stories".

- Since the scope of the Journal had expanded to Indirect Taxes, Allied Laws and Accounting & Auditing, the name of the "Income Tax Review" was changed to "The Chamber's Journal" from October, 2012.

- The 51st Issue of the Journal was on "50 Supreme Court Landmark Judgments on Direct Taxes".

- At the occasion of the 90th year Celebration of the Chamber, a special issue on "Vision 2025-Tax Laws & Administration" was published.

- The April 1994, issue was on "Personal Data Diary".

- A Special issue paying tribute to the legend, Late Shri N. A. Palkhiwala, was published in December 2002.

- On completion of 36 years of The Journal in July 2011, the issue was published on "Embracing Change".

- The June 2013 issue was dedicated to Late Shri B. C. Joshi.

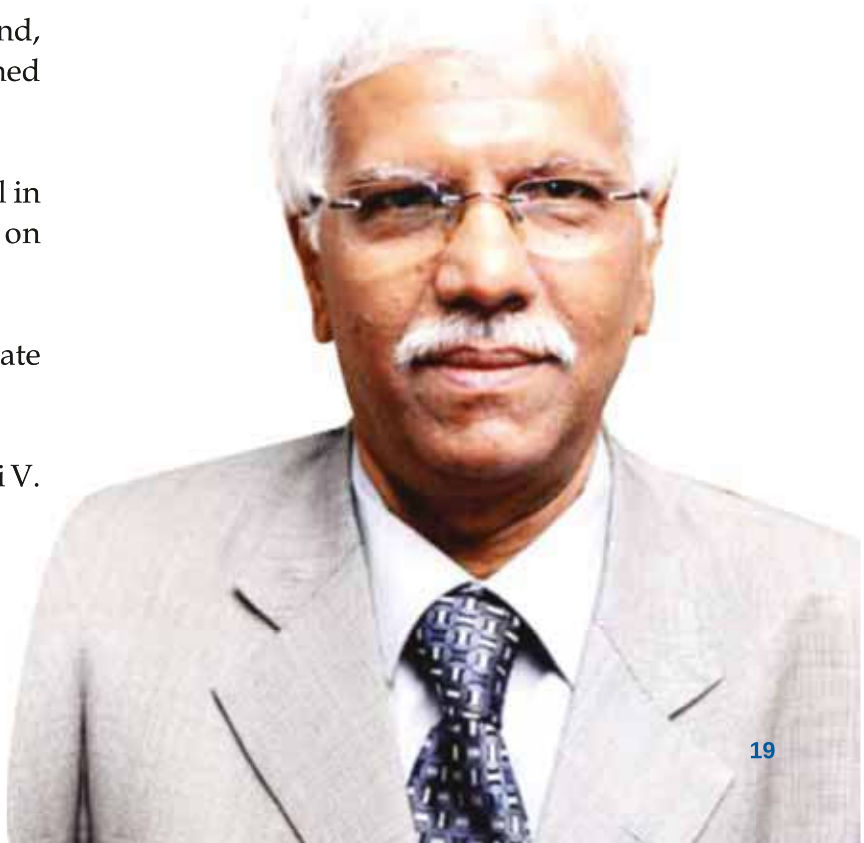
- A Special issue paying tribute to Late Shri V. H. Patil was published in October 2021.

- The journal has kept pace with the changing trends in technology. In 2018-2019, the first soft copy (pdf file) of the journal was released and in 2023-2024, option was given to the subscribers to opt for a soft (pdf) copy of the journal instead of a hard copy.

- During the year 2020-21, the year of the COVID-19 pandemic, not a single issue of the journal was missed. All 12 issues were sent, to the subscribers in soft copy.

Friends these are some of the unforgettable moments of this Journal in its journey over the last 50 years. As the times will change, so will the Journal but I am confident that the good work started by our seniors way back in 1975 will be continued and the Journal will continue to be well regarded and respected by professionals and tax and judicial officials alike.

Kishor Vanjara
Tax Consultant
Past President



Members of the Managing Council 1975-76



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Outstanding Events



Shri O.V. Kuruvilla inaugurating Income Tax Review

EVOLVING APPROACHES TO TREATY INTERPRETATION : INDIAN COURTS





Dr. Ashrita Prasad Kotha

Palak Sethi
Advocate

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Overview

Treaty interpretation is necessitated to discern the scope and meaning of various terms. In the context of tax treaties, it particularly entails the reconciling of competing interests at play in a principled manner. In Azadi the Supreme Court remarked that tax treaties cannot be interpreted according to the ordinary principles of statutory interpretation. Almost two decades since the remark in Azadi set the ball rolling on treaty interpretation, Indian Courts have responded in various ways. This piece examines the trends therein and the principles and materials relied upon. It is found that Indian judicial authorities tend to prefer a contextual and purposive approach rather than the textual one. Indian judicial authorities have emphasized the importance of workability, harmonization, holistic and subject matter specific reading while relying on The Vienna Convention on the Law of Treaties, 1969 principles as well as supplementary materials such as OECD and UN Model Convention and related Commentary.

1. Introduction

Countries seek to enter double taxation avoidance agreements (DTAAs or tax treaties) to facilitate inter se cross-border trade and foster economic relations. Reaching consensus on various matters requires countries to negotiate and make compromises along the way[1]. Taxpayers rely on tax treaties to inter alia avoid double taxation and minimize tax liability. Countries and taxpayers represent the two distinct user groups of tax treaties[2]. Treaty interpretation is necessitated to discern the scope and meaning of various terms[3].



1. *Ensco Maritime Ltd. vs. Deputy CIT [2004] 91 ITD 459 (Delhi); Mashreq Bank PSC vs. CIT 2025 SCC OnLine ITAT 1038.*
2. *Eduardo A. Baistrocchi, The International Tax Regime and the BRIC World: Elements for a Theory, Oxford Journal of Legal Studies , Vol. 33, No. 4 (2013), pp. 733-766.*
3. *Michael Lang, Introduction to the Law of Double Taxation Conventions, Linde Publications, 2021, p.13.*

In the context of tax treaties, it particularly entails the reconciling of competing interests at play in a principled manner[4].

Tax treaties drafted by diplomats rather than parliamentarians lack statutory precision and pose an interpretational conundrum.

In Azadi the Supreme Court remarked that tax treaties are *"entered into at a political level and have several considerations"*[5]. Most fundamentally, tax treaties cannot be interpretated according to the ordinary principles of statutory interpretation[6]. Thus, tax treaties drafted by diplomats rather than parliamentarians lack statutory precision and pose an interpretational conundrum[7].

Almost two decades since the remark in *Azadi* set the ball rolling on treaty interpretation, this piece seeks to identify the principles and materials that Indian Courts draw from, to resolve interpretation conflicts.

2. Approaches to interpretation

Various approaches have long existed in international law : (i) grammatical / literal which requires strict interpretation of language, (ii) systematic / contextual which relies on context to give meaning to the text[8], (iii) teleological / purposive which looks to the object and purpose of the treaty[9], and (iv) historical that allows reference to preparatory materials to decipher intention of parties when signing the treaty.

One would still need us to identify the most appropriate one[10]. The Vienna Convention on the Law of Treaties, 1969 (VCLT) codifies principles for interpreting treaties.

Article 31 contains the general rule of interpretation. Article 31(1) mandates interpretation of treaties in good faith, giving terms their ordinary meaning within context and in view of the object and purpose. Article 31(2) elaborates that the context includes the treaty's text, preamble, annexes, and any related agreements or instruments accepted by the parties. Article 31(3) further stipulates that subsequent agreements, practices, and relevant rules of international law can also be considered for treaty interpretation. Article 31(4) allows attribution of a special meaning if the "*parties so intended*". Article 32 permits recourse to supplementary means such as "*preparatory work of the treaty and the circumstances of its conclusion*" when needing to confirm the meaning resulting from Article 31 or to determine meaning when Article 31 "*leaves the meaning ambiguous or obscure…or leads to a result which is manifestly absurd or unreasonable*". Article 33 states that if a treaty exists in two or more languages, each text has the same authority, unless the treaty itself provides one version to prevail over another.

The VCLT principles bring together different strands of the traditional approaches - ordinary meaning, context, object and purpose

4. *While treaty interpretation issues may also be taken up through mutual agreement procedure (MAP), taxpayers tend to prefer courts as MAP is effectively controlled by contracting states. MAP interpretations are not legally binding.*
5. *Azadi Bachao Andolan vs. Union of India [2003] 263 ITR 706 (SC), para 121.*
6. *Id. at para 120.*
7. *See Ensco Maritime Ltd. supra note 1; See Azadi supra note 5; Hindalco Industries Ltd. vs. Assistant Commissioner of Income-tax [2005] 2 SOT 528 (Mumbai); JCIT vs. Merrill Lynch Capital Market Espana SA SV [2020] 180 ITD 627 (Mumbai - Trib.).*
8. *See Merrill Lynch supra note 7.*
9. *See Azadi supra note 5; Mashreqbank PSC vs. DDIT [2007] 108 TTJ 554 (Mumbai)*
10. *Aseem Chawla, "Interpretation of Tax Treaties: An Art Yet to be Mastered" National Law School of India Review: Volume 23: Issue. 2, (2012), p.3 available at: https://repository.nls.ac.in/nlsir/vol23/iss2/1.*



and historical materials. Article 31 "*does not provide for a rule under which one interpretation method takes precedence over another*.[11]" It thus needs to be seen how these principles apply and interact with one another in real cases.

3. Application of VCLT Principles

The VCLT principles are general, hence, it must be asked whether they are suitable for tax treaties[12]. Vogel observed that while the VCLT principles "*cannot make allowances for the peculiarities of tax treaties*" it settles crucial issues such as non-relevance of the subjective intent of parties[13]. It also needs to be seen if VCLT is applicable given that India is not a signatory to the convention.

Indian Courts have not been deterred by India being a non-signatory. Courts have held that VCLT applies as it is a manifestation of customary international law, equally applicable to tax treaties. This position, first taken by Indian tribunals and lower Courts[14] has now been validated by the Supreme Court[15]. Interestingly, one does not see the same kind of adoption in non-tax treaties[16].

3.1 Article 31: Good faith, context, object and purpose

Article 31 is centered around good faith. At the outset, the notion is that treaty terms are not meant to be redundant. Good faith requires that parties honor promises and act fairly[17].

Courts have routinely mentioned good faith but what if contracting states interpret promises differently? This was evident from the *Nestle SA*[18] judgment of the Supreme Court. The issue was whether taxpayers could rely on the promise made in the Most Favored Nation (MFN) clause in the India-Switzerland tax treaty to enjoy the benefits of lower rates in subsequent treaties with non-OECD countries (Lithuania and Colombia). In *Concentrix and Optum Global*[19] the Delhi High Court granted MFN benefit based on the principle of "*common interpretation*" which requires consistent interpretation by tax authorities and courts of contracting states.

11. *See Lang supra note 3, p.19.*
12. *Id. at p.13.*
13. *Klaus Vogel, Double Tax Treaties and Their Interpretation, Berkeley Journal of International Law, Volume 4, Issue 1 (1986), pp.34-35.*
14. *See Hindalco supra note 7; Sanofi Pasteur Holding SA and Ors. vs. The Department of Revenue Ministry of Finance, Government of India [2013] 354 ITR 316(AP); DIT vs. KLM Royal Dutch Airlines (2017) 392 ITR 218.*
15. *Ram Jethmalani vs. UOI [2011] 339 ITR 107 (SC); Assessing Officer (International Taxation) vs. Nestle SA [2023] 458 ITR 756 (SC).*
16. *Vik Kanwar, Treaty Interpretation in Indian Courts Adherence, Coherence, and Convergence in The Interpretation of International Law by Domestic Courts: Uniformity, Diversity, Convergence, Helmut Philipp Aust (ed.) and Georg Nolte (ed.), Oxford University Press (2016).*
17. *Mark E. Villiger, Commentary on 1969 Vienna Convention on the Law of Treaties 2009, Article 31 at p.425.*
18. *Nestle supra note 15.*
19. *Concentrix Services Netherlands B.V. vs. Income-tax Officer (TDS) [2021] 434 ITR 516 (Delhi).*

Supreme Court interpreted "*…is a member of OECD"* to have a present significance based on the context. MFN benefit was denied as subsequent treaty partners were not OECD members when entering the DTAA and a separate notification under section 90(1) of the Income Tax Act, 1961 importing the MFN benefits had not been notified. The latter constituted subsequent practice which was relevant as per Article 31(3)b). This position has been affirmed subsequently[20].

Supreme Court relied on Aust's work: "*however precise the treaty text appears to be, the way in which it is actually applied by the parties is usually a good indication of what they understand it to mean, provided the practice is consistent, and is common to, or accepted by, all the parties.*" Basically, subsequent practice was looked at as part of larger context for interpretation without commenting on whether the notification requirement was contrary to good faith, giving primacy to formal domestic procedures. The decision has been criticized for neither upholding the good faith precept nor Article 51 of the Constitution requiring treaty obligations to be respected[21]. Moreover, authors pointed that the subsequent practice cited was incomplete[22]. In the aftermath of the case, the Swiss authorities suspended the MFN treatment for India[23].

In *Azadi*, ordinary meaning was explained to be the general meaning such as would be attributed by a diplomat rather than a lawyer[24]. Courts are to be guided neither by dictionary[25] nor literal meaning[26]. As is evident below, emphasis is on the objects of the treaty. Ordinary meaning is contrasted with special meaning in Article 31(4) which allows parties' intentions to be relied upon.

Upon identifying the common thread in the related scheme of provisions, "property" was interpreted narrowly to avoid incongruous results, ensuring that taxability of subsidiary transactions (payment of training fee) aligns with the principal transaction (sale of know-how)

In *Hindalco*[27], the tribunal examined whether training fees paid by Hindalco to a US company was taxable in India (the source state). Article 12(5)(a) of the Indo-US DTAA specifically excludes payments for services "*inextricably and essentially linked, to the sale of property*". Hindalco argued that the fees were captured by the exclusion clause. The Tribunal laid down that treaty terms must be read harmoniously, terms must be given a workable meaning and understood considering the subject matter. Upon identifying the common thread in the related scheme of provisions, "property" was interpreted narrowly to avoid incongruous results, ensuring that taxability of subsidiary

20. *See Income-tax Officer vs. Deccan Holdings B.V. [2025] 472 ITR 639 (SC).*
21. *B Kuźniacki and S. van Weeghel, VCLT and the Peaceful Coexistence of Tax and Investment Treaties: A Case Study of Limited MFN Clauses and the FET Standard, World Tax Journal 2025 (Volume 17), No. 1.*
22. *Deepak Chopra and Priya Tandon, Dark Days for Treaty Interpretation, Dark Days for Treaty Interpretation, available at https://www.azbpartners.com/bank/dark-days-for-treaty-interpretation/.*
23. *Vikas Dhoot, 'Switzerland Withdraws MFN Status from India' (The Hindu13 December 2024) <https://www.thehindu.com/business/Industry/switzerland-scraps-mfn-status-to-india-dividend-income-to-face-higher-tax/article68981505.ece> accessed 20 March 2025.*
24. *See Azadi supra note 5.*
25. *K.P. Varghese vs. ITO [1981] 131 ITR 597 (SC), the Court in the context of statutory interpretation relied on Justice Hand's observation that words in their literal sense are primarily and ordinarily the most reliable source for interpretation but the court must not make "a fortress out of the dictionary". This case is relied on by various courts and tribunals in treaty interpretation cases; See KLM Royal Dutch Airlines supra note 14 at para 28.*
26. *See Azadi supra note 5, Deputy Commissioner of Income-tax vs. Boston Consulting Group P. Ltd. [2005] 94 ITD 31 (Mumbai).*
27. *See Hindalco supra note 7 at para 30.*

transactions (payment of training fee) aligns with the principal transaction (sale of know-how). Interestingly, it has been acknowledged that this principle applies to tax legislation too. The principles identified here, somewhat of a logical extension of VCLT, have served as primary guidance for subsequent cases.

A similar approach of finding context from within the particular instrument has been affirmed by other tribunals too[28]. Reliance on slightly different language in another treaty of one of the countries with a third country is not part of the context intended by the VCLT[29]. As per Article 31, courts may place reliance on the preamble and annexes or any agreement or instrument in relation to the treaty, accepted by all parties to the treaty. In *Azadi*[30] the Supreme Court relied on the preamble when it had to weigh the legitimacy of treaty shopping as against perceived revenue losses. Taking a holistic view of the India-Mauritius DTAA, the preamble and the absence of an anti-abuse rule the Supreme Court held that treaty shopping may even have been intended and tolerated[31]. Such questions arose with respect to other DTAAs too[32]. While Azadi relied on the preamble, it did not make specific reference to the VCLT.

Summing up, "*If text is the texture, context is what gives the colour. That interpretation is the best which makes the textual interpretation match contextual one.*[33]"

Summing up, "If text is the texture, context is what gives the colour. That interpretation is the best which makes the textual interpretation match contextual one."

3.2 Article 32: OECD and UN Model and Commentary

Supplementary means can be employed only to confirm or determine the interpretation under Article 31. The Authority for Advance Ruling relied on press releases and speeches by high-ranking officials delivered at the time of signing the treaty to confirm object and purpose as per Article 32[34].

India's tax treaties are based on the OECD Model Tax Convention (OECD Model) and/or the UN Model Tax Convention (UN Model)[35]. Neither is the OECD Model a binding instrument nor is India an OECD member. However, OECD hopes that its Commentary will "*be of great assistance in the application and interpretation of the conventions*"[36]. The key question though is about the applicability of OECD and UN Model and Commentary.

Vogel commented that with respect to non-OECD countries OECD Model and Commentary may only have bearing when "*(1) the language of the provision coincides with*

28. *See Boston Consulting supra note 26; See Mashreqbank supra note 9.*
29. *See KLM Royal Dutch Airlines supra note 14.*
30. *See Azadi supra note 5.*
31. *Id. The court held that treaty shopping was not per se illegal and that some developing countries "tolerate" treaty shopping in the interest of long-term development. It is a tax incentive to attract scare foreign capital or technology and is similar to grants or tax holidays.*
32. *See, for example, Meera Bhatia vs. ITO [2010] 38 SOT 95 (MUM.) where a similar double non-taxation instance arose under the India-UAE DTAA.*
33. *See Ensco Maritime supra note 1.*
34. *In re Abdul Razak A. Meman [2005] 276 ITR 306 (AAR).*
35. *DP Sengupta, India in The Impact of the OECD and UN Model Conventions on Bilateral Tax Treaties, Michael Lang, et al. (eds.), Cambridge Tax Law Series (2014), p.550.*
36. *OECD Model Tax Convention on Income and on Capital 2017, Introduction, para 29.2.*



the OECD Model and (2) its context suggests no other interpretation." This would be a facts specific exercise. As the OECD and UN Model are quite similar, even when developing countries rely on UN Model, the OECD Model and Commentary may be relied upon[37]. Despite some arguments to the contrary, Lang argues that only the OECD Model and Commentary "*which existed at the time the bilateral treaty was concluded may be taken into account*[38]."

In particular, the ITAT has commented that the OECD Commentary can be relied upon as part of Article 32[39]. More generally speaking, Indian Courts have approved of Lord Radcliffe's opinion that OECD Commentary constitutes "*international tax language*"[40]. OECD and UN views are thought to be "*contemporanea expositio*" as these have helped standardize tax treaties[41]. There is a presumption that even non-OECD countries importing the language of the OECD Model are aware of the meaning and implications of the words ("*unless a contrary intention is specifically expressed*")[42] and thus, the commentaries have persuasive value[43]. Taxpayers can rely on these documents to understand their liability if the treaty is identical to the OECD or UN Model in case no local court decisions clarify the meaning or take a different view[44].

Courts have extensively relied on the OECD Commentary for treaty interpretations, particularly in relation to provisions such as Article 5. In the *Formula One World Championship* (FOWC) case[45] where the Court had to assess the non-resident's liability in India, OECD Commentary and academic scholarship (Baker and Vogel) were extensively invoked. The court concluded that the Buddh International Circuit constituted FOWC's "fixed place" of business as it satisfied the characteristics of stability, productivity, and dependence. This interpretation was followed in *E-Funds IT Solution Inc.*[46]

There is one Supreme Court decision that took a contrary stance. In *Kulandagan Chettiar*[47] the Supreme Court held that OECD Commentary or foreign cases are "*unnecessary*" as taxation policy is a sovereign prerogative. The Court felt that the treaty provisions were quite clear on the contested aspects (taxation of immovable property and capital gains). The taxpayer's counsel argued that the OECD Model came into effect from 1977 while the Indo-Malaysian DTAA was signed in 1976. Hence, the countries could not have known or assented to OECD's Commentary. In other words, the OECD Commentary could not have been the preparatory work for an already concluded DTAA. Although the Court does

37. *See Vogel supra note 13, p.42.*
38. *See Lang supra note 3, p.19.*
39. *DCIT vs. Roxon Oy [2007] 106 ITD 489 (MUM.); In Engineering Analysis Centre of Excellence (P.) Ltd. vs. Commissioner of Income-tax [2021] 432 ITR 471 (SC), the Supreme Court made no direct comment on the matter but relied on an Australian case that relied on the Commentaries under Article 32. There are different views on which VCLT provision can form the basis for invoking the OECD Model and Commentary. See, Lang supra note 3, p.19.*
40. *Commissioner of Income-tax vs. Visakhapatnam Port Trust [1983] 144 ITR 146 (Andhra Pradesh).*
41. *Graphite India Ltd. vs. DCIT 86 ITD 384.*
42. *Metcham Canada Inc vs. DCIT [2006] 100 ITD 251 (Mumbai).*
43. *Motorola Inc vs. DCIT [2005] 95 ITD 269 (Delhi) (SB); See Engineering Analysis supra note 39.*
44. *See Engineering Analysis supra note 39.*
45. *Formula One World Championship Ltd vs. Commissioner of Income Tax [2017] 394 ITR 80 (SC).*
46. *ADIT vs. E-Funds IT Solution Inc [2017] 399 ITR 34 (SC).*
47. *CIT vs. P.V.A.L. Kulandagan Chettiar [2004] 267 ITR 654 (SC).*

not explicitly cite this reason, this is a crucial fact and hence, may provide rationalization for why this approach is not to be taken as the dominant one.

Since 1997, non-OECD members have also been able to express contrary positions[48] to the OECD Model and Commentary. Can such positions impact interpretation of relevant articles?

This question was discussed at length in *Engineering Analysis*[49], where the Supreme Court noticed an Indian reservation when examining the concept of royalties under Article 12 of the Indo – US tax treaty. The position used phrases like "*reserves the right to*" and "*is of the view that some of the payments referred to may constitute royalties.*" The court held that the reservation was unclear, compared to India's definitive stance on the preceding provisions. India categorically disagreed with paras 9.2 and 9.3 of the OECD Commentary dealing with payment for a roaming call and spectrum license, respectively. Despite the position, no amendments were made to DTAAs to alter the definition of royalties after India's position was taken[50]. Similarly in the case of *New Skies Satellite BV*[51], the Delhi High Court held that mere positions taken with respect to the OECD Commentary do not alter the DTAA's provisions, unless it is amended by way of bilateral re-negotiation. In *Right Florists*[52], the tribunal held that reservations are relevant only to the extent that they affect the interpretation of tax treaties entered into after the reservations are made.

When Courts deal with situations where the treaty provisions draw from the OECD and UN Models which take an identical approach, UN materials are cited in corroboration[53]. Also, there are treaty terms/concepts that do not exist in the OECD model such as fees for technical services[54] and force of attraction[55] where Courts seek recourse to the UN Model and Commentary. Even in an instance where the UN Model and the relevant treaty provision in the India-Spain DTAA were not identical, UN Commentary was helpful to understand the particular evolution of the capital gains provision. In particular, the UN Commentary supplied the "*historical background and justification*" of the specific provision[56].

The court held that the reservation was unclear, compared to India's definitive stance on the preceding provisions.

In a case where the taxpayer claimed that its Indian shipping operations were casual and not taxable as per Article 8A (2) of the India-Netherlands DTAA, Tribunal had to interpret the phrase "more than casual". Relying on the UN Commentary and Klaus Vogel's work, it held that it includes both regular and frequent shipping visits as well as

48. *Positions to the OECD Model are unlike reservations strictly speaking as understood under Article 2(1)(c) of the VCLT as reservations can only be made with respect to treaties.*
49. *See Engineering Analysis supra note 39.*
50. *For example, the India-Morocco tax treaty incorporated a definition of royalties that closely aligns with the OECD Model Commentary. Similarly, recent amendments to the India-Singapore and India-Mauritius tax treaties retained definitions of royalties that are similar to the OECD's definition.*
51. *Director of Income Tax vs. New Skies Satellite BV [2016] 382 ITR 114 (Delhi).*
52. *ITO vs. Right Florists Pvt. Ltd [2013] 25 ITR(T) 639 (Kolkata - Trib.).*
53. *Assistant Director of Income Tax vs. Valentine Maritime (Mauritius) Ltd. 2010 SCC OnLine ITAT 2487.*
54. *Springer Verlag GmbH vs. CIT [2022] 197 ITD 173 (Delhi-Trib.); International Management Group (UK) Ltd. vs. Commissioner of Income Tax [2024] 466 ITR 514 (Delhi).*
55. *See Roxon OY supra note 39.*
56. *See Merrill Lynch supra note 7.*

irregular and isolated visits, if planned. Since, the taxpayer's ships visited Indian ports on an "*as and when required*" basis, the visits were planned and therefore, taxable in India[57].

India's close involvement provides a strong reason to rely on the UN Commentary:

"The UN's 'Committee of experts on International Cooperation in Tax Matters', which reviews and updates the UN Model Convention Commentary, not only has presence, but also very active and laudable contribution, from India. In this view of the matter, the views so expressed in the UN Model Convention Commentary, particularly in the absence of any specific reservations by India, can be reasonably construed to be acceptable to the Indian tax administration as well.[58]*"*

Recently, CBDT has clarified that UN Commentary may be used as an additional source when invoking the Principal Purpose Test[59]. This reinforces the above quote.

4. Conclusion

DTAAs are unique in as much as these are akin to "*mini legislation containing in themselves all the relevant aspects or features which are at variance with the general taxation laws of the respective countries*"[60].

Two decades since *Azadi* alerted to the need to identify new principles for treaty interpretation, Indian Courts responded in various ways. It is now well understood that agreements are not the same as statutes.

VCLT principles and OECD and UN Model and Commentaries are relied upon. India



being a non-signatory VCLT does not deter the adoption of VCLT as it perhaps serves the function of a "*common minimum interpretive canon*"[61]. While applying the VCLT, Courts look at a wide range of material such as the scheme and logic of the relevant provisions, preamble, subsequent practice and supplementary material. We have seen more expositions on context, object and purpose rather than good faith, leaving room for evolution in the years to come. UN Model and Commentary are also now being cited often, when interpreting terms not in the OECD Model.

The common thread that emerges is a preference for contextual and purposive reading rather than the textual approach. Statutes create tax liability and thus warrant strict reading. Treaties allocate and manage relations among states and thus, workability, harmonization, holistic and subject matter specific reading are of paramount importance. These principles articulate and extend the underlying rationale of VCLT. While some of these principles are not entirely distinct from the ones used to interpret procedural provisions in tax statutes, when in doubt, context, object and purpose save the day.

57. *James Mackintosh vs. ACIT [2005] 93 ITD 466 (MUM.).*
58. *Birla Corporation Ltd vs. Asstt. CIT [2015] 153 ITD 679 (Jabalpur – Trib.).*
59. *Circular No. 1/2025 [F. NO. 500/05/2020/FT&TR-II], dated 21-01-2025*
60. *CIT vs. VR. S. R. M. Firm [1994] 208 ITR 400.*
61. *See Vik Kanwar supra note 16, p.256. CIT vs. VR. S. R. M. Firm [1994] 208 ITR 400.*

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MLI AND IMPACT ON TREATY INTERPRETATION IN INDIA (OTHER THAN PPT)





Shreya Rao
Advocate

Pragya Kaushik
Advocate

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Overview

*The multilateral instrument (**"MLI"**) incorporates BEPS measures in existing bilateral tax treaties to broaden tax base and prevent treaty shopping, tax evasion etc. It entered into force in India on October 01, 2019. MLI's application to India's treaties potentially impacts decades of case law applicable to cross-border taxpayers on various issues, like taxation of business profits, eligibility of taxpayers to avail treaty benefits etc. This paper first examines the interplay between the Indian General Anti-Avoidance Rules (**"GAAR"**) and two notable anti-abuse provisions of the MLI, while applying tax treaties domestically.*

Once the MLI applies, subject to the GAAR barriers, individual issues and their relevant case law must be examined to understand MLI's impact. The paper examines two such potential issues. The first issue is the practice of splitting-up of contracts, where one composite business activity is split into multiple phases performed separately, by different entities, in different countries, to avoid taxation of profits from such phases in all countries. The second issue is restructuring of the nature of powers of agents appointed by business in various countries, to avoid taxation of profits from such agency arrangements in these countries.

Introduction

The Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (**"MLI"**) entered into force internationally on July 01, 2018[1] and domestically on October 01, 2019[2]. Now, over half a decade after, it is useful to introspect and ask whether the world looks different post MLI. If yes, how?

But before that, what is the MLI? Historically, states faced difficulties



1. *https://www.oecd.org/en/topics/sub-issues/beps-multilateral-instrument.html.*
2. *https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/beps-mli-signatories-and-parties.pdf.*

with profit shifting by taxpayers, who by diversion to low or nil-tax countries, avoided paying taxes in both the country of residence and the countries from which the profits were earned. Usually little to no-income-earning economic activity would happen in these low / nil-tax countries[3]. To counter these practices, called 'base erosion and profit shifting' (**"BEPS"**), the OECD Committee on Fiscal Affairs along with the G20 countries prepared a BEPS Package in November 2015. The BEPS Package provided measures to countries to ensure that profits were taxed where

The MLI was conceptualized as a multilateral treaty that accomplished a large-scale modification of existing bilateral treaties by allowing countries to "opt in" or "opt out" of specific provisions.

profit-generating economic activities were performed, and value was created[4]. BEPS measures were then required to be incorporated into bilateral tax treaties, and the MLI was conceptualized as a multilateral treaty that accomplished a large-scale modification of existing bilateral treaties by allowing countries to "opt in" or "opt out" of specific provisions[5]. It therefore co-exists with existing bilateral treaties specified by the MLI signatories (i.e. Covered Tax Agreements or **"CTAs"**) and modifies them to implement BEPS measures[6].

This incorporation of MLI provisions into India's CTAs potentially impacts decades of case law applicable to cross-border taxpayers.

How is the MLI made applicable in India? India is a dualist country i.e. international treaties do not automatically become part of domestic law without an enactment by the domestic legislature[7]. Tax treaties apply in India by virtue of Section 90 of the Indian Income Tax Act, 1961 (**"ITA"**)[8]. India agreed to incorporate some core provisions of the MLI into its CTAs[9] and therefore, MLI provisions may also be considered enforceable in India by virtue of Section 90 of the ITA. This incorporation of MLI provisions into India's CTAs potentially impacts decades of case law applicable to cross-border taxpayers.

3. *Explanatory Statement to the MLI, available at https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf/_jcr_content/renditions/original./explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf.*
4. *Explanatory Statement to the MLI, available at https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf/_jcr_content/renditions/original./explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf.*
5. *Explanatory Statement to the MLI, available at https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf/_jcr_content/renditions/original./explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf.*
6. *Explanatory Statement to the MLI, available at https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf/_jcr_content/renditions/original./explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf.*
7. *Article 253, the Constitution of India.*
8. *Section 90, ITA.*
9. *MLI Position of India, available at https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/beps-mli-position-india-instrument-deposit.pdf.*

This paper first examines a precondition for applicability of MLI under domestic law and then illustrates two possibilities of impact.

Impact of Indian GAAR on applicability of MLI

The Indian General Anti-Avoidance Rules (**"GAAR"**), a part of the ITA, are strict, overarching anti-abuse provisions that override tax treaties. The GAAR came into effect in India from April 01, 2017[10]. It targets any "impermissible avoidance arrangement" (**"IAA"**), i.e. any business arrangement, including any step or any part thereof, of which the main purpose is to obtain a tax benefit, and which contains one or more of the following specified elements typically found in abusive tax practices[11]:

- It creates rights or obligations not ordinarily created between in arm's length dealings;
- It directly or indirectly results in abuse or misuse of ITA;
- It lacks or is deemed to lack commercial substance, wholly or partly; or
- It is entered into or undertaken by means or in a manner not ordinarily used for bonafide purposes.

Once an arrangement is declared to be an IAA, severe tax consequences are imposed, including denial of treaty benefits, disregarding any transaction or any party thereto etc.[12]

How does the Indian GAAR interplay with the MLI and particularly, MLI's anti-abuse provisions, while applying tax treaties domestically?

Two notable anti-abuse provisions in the MLI are the Principal Purpose Test (**"PPT"**)[13] and the Simplified Limitation of Benefits (**"SLOB"**)[14]. Either or both provisions are incorporated in many of India's CTAs. Subject to certain exceptions, the SLOB provides that a taxpayer can avail of treaty benefits (either income-specific benefits or all the treaty benefits) only if they fulfil certain eligibility criteria. The eligibility criteria differ for different kinds of taxpayers, e.g. individuals, companies etc. These are objective criteria which ensure that the taxpayer is a legitimate resident of the treaty parties and is an entity of substance and not a sham entity. For example, eligibility criteria for companies include the principal class of shares being listed on a recognized stock exchange and the criteria for persons other than individuals include that a minimum of 50% shares should be directly / indirectly owned by residents of the same country as that person, for at least half of the concerned year.

The PPT is broader and overrides all other treaty provisions. It provides that a taxpayer cannot avail a treaty benefit if, considering all facts and circumstances, it's reasonable to conclude that obtaining that benefit was one of the principal purposes of any transaction or arrangement that directly / indirectly resulted in that benefit. The only relief from PPT is if the taxpayer is able to prove that granting of

Two notable anti-abuse provisions in the MLI are the Principal Purpose Test ("PPT") and the Simplified Limitation of Benefits ("SLOB").

10. *Section 95(2), ITA.*
11. *Sections 95(1) and 96, ITA.*
12. *Section 98, ITA.*
13. *Article 7(1), MLI.*
14. *Article 7(8) to 7(13), MLI.*

The only relief from PPT is if the taxpayer is able to prove that granting of treaty benefit in those circumstances was in line with the object and purpose of the treaty provisions.

treaty benefit in those circumstances was in line with the object and purpose of the treaty provisions. PPT ensures that treaties apply according to the purpose for which they were entered into, i.e. to provide benefits in respect of bona fide transactions as opposed to arrangements with principal objective being to secure favorable tax treatment. This edition has a separate piece dealing with PPT in detail and the authors do not therefore examine it in this piece.

How does the GAAR intersect with PPT and SLOB? The default position under law is that in case of a taxpayer to whom the ITA and a tax treaty both apply, tax treaty provisions override the ITA, and ITA provisions apply only if they are more beneficial to the taxpayer[15]. However, if the GAAR applies, this position no longer holds true, and GAAR is applicable even if there is a more favorable treaty provision[16].

This implies that in a situation where we evaluate the applicability of SLOB, PPT and GAAR, SLOB and PPT will only become relevant if the GAAR threshold is not breached. Whether the GAAR threshold is easy to trigger in a given situation, is difficult to gauge. This is because the tests under GAAR are very subjective and extremely wide in scope, especially compared to the PPT. The GAAR looks at multiple angles, i.e. main purpose, commercial substance, kinds of rights or obligations between parties, to see if the arrangement is an IAA or not etc. Further, it can apply to any step or part or the arrangement in the same way as it applies to the arrangement as a whole[17]. An arrangement can be presumed to have been entered into or undertaken for the main purpose of obtaining a tax benefit merely if the main purpose of a step or part of the arrangement is to obtain a tax benefit, even if the main purpose of the arrangement as a whole was not to obtain the benefit[18]. There are also no judicial precedents to clarify the contours of GAAR and provide clarity to taxpayers. Given its nature and breadth, if GAAR does not apply, PPT thresholds may also not apply, particularly if the taxpayer is able to demonstrate the alignment of the transaction with the object and purpose of the treaty benefit provision.

With SLOB, one would need to evaluate whether the specified eligibility criteria are fulfilled, in order for the treaty benefits to become available. There might be cases where even though GAAR is not triggered, an entity can still trigger SLOB restrictions, since they are specific bright line tests that do not always sit within the contours of the GAAR.

A) Splitting up of contracts

Once the MLI is considered applicable based on the domestic law barriers detailed above, individual issues maybe exampled in relation to the impact of the MLI. One example of such an issue relates to the practice of splitting up of contracts. Under this practice, one composite business activity gets split into

15. *Section 90(2), ITA.*
16. *Section 90(2A), ITA.*
17. *Explanation to Section 95, ITA.*
18. *Section 96(2), ITA.*

multiple phases, e.g. preparation, installation etc. Each phase is performed separately, sometimes in short durations, by different entities, in different countries, so as to avoid breaching the permanent establishment (**"PE"**) threshold applicable in tax treaties.

One instance of such a PE threshold is when a building site or a construction or installation project (**"Site"**) continues for more than a specified threshold period (usually a year or 6 months). Closely connected enterprises escape the trigger of this PE threshold by splitting their composite contracts into multiple phases. Each phase continues for less than the specified threshold period in different countries and each phase is performed by a separate but connected / associated / group entity.

This splitting up has long been recognized as being an issue and agitated through case law. One example is the Delhi High Court decision in ***National Petroleum Construction Company***[19]. The Court held that a PE constituted by a building site, or a construction project would commence on the commencement of activities relating to



19. *[2016] 383 ITR 648 (Delhi). In this case, a UAE-based company was engaged in fabrication of petroleum platforms, pipelines and other equipment. It also undertook contracts for installation of petroleum platforms, submarine pipelines etc. at various sites. This UAE-based company entered into contracts with Oil and Natural Gas Corporation (an Indian company) for the installation of petroleum platforms and submarine pipelines. In pursuance of these contracts, while the platforms were designed, engineered and fabricated overseas, activities related to survey, installation and commissioning were performed in India. The Court, inter alia, decided on the issue whether the duration of the project activities had exceeded the specified threshold period of 9 months under Article 5(2)(h) of the India-UAE DTAA, so as to result in a PE in India.*

the project or site. The work at site or project must commence for a PE to arise, irrespective of whether the work relates to planning or actual execution of construction works or assembly activities. Preparatory work at site, like construction of site office, planning office or preparing the site should also be counted while calculating the PE's duration. It held that establishment of an office or any work which directly serves the operations at site should also be taken as a part of the building site or construction project.

Another good example is the decision in ***Valentine Maritime (Gulf) LLC***[20] of the Indian tax tribunal. The tribunal decided on the question of whether duration of activities undertaken by a UAE-resident company at various projects for the same client in the same geographical area, should be added together to determine whether specified PE threshold period was exceeded. The tribunal held that duration of various business activities, sites or projects should be aggregated only if the nature of these activities, their interconnection and interdependence are such that these activities can be viewed as a coherent whole, in conjunction with each other. It is irrelevant whether activities conducted are for the same or different principals (directly or through a sub-contractor) and in the same geographical area. On facts, the tribunal held that duration of contracts cannot be aggregated because the contracts were for different purposes and couldn't be treated as interconnected or interdependent and thus there was no PE in India.

MLI has added an additional, specific counter-abusive measure which provides that, for determining whether the specified threshold period is exceeded.

MLI has added an additional, specific counter-abusive measure which provides that, for determining whether the specified threshold period is exceeded, the following periods shall be added to the aggregate time spent by an enterprise in undertaking activities at a Site[21]:

a) Where the enterprise carries on activities in another state at the Site or carries on supervisory or consultancy activities in connection with the Site and these activities are undertaken during one or more time periods that in total exceed 30 days without exceeding the threshold period provided in the tax treaty; and

b) Where connected activities are undertaken in the other state at (or, if the treaty applies to supervisory or consultancy activities, in connection with) the same Site during different time periods, each exceeding 30 days, by one or more closely related enterprises.

20. *[2011] 45 SOT 359 (Mumbai). In this case, a UAE-resident company had carried out 2 projects in India for a client, in relation to Jamnagar Refinery Complex. While one contract was for equipment-installation work, the other contract was for accommodation and hook support for client's project on high seas at Jamnagar. The duration of the first contract was 8 months and 4 days, and the duration of the second contract was 8 months and 24 days. The aggregate duration of these two contracts, after excluding overlapping days, was 294 days, thus exceeding the specified threshold limit of 9 months under Article 5(2)(h) of the India-UAE tax treaty. The Indian revenue argued that these 2 contracts should be treated as geographically and commercial coherent, because they were executed in the same geographical area and for the same client. Thus the Indian revenue determined that the UAE company had a PE in India since the aggregate duration of these two contracts exceeded 9 months-threshold period. The UAE company challenged this determination before the tribunal.*
21. *Article 14(1), MLI.*

Further, determining whether activities are 'connected' will depend on the facts and circumstances of each case; the following factors may be looked at for this determination[22]:

a) Whether contracts relating to different activities were concluded with the same person or related persons;

b) Whether the conclusion of additional contracts with a person is a logical consequence of a previous contract concluded with that same person or related persons

c) Whether, in the absence of tax planning considerations, the activities would have been covered by a single contract;

d) Whether the nature of work under the different contracts is same or similar;

e) Whether the same employees are performing the activities under different contracts

It seems that MLI explicitly codified the principles already followed by the Indian judiciary while deciding on issues of constructions/installation PEs. Post-MLI, determining a PE's duration is easier, with the relevant principles clearly laid down. The idea is to ensure that activities which are in substance, effectively, interconnected and interdependent and which are undertaken on, around or in relation to a project/Site must be viewed as a composite, coherent whole to determine a PE's duration. This idea was largely followed by pre-MLI judicial anti-abuse measures and MLI[23]. The MLI amendments are thus clarificatory in nature.

B) Agency arrangements

Businesses typically appoint agents across various countries, who have powers such as negotiation and conclusion of contracts, securing orders from customers etc. Treaties specify situations in which the profits from such arrangements are taxable in the countries in which they exist. Taxpayers have historically avoided triggering this PE by restructuring the nature of agents' powers, for example by granting on ground agents the ability to negotiate contracts but not conclude them. Given that substantial negotiation often takes place on ground, this practice is frequently alleged to trigger PE thresholds. MLI has amended tax treaties to bring such agency arrangements within the tax net[24].

A person (not an independent agent) acting in a state for or on behalf of an enterprise of the other state is treated as the enterprise's dependent agent PE (**"DAPE"**) if such person has and habitually exercises in the first state, an authority to negotiate and enter into contracts for and on behalf of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise[25]. A common question that arises is what kind of activities get covered under this authority to negotiate and enter into contracts by the agents. Article 12(1) of MLI has further expanded the scope of this provision; it now states that a PE of an enterprise shall arise in a state if:

22. *Paragraph 53, OECD Commentary on Article 5 of the OECD Model Tax on Income and on Capital.*
23. *Paragraphs 51, 53 and 57, OECD Commentary on Article 5 of the OECD Model Tax on Income and on Capital.*
24. *Article 12, MLI.*
25. *For e.g. Article 5(8)(a) of the India-Singapore tax treaty or Article 5(4)(a) of the India-UK tax treaty etc.*

A) a person, while acting in a state on an enterprise's behalf, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise; AND

B) These contracts are:

- In the enterprise's name; or
- For the transfer of ownership or, or for granting of right to use, property owned by the enterprise or that the enterprise has the right to use; or
- For the provision of services by that enterprise.

In this case, the enterprise is deemed to have a PE in that state in respect of any activities (excluding some specified activities) which such person undertakes for the enterprise[26].



Before MLI was introduced, Indian tax tribunal rendered an interesting decision in ***eBay International AG***[27]. In this case, a Swiss company operated websites in relation to their India operations, assisted by two Indian group companies which exclusively provided marketing, promotional and customer support services to it. On specific facts, it was held that by simply providing these services, the Indian group companies did not negotiate or enter into contracts for or on behalf of the Swiss company and thus no DAPE arose.

Another case to note is that of the tax tribunal in ***Net App B.V.***[28]. In this case, a Netherlands-based company (**"Company"**) was engaged in the business of selling storage system equipment and products, including in India. An Indian group company provided marketing and sales support services to the Company, including assistance in organizing trade shows, determining market trends, competition analysis, assistance in pre-sales marketing etc. One interesting argument made by the Indian revenue was that the Indian agent had the authority to conclude contracts by virtue of the Company and Indian agent having common directors who are eligible to sign contracts on behalf of both the companies. The tribunal noted that:

A) common directorship is not relevant to determine whether the Indian agent has the authority to conclude contracts on Company's behalf.

B) The revenue should factually establish the role of Indian agent regarding its actual authority to conclude contracts.

26. Article 12(1), MLI.
27. [2013] 140 ITD 20 (Mumbai).
28. [2017] 78 taxmann.com 97 (Delhi-Trib.)

There is no possible one-size-fits-all formula which for the application of post-MLI DAPE provisions. Enterprises should brace for a closer scrutiny into their agents' activities, the nature of business and the nature of contracts involved.

The tribunal ultimately held that the revenue couldn't produce any credible evidence to show that the Indian agent was vested with the authority to conclude contracts on the Company's behalf and that it habitually exercised such authority and thus the Company did not have any PE in India.

How do these positions fare now in light of MLI?

Right off the bat, the kinds of contracts covered have increased; the DAPE risk arises not just where contracts are legally enforceable between the enterprise and other parties to the contract but also where the contractual obligations in effect, must be performed by the enterprise, and not by the person contractually bound to perform them[29].

The OECD Commentary clarifies that the expanded DAPE provision covers cases where the conclusion of contract results directly from certain activities (e.g. sales, marketing and promotional activities) conducted in a state, even if the contract is concluded outside that state[30]. Mere marketing and promotion activities not directly resulting in conclusion of contracts will not result in a DAPE[31]. What is the meaning of "directly resulting"? It will depend on the facts of each case; a mere marketing/support activity in the case of one business may end up triggering a DAPE for another business if it directly leads to conclusion of contracts. The OECD Commentary also states that the frequency and extent of actions relevant to determine whether the agent "habitually" concludes contracts or plays the principal role leading to concluding routinely concluded contracts (without material modifications by the enterprise) depends on the nature of contract and the business[32].

There is no possible one-size-fits-all formula which for the application of post-MLI DAPE provisions. Enterprises should brace for a closer scrutiny into their agents' activities, the nature of business and the nature of contracts involved. This is especially so where agents perform marketing, promotional or support activities. It would be interesting to see how enterprises will now try to disconnect such activities of agents from conclusion of contracts or try to explain away such a connection between the two.

Conclusion

Given the nascency of MLI provisions, their impact is required to be seen on a case-by-case basis. This is rendered more complex by the fact that MLI provisions may not be universally applicable and may depend on which provisions are chosen by treaty partners to be included in the treaties. India has chosen to include most of the key anti-abuse provisions in its CTAs. The application of India's CTAs, as amended by MLI, especially in the presence of GAAR, will witness an interesting evolution of jurisprudence. ■

29. *Paragraph 91, OECD Commentary on Article 5 of the OECD Model Tax on Income and on Capital.*
30. *Paragraph 88, OECD Commentary on Article 5 of the OECD Model Tax on Income and on Capital.*
31. *Paragraph 89, OECD Commentary on Article 5 of the OECD Model Tax on Income and on Capital.*
32. *Paragraph 98, OECD Commentary on Article 5 of the OECD Model Tax on Income and on Capital.*

ENTITLEMENT TO TAX TREATY BENEFITS : THE LITMUS TESTS OF GAAR AND PPT



Gouri Puri
Advocate

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Overview

The article explores the evolution of India's tax policy concerning tax treaty benefits, focusing on the General Anti-Avoidance Rule (GAAR) and the Principal Purpose Test (PPT). Initially, tax treaties like the India-Mauritius treaty were used to attract foreign investments, as upheld by the Supreme Court in the Azadi Bachao Andolan case. However, policy shifts occurred following high-profile cases like Vodafone, leading to the introduction of GAAR and the removal of certain tax exemptions. GAAR, codified under Indian law, allows tax authorities to re-characterize transactions primarily aimed at obtaining tax benefits. The PPT, introduced through the Multilateral Instrument (MLI), denies treaty benefits if one of the principal purposes of a transaction is to gain such benefits, unless it aligns with the treaty's objectives. The article discusses the interface between GAAR and PPT, their prospective application, and the need for clear legal standards to ensure tax certainty for foreign investors. It concludes by highlighting the importance of documenting non-tax reasons for investment structures to access treaty benefits, given the global shift towards combating treaty abuse.

Introduction

The evolution of Indian tax policy, treaty law and practice around entitlement to tax treaty benefits ties in deeply with India's economic growth story. In 2002, the Indian Supreme Court blessed the Mauritian investment route basis the sufficiency of the tax residence certificate as proof of entitlement to tax treaty benefits. In the context of foreign capital inflows, the Azadi Bachao Andolan ruling[1] noted that "although the Indian economic reforms since 1991 permitted such capital transfers, the amount would have been much lower without the India-Mauritius tax treaty." Tax treaties were clearly recognized as a mode of incentivizing foreign investments into India. Seemingly, a policy shift occurred when Hutchison exited from its Indian telecom business sans payment of Indian taxes. The ensuing decade saw the Vodafone and the Aditya Birla Nuvo rulings followed by a spate of retroactive amendments, introduction of GAAR and the withdrawal of the capital gains tax exemption on direct sale of

"Although the Indian economic reforms since 1991 permitted such capital transfers, the amount would have been much lower without the India-Mauritius tax treaty."

1. *Union of India v. Azadi Bachao Andolan [2003] 132 Taxman 373 (SC).*

shares under the Mauritius, Cyprus and Singapore tax treaties. To keep the transition smooth and retain investor confidence, GAAR was deferred, and the Government issued reassurances from time to time that the policy shift would not impact existing investments. Nevertheless, cases challenging the substance of investment structures (which also somewhat came to subsume arguments around beneficial ownership) emerged from time to time. Bad facts such as, the director of a foreign parent instead of the Mauritian entity signed the investment agreement into India, routing of funds from an overseas bank account that is not in Mauritius, arguments around "permitted transferee", became the way to challenge the substance of tax treaty claims. Indian courts, however, have remained

Neither GAAR nor the PPT provide for brightline rules to check economic substance but operate off a smell test, which is to be applied to the facts and circumstances of each case.

largely consistent in upholding the legacy of the Azadi Bachao Andolan case. As global headwinds turned to combat base erosion and profit shifting, the last decade ended with the adoption of the Multilateral Instrument (MLI) across nations that resulted in the incorporation of the PPT in several of India's tax treaties to prevent treaty shopping. Armed with GAAR and PPT to tackle treaty abuse, the present-day India stands at interesting crossroads. As its GDP grows, India exudes a new confidence that is not reliant on tax incentives for attracting investments. Yet, as an emerging economy it cannot become complacent on the importance of tax certainty to foreign investors. This calls for clear legal standards around the implementation of GAAR and PPT. The recent circular issued by



the CBDT to give guidance around the application of the PPT seems to acknowledge this. Against this backdrop, this article focuses on (i) the interface of GAAR and the PPT; (ii) prospective v. retroactive application of the PPT; and (iii) interpretation of the PPT considering the objective of the tax treaty.

Interface of GAAR & PPT

Even before delving into technicalities, there are several commonalities that exist between GAAR and PPT. First, both anti-abuse rules can be used to contest treaty shopping. Second, while both GAAR and PPT are largely untested in Indian courts (barring the covert extension of these principles in the treaty entitlement cases agitated by the revenue), they loom large over deal making and structuring foreign investments into India. Third, neither GAAR nor the PPT provide for brightline rules to check economic substance but operate off a smell test, which is to be applied to the facts and circumstances of each case.

GAAR finds its source under Indian domestic law and codifies the substance over form doctrine[2]. GAAR empowers tax authorities to re-characterize transactions that qualify as an impermissible avoidance arrangement. A transaction or structure qualifies as an impermissible avoidance arrangement if its

2. *Section 97 of the Income-tax Act, 1961.*

'main purpose' is to obtain a tax benefit, and it *inter-alia* results, directly or indirectly, in the misuse, or abuse, of the provisions of the Income-tax Act and/or lacks commercial substance. Moreover, a transaction is deemed to lack commercial substance if it involves the location of an asset or of a transaction or of the place of residence of any party which is without any substantial commercial purpose other than obtaining a tax benefit for a party. In the context of treaty shopping, the FAQs issued by the Central Board of Direct Taxes (CBDT)[3] acknowledge that if the jurisdiction of a foreign investor is finalized based on non-tax commercial considerations, GAAR will not be invoked merely on the ground that the investor is located in a tax friendly jurisdiction. Pending judicial scrutiny, the market's interpretation around GAAR and extant judicial anti avoidance rules has been that so long as an investor is able to demonstrate non-tax reasons for channelizing investments through a jurisdiction and that the situs of the significant people functions and decision-making connected with that investment sits within such jurisdiction, treaty benefits should be available (even where tax considerations impact the investment structure).

If the jurisdiction of a foreign investor is finalized based on non-tax commercial considerations, GAAR will not be invoked merely on the ground that the investor is located in a tax friendly jurisdiction.

The other key nuance surrounding GAAR is that it is a domestic law measure that overrides tax treaties. A key question that has often arisen is whether India can unilaterally override tax treaties through its domestic GAAR and if that would be in breach of its international law obligations. Some countries take the view that since taxes are imposed by way of domestic law, the abuse of tax treaties could also be characterized as an abuse of domestic law[4]. In this respect, the 2017 OECD Commentary notes *"where the application of provisions of domestic law and of those of tax treaties produces conflicting results, the provisions of tax treaties are intended to prevail. This is a logical consequence of the principle of pacta sunt servanda which is incorporated in Article 26 of the Vienna Convention on the Law of Treaties."* Here, a distinction has been drawn between abuse cases where taxpayers circumvent the limitations prescribed in the tax treaty



3. *CBDT circular no. 7 of 2017, dated 27.01.2017*
4. *2017 OECD Commentary*



(such as treaty shopping) versus cases where a person circumvents the provision of domestic tax law by using the tax treaty. In relation to the first, GAAR would have no conflict with a tax treaty, considering the proper construction of tax convention allows the Contracting State to disregard abusive transactions and would be in line with the object and purpose of tax convention[5]. However, in relation to the second category of cases the interaction between tax treaties and GAAR will need to be carefully evaluated. A PPT or LOB by itself may be deficient to address such a situation[6]. For instance, a case where a non-resident (with its core business operations in the country where it is resident) invests through an SPV to avoid the application of Indian indirect transfer rules.

Admittedly, the PPT is couched as the GAAR of tax treaties to combat treaty abuse (which supplements the existing specific anti avoidance rules such as the LOB clause in tax treaties). OECD's Final Report on Action Plan[7] 6 recognizes that a domestic GAAR could prevent treaty shopping, yet it was felt that a more direct approach involved the drafting of anti-abuse rules to be included in treaties. Under the PPT rule, if one of the principal purposes of transactions or arrangements is to obtain treaty benefits, these benefits would be denied unless it is established that granting these benefits would be in accordance with the object and purpose of the provisions of the treaty. Notably, in comparison to GAAR, PPT is more stringent. As OECD's Final Report on Action Plan 6 notes, the reference to "one

5. *OECD (2015), Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. http://dx.doi.org/10.1787/9789264241695-en*
6. *Ibid*
7. *See supra note 6.*

In case of tax treaties where the PPT has been incorporated pursuant to the MLI, the PPT would become effective from the date of effectiveness of the MLI in relation to the specific tax treaty (i.e. ratification of the MLI by the treaty partner).

of the principal purposes" in that obtaining benefits under a tax treaty need not be the sole or dominant purpose for the establishment, acquisition or maintenance of the person and the conduct of its operations. It is sufficient that at least one of the principal purposes was to obtain treaty benefits. This makes the PPT a higher threshold to satisfy. The final action report further provides that a purpose will not be a principal purpose when it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining the benefit was not a principal consideration and would not have justified entering any arrangement or transaction that has, alone or together with other transactions, resulted in the benefit. Therefore, from a practical standpoint the smell test underlying the subjective tests of GAAR and PPT would both look to business reasons and the commercial narrative underlying the transaction or investment structure. This becomes abundantly clear from the illustrations on the application of PPT that are set out under the Final Report on Action Plan 6. Some of the key indicia of substance would include the following:

- *Underlying rationale for locating the entity in the relevant jurisdiction (for instance, better access to skilled labor, reliable legal system, business friendly environment, political stability, sophisticated banking industry, membership of a regional grouping, etc.)*
- *History of the investor's legacy and business ecosystem in the relevant jurisdiction*
- *Listing on the stock exchange of the relevant jurisdiction*
- *Details of investments in countries other than India from the relevant jurisdiction (proportion of such investments)*
- *Significant people functions performed in the relevant jurisdiction (office space, number of employees, business expenses incurred in the relevant jurisdiction, qualifications and experience of the board and the senior management, operation and management of bank accounts in the relevant jurisdiction)*
- *Compliance with local substance requirements in the relevant jurisdiction*
- *In case of a fund, are the investors predominantly from a single jurisdiction or is the ownership structure broad based*
- *In case of an SPV, the commercial rationale for routing investments into India through such SPV (management of regional operations, proximity in time zones, ring-fencing certain investments, etc.)*

Prospective v. Retrospective application of PPT

With amendment of the India-Mauritius tax treaty to include the PPT, considerable confusion arose around the date of effectiveness of the PPT. The CBDT has clarified that in cases where the PPT has been negotiated bilaterally, the PPT would apply from date of entry into force of the tax treaty or the amending protocol that incorporates the PPT. In case of tax treaties where the PPT has been incorporated pursuant to the MLI, the PPT would become effective from the date of effectiveness of the MLI in relation to the specific tax treaty (i.e. ratification of the MLI by the treaty partner). Therefore,

the PPT will operate prospectively. Notably, prospectivity is seen from the viewpoint of taxes levied for tax years following the date of the PPT becoming effective. There is no grandfathering of income that is taxable in the tax years following the effectiveness of the PPT but emanates from investment structures or arrangements that may have been put into place pre-PPT era (unless the object and purpose of the tax treaty shields such income).

Contextual interpretation of PPT

The PPT results in the denial of tax treaty benefits unless it is established that granting these benefits would be in accordance with the object and purpose of the provisions of the treaty. As the Final Report on Action Point 6 notes this allows the person to whom the benefit would otherwise be denied the possibility of establishing that obtaining the benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the tax treaty. In the Indian context, the Supreme Court in the Azadi Bachao Andolan[8] case had discerned "encouragement of mutual trade and investment" as the objective and purpose of capital gains tax exemption under the India-Mauritius tax treaty. The Supreme Court went on to observe that "developing countries need foreign investments, and the treaty shopping opportunities can be an additional factor to attract them". Considering this, the guidance issued by the CBDT on the application of PPT[9] insulates the capital gains that were specifically grandfathered under the Mauritius, Singapore and Cyprus tax treaties from the PPT.

The Supreme Court went on to observe that "developing countries need foreign investments, and the treaty shopping opportunities can be an additional factor to attract them".

On the other hand, the Multilateral Instrument has also amended the preamble to tax treaties to provide that "the States that enter into a tax treaty intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements". The Final Report on Action Plan 6 further notes that since the title and preamble form part of the context of the tax treaty and constitute a general statement of the object and purpose of the tax treaty, they should play an important role in the interpretation of the provisions of the tax treaty. Therefore, the object and purpose of the tax treaty will merit evaluation on a case-to-case basis.

Conclusion

The Blackstone and Tiger case are presently pending before the Indian Supreme Court. The outcome of these cases will be critical to the development of treaty law and practice in India. However, there is little room to argue against the fact that there has been a significant policy shift in India and globally around combating treaty abuse. In such light, tax practitioners and foreign investors need to be meticulous in documenting a non-tax narrative to access treaty benefits going forward.

■

8. *See supra note 2.*
9. *CBDT circular 1 of 2025, dated 21.01.2025*

INTERPRETATION OF BENEFICIAL OWNERSHIP IN INDIA : A SHIFT IN JUDICIAL TRENDS?





Bijal Ajinkya
Advocate

Akshara Shukla
Advocate

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Overview

In this Article, the authors have explored the origin and evolution of beneficial ownership, globally and under Indian tax laws. The article explores the contours of definition of 'beneficial ownership' internationally as well as its usage in double taxation avoidance agreements entered into by India, for identifying taxation rights according treaty benefit. Not only this, beneficial ownership also forms the basis for anti-abuse mechanisms being introduced in the tax treaties for countering treaty abuse for profit shifting and tax evasion. Under domestic Indian tax laws, while 'beneficial ownership' has not been defined, the sufficiency of tax residency certificate for allowing treaty benefit to tax payers has been deliberated upon through delegated legislation and judicial pronouncements. This article analyses the course taken by the judiciary from accepting and reaffirming tax residency certificate as an objective requirement to avail treaty benefit to altering the approach and looking through the transactions to determine beneficially ownership, whether necessitated by tax treaties or not.

1. Introduction

Taxation laws across the globe are in continual phase of evolution. In last couple of decades, with transactions transcending borders, domestic and international tax governance has felt the need to redefine the traditional mechanisms of identifying the tax incidence and adopt a more fact based approach which is also globally aligned. The question is no longer limited to countries adopting a resident or source based taxation regime resulting in tussles over taxation rights. It has transcended to developing more hybrid set of rules which recognise actual control and economic rights over income and assets, as against conventional concepts of legal ownership. Hence, the concept of "beneficial ownership" has gained relevance in bilateral tax treaties and judicial interpretations, for allocating taxation rights and grant of tax treaty benefits.

The concept of "beneficial ownership" has gained relevance in bilateral tax treaties and judicial interpretations, for allocating taxation rights and grant of tax treaty benefits.

Even though beneficial ownership has been a subject matter of legislative and judicial deliberation, it has neither been defined under the domestic tax laws of India nor

under the bilateral tax treaties. Back in 2003, Financial Action Task Force (**FATF**) Glossary introduced the definition of 'beneficial owner' as natural person(s) who ultimately owns or controls a legal person and/or the natural persons on whose behalf transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.

As a corollary to this, where recipient of an income acts only in capacity of an agent or a nominee, they would not be considered as a beneficial owner of such income for the purposes of application of tax treaty.

Subsequently, in 2019, OECD published a Beneficial Ownership Implementation Toolkit (**Implementation Toolkit**) which was developed by Inter-American Development Bank and Global Forum on Transparency and Exchange of Information for Tax Purposes. For this purposes the Implementation Toolkit adopted the definition of FATF Glossary and defined 'beneficial owner' as natural persons who ultimately owned or controlled a legal entity or arrangement, such as a company, a trust, a foundation etc.

Thus, concept beneficial ownership goes beyond the contours of legal ownership and is a factual determination involving a substance over form approach which takes into account several factors such as decision-making authority, risk assumption, economic reality etc.

Recognising Beneficial Ownership in Tax Treaties

Under tax treaties, beneficial ownership is used as a mechanism to identify taxation rights especially with respect to passive incomes. Under the OECD model of Tax Treaties taxation rights on such passive income are granted to the contracting state in which the beneficial owner resides. Similarly, even the UN Model of Tax Treaties acknowledge beneficial ownership for incomes such as dividends, royalty, interest and even fees for technical services (FTS) for the purposes of identifying taxation rights.

In this context and based on the principles laid out in OECD Model Tax Convention on Income and Capital, 2017, beneficial ownership has been recognised as having recipient's unconstrained right to enjoy the income earned, without there being any obligation on such recipient to pass on such income. As a corollary to this, where recipient of an income acts only in capacity of an agent or a nominee, they would not be considered as a beneficial owner of such income for the purposes of application of tax treaty.

India's tax treaties with several countries such as United States, United Kingdom, Singapore and Mauritius provide for reduced rate of withholding tax for dividend or interest income if the beneficial owner of the dividend is tax resident in the contracting countries. Similarly, even for income in the nature of Royalty and FTS, India's tax treaty with countries such as US, UK, Singapore provides a cap on rates of taxation in the source state



on such income if the beneficial owner of such income resides in the other contracting state.

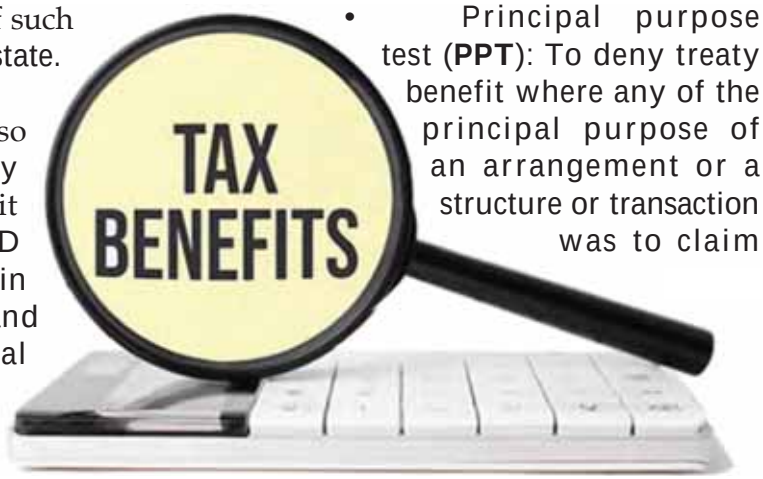
Identification of beneficial ownership also forms basis for framework developed by OECD to counter treaty abuse and profit shifting to low tax jurisdictions. OECD along with G20 nations launched certain action plans to address Base Erosion and Profit Shifting (**BEPS**) by multinational corporations. To implement these measures, BEPS Action Plan 15 introduced multi-lateral instrument (**MLI**). For the MLI to be effective, countries which have a tax treaty in place are required to sign the MLI and notify such tax treaty as a covered tax agreement (**CTA**). Countries that signed MLI and notified the tax treaty as CTA are required to implement the following, as a minimum standard, in such CTA:

(a) An express statement stating a common intention for eliminating double taxation without creating opportunities for tax evasion or avoidance which result in no tax or reduced tax; and

(b) Implementation of either of the following:

- Limitation of benefit (**LOB**) clause: This ensures that the treaty benefit is limited to only 'qualified persons' i.e. persons having sufficient presence in the relevant jurisdiction based on their legal nature, ownership and activities.

Tax treaties between India and various other countries (for instance, Singapore, Netherlands, Japan, UK, Luxembourg, UAE) have been notified as a CTA which now includes PPT as a minimum standard.



- Principal purpose test (**PPT**): To deny treaty benefit where any of the principal purpose of an arrangement or a structure or transaction was to claim such benefit, unless such benefit is in accordance with the object and purpose of the relevant provisions of the tax treaty.

- A combination of LOB and PPT i.e. inclusion of PPT with a simplified or detailed LOB clause

Pursuant to above, tax treaties between India and various other countries (for instance, Singapore, Netherlands, Japan, UK, Luxembourg, UAE) have been notified as a CTA which now includes PPT as a minimum standard. Accordingly, entities that are tax resident of countries which have included PPT in their tax treaties with India could be required to demonstrate that none of the principal purpose of their arrangement or structure was to claim the tax treaty benefit.

As recent as on 21 January 2025, India has also notified detailed guidance for application of PPT under its tax treaties. The Central Board of Direct Taxes (**CBDT**), vide Circular No. 1 of 2025 dated 21 January 2025, has clarified that PPT provisions under tax treaties entered into by India are intended to be applied only prospectively. Further, it has also been clarified that bilateral commitments made by India in the form of grandfathering provisions under its tax treaties entered into with

jurisdictions such as Cyprus, Mauritius and Singapore, shall remain outside the purview of PPT provisions. However, there are still certain key countries that have not notified tax treaty with India as a CTA (including US and Mauritius).

Evolution of beneficial ownership in India for application of treaty benefit

As stated above, several tax treaties entered into by India with different jurisdictions provide for a reduced rate of taxation with respect to certain passive incomes such as dividends, royalty or FTS, if the beneficial owner of such income is tax resident in the other contracting jurisdiction.

Income Tax Act mandates furnishing of a valid tax residency certificate (TRC) by the non-resident income recipient, which is issued by its home jurisdiction for the relevant year.

India follows a mix of source based and residence based taxation and therefore where such income of non-residents is sourced in India it may be subjected to tax in India under the provisions of Income Tax Act, 1961 (**Income Tax Act**). However, Income Tax Act, through section 90 sub-section (2) provides for non-residents to be taxed as per the beneficial provisions of the applicable tax treaty, however, the application of the tax treaty and the beneficial provisions therein, is not automatic.

Income Tax Act mandates furnishing of a valid tax residency certificate (**TRC**) by the non-resident income recipient, which is issued by its home jurisdiction for the relevant year. Over time, relevance of TRC was reinstated through delegated legislations of Central Board of Direct Taxes (**CBDT**).

CBDT, vide Circular No. 682 dated 30 March 1994 (**Circular No. 682**), had clarified that any resident of Mauritius, deriving capital gains from alienation of shares of Indian Companies, will be taxable on such capital gains in Mauritius only, under the Mauritius Tax law, with no liability arising under Indian tax law. The Circular was clarificatory nature and did not make a distinction on the residential status of legal owner and the beneficial owner of such capital gains. Given the same, upon reading section 90(2) with Circular No. 682, it was clear that residency (determined through TRC as provided under Income Tax Act) was given precedence over and above the concept of beneficial ownership. This was further supported by the language of India Mauritius Tax Treaty, wherein beneficial ownership was applied for incomes in the nature of dividends, interest and FTS but not for capital gains.

Subsequently, vide Circular No. 789 dated 13 April 2000 (**Circular No. 789**) pertaining to dividends earned by Mauritius based investors, CBDT further clarified that furnishing a TRC was sufficient proof of status of residence as well as beneficial ownership for applying the treaty benefits under India Mauritius tax treaty.

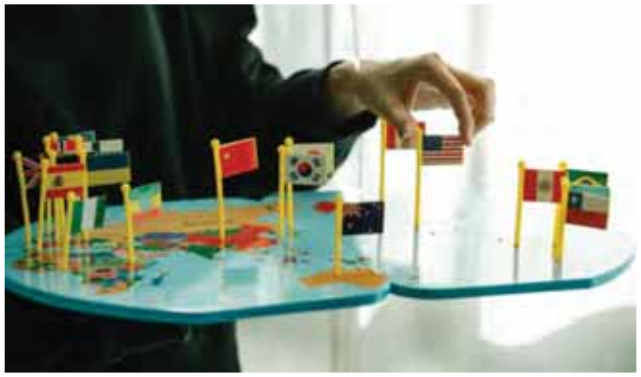
However, the objective condition of furnishing TRC has been put to test by judiciary upon allegations treaty abuse and in certain



instances Indian Courts have resorted to adopting a substance over form approach to accord or deny treaty benefit. One of the earliest instances was the challenge of the vires of Circular No. 789 in the case of ***Union of India vs. Azadi Bachao Andolan [2003] 132 Taxman 373 (SC)***. While upholding the validity of the said Circular No. 789, which mandated furnishing of TRC, the Supreme Court also recognised the concept of 'treaty shopping' and in such instances, acknowledged the requirement of courts to overlook the formal structure to look through the economic substance of the transaction.

The question of conclusive nature of TRC was again deliberated by Supreme Court in the case of ***Vodafone International Holdings B.V. vs. Union of India [2012] 17 taxmann.com (SC).*** Even here, while Supreme Court did uphold the conclusive nature of TRC as mandated under Circular No. 789, it also observed that the same would not deter the tax authorities to question the role of overseas corporate bodies in subterfuge structures which are devised with the intention to evade tax. Thus, the Supreme Court took the view that while TRC can be treated as conclusive evidence of residential status for applying tax treaty benefit, its relevance can be overlooked in instances of treaty abuse.

As a consequence of the landmark litigation of ***Vodafone International Holdings (supra),*** the Income Tax Act was retrospectively amended



to accommodate source based taxation of capital gains from indirect transfers. However, the impact of such retrospective amendment on provisions of tax treaties was evaluated by Andhra Pradesh High Court in ***Sanofi Pastuer Holding SA vs. Department of Revenue, Ministry of Finance [2013] 30 taxmann.com 222 (Andhra Pradesh)***, wherein shares of an SPV, incorporated in France and having wholly owned subsidiary in India, were sold by the shareholders in France to another French entity. Before Andhra Pradesh High Court the tax authorities argued that the transaction warranted piercing of corporate veil and that French SPV was colourable device engineered for tax avoidance. It was the contention of the tax authorities that the shareholders of the French SPV (i.e. the Sellers) were the beneficial owners of the shares of Indian wholly owned subsidiary, therefore, sale of shares of target French SPV may be deemed as alienation of shares of Indian subsidiary and accordingly taxable in India. The High Court, while rejecting the contention of tax authorities, had held that taxation rights on gains arising from alienation of shares in this case were to be determined as per Article 14(5) India France tax treaty, which allocates the taxation rights to France. The said clause (5) of Article 14 did not incorporate a "see through" approach and accommodating the same would transgress the negotiated terms of India France tax treaty. Thus, the capital gains arising from such transaction, which have been allocated to France under tax treaty, would be subjected to double tax in both India and France by an artificial and strained construction of Article 14(5). Thus, to accord certainty to terms of tax treaty, evaluation of beneficial ownership was denied by the High Court where articles of tax treaty did not warrant the same.

Further on, Punjab & Haryana High Court, in the case of ***Serco BPO (P.) Ltd. vs. Authority for Advance Rulings, New Delhi [2015] 60***

While beneficial ownership has been used under tax treaties to provision for tax treaty benefits on passive income, tax authorities have time and again used the beneficial ownership test to evaluate tax treaty benefit on capital gains in the hands of non-resident assessee.

taxmann.com 433 (P&H), also adjudicated on relevance of beneficial ownership while determining the taxation rights on capital gains arising in the hands of Mauritius based shareholders of Indian Company. Before the High Court the tax authorities had contended that since the Mauritius based shareholders had no other business interest in Mauritius, they were to be treated as subterfuge entities designed for tax avoidance through Mauritius. Given this, the tax authorities argued for rejection of TRC of Mauritius based shareholders and that beneficial ownership of shares of Indian target was with the shareholders of Mauritius entities. Hence, India Mauritius tax treaty could not applied to determine taxation rights on capital gains arising from sale of shares of Indian target in this case. The High Court rejected the application of beneficial ownership test by tax authorities and upheld the sanctity of Circular No. 789. As per the High Court, the said Circular No. 789 was a statutory circular issued under section 119 of the Income Tax Act basis which, it was incumbent on Indian tax authorities to accept the TRC. As per High Court, questioning the validity of TRC issued by Mauritius tax authorities may be considered to be in contravention to the tax treaty between the two countries and a resultant erosion of faith and trust reposed by both jurisdictions in each other.

Furnishing of TRC was also considered sacrosanct by the Bombay High Court in the case ***Director of Income Tax (IT) vs. Universal International Music B.V. [2013] 31 taxmann.com 22 (Bombay)***, to allow non-resident assessee to avail the benefit of lower tax rates on royalty income under the India Netherlands DTAA.

While beneficial ownership has been used under tax treaties to provision for tax treaty benefits on passive income, tax authorities have time and again used the beneficial ownership test to evaluate tax treaty benefit on capital gains in the hands of non-resident assessee. Interestingly, this approach was resented by Mumbai bench of Income Tax Appellate Tribunal (**ITAT**), in the case of ***Blackstone FP Capital Partners Mauritius V Ltd vs. Deputy Commissioner of Income Tax International Taxation [2022] 138 taxmann.com 328 (Mumbai – Trib.)***, wherein the Mumbai Bench has questioned the adoption of beneficial ownership test to deny treaty benefit on capital gains. The tax authorities had objected to claim of India Mauritius Tax Treaty benefit by a company tax resident in Mauritius, on account of Mauritius company being a wholly owned subsidiary of a Cayman Island entity. Thus, the tax authorities alleged that Cayman Island entity was in fact the beneficial owner of capital gains and therefore benefits of India Mauritius Tax Treaty could not be extended on such capital gains. The ITAT, however, dismissed the allegation of tax authorities and held that wherein tax treaties expressly provide for beneficial ownership as sine qua non for entitlement to treaty benefit for certain income streams, in absence of such express provision, application of the same cannot be inferred or assumed. Thus, where tax treaty article governing capital gains does not require beneficial ownership as a prerequisite to avail treaty benefit, the same cannot be read into it.

Thus, in so far as the above rulings were concerned, the judiciary did not question the conclusive nature of TRC to accord treaty benefit unless there was an implication of

treaty abuse. Until as recent as in 2023, this position was reiterated by Delhi High Court in ***Blackstone Capital Partners (Singapore) Vi Fdi Three Pte. Ltd. vs. ACIT [2023] 146 taxmann.com 569 (Delhi)***, where the Delhi High Court held that the TRC is the only statutory evidence to determine eligibility for tax treat benefit. Thus, the attempt of revenue authorities to go beyond TRC was considered inconsistent with Indian Government's policy and assurances to Foreign Investors. However, the ruling of Delhi High Court was appealed against before the Supreme Court and the Supreme Court stayed the application of Delhi High Court ruling.

The stay granted by Supreme Court can be seen as symbolic of a gradual yet noteworthy shift in judicial perception on relevance of TRC. In 2020, Authority of Advance Ruling (**AAR**) in the case of ***Tiger Global International III Holdings, In re [2020] taxmann.com 878 (AAR – New Delhi)*** denied tax treaty benefit to the Mauritius Shareholder by identifying US tax resident as the beneficial owner of the shares being alienated. The AAR held that the entire arrangement was prima facie being undertaken with the intention of avoiding taxes in India.



On appeal before the High Court, the AAR ruling was overturned and the High Court held that tax authorities could go beyond TRC to invoke substance over form test only for subterfuge arrangements created for tax avoidance. However, the onus would then be on tax authorities to establish that such transactions were sham or colourable and mandated piercing of corporate veil. The High Court also held that beneficial ownership test could only be invoked in situations where taxpayers hold assets in trust with a legal obligation of passing on the income to the beneficial owner. However, the ruling of Delhi High Court has also been stayed as a consequence of the special leave petition filed by assessee before the Supreme Court and the much anticipated verdict of the Supreme Court has now been reserved.

However, prior to ruling of Delhi High Court being stayed, Delhi Bench of ITAT, in the case of ***SC Lowy P.I. (LUX) S.A.R.L, vs. ACIT [2025] 170 taxmann.com 475 (Delhi – Trib)***, relied on the Delhi High Court ruling in Tiger Global (supra) and allowed a SEBI Registered CAT – II Foreign Portfolio Investor to claim benefits under the India-Luxembourg tax treaty. As per ITAT, TRC of the taxpayer along with satisfaction of conditions under LOB clause of tax treaty was sufficient for allowing taxpayer to claim tax treaty benefit. Tax Authorities were not allowed to question the arrangement, unless anything

cogent was brought on record to doubt the principal purpose of the transaction which directly resulted in benefit under the tax treaty.

Conclusion

Interestingly, the judicial discord over the final word of TRC is not just restricted to Indian Courts. The position is deliberated upon globally. For instance, Spanish Supreme Court in the case of ***Don Artemio [TS-427-FC-2023]*** has also held that validity of TRC issued by the government of another contracting state cannot be outrightly challenged and conflict of tax residency can be resolved by resorting to tie breaker rules under the DTAA. However, Supreme Court of Italy in the case of ***Ovvio Italia spa [TS-118-FC-2021(ITL)]*** has held that TRC is not the decisive test for establishing beneficial ownership. The burden of proof has been laid on the taxpayer to establish beneficial ownership.

Interestingly, the judicial discord over the final word of TRC is not just restricted to Indian Courts. The position is deliberated upon globally.

Thus, while the Circular No. 789 continues to hold good and TRC is still considered an objective test for determining applicability of tax treaty and the benefits therein, it may not have the final word with respect to determination of Beneficial Ownership. Judicial authorities have shown inclination to go beyond TRC and adopt a more subjective approach for evaluating tax residency and application of treaty with respect to granting treaty benefits for capital gains as well as dividends, interest income and royalty income. While onus of establishing the requirement to pierce the corporate veil is still on the tax authorities, Indian courts appear to be open to the idea of adopting a look through approach rather than only relying on TRC.

Having stated the above, the application of 'beneficial ownership' for identifying taxation rights and availing treaty benefits in case of passive incomes has to be viewed separately from its usage for identifying taxation rights on capital gains. The specific question of applying beneficial ownership test for capital gains would require additional judicial examination considering the language of tax treaties do not require beneficial ownership to be evaluated for capital gains. Thus, TRC continues to be the only objective requirement. However, with anti-abuse provisions such as PPT and LOB being put in place, the Indian court may go beyond TRC to examine the substance of a transaction and identify subterfuge structures being used for tax evasion. For this purpose, the term 'beneficial ownership' may be considered as being generically used to pierce the corporate veil and identify instances of treaty abuse. On the other hand, in cases of passive incomes such as dividends, interest income, FTS or Royalty, the language of tax treaties itself provide for 'beneficial ownership' to be ascertained. In such a case, furnishing TRC simpliciter may not suffice despite the requirement under Income Tax Act and the CBDT Circulars. Thus, while the taxpayer may rely on the TRC, being an objective establishment of tax residency, the tax administration may not and may proceed to adopt look through approach for determining beneficial ownership.

DECODING THE MEANING OF PLACE OF EFFECTIVE MANAGEMENT : A COMPREHENSIVE ANALYSIS





CA Vinita Krishnan *CA Sneh Shah*

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Overview

*The concept of Place of Effective Management (**"POEM"**) has become a pivotal factor in determining the tax residency of companies under international tax law. It is especially relevant in the context of cross-border and outbound structures, where companies are incorporated in one jurisdiction but have their controlling shareholders and key decision makers in the other. Similarly, in the case of certain fund structures, the location of decision-making is vital in establishing tax residency and corresponding tax implications. With increasing globalization and complex cross-border arrangements, understanding and applying POEM rules is crucial for ensuring compliance with tax regulations and avoiding unintended tax consequences. This article explores the POEM rules under Indian tax law including certain key principles set out in Indian judicial precedents, and India's position as compared to the global standards in this regard.*

Evolution of the Concept of Poem under Indian Tax Law

Until 2017, Indian domestic law deemed a foreign company a tax resident of India only if its control and management was situated wholly in India. For non-corporate entities (such as partnerships, trusts, and associations of persons other than individuals), the residency test has always been based on the control and management being wholly in India. However, the concept of POEM was prevalent under India's tax treaties, as the tie-breaker test in case of dual residency of corporate / non-corporate taxpayers other than individuals. That said, neither Indian domestic law nor the treaties provided any guidance or rules for determination of such situs of "control and management" and hence historically, the principles in this regard have largely been derived from judicial precedents.

With increasing globalization and complex cross-border arrangements, understanding and applying POEM rules is crucial for ensuring compliance with tax regulations.

Since 2017, a foreign company is considered a tax resident if its POEM is in India.

Interestingly, the Multilateral Instrument (**MLI**)[1] has modified Article 4 (residency) of the tax treaties to replace POEM as the tie breaker test; with a resolution based on Mutual Agreement Procedure (MAP). India has not made any reservations with respect to Article 4 and hence India's tax treaties will be modified to this extent[2], with other countries that have not stated any reservations. Hence, while as on date, POEM is the test for corporate residency under Indian domestic law, the tie-breaker test under India's tax treaties (to the extent of Covered Tax Agreements[3] under the MLI) no longer provide for POEM as the relevant test. Having said that, Article 4 (under the MLI) does provide for the competent authority to consider factors such as POEM in cases of dual residency of all persons other than individuals.

A safe harbour provision is prescribed whereby the POEM test would not apply to foreign companies having a turnover or gross receipts of up to INR 50 crores in a financial year.

With the introduction of POEM as the test of corporate residency under Indian domestic law in 2017, the Government of India (GoI) also introduced certain guiding principles for determination of POEM (**"POEM Rules"**) which set out certain objective and subjective criteria for determination of POEM. Hence as on date, the POEM Rules form India's basis of evaluating the jurisdiction in which a company could be considered as having its POEM. However, a safe harbour provision



is prescribed whereby the POEM test would not apply to foreign companies having a turnover or gross receipts of up to INR 50 crores in a financial year. For completeness, if a foreign company is deemed to have a POEM in India, some of the consequences include: (a) its global income would be taxed in India at 38%, and (b) it would not be eligible for tax treaty benefits.

OECD Position on POEM and India's Stance in this Regard

As per the OECD commentary, POEM would be the place where:

(a) The entity is actually managed; or

(b) key management and commercial decisions that are necessary for the conduct of the entity's business as a whole are made.

While as on date, the definition of POEM under Indian domestic law is borrowed from (b) above, it is interesting to note that India had earlier expressed a reservation against this definition on the basis that the place where the main and substantial activity of an entity is

1. *The MLI is a result of the ambitious G20/OECD BEPS Project, a collaborative initiative by multiple jurisdictions to mitigate Base Erosion and Profit Shifting (BEPS). The MLI modifies the application of tax treaties globally without the necessity for separate bilateral amendments.*
2. *In terms of certain key tax treaties – (a) India's tax treaties with USA and Mauritius are not covered by the MLI (USA is not a signatory to the MLI) and (b) Singapore has expressed a reservation against Article 4; and hence POEM continues to be the tie-breaker test under these treaties. As regards India's tax treaties with the Netherlands and UK – they are modified by the MLI and hence the MAP procedure shall apply.*
3. *Covered Tax Agreements essentially refer to existing bilateral tax treaties between jurisdictions that have opted to modify their agreements based on the MLI.*

carried out, should also be taken into account when determining the POEM.

The OECD does not provide any specific criteria for determination of POEM, but notes some factors which are relevant to consider for determining POEM such as the location where the board of directors or equivalent body typically meets, where senior day to day management is carried out, etc. Indian domestic law on the other hand, has provided for specific rules and defined criteria (under POEM Rules) basis which the POEM of a company is to be determined. As mentioned, the POEM Rules provide for a primary test based on "active business", a concept which is not suggested or considered by the OECD or UN in the context of POEM.

In 2017, the OECD replaced POEM as the tie-breaker test for dual residency under tax treaties with a resolution based on MAP. Article 4 of the MLI aligns with this change, and India has not opposed it, showing consistency with the OECD. However, India's POEM rules presume that if a company's POEM exists both in India and another country, it's POEM will be considered to be in India if predominantly managed from India. Typically, tax treaties do not define the tie-breaker rule, allowing contracting states to use their domestic law definitions unless the context otherwise requires. This stance can make resolving issues through MAP cumbersome and lengthy, leading to potential hardship and tax uncertainty.

Indian Jurisprudence on The Meaning of "Control and Management" and Corporate Residency

As mentioned, until the introduction of the POEM Rules, there were no defined criteria

India's POEM rules presume that if a company's POEM exists both in India and another country, it's POEM will be considered to be in India if predominantly managed from India.

for determining the situs of "control and management" and hence principles were derived from judicial precedents in this regard. Additionally, some of these precedents pertain to the test of residency under erstwhile law (requiring control and management to be situated wholly in India), with POEM being a comparatively stricter concept. That said, while the POEM Rules are now introduced, the principles set out in these precedents would still be relevant in terms of interpretation of the subjective criteria as set out in the POEM Rules. An overview of certain key precedents in this regard is provided below.

The old and established – setting the principles of the concept of "control and management"

The House of Lords' decision in the case of ***De Beers Consolidated Mines Ltd [1906]***[4] marks the origin of numerous Indian precedents regarding corporate residency, as well as the interpretation and situs of "control and management". In this landmark decision, the House of Lords famously stated:

"In applying the conception of residence to a company, we ought, I think, to proceed as nearly as we can upon the analogy of an individual. A company cannot eat or sleep, but it can keep house and do business. We ought, therefore, to see where it really keeps house and does business. An individual may be of foreign nationality, and yet reside in the United Kingdom. So may a

4. *5 TC 198 (HL)*

company. Otherwise, it might have its chief seat of management and its centre of trading in England, under the protection of English law, and yet escape the appropriate taxation by the simple expedient of being registered abroad and distributing its dividends abroad."

The House of Lords in this decision also noted that for the purpose of income tax laws, a company resides where its real business is carried on, and the real business is carried on where the central management and control actual abides.

Relying on the De Beers decision, the Supreme Court of India in the case of ***V.V.R.N.M Subbaya Chettiar [1950]***[5], observed that the "control and management" of a company is where the "head and brain" is situated; and the term "situated" implied the functioning of such power at a particular place with some degree of permanence. Additionally, the court observed that the expression "control and management" means de facto control and management and not merely the right or power to control and manage. These principles have been upheld by Indian courts in several other precedents.

The aforesaid decisions have all been considered and upheld by the Supreme Court in the recent case of *Mansarovar Commercial Private Ltd. [2023].*

Thereafter, the High Court of Bombay, in the case of ***Narrotan and Pereira Ltd [1953]***[6] set out the following important principle:

In construing the expression "control and management" it is necessary to bear in mind the distinction between doing of business and the control and management of business. Business and the whole of it may be done outside India and yet the control and management of that business may be wholly within India.

Another salient principle was observed by the Supreme Court in the case of ***Erin Estate [1959]***[7] in the context of de jure right to control. The court in this case observed as under:

Theoretically, if the partners reside in India they would naturally have the legal right to control the affairs of the firm which carries on its operations outside India. The presence of this theoretical de jure right to control and manage the affairs of the firm which inevitably vests in all the partners would not by itself show that the requisite control and management is situated in India. It must be shown by evidence that control and management in the affairs of the firm is exercised, may be to a small extent, in India before it can be held that the control and management is not situated wholly without the taxable territories.

Hence, this principle of the Supreme Court could be interpreted to mean that the situs/ residency of the directors of a company (being the persons in charge of the management of the company) would not by itself be indicative of the situs of control and management.

The aforesaid decisions have all been considered and upheld by the Supreme Court in the recent case of ***Mansarovar Commercial Private Ltd [2023]***[8]. Briefly, the facts of this case concerned certain companies registered in Sikkim, wherein basis several factors it was

5. *19 ITR 168 (SC)*
6. *23 ITR 454 (Bom)*
7. *MANU/SC/0080/1958 : 1959 SCR 573;*
8. *MANU/SC/0080/1958 : 1959 SCR 573;*

observed that the control and management of such companies was effectively granted to an accountant based in India. The Indian accountant essentially had the authority to determine who the directors of the Sikkim companies should be and also had in its possession the blank cheque books, rubber seals and books of account of the companies. Further, the bank accounts were operated by persons resident in India. The Supreme Court in this case emphasized on the concept of de facto control and power (and not de jure control and power) and held that the control and management of the Sikkim companies was in fact with the accountant and hence resided in India.

In the context of an outbound structure:

Decision of the Income Tax Appellate Tribunal ("ITAT") Delhi in the case of Radha Rani [2007][9]:

This case pertained to a company incorporated in Singapore, whose 99% shareholding was held by "G" (a resident in India) and 1% shareholding was held by J (a resident of Singapore). Both G and J were directors of the company having equal voting power. The company did not have any employees in Singapore and the office in Singapore was used merely for registered address purposes. The tax officer noticed that while a board meeting of the company was held in Singapore, G was present in India at the time the board meeting was held; and accordingly contended control and management of the company was wholly in India.

The ITAT Delhi ruled in favour of the company on the basis of the following principles:



- The ITAT Delhi first reiterated the well-settled principle that "control and management" did not mean the carrying on of day-to-day operations.
- It further noted that while the situs of the board of directors should determine the place of control and management, this does not mean where one of the directors normally reside, but where the board actually meets for the purpose of determination of key issues relating to the company.
- In the days of technological advancements conducting meetings by telephonic conversations or video conferencing process is very much prevalent in the world and, therefore, the actual presence of a person at the exact place of meeting or conference may not be necessary.
- The operation of bank account of the company by 'G' alone would not determine the position and status of control and management as such power had been conferred on her in the board meeting held in Singapore.

9. 16 SOT 495 (Del)

This decision establishes important principles that are relevant today, emphasizing that the residency of directors is not crucial, and highlighting that physical presence is not necessary, especially in light of modern technological advancements.

- With respect to the tax officer's contention that affairs of the company mainly comprised and related to matters in India like funds, investments and loans, the ITAT Delhi noted that what is relevant is from where the business is being conducted rather than where it is actually conducted.

This decision establishes important principles that are relevant today, emphasizing that the residency of directors is not crucial, and highlighting that physical presence is not necessary, especially in light of modern technological advancements.

In the context of investment structures:

Decision of the Authority for Advance Rulings ("AAR") in the case of Moody Analytics USA [2012][10]:

This case concerned the sale of shares of an Indian company (**"CRIL**") by a company incorporated in Mauritius (**"CMRL"**). CMRL sought to claim the exemption under the India-Mauritius tax treaty, however the tax department challenged the same on the basis that, the control and management was with an individual (**"RK"**) based in the UK, who pursuant to a business advisory agreement, was allegedly in charge of management of the entire transaction at his own discretion.

The court, however, observed that RK was given the authority to manage the transaction only basis the decision of the board of directors of CMRL. Further, RK was just taking care of the details of the transaction as authorized by the board of directors of CMRL, but his role in the transaction did not indicate that the control and management of CMRL was vested in him. Hence, CMRL was entitled to claim the benefit of the tax treaty.

Decision of the ITAT Delhi in the case of Saraswati Holding Corporation Ltd. [2005][11]

This case pertains to a situation wherein a company incorporated in Mauritius had authorized three persons in India (via a power of attorney (**POA**)) to carry out its India investment activities and such POA holders were entitled to take decisions on behalf of the company. The tax officer noted that investments and divestments were made in a short span of time of 3 to 4 days and hence this indicated that active decisions were taken in India.

However, the Tribunal noted that the POA merely granted the individuals the right to conduct the day-to-day affairs of the business in India and this was not sufficient basis to conclude that the control and management of the company was in India. The Tribunal observed as follows:

"The words 'control and management of affairs' refer to head and brain, which direct the affairs of policy, finance, disposal of profits and such other vital things consisting the general and corporate affairs of the company"

10. *24 taxmann.com 41*
11. *16 SOT 535 (Del)*

Decision of the AAR in P. No. 10 of 1996:

In this decision, the AAR reviewed a typical fund structure comprising an Investor Company (**"IC"**), Investment Manager (**"IM"**); investment company, advisory board and investment advisors.

With respect to the IC, the AAR held that as per Article 4(3) the POEM of a Mauritian company had to be either in India or Mauritius and could not lie in a third country. Further, basis factors such as (a) local directors having appropriate calibre; (b) company secretary being resident in Mauritius; (c) registered office and accounting records being in Mauritius; and (d) board meeting being chaired in Mauritius – the POEM of the IC could be considered as in Mauritius.

As regards the IM, the AAR noted that certain additional factors had to be considered given the role of the investment committee, advisory board and Indian investment advisors. However, the AAR noted that though the IM had certain restrictions placed on its functioning by the introduction of such other bodies; the final decision rested with the IM's own board of directors. Further, regardless of any delegation, the IM remained responsible for all decisions and acts of any delegate. Additionally, while the IM would to a considerable extent rely on the investment advisors, the investment advisor did not have any decision-making authority. Accordingly, the POEM of the IM was not in India.

Notably, Indian tax law includes a specific regime under which a foreign fund can be exempt from the POEM provisions, provided it meets certain prescribed criteria. However, these criteria are quite stringent, and as a result, only a limited number of fund structures have opted for this regime to date.

Central Board of Direct Taxes ("CBDT") issued Circular 789 of 2000/ Circular 1 of 2003 and certain landmark judicial precedents:

While evaluating the entitlement of Mauritian residents to tax treaty benefits under the India-Mauritius Tax Treaty, Revenue authorities have often sought to evaluate whether the 'control and management' of such Mauritian entity is located in Mauritius. In this regard, the CBDT issued Circular 789 of 2000 which stated that a tax residency certificate (**TRC**) issued by Mauritian authorities will constitute sufficient evidence for accepting the status of residence as well as beneficial ownership for applying tax treaty benefits. However, Circular 1 of 2003 clarifies that in case of situations where a company was considered as tax resident of both India and Mauritius, residency would have to be determined as per the tie-breaker test (i.e., based on the POEM of the entity). Both circulars continue to have a binding force.

Circular 789 of 2000 was upheld by the Supreme Court in the case of ***Azadi Bachao Andolan***[12]. However, entitlement to benefits under the India-Mauritius tax treaty continues to be a contentious issue, with Revenue authorities continuing to invoke the control and management test while evaluating the residential status of Mauritian entities. In the case of ***in re: AB Mauritius***[13], AAR Delhi denied benefits under the India-Mauritius tax treaty to a Mauritian entity for the reason, inter-alia, that such entity was not controlled by the board of directors in Mauritius and was instead controlled by the parent company situated in the United States. Similar rulings

12. 263 ITR 706 (SC)
13. [2018] 90 taxmann.com 182 (AAR - New Delhi)

were rendered by the AAR in the case of ***Bid Services Division***[14] and ***Tiger Global International II Holdings***[15] as well, wherein the control and management test was applied to determine the residential status of the Mauritian entity. However, the AAR's rulings in Bid Services Division and Tiger Global International II Holdings were quashed by the Bombay[16] and Delhi High Court[17] respectively, which deferred to the TRC of the entities in line with Circular 789 of 2000.

It may be noted that the issue of whether control and management test can be applied to evaluate the residential status of a Mauritian entity (i.e., in the absence of any allegation of such entity also being an Indian resident under the IT Act) is presently sub-judice before the Supreme Court in the case of ***Tiger Global International II Holdings***[18], wherein the revenue authorities have filed a special leave petition against the favorable ruling of the Delhi High Court.

Precedents in the context of the shipping sector

Decision of the ITAT Mumbai in the case of Integrated Container Feeder Service [2005][19]

This decision pertained to a company incorporated in Mauritius, engaged in the operating of ships in international traffic from India. The company claimed that its effective management was located in Mauritius on the basis that the meetings of its board of directors took place in Mauritius and important policy decisions were taken in such meetings.

The ITAT Mumbai held against the company. It observed that while the board meetings of the company were held in Mauritius, the meetings were held just as necessary formalities to maintain its corporate status and to obtain a Tax Residency Certificate. In reality, all instructions and correspondence to the shipping agents were made from Dubai (where the owners were based); and all the staff, officers and captain were sitting in Dubai. Further, the company did not bring any evidence on record to depict that any activities were conducted from Mauritius other than the holding of board meetings. Lastly, with respect to the CBDT Circular 789 (upholding the validity of a TRC as a complete test for residency); the Tribunal noted that the circular was applicable for specific articles and not relevant as far as Article 8 was concerned.

Decision of the ITAT Mumbai in the case of Bay Lines (Mauritius) [2018][20]

In a similar decision, the ITAT Mumbai denied the benefits of Article 8 (Shipping and air transport) to a company incorporated in Mauritius on the basis that the POEM of the company was neither in Mauritius or in India and was in a third country (UAE) and hence the benefits of Article 8 were not available in such case. The Tribunal, basis a perusal of board minutes, noted that all key decisions were left to an agent based in the UAE and were of routine nature. The Mauritian resident directors on the board of the company were present only to satisfy the requirements of the Mauritius government and key policy decisions were taken in UAE where the

14. (AAR No. 1270 of 2011, dated 17 February 2020).
15. (AAR Nos. 4,5 & 7 of 2019, AAR - Delhi)
16. [2023] 148 taxmann.com 215 (Bombay)
17. [2024] 165 taxmann.com 850 (Delhi)
18. SLP(C) No. 002640 - / 2025
19. 96 ITD 371 / 278 ITR (AT) 182 (Mum)
20. TS-73-ITAT-2018(Mum)

shareholders were based. Importantly, the Tribunal upheld the principle set out in Klaus Vogel's commentary as per which if the effective management of a company was not situated in one of two contracting states but was in a third state, the benefits of Article 8 would not be available.

Interplay of the above Judicial Precedents with the Poem Rules

The precedents from Indian courts discussed above, all predate the introduction of the POEM Rules and it is therefore, now necessary to assess how these principles set out by the judiciary, align with the POEM Rules.

The overarching principle set out in the Indian precedents i.e., it is de facto control and management and not de jure control and management, aligns with the basis of the POEM Rules i.e., substance over form. However, there are some nuances to note which are discussed below.

The overarching principle set out in the Indian precedents i.e., it is de facto control and management and not de jure control and management, aligns with the basis of the POEM Rules i.e., substance over form.

As per the POEM Rules, a foreign company engaged in "active business outside India" (defined basis objective criteria) is deemed to have its POEM outside India if majority meetings of its board of directors is outside India. However, Indian courts[21] in the precedence discussed above, have emphasized on the distinction between the "doing" of business and the "management" of business and noted that while business and the whole of it may be done outside India, yet the control and management of that business may be wholly within India.

Another aspect to note is that the POEM Rules heavily emphasize on is the delegation of the decision-making authority and provides that if such authority is de facto delegated to the senior management, or any other person such as a shareholder, promoter, strategic, legal or financial advisor – the POEM of the company would ordinarily vest where such person resides. In this regard, it is noteworthy that in certain precedents[22], where key decisions were executed by advisors or authorized representatives based in India, the Indian courts gave benefit to the fact that such advisors and representatives were appointed by the board of directors of the relevant company, and hence while they were carrying out the business affairs of the company, it could not be said that the effective management vested with them. While delegation of authority is always a fact-based analysis, the POEM Rules seem to adopt a stricter approach in this regard.

In Conclusion

The POEM Rules and relevant judicial precedents (as discussed above) offer reasonable guidance on how the decision-making structure of a foreign company should be organized to mitigate POEM risks. Based on this review, some practical guidelines which may be implemented in this context are outlined below:

21. Narrotan and Pereira Ltd [1953]
22. Moody Analytics USA [2012] & Saraswati Holding Corporation Ltd. [2005

- **Decision making body:** As an overarching principle, the decision-making authority should be solely with the board of directors (**"BoD"**) and such authority should not be delegated to any person resident in India (explicitly or in implied terms). A robust BoD should be formed and all the decisions for the foreign company should be taken by such BoD in meetings held outside India.

- **Composition of BoD:** The BoD should predominantly comprise of non-resident experts with sector-specific proficiency and capabilities. Even if Indian residents are on the board of directors, they should be in minority, the non-resident directors should possess superior qualifications, professional expertise, and technical knowledge in comparison to the Indian tax resident directors. Further, no BoD meeting should be chaired by an Indian tax resident and no special rights should be provided to any directors based in India.

- **Role of Indian persons:** No Indian tax resident (including advisor/ fund advisor) should not provide any comments or suggestions or recommendations with respect to the key decisions in an individual capacity. Any insights or advice to be provided by Indian persons should be pursuant to a non-binding advisory framework.

- **BoD decisions and minutes of meetings:** Decisions of the board should be taken after adequate deliberation and on a unanimous or majority basis. There should be an adequate record of such deliberations and decisions in the minutes of meetings of such board. This is to ensure that the board is not viewed merely as a rubber-stamping advice given by any Indian resident.

- **Meetings through electronic mode:** Optically, it is preferable that any Indian resident directors should physically attend board meetings in the foreign county. Electronic participation should be discouraged; if necessary, involvement should be to provide inputs, not decision-making.

- **Shareholder control:** Indian shareholders should not have the authority to limit the authority of the board of directors or senior management of the foreign company, in any form. Further, shareholder control should be limited to "protective rights" i.e., rights for protection of its investment and include control over rights such as change in nature of business, change in auditor etc. That said, POEM Rules permit the following of general and objective principles of the global policy for routine matters such as pay-roll functions, accounting, human resources, IT infrastructure etc; and hence where required, a global policy could be formulated for this purpose.[23]

- **Remuneration:** Remuneration paid to Indian resident board members should not be disproportionate to that of the others. A disproportionate remuneration may imply that their input and contribution is more valuable than the

23. *Vodafone International Holdings B.V vs. Union of India*



others and therefore they are the key decision makers.

- **Bank account signatories:** The principal bank account should be in its jurisdiction of incorporation with the local directors having the authority to operate such account. The bank signatories should be tax non-residents of India.

- **Negotiation and signatories to contracts:** All agreements and vendor or customer contracts should be negotiated, concluded and signed outside India. Foreign company's BOD should be wholly responsible for (i) hiring; and (ii) termination of employment of their employees.

Although there is no "one-size-fits-all" approach, and each case requires a thorough examination of its facts, adherence to the guidelines outlined above should ideally assist a foreign company in minimizing the risk of being deemed to have POEM in India.

■

WHEN TREATIES SPEAK BUT COURTS REMAIN SILENT



Ms. Seema Jariwala

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Overview

The article examines the principle of pacta sunt servanda in international tax treaties, highlighting its significance in ensuring that treaty obligations prevail over domestic law. It references the Vienna Convention on the Law of Treaties (VCLT), particularly Articles 31 and 27, which uphold the sanctity of treaties and prohibit domestic laws from overriding them. Although India is not a signatory to the VCLT, its Supreme Court has consistently applied this principle.

The article then critically examines the Most Favored Nation (MFN) clause in tax treaties, highlighting inconsistencies in its judicial interpretation. Courts have diverged on whether MFN benefits automatically apply or require formal protocol amendments. This has led to uncertainty in cross-border taxation.

The author critiques India's judiciary for deviating from logical treaty interpretation, arguing that strict adherence to the principle of pacta sunt servanda is crucial. The piece concludes by urging courts to uphold international obligations and consider the existing immediate judicial precedent before them, rather than delving into history and distorting well-established principles due to domestic considerations.

The principle of *pacta sunt servanda* is a fundamental tenet in international tax treaty law, affirming that treaty obligations hold paramount authority. This principle, articulated in Article 31 of the Vienna Convention on the Law of Treaties (VCLT), 1969, is widely recognized as reflecting customary international law.

Article 27 of the VCLT further reinforces this stance by stating that *"no party to a treaty might attempt to justify its failure to perform any of its international treaty obligations by invocation of its municipal law"*. Even though India is not a signatory to the VCLT, the Supreme Court of India has consistently embraced this interpretative approach in construing

The principle of *pacta sunt servanda* is a fundamental tenet in international tax treaty law, affirming that treaty obligations hold paramount authority. This principle, articulated in Article 31 of the Vienna Convention on the Law of Treaties (VCLT), 1969, is widely recognized as reflecting customary international law.

treaty provisions, as evidenced in landmark rulings such as ***Engineering Analysis***[1] and ***Ram Jethmalani***[2]. Additionally, Article 51(c) of the Indian Constitution mandates the State to foster respect for international law and treaty obligations.

This commitment to treaty obligations is particularly significant in the context of the Most Favoured Nation (MFN) clause, a pivotal feature in India's Double Taxation Avoidance Agreements (DTAAs). The MFN clause ensures that treaty partners receive treatment no less favorable than that granted to other nations in comparable treaties. Despite its fundamental importance, the interpretation and application of the MFN clause in India have witnessed significant judicial oscillation in the recent ***Nestlé***[3] ruling, leaving taxpayers in a state of uncertainty. The evolving jurisprudence, coupled with the tax administration's reluctance to accept the automatic application of the MFN clause, has led to a complex and often contentious landscape.

Historical and Legal Evolution of the MFN Clause

The MFN clause, as embedded in India's DTAAs, derives its essence from the principles of non-discrimination and fair treatment. Originating in the broader context of trade

The United States incorporated an MFN clause in its first treaty—the 1778 Treaty of Alliance with France.

law, the MFN principle ensures that a country grants to its treaty partner the same favorable treatment it provides to a third country. In international taxation, this translates to extending benefits such as lower withholding tax rates or exemptions agreed upon with a third country to all qualifying treaty partners.

Its origins can reportedly be traced back to the twelfth century, although the phrase itself appears to have first emerged in the seventeenth century. With the expansion of global commerce in the fifteenth and sixteenth centuries, MFN clauses became increasingly prevalent in treaties. The United States incorporated an MFN clause in its first treaty—the 1778 Treaty of Alliance with France. Throughout the nineteenth and twentieth centuries, these clauses were frequently included in treaties, particularly in Friendship, Commerce, and Navigation agreements[4], which sought to promote economic cooperation and prevent discriminatory trade practices. MFN treatment was later established as a core principle of commercial policy under the Havana Charter[5], where member states committed

1. *Engineering Analysis Centre of Excellence (P.) Ltd. vs. CIT [2021] 125 taxmann.com 42 (SC)*
2. *Ram Jethmalani vs. Union of India (2011) 8 SCC 1*
3. *Assessing Officer (International Taxation) vs. Nestlé SA [2023] 155 taxman.com 384 (SC)*
4. *https://doi.org/10.1787/c7abd09b-en OECD Working Paper - "The most favoured nation and non-discrimination provisions in international trade law and the OECD codes of liberalisation."*
5. *The United Nations Conference on Trade and Employment, held in Havana, Cuba, in 1947, adopted the Havana Charter for the International Trade Organization which was meant to establish a multilateral trade organization. For various reasons, the charter never came into force. Pending the entry into force of the Havana Charter, a mechanism was needed to implement and protect the tariff concessions negotiated in 1947. To do so, it was decided to take the Chapter on Commercial Policy of the Havana Charter and convert it, with certain additions, into the General Agreement on Tariffs and Trade. To bring the GATT into force quickly, a Protocol of Provisional Application was developed. Thus, the GATT was born. The GATT 1947 Agreement was brought into the Uruguay Round agreements by GATT 1994.*
   Source: https://www.wto.org/english/docs_e/legal_e/prewto_legal_e.htm
   India has been a member of the GATT since 8 July, 1948
   Source: https://www.wto.org/english/thewto_e/countries_e/india_e.htm

to minimizing discrimination against foreign investors[6].

MFN clauses in tax treaties, as well as in bilateral trade agreements, originate from the special relationship between contracting states. Such relationships may stem from various factors, including historical colonial ties or deep economic interdependence. In some cases, the negotiation of a unilateral MFN clause reflects the predominant economic strength of one contracting state, compelling the other to extend similar benefits to future treaty partners[7].

India's tryst with MFN clauses predates its economic liberalization of the early 1990s, a period when the country faced significant challenges in attracting foreign direct investment (FDI). In an economy dominated by licensing controls, foreign investments were often viewed with skepticism rather than encouragement. A review of MFN clauses in India's tax treaty network[8] suggests that most were introduced as an incentive to attract FDI as the country transitioned toward a more open economy.



The MFN clause typically requires the fulfillment of three key conditions for its invocation.

The MFN Controversy

The MFN clause typically requires the fulfillment of three key conditions for its invocation: (i) India must have entered into a DTAA with a third country after the date of the relevant DTAA containing the MFN clause; (ii) the DTAA with the third country must offer a lower tax rate or a more favorable scope of taxation concerning specific income, such as dividends; and (iii) the third country must be a member of the Organisation for Economic Co-operation and Development (OECD). If these conditions are satisfied, the more favorable tax treatment under the DTAA with the third country becomes applicable to the original DTAA containing the MFN clause.

The MFN controversy has two primary aspects:

(A) **Issue A**: Whether the MFN clause requires specific notification to be operationalized.

(B) **Issue B:** Whether it extends to favorable terms provided in treaties with non-OECD countries that later attain OECD membership.

Issue A: The Requirement of Notification

The Ministry of External Affairs has outlined that India ensures its ability to discharge treaty obligations by amending domestic laws or enacting enabling legislation before

6. *https://www.oecd.org/daf/inv/investment-policy/WP-2004_2.pdf*
7. *https://www.steuerlehre.rw.fau.de/files/2017/03/Tax-Treaties-and-Most-Favoured-Nation-Treatment.pdf*
8. *Please refer to India's treaties with France (1992), Netherlands (1988), Switzerland (1994), Belgium (1993), Spain (1993), Sweden (1994), Canada (1996), UK (1993)*

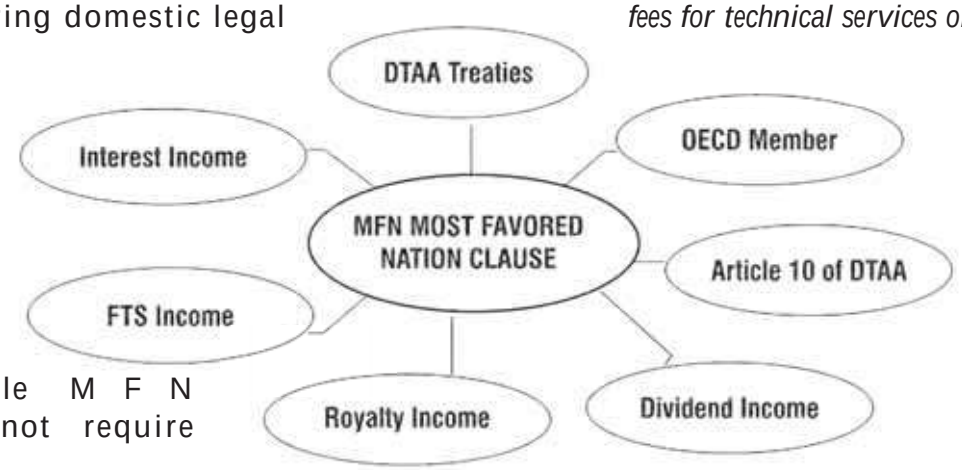
ratifying or acceding to international treaties and agreements[9]. This approach is intended to maintain legislative harmony and clarity. A plain reading of Section 90(1) also indicates that notification is required for a DTAA entered into by the Central Government, including any bilateral amendments via protocol. However, an amendment is distinct from a notification. Conceptually and legally, these are different processes.

The judiciary's insistence on an express notification under Section 90(1) to operationalize MFN clauses embedded in tax treaties and their protocols raises critical questions. Given that protocols are signed, ratified, and form an integral part of treaties[10], their self-executing nature should ideally obviate the need for additional procedural formalities, such as a separate notification. Requiring express notification for provisions already agreed upon and ratified appears redundant, particularly when India's legislative framework already recognizes treaties and their integral protocols as binding. Such a procedural requirement undermines the efficiency of treaty implementation and creates unnecessary legal friction, despite India's established practice of honoring treaty obligations after ensuring domestic legal readiness.

MFN clauses in India's tax treaties can be classified into two categories based on their applicability requirements. The first category consists of automatically applicable MFN clauses, which do not require additional notification, negotiation, or procedural formalities for enforcement. The second category includes MFN clauses that are contingent upon the fulfillment of additional conditions, such as further negotiations, mutual consultations, or formal notification process.

For instance, treaties such as the India-France DTAA, India-Sweden DTAA, and India-Switzerland DTAA provide for the automatic invocation of the MFN clause, seamlessly aligning the tax treatment with that of a third country. In contrast, the India-Finland DTAA, India-Philippines DTAA and India-Saudi Arabia DTAA require additional negotiation and formal notification before the MFN clause can be applied to dividend income. A standard formulation of an MFN clause with automatic application can be seen in the India-France DTAA: -

"In respect of articles 11 (Dividends), 12 (Interest) and 13 (Royalties, fees for technical services and payments for the use of equipment), if under any Convention, Agreement or Protocol signed after 1-9-1989, between India and a third State which is a member of the OECD, India limits its taxation at source on dividends, interest, royalties, fees for technical services or



9. *Cabinet Secretariat's O.M. No. 1/13/2/2010-Cab., dated 23 August 2011*
10. *The protocol in the India-France DTAA states that: "At the time of proceeding to the signature of the Convention between France and India for the avoidance of double taxation with respect to taxes on income and on capital, the undersigned have agreed on the following provisions which shall form an integral part of the Convention"*

payments for the use of equipment to a rate lower or a scope more restricted than the rate of scope provided for in this Convention on the said items of income, the same rate or scope as provided for in that Convention, Agreement or Protocol on the said items income shall also apply under this Convention, with effect from the date on which the present Convention or the relevant Indian Convention, Agreement or Protocol enters into force, whichever enters into force later."

In contrast, a standard formulation of an MFN clause that is contingent upon the fulfillment of additional conditions can be seen in the India-Finland DTAA: -

"It is agreed that if after coming into force of this Agreement, any agreement or convention between India and a Member State of the Organisation for Economic Cooperation and Development provides that India shall exempt from tax dividends, interest, royalties or fees for technical services (either generally or in respect of specific categories of dividends, interest, royalties or fees for technical services) arising in India, or limit the tax charged in India on such dividends, interest, royalties or fees for technical services (either generally or in respect of specific categories of dividends, interest, royalties or fees for technical services) to a rate lower than that provided for in paragraph 2 of Article 10 or paragraph 2 of Article 11 or paragraph 2 of Article 12 of the Agreement, such exemption or lower rate shall be made applicable to the dividends, interest, royalties or fees for technical services (either generally or in respect of those specific categories of dividends, interest, royalties or fees for technical services) arising in India and beneficially owned by a resident of Finland and dividend, interest, royalties or fees for technical services arising in Finland and beneficially owned by a resident of India under the same conditions as if such exemption or lower rate had been specified in those paragraphs. The competent authority of India shall inform the competent authority of Finland without delay that the conditions for the application of this paragraph have been met and issue a notification to this effect for application of such exemption or lower rate." (emphasis supplied)

Furthermore, certain protocols adopt a hybrid approach, distinguishing between different income categories. For example, the Protocol to the India-Switzerland DTAA[11] ensures automatic applicability of the MFN clause for dividends, royalties, and fees for technical services but only when the tax rate in the source country under its DTAA with a third country is lower. However, if the scope of taxation in the third-country DTAA is more restrictive, formal renegotiation and notification are required before extending MFN benefits.

Treaty interpretation principles establish that variations in treaty language reflect the contracting states' differentiated intent. Imposing a notification requirement on all MFN clauses, even where absent from the plain text, contravenes the "plain meaning" rule enshrined in Article 31(1) of the VCLT. Additionally, Article 31(2) extends treaty

11. *In respect of Articles 10 (Dividends), 11 (Interest) and 12 (Royalties and fees for technical services), if under any Convention, Agreement or Protocol between India and a third State which is a member of the OECD signed after the signature of this Amending Protocol, India limits its taxation at source on dividends, interest, royalties or fees for technical services to a rate lower than the rate provided for in this Agreement on the said items of income, the same rate as provided for in that Convention, Agreement or Protocol on the said items of income shall also apply between both Contracting States under this Agreement as from the date on which such Convention, Agreement or Protocol enters into force.*
If after the date of signature this Amending Protocol, India under any Convention, Agreement or Protocol with a third State which is a member of the OECD, restricts the scope in respect of royalties or fees for technical services than the scope for these items of income provided for in Article 12 of this Agreement, then Switzerland and India shall enter into negotiations without undue delay in order to provide the same treatment to Switzerland as that provided to the third State." (emphasis supplied)

interpretation beyond the text to include instruments such as preambles and protocols. A comparative analysis of India's treaty practice underscores the need for a textualist approach that respects the deliberate drafting choices within each DTAA.

The integrity of international tax treaties rests on the pillars of consistency, reciprocity, and good faith—principles that are jeopardized when judicial interpretation diverges from the mutual intent of sovereign signatories.

Article 73 of the Indian Constitution delineates the executive's power to implement treaty obligations while ensuring harmony with domestic laws. The Supreme Court, in ***Gramophone Company of India Ltd. vs. Birendra Bahadur Pandey***[12], held that domestic laws must align with India's treaty commitments. Though Article 51(c) is not explicitly referenced in deliberations on Article 253[13], the Supreme Court has reinforced the state's duty to honor treaty commitments. Thus, once India enters a bilateral agreement granting concessional benefits, the government cannot subsequently renege on or deny those benefits if claimed in accordance with the treaty.

The integrity of international tax treaties rests on the pillars of consistency, reciprocity, and good faith—principles that are jeopardized when judicial interpretation diverges from the mutual intent of sovereign signatories.

The Supreme Court has consistently upheld the primacy of international tax treaty obligations. In ***Union of India vs. Agricas***[14], a three-judge bench unequivocally held that domestic law cannot override treaty commitments. Numerous rulings affirm this principle, emphasizing the primacy of international agreements entered into by the Government of India[15]. However, in the Nestlé ruling, the Court departed from this jurisprudence, selectively citing precedents



12. *Gramophone Company of India Ltd. vs. Birendra Bahadur Pandey AIR 1984 SC 687*
13. *Article 253 is situated within Chapter I of Part XI of the Indian Constitution, which deals with the "Distribution of Legislative Powers." Notably, this provision empowers Parliament to enact laws necessary to implement international treaties and agreements entered into by the Union*
14. *Union of India vs. Agricas LLP 2020 SCC Online SC 675*
15. *For illustration, see Commissioner of Customs, Bangalore vs. G.M. Exports (2016) 1 SCC 91; Gramophone Co. of India Ltd. vs. Birendra Bahadur Pandey (1984) 2 SCC 534; Engineering Analysis (Supra Note 9)*

while overlooking authoritative decisions affirming the sanctity of treaty obligations.

No constitutional requirements exist to require a separate notification for implementing individual provisions of duly notified treaties and protocols. Applying these principles to automatically applicable MFN clauses in India's DTAAs clarifies that such clauses do not necessitate separate notification as a precondition for applicability. Consequently, reading an additional notification requirement into the Protocol would be unwarranted and contrary to the plain textual meaning and settled principles of treaty interpretation.

Nestlé ruling overlooks linguistic distinctions in the treaty. More significantly, it fails to recognize that the treaty simultaneously contains self-operational MFN clauses and MFN clauses requiring negotiation. Such a negotiation requirement cannot be inferred where it is absent in drafting style and substance. Any contrary interpretation would amount to rewriting the law rather than adhering to the agreed treaty framework.

Issue B: MFN Clause and Non-OECD Countries Attaining OECD Membership

The second issue pertains to whether the MFN clause extends to favorable terms provided in treaties with non-OECD countries that subsequently attain OECD membership. The key question is whether the third country must be an OECD member at the time of signing its DTAA with India or if its subsequent accession is sufficient for MFN benefits.

A textual analysis of MFN clauses in Indian tax treaties suggests that there is no explicit requirement that the third country must be an OECD member at the date of signature of its DTAA with India. Notably, in the India-Netherlands DTAA, the absence of language

The Supreme Court has consistently upheld the primacy of international tax treaty obligations. In Union of India v. Agricas, a three-judge bench unequivocally held that domestic law cannot override treaty commitments.

stipulating a specific OECD membership date indicates that the contracting parties did not intend to impose such a restriction. If such a requirement had been envisioned, it would have been explicitly articulated. The Protocol appended to the India-Netherlands DTAA signed with the original treaty is reproduced below:-

"IV. Articles 10, 11 and 12

1. …...

*2. **If after the signature of this convention under any Convention or Agreement between India and a third State that is a member of the OECD, India should** limit its taxation at source on dividends, interests, royalties, fees for technical services, or payments for the use of equipment to a rate lower or a scope more restricted **than the rate** or scope **provided for in this** Convention on the said items of income, then as from the date on which the **relevant Indian Convention or Agreement** enters into force the same rate or scope **as provided for in that Convention or** Agreement on the said items of income **shall also apply under this Convention."***

Further, clauses I and II of the Protocol appended to the **India-Netherlands Double**



Taxation Avoidance Agreement (DTAA) explicitly reference the **date of signature** as a defining element of their applicability. The relevant provisions of these clauses are articulated below:

I. Ad Article 7

.....

1. Where the law of the State in which a permanent establishment is situated imposes in accordance with the provisions of subparagraph (a) of paragraph 3 of Article 7 a restriction on the amount of the executive and general administrative expenses which may be allowed as a deduction in determining the profits of such permanent establishment, it is understood that in determining the profits of such permanent establishment the deduction in respect of such executive and general administrative expenses in no case shall be less than what is allowable under the Indian Income-tax Act ***as on the date of signature of this Convention****. (Emphasis supplied)*

II. Article 8A

It is understood that in case the percentage as is specified in section 44B of the Indian Income-tax Act ***as on the date of signature of this Convention*** *for the purpose of determining the amount of shipping profits is reduced by any change in the Indian law, the percentage as is mentioned in sub-paragraph (b) of paragraph 2 of Article 8A will be reduced in the same proportion." (Emphasis supplied)*

It thus appears that, during the course of diplomatic negotiations for the India-Netherlands tax treaty, the deliberate omission of such expressions from the Most Favoured Nation (MFN) clause was a matter of considered intent. Consequently, a compelling inference may be drawn that the treaty drafters did not envisage a requirement for the Third Country, with which India subsequently enters into a tax treaty, to be an OECD member as of the date of signature of the India-Netherlands DTAA. Had such an intention existed, the provision would have been expressly framed to stipulate that the Third Country "is a member of the OECD at the date of signature." The conspicuous absence of these words underscores this interpretation. This would mean attempting to connect and read "is" with a disjointed phrase ''as on the date of signature".

International treaty practice further supports this interpretation. For example, the Australia-Netherlands DTAA explicitly links MFN benefits to the OECD membership status of a third country at the date of signing. The deliberate use of such language in certain treaties—but not in the India-Netherlands DTAA—demonstrates that where OECD membership timing is a critical factor, it is expressly stipulated. The absence of such a clause in the India-Netherlands DTAA implies that subsequent OECD membership should not preclude MFN invocation. The Australia – Netherlands protocol to this DTAA provides as under:

"6. General.

(a) Where one of the States is entitled to tax the profits of an enterprise, that State may treat as profits of the enterprise, profits from the alienation of capital assets of the enterprise, not being profits that consist of income to which paragraph (1) of Article 13 applies.

(b) If, in an Agreement for the avoidance of double taxation that is subsequently made between Australia and ***a third State being a State that at the date of signature of this Protocol is a member of the Organisation for Economic Co-operation***

> ***and Development**, Australia shall agree to limit the rate of its taxation:*
>
> *(i) on dividends paid by a company which is a resident of Australia for the purposes of Australia tax to which a company that is a resident of the third State is entitled, to a rate less than that provided in paragraph (2) of Article 10; or*
>
> *(ii) on interest arising in Australia to which a resident of the third State is entitled, to a rate less than that provided in paragraph (2) of Article 11; or*
>
> *(iii) on royalties arising in Australia to which a resident of the third State is entitled, to a rate less than that provided in paragraph (2) of Article 12,*
>
> *the Government of Australia shall immediately inform the Government of the Kingdom of the Netherlands in writing through the diplomatic channel and shall enter into negotiations with the Government of the Kingdom of the Netherlands to review the provisions specified in sub-paragraphs (i), (ii) and (iii) above in order to provide the same treatment for the Netherlands as that provided for the third State."* (Emphasis supplied)

The phrase *"if, in an Agreement for the avoidance of double taxation that is subsequently made between Australia and a third State being a State **that at the date of signature of this Protocol is a member of the Organisation for Economic Co-operation and Development**"* demonstrates that the DTAA partners deliberately made the date of OECD membership a relevant criterion for triggering the MFN clause. Similar language appears in other Dutch treaties, such as the Latvia-Netherlands DTAA and the Lithuania-Netherlands DTAA, reinforcing this drafting pattern.

The Australia-Netherlands DTAA was concluded on March 17, 1976, with its second protocol signed on June 13, 1986—predating the India-Netherlands DTAA. This chronology suggests that when negotiating the India-Netherlands DTAA, the contracting states were fully aware of Dutch treaty practices, particularly the explicit reference to OECD membership dates in comparable agreements. The absence of such a stipulation in the India-Netherlands DTAA, therefore, is not an inadvertent omission but a conscious policy decision by both treaty partners. Accordingly, in the absence of a formal amendment to the Protocol, neither India nor the Netherlands can retroactively impose the requirement of a specific OECD membership date as a condition for invoking the MFN clause. The treaty text reflects a clear intent to exclude this criterion, and retrospective reinterpretation would contradict the foundational principle that treaty provisions must be applied as agreed upon by the contracting states. Moreover, as a settled legal principle, when two interpretations are possible, the one that best effectuates the treaty's underlying objective should prevail[16].

Notably, the inclusion of OECD membership as a determinative factor is not unique to the Netherlands' treaty network. This drafting approach extends to agreements with other jurisdictions following a similar framework. For instance, the MFN clause in the Protocol to the DTAA between Belgium and Estonia adopts a parallel formulation, as illustrated below:

16. *Bajaj Tempo Ltd. vs. Commissioner of Income Tax (1992) 3 SCC 78*

"6. Article 12, paragraphs 2 and 3

If in any convention for the avoidance of Double taxation concluded by Estonia with a third state, being a member of the Organisation for Economic Co-operation and Development (OECD) at the date of signature of this convention, Estonia after that date would agree to exclude any kind of rights or property from the definition contained in paragraph 3 or exempt royalties arising from Estonia from Estonian tax on royalties or to limit the rates of tax provided in paragraph 2, such definition or exemption or lower rate shall automatically apply as if it has been specified in paragraph 3 or paragraph 2 respectively". (Emphasis supplied)

The foregoing discussion demonstrates that the Nestlé ruling selectively relied on international jurisprudence and relevant Supreme Court precedents while conspicuously disregarding established international state practices that should have informed a more comprehensive interpretation. Furthermore, the interpretation that favorable terms granted to non-OECD countries, which later attained OECD membership, remain applicable aligns with the principles laid down by the Supreme Court.



In ***P. Anand Gajapathi Raju vs. PVG Raju***[17], the Supreme Court held that the phrase "*which is the subject of an arbitration agreement*" does not necessarily imply a pre-existing agreement; rather, it includes agreements that come into existence while court proceedings are pending. Furthermore, the term "is" though typically associated with the present tense, can, depending on the context, also carry a future meaning. It is not confined to denoting only present circumstances. Thus, interpreting "is" rigidly in the present tense would unduly narrow its application. Similarly, in ***F.S. Gandhi vs. Commissioner of Wealth Tax***[18], the Court ruled that the term "is" inherently carries a broader temporal scope, encompassing not only the present but also the future. Black's Law Dictionary also acknowledges that while "is" primarily denotes the present, it frequently conveys a future connotation and, where contextually appropriate, may even imply past circumstances.

The term "is" is heterological—meaning it denotes existence at a specific point in time. A parallel can be drawn with the use of "is" in Article 10(1) of the India-Netherlands and India-Switzerland DTAAs, where the phrase "is a resident" appears. It is undisputed that to claim the benefit of Article 10, a taxpayer must be a resident of Switzerland or the Netherlands at the time the provision is invoked. Similarly, Article 27 of the India-Netherlands DTAA, which governs tax exemptions for diplomats, states: "*2. For the purposes of the Convention an individual who is a member of a diplomatic or consular mission of one of the States*". Here, too, the requirement is that the individual be a member of a diplomatic or consular mission at the time Article 27 is applied—not when the treaty was signed or when diplomatic relations were first established.

17. *P. Anand Gajapathi Raju vs. PVG Raju (2004) 4 SCC 539*
18. *F.S. Gandhi vs. Commissioner of Wealth Tax (1990) 3 SCC 624*

Applying the same principle to the MFN clause, the word "is" must be understood in a similar temporal context—meaning that Lithuania and other countries must be OECD members at the point when the MFN benefit is invoked.

Although the Nestlé ruling referred to these precedents in paragraph 50, it interpreted "is" narrowly by focusing only on its present-tense usage, emphasizing that it "normally refers to the present." This restrictive approach overlooked the broader interpretative framework established in prior rulings.

A proper analysis demonstrates that the MFN clause is not confined to a rigid temporal reading but extends to favourable treaty terms granted to non-OECD countries that subsequently attain OECD membership. This interpretation aligns with landmark judgments such as Steria[19] and Concentrix[20], established principles of international treaty interpretation, and the Supreme Court of India's jurisprudence—reinforcing a coherent and purposive application of the MFN clause.

Moreover, the mechanism under Section 90(2) of the Income-tax Act provides a practical safeguard. It allows taxpayers to choose between the domestic tax regime and the DTAA, ensuring that MFN benefits can be invoked only when demonstrably advantageous. The burden of proof remains with the taxpayer, who must establish before the Assessing Officer that a third country's DTAA with India is a valid reference due to its OECD membership. The Assessing Officer, vested with broad statutory powers, including the authority to summon records and verify claims, possesses ample discretion to ascertain the veracity of the taxpayer's assertions, including the OECD membership status of the referenced third country.

A holistic analysis of treaty text, international practice, and judicial precedent suggests that MFN benefits should extend to non-OECD countries that later attain OECD membership. This interpretation aligns with established principles of treaty interpretation, particularly the doctrine that ambiguous provisions should be construed in a manner that effectuates their intended purpose. The Nestlé ruling's restrictive interpretation of "is" disregards both international treaty practice and Supreme Court jurisprudence, which favor a dynamic and purposive reading of treaty provisions.

Consequently, absent an explicit stipulation requiring OECD membership at the date of signature, India's MFN clauses should be interpreted to extend benefits to countries that subsequently join the OECD. Such an approach maintains consistency with India's international obligations and ensures that treaty benefits are applied in a fair and predictable manner.

Reinforcing Common Interpretation in Bilateral Tax Treaties

The principle of common interpretation underscores that tax treaties, as bilateral (or multilateral) agreements, should be construed in a manner that reflects the mutual intentions and understanding of both contracting states[21]. When disputes arise regarding the interpretation of specific provisions—particularly where conflicting domestic interpretations exist—courts and tax authorities often accord significant weight

19. *Steria (India) Ltd. vs. CIT [2016] 72 taxmann.com 1*
20. *Concentrix Services Netherlands B.V. vs. ITO (TDS) [2021] 127 taxmann.com 43*
21. *Klaus Vogel, Double Tax Treaties and Their Interpretation, (1986)*

to how the other contracting state, particularly the dominant or residence country, has historically interpreted or applied the treaty.



This principle finds recognition not only in public international tax law but also in private international law, particularly in the realm of conflict of laws. Such an approach fosters consistency, reciprocity, and mutual trust in cross-border tax matters. It aligns with Article 31(1) of the VCLT, which mandates that treaties be interpreted in good faith, in accordance with the ordinary meaning of their terms, in context, and in light of their object and purpose. Where the dominant country's interpretation reflects a consistent administrative or judicial practice, it frequently assumes a persuasive—if not decisive—role in ensuring uniform application and mitigating risks of double taxation or treaty abuse.

A pertinent example illustrating the consequences of divergent treaty interpretations is Switzerland's recent decision to suspend the Most Favored Nation (MFN) clause in its tax treaty with India, effective 1 January 2025[22]. This action was a direct response to the Indian Supreme Court's ruling in the ***Nestlé (supra)*** judgment. The development highlights the significance of a harmonized interpretative approach, as unilateral interpretations by one jurisdiction—without due consideration of the counterpart's position—can provoke retaliatory measures, heighten tax burdens, and strain diplomatic relations.

Moreover, the principle of common interpretation is well-established in common law jurisdictions[23], with courts, including the Supreme Court of India, having reaffirmed it on multiple occasions. In the landmark ruling in ***Azadi Bachao Andolan***[24] case, the Supreme Court emphasized that tax treaties, unlike statutory legislation, are political instruments shaped by negotiation and compromise, often lacking the precision of domestic laws. Citing Francis Bennion and Lord Wilberforce, the Court recognized that treaty interpretation is not bound by technical rules but rather follows broad, internationally accepted principles. Given the negotiated nature and inherent compromises in treaties, a consistent and uniform interpretation across contracting states is essential to maintaining the intended balance and reciprocity of treaty provisions.

In this context, the Dutch government's official clarification, dated February 28, 2012, is particularly relevant. It affirmed that the MFN clause in the India-Netherlands DTAA entitles Dutch tax residents to benefit from the

22. *Secrétariat d'Etat aux questions financières internationales SFI- Suspension of the application of the most favoured nation clause of the protocol to the Agreement between the Swiss Confederation and the Republic of India for the avoidance of double taxation with respect to taxes on income*
23. *For illustration, see Corocraft vs. Pan American Airways Inc. (1968) 3 WLR 1273 ((1283); Ulster Swift Ltd. vs. Taunton Meat Haulage Ltd. (1977) 1 WLR 625 (631); Fothergill vs. Monarch Airlines (1980) 3 WLR 209*
24. *Union of India vs. Azadi Bachao Andolan (2004) 10 SCC 1.*

5% dividend tax rate under the India-Slovenia DTAA from the date Slovenia became an OECD member (21 August 2010), despite the India-Slovenia DTAA entering into force on 17 February 2005. The Netherlands has adhered to this interpretation for over a decade, with Indian companies and their Dutch subsidiaries routinely availing themselves of the reduced tax rate. However, the Supreme Court of India, in its ruling, disregarded this consistent interpretation adopted by its treaty partner. This oversight not only contravenes the principle of common interpretation but also undermines the well-established principle of good faith enshrined in the VCLT.

Ultimately, reinforcing the principle of common interpretation is imperative to ensuring legal certainty, preventing tax disputes, and preserving the integrity of international tax agreements. A failure to do so risks fostering inconsistent treaty applications, economic inefficiencies, and diplomatic discord between contracting states.

Conclusion

The Supreme Court's ruling in Nestlé represents a significant and concerning departure from well-anchored principles of treaty interpretation. By insisting upon a mandatory, explicit notification under Section 90(1) as a precondition to operationalizing the MFN clause—despite the clause being an integral, ratified component of the treaty—the Court effectively undermines the automatic application of obligations voluntarily undertaken by India in its bilateral conventions. This requirement disregards not only the self-executing nature of protocols embedded within DTAAs but also the fundamental principle of pacta sunt servanda and the constitutional mandate to honor treaty commitments in good faith.

Furthermore, the Court's static interpretation of the expression "is" and its imposition of a condition regarding the relevant date of OECD membership—despite India's clear departure from such practice in contrast to the Netherlands' treaties with other jurisdictions—amounts to a post-facto reinterpretation, contrary to the original intent of the contracting parties. Unlike other treaties where the date of OECD membership was explicitly referenced, omitting such language in India's DTAAs reflects a deliberate policy choice, not inadvertence. Imposing additional requirements through administrative or judicial channels now risks unilateral distortion of a mutually negotiated treaty framework, undermining consistency, reciprocity, and trust.

The resulting divergence, highlighted by Switzerland's suspension of the MFN clause, exemplifies the diplomatic and economic fallout from failing to adhere to the principle of common interpretation. Moving forward, it is imperative that India aligns its interpretative stance with the spirit, text, and mutual understanding underlying its international tax treaties, rather than introducing procedural roadblocks that hinder the seamless and faithful execution of treaty commitments. ■



ATTRIBUTION OF PROFITS TO PERMANENT ESTABLISHMENTS : CHANGING INTERPRETATION POST OECD BEPS





CA Fatema Hunaid ***CA Gaurav Sethia***

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Overview

In an era of globalization and digitalization, traditional tax principles are struggling to keep up with modern business models. This article delves into the evolving landscape of profit attribution to Permanent Establishments (PEs) in light of the OECD's Base Erosion and Profit Shifting (BEPS) project. Historically, PEs required a physical presence for taxation, but digital businesses have exposed loopholes, leading to tax avoidance.

The OECD's BEPS Action Plan 7 redefines PE, targeting artificial avoidance and ensuring profits are taxed where value is created. India, a significant market for multinationals, has proactively aligned its tax framework with various changes, including rules around Significant Economic Presence (SEP) and expanded the scope of 'Business Connection' to include digital transactions. However, challenges persist due to inconsistent judicial interpretations and the complexities of digital economies.

The article explores India's legislative amendments, judicial rulings, and the impact of BEPS Action Plan 7 and Pillar One on profit attribution towards PEs. It highlights the need for a fair and predictable taxation system, addressing the compliance burdens and the risk of double taxation. As India navigates this complex landscape, the article underscores the importance of aligning transfer pricing policies with global standards to ensure equitable profit distribution.

Introduction

Globalization and digitalization of businesses especially over the last two decades, has been transforming and disrupting businesses and contributing to rising complexities in the landscape of international taxation forcing countries to cooperate more closely to ensure a fair taxation regime worldwide. Traditional principles of profit attribution, which heavily relied on the concept of physical presence, struggle to keep pace with contemporary business models that derive substantial value from intangible assets, user engagement, and data-driven operations. In today's dynamic digital economy, businesses can operate and generate revenue in markets where they lack physical presence, thereby creating blind spots in the existing framework for profit allocation.

Historically, the concept of Permanent Establishment (PE) formed the cornerstone of international tax rules, permitting countries to tax profits only when a foreign enterprise maintained a physical presence within the jurisdiction. This physical presence requirement

allowed businesses to exploit loopholes, resulting in tax avoidance strategies resulting in no taxation or double non-taxation.

The OECD's Base Erosion and Profit Shifting (BEPS) project, particularly Action Plan 7, aimed to address these deficiencies by redefining the concept of Permanent Establishment (PE) and expanding the scope of profit attribution. BEPS Action Plan 7 introduced vital changes to the definition of PE, targeting artificial avoidance of PE status through commissionaire arrangements and restructuring of preparatory or auxiliary activities alongside specific exclusions and anti-fragmentation rules. These reforms are designed to ensure that profits are taxed where value is created, closing loopholes that allowed multinational enterprises (MNEs) to shift profits to low-tax or favourable jurisdictions.

BEPS Action Plan 7 introduced vital changes to the definition of PE, targeting artificial avoidance of PE status through commissionaire arrangements and restructuring of preparatory or auxiliary activities alongside specific exclusions and anti-fragmentation rules.

India, being one of the fastest-growing economies and a significant market for multinational enterprises (MNEs), has been trying to take proactive steps to adjust its internal tax framework to align with these developments. The Indian tax authorities have introduced substantial changes through the Finance Act and other legislative amendments, emphasizing the concept of Significant Economic Presence (SEP) and profit attribution. This shift reflects India's growing assertion in shaping the international tax landscape, particularly concerning digital businesses.

Despite these proactive measures, the Indian judiciary and tax administration have faced challenges in establishing a consistent framework for profit attribution. Divergent judicial views, conflicting interpretations of the functional, asset, and risk (FAR) analysis, and the growing influence of digital platforms have made profit attribution to PEs a contentious issue. This article explores India's evolving approach to profit attribution, the complexities in establishing a PE status, and the impact of BEPS Action Plan 7 and Pillar One.

1. Indian provisions on profit attribution and SEP

Rule 10 & its shortcomings

The Indian Income-tax Act, 1961 provides the core framework for attribution of profits owing to 'business connection in India.

Attribution in accordance with Arm's Length Principle finds reference in the CBDT Circular No. 5/2004 which provides, *"profits to be attributed to a PE are those that PE would have made if, instead of dealing with its Head Office, it had been dealing with an entirely separate enterprise under conditions and at prices prevailing in the ordinary market. This corresponds to the arm's length principle."*.

If however, the assessing officer (AO) is of the opinion that actual amount of income pertaining to a business connection in India cannot be accurately determined, Rule 10 of the Income Tax Rules is applicable. Rule 10 of the Indian Income Rules pertains to determination of income in cases of non-residents. The rule provides wide discretion to the tax authorities to estimate profits and levy tax based on perceived economic activity within India resulting in use of discretionary and ad-hoc approach.

SEP provisions significantly widen the scope of 'Business Connection' in India, bringing within its ambit transactions involving goods, services, or property carried out by non-residents with any person in India, even without a physical presence.

The Rule does not provide a structured methodology for profit attribution. This has led to an inconsistent and arbitrary determination of taxable income, often based on subjective judgment by the AOs (which is discussed in detail, later in the article). While various cases have been concluded based on Transfer Pricing (TP) guidelines and FAR based approach, the ad hoc approach empowers the tax authorities to attribute profits to an activity, even without a well-defined formula. Further, the discretionary nature of Rule 10 increases the risk of double taxation, as foreign tax authorities may not accept the basis for profit attribution determined under an ad hoc approach.

Rule 10, despite its broad scope, lacks the pedagogy for fair and predictable mechanism for profit attribution.

Background and thresholds for Significant Economic Presence

SEP was introduced in 2018 as part of India's efforts to address the challenges posed by the digital economy and BEPS. SEP provisions aim to tax income from digital transactions that previously escaped taxation in any jurisdiction.

SEP provisions significantly widen the scope of 'Business Connection' in India, bringing within its ambit transactions involving goods, services, or property carried out by non-residents with any person in India, even without a physical presence.

The thresholds for SEP are set at (a) revenue threshold - aggregate amount of payment for specified transactions (including goods, services, properties), with a person in India exceeds INR 20 million (during a year) or (b) user threshold - non-resident undertakes systematic and continuous soliciting of business activities or engages in interaction with 300,000 or more users in India. However, there has been a recent proposal to exclude transactions confined to the purchase of goods in India for export from constituting SEP.

The implementation of SEP provisions also presents several challenges and compliance issues for both non-residents and Indian taxpayers.

Issues in determining SEP

There are a few important issues in relation to SEP provisions in India summarized below, underscoring the need for further clarifications



and amendments to the SEP provisions to reduce compliance burdens and ensure a fair and effective taxation system:

- **Compliance Burden**: One of the primary issues with SEP provisions is the significant compliance burden they impose on non-residents and Indian taxpayers. Indian buyers are required to withhold upto 38% tax on imports if the non-resident seller does not provide necessary documentation, such as a tax residency certificate, Form 10F, and a declaration of no business connection or permanent establishment in India. This can lead to substantial compliance challenges and increased administrative costs.

- **Thresholds for SEP**: The thresholds mentioned in the provisions are generally considered low and may require revisions.

- **Tracking and Monitoring:** Another significant challenge is tracking and monitoring the number of users and transactions to determine SEP applicability. Non-residents may find it difficult to track users in India, especially if the access or purchase is made by non-residents visiting India for leisure purposes.

2. BEPS Action Plan 7 (AP 7)[1]

Objective and Key Takeaways

The OECD launched the BEPS project in 2013 to address the challenges posed by global business structures that artificially shift profits to low-tax jurisdictions. The primary goal was to close gaps in international tax rules that allowed multinational enterprises (MNEs) to minimize their tax liabilities by artificially avoiding the creation of a taxable presence in source countries.

AP 7 specifically targeted the avoidance of artificial PE status, which is one of the most common tools used to shift profits while minimizing tax liability in the source country.

Key Reforms Under AP 7

Expanded Agency PE Definition

Traditionally, a dependent agent PE existed only if an agent had formal authority to conclude contracts on behalf of the foreign principal. Businesses often exploited this route by employing agents who facilitated transactions without formally concluding contracts.

Under AP 7, the definition of agency PE was expanded to include situations where the agent:

- Habitually plays the principal role in concluding contracts, even if they lack formal signing authority.

- Engages in negotiations that in-effect result in contracts being finalized abroad.

This broader interpretation ensured that businesses could no longer circumvent PE status through strategic delegation.

Revised Activity Exemptions

Previously, preparatory or auxiliary activities such as storage, warehousing, or delivery were exempt from PE recognition. However, AP 7 marginalized these exemptions, ensuring that:

- Only activities genuinely preparatory or auxiliary in nature would be excluded.

1. *Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7 - 2015 Final Report published on 5 October 2015*

- Core business functions disguised as auxiliary activities would now trigger PE recognition.

Anti-Fragmentation Rule

To address the practice of breaking down the business functions across related entities to avoid PE status, AP 7 introduced the anti-fragmentation rule. Under this rule, related entities performing complementary activities may be treated as a unified business, thereby triggering PE status. This signifies the intent of aggregation approach as guided by OECD while evaluating any transaction.

3. Different approaches for determining profit attribution

Additional useful references can be made to OECD's Authorised approach & CBDT's 2019 report on profit attribution - to understand PE attribution.

The Authorised OECD Approach

The AOA focuses on aligning profit attribution with value creation, emphasizing the importance of substance and economic activity i.e. core functions of each entity involved, identification of significant people functions, not just legal but economic ownership of assets. In addition to routine assets, a key factors which gain significance is capital or funding i.e. attribution of free capital to align with functions performed by a PE entity. In summary, the Authorized OECD Approach (AOA) is based on a two-step process:

— Identifying the functions performed, assets employed, and risks assumed (FAR analysis).

— Applying the arm's length principle to attribute profits based on the functional profile of the PE.

CBDT Committee's 2019 Report on Profit Attribution

In 2019, the Central Board of Direct Taxes (CBDT) had a detailed report proposing a new framework for profit attribution to PEs in India. The key recommendations included:

- **Fractional Apportionment Approach:** The Fractional Apportionment Approach was proposed as an alternative to the traditional methods of profit attribution to a PE. The key features of this approach include:

  — **Apportionment of Profits:** Profits are apportioned based on a formula that considers various factors such as sales, assets, and employees. This method seeks to allocate profits more fairly by considering the economic activities carried out in the source country. For SEP cases, users are added as a fourth factor.

  — **Demand and Supply Factors:** The approach considers both demand-side and supply-side factors in profit attribution. This ensures that the contribution of the market jurisdiction (where the customers are located) is recognized.

  — **Simplification:** By using a formula-based approach, the Fractional Apportionment method aims to simplify the process of profit attribution and reduce disputes between tax authorities and taxpayers

- Floor rate for profit attribution: To protect India's revenue interests, the committee recommended a floor rate of 2% of gross revenue or turnover derived from Indian operations, in cases where

the global enterprise records losses. The floor rate represents a safeguard against profit shifting and ensures that India receives a minimum level of tax revenue.

- **Avoiding Double Taxation:** The report recommends alignment with transfer pricing rules to avoid double taxation risks.

The report also highlighted significant adverse consequences for developing economies like India, which are primarily importers of capital and technology. Subsequently, in 2021 India announced that it had joined the majority of the members OECD / G20 Inclusive Framework on Base Erosion and Profit Shifting adopting a high-level statement containing an outline of a consensus solution to address the tax challenges arising from the digitalisation of the economy.

4. Interesting judicial rulings tracing the evolution of attribution of profits in India

Rulings from British India

Anglo French Textile Company Limited vs. Commissioner of Income Tax (CIT)[2] is one of the early rulings in Indian Judiciary on attribution dating to the year 1952. The Supreme Court ('SC') considered figure of 10% on British Indian sales as reasonable for attribution, basis the extent of operations carried out in British India.

Similarly, in ***Hukum Chand Mills Limited vs. CIT***[3], basis facts of the case, 15% allocation was considered reasonable for operations relating to contracts undertaken in British India. During the pre-independence era, the territory of British India was delineated from Indore, where the company operated textile manufacturing mills.

Pronouncements based on Rule 10/ adoption ad-hoc approach

In the past, rulings pertaining to profit attribution were pronounced considering Rule 10 along with specific provisions in the Act. In ***DDIT vs. Nipro Asia Pte Ltd***[4], the AO, in absence of any correct TP study, adopted provisions of Rule 10 using 'selective figures' from public websites. The Income Tax Appellate Tribunal (ITAT) rejected AO's computation (negating use of publicly available data) and assessed income based on provisions that allowed presumptive profit rate of 10% of the total sales in India and 30% of such profits to the Indian PE i.e. at 3% (30% of 10%).

Similarly, in ***Galileo International Inc.***[5], 15% profit attribution was considered sufficient owing to the role played by PE in negotiating contracts.

Importance of FAR analysis in Arms-Length attribution of profits

Landmark decision by SC in ***Morgan Stanley and Co. Inc.***[6]. throws light on the importance of transfer pricing analysis in attribution of profits to PE. It lays, "The impugned ruling is correct in principle insofar as the associated enterprise, that also constitutes a PE, has been remunerated on an arm's length basis taking into account all the risk-taking functions of

2. *CIVIL APPEAL NO. 12 of 1952*
3. *Hukum Chand Mills Ltd vs. CIT (1976) 103 ITR 548 (SC)*
4. *ITA No.4078/Del/2013*
5. *ITA NOS. 654/2012, 656/2012, 659/2012 & 661/2012*
6. *DIT (Int taxation) vs Morgan Stanley and Co. Inc. [(2007)292 ITR 416 (SC)]*

the enterprise. In such cases, nothing further would be left to be attributed to the PE."

Similarly, in ***Rolls Royce Singapore Private Limited***[7], it was emphasized that profits attributable to PE in India is made having regard to FAR Analysis. The AO held that 25% of the profits on sale of spare parts to customers in India was chargeable to tax which was reduced to 10% by CIT(A)[8] and upheld by ITAT. To substantiate this reduction, it explained, "The risk assumed by PE in India is very limited. It is only performing the functions of soliciting contracts for sale of assessee's products or promoting the sales. All other main or core activities regarding the arrangements or acquisition of products supplied by the assessee company to the Indian customers are performed in Singapore." Hence, a detailed transfer pricing analysis is imperative. Further it is important to note the ruling specifies that even if Rolls-Royce incurred losses globally, its Indian PE was still liable for taxes based on the profits derived from its local operations.

Other approaches including formulary apportionment and global losses

In 2013, in ***Convergys Customer Management Group Inc. vs. ADIT***[9], the revenues approach of profit attribution to PE by adopting global revenues in proportion of number of employees was rejected by the ITAT. The Tribunal used end customer revenue as the base to which a global operating income percentage was applied to arrive at profits attributable to the Indian operations.



In the recent ruling by the Delhi High Court (HC) in the case of ***Hyatt International Southwest Asia Ltd***[10], there was a significant shift from ***Nokia Solutions and Networks India Pvt. Ltd***[11], enabling Indian tax authorities to attribute income to PEs, solely based on their local operations. The Delhi HC was of a firm opinion that the argument of global income or profit being relevant, or determinative was totally unmerited and misconceived and that the decision in the Nokia ruling, had been misinterpreted to place reliance on global losses for income attributable to the PE.

5. BEPS 2.0 Pillar One and thoughts around it

BEPS Pillar One details allocation of taxing rights to the countries where businesses derive substantial economic value through user engagement and customer base, even in the absence of physical presence. These are currently focused on largest and most profitable multinational enterprises across the globe.

7. *Rolls Royce Singapore vs. ADIT, [(2011) 202 Taxman 45 (Delhi)]*
8. *Commissioner of Income Tax (Appeals)*
9. *ITA Nos. 1443/Del/2012 &5243/Del/2011 and ITA No. 1376/Del/2012*
10. *ITA 216/2020, ITA 217/2020, ITA 218/2020, ITA 219/2020, ITA 140/2021, ITA 36/2022, ITA 201/2023, ITA 215/2023*
11. *Nokia Solutions and Networks India Pvt. Ltd. vs. CIT, [2014] 359 ITR 342 (Del HC)*

Impact on digital economies and virtual business models

The ability to monetize data and user participation without physical presence leads to revenue generation without corresponding taxation. Pillar One aims to address this imbalance by establishing user engagement as a taxable nexus.

Additionally, the expansion of the PE definition under AP 7 and the new nexus-based approach under Pillar One means that businesses can now be taxed in jurisdictions where they derive value from user engagement, even without physical presence. This concept of a 'virtual PE' allows countries to tax companies based on their significant and sustained engagement with the market.

However, determining the share of profits attributable to digital user engagement remains complex due to difficulties in valuing intangible assets and user data. The challenges in profit allocation arise from the need to accurately assess the value created by user engagement and the data generated, which are often intangible and difficult to quantify.

Brief impact of Pillar One on India

India stands to gain additional tax revenue from MNEs operating in the Indian market, particularly in the tech and digital sectors. The implementation of Pillar One will allow India to tax a portion of the profits generated by these companies. This could be significant for India, as it has a large and growing digital economy with substantial user engagement.

As a pre-condition for the implementation of the BEPS Pillars, a country is expected to take steps towards abolition of digital services taxes or any other similar measures. The recent removal of the equalization levy with effect from 1 April 2025 was necessary for India to integrate into the global tax framework without it being a hindrance. The Government of India has also shown its intent to align to the proposed guidelines, post addressing of the reservations and suggestions made.

Challenges ahead include:

Achieving a global agreement on how to allocate profits remains challenging due to diverging national interests across nations. Out of the 136 nations that signed up to the two pillar Inclusive Framework, consensus has not yet been reached on the implementation of Pillar 1. The global consensus challenge is a significant hurdle in the implementation of Pillar One.

Despite the profit allocation formula, there is a risk of double taxation if countries interpret the rules differently or fail to agree on dispute resolution mechanisms. Additionally, India's SEP rules may overlap with Pillar One's allocation, creating further complexities in the tax landscape.

Achieving a global agreement on how to allocate profits remains challenging due to diverging national interests across nations.

6. Preparedness of the taxpayer and things to keep in mind

MNCs with supply chains or consumer base in India, should focus on the following key factors to better prepare for navigating the complex & evolving profit attribution landscape:

— **Consistency in approach:** Taxpayers should align their transfer pricing policies with the FAR-based approach



recommended by the OECD (AOA), which is in line with various Indian court rulings.

— **Documentation and compliance:** Robust documentation of functional analysis, market contribution, and value creation is critical. In cases of intangibles, a detailed DEMPE analysis is highly recommended.

– **Monitoring regulatory changes:** Taxpayers need to stay updated on developments like Pillar One, SEP, etc. to ensure appropriate measures are undertaken to mitigate potential challenges.

— **Dispute resolution mechanisms:** India's aggressive approach to profit attribution could lead to more disputes; therefore, taxpayers could explore advance pricing agreements (APAs).

— **Technology and digital footprint:** With India focusing on user-based taxation, taxpayers should evaluate their digital presence and user engagement strategies.

— **Distortion of Financial Reporting:** Incorrect profit allocation between the parent company and its PE may lead to inaccurate financial statements, affecting the financial performance and tax compliance of the business.

Conclusion

India's approach to profit attribution is at a critical juncture. The interplay of the OECD's AOA, India's domestic framework under the CBDT report of 2019 and Rule 10 reflects the ongoing push & pull between supply-side and market-based profit allocation. Various judicial precedents have laid down important principles but have not resolved the underlying inconsistencies & challenges of the new age digital economy.

Pillar One introduces a new variable that could reshape India's profit attribution landscape. For taxpayers, navigating this complex environment requires a balanced approach, combining robust functional analysis with a clear understanding of market-based profit drivers. At present, India's stance on profit allocation emphasizes the need for a fair and equitable distribution of profits to market jurisdictions, particularly for developing and emerging economies. The proposed solution, comprising Pillar One and Pillar Two, aligns with India's advocacy for considering demand-side factors in profit allocation and addressing cross-border profit shifting. While India remains committed to a consensus-based, implementable solution that ensures meaningful and sustainable revenue allocation, MNCs with current/proposed supply chain integration with India would need to track developments on profit attribution to India, rather closely.

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LATEST TRENDS IN PRINCIPLES OF INTERPRETATION IN INTERNATIONAL TAX



CA Daksha Baxi

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Overview

The author has traced the development of bilateral treaties for the growth of cross border commerce and international trade and discussed how the various model conventions and their commentaries have evolved to provide the tools of interpretation of treaties. Author also discusses the role of Customary International law, codified in the Vienna Convention on the Law of Treaties relied upon by the Indian courts while interpreting tax treaties as well as the role of commentaries on model conventions. Finally, the author dives deeper into the latest trend of interpretation as prescribed and used by the Supreme Court in the case of Nestle SA of the Netherlands. It is perhaps the first time that court has delved into the dualist approach to implementation and interpretation of tax treaties prescribed by the Indian Constitution. The risk of the parliament rejecting the provisions of a treaty entered into by the executive arises and the author highlights the saving grace under law by way of notification of the provisions in the official gazette, which has been the practice followed by the executive as per section 90(1) of the Income Tax Act. The author concludes that such notification would become a major tool for relying on the beneficial provisions of a DTAA.

Relevance of International Tax in growing international trade, commerce and movement of people

What does international tax mean to us? Are we concerned with how other countries tax income of their residents? Not really, but we would be concerned if one of us is in a situation, where we are not only taxed in India but also in another country with which or in which we do business and earn income. Similarly, persons living and established outside India and doing business in and with

The author dives deeper into the latest trend of interpretation as prescribed and used by the Supreme Court in the case of Nestle SA of the Netherlands.

India could face this situation. Understanding and ensuring that we as Indian residents are not taxed both in India and the other country and vice-e-versa for the residents of other countries is the area of international taxation.

For growth of trade and commerce, it is legitimate to expect that income arising from transactions of a varied nature involving flow of capital, intellectual property, goods and

services are not doubly taxed. It is also necessary for the legitimate claimant of tax to receive their dues. This calls for some sort of organised understanding between and inter-se countries on how they will tax the residents of the other country for income sourced in their state.



Emergence of Double Taxation Avoidance Agreements

This is sought to be done by entering into double taxation avoidance agreements ("DTAA" or "DTC") also referred to as Tax Treaties. This brings us to trace the evolution of double taxation avoidance agreements. The first comprehensive international treaty was signed between the Austro-Hungarian Empire and Prussia (present day Germany) on 21st June 1899

Understanding and ensuring that we as Indian residents are not taxed both in India and the other country and vice-e-versa for the residents of other countries is the area of international taxation.

("Treaty"), focused on the prevention of double taxation. At the base of the Treaty was the principle of 'reciprocity' between the treaty partners. Later international institutions emerged. They sought to create 'Model Tax Conventions' to provide a standard template, which would be adopted by their member countries so as to have harmonious manner of avoiding double or non-taxation.

A widely recognized norm of international tax law is that individuals or entities are taxed in the country of residence on their worldwide income. However, it is also recognised that where the income has a source within another jurisdiction, that country should have a right to tax such income – the nexus approach. This requires nations to allocate right to tax the income between them equitably – whether on the basis of residence or on the basis of source.

Two model convention models emerged : (i) by the Organisation of Economic Co-operation and Development ("OECD") and (ii) by the United Nations("UN")

While the two model conventions have more or less similar standard format, they are different in their fundamental approach:

- OECD is residence based. Source country taxation is recognised, but it is severely restricted

- UN is focused on both source and residence. It seeks to achieve more equitable balance between taxation rights of capital importing and exporting countries.

This difference is because OECD is a group of developed nations who are exporters of capital. UN- which was formed after World War II as League of Nations- has sought to give a model to the capital importing countries who have abundant natural resources but lack capital. Hence, UN Model

seeks to protect the taxing rights of the capital importing countries. Additionally, USA has its own model, which is the base for the DTAAs entered by the US with the rest of the countries of the world. The US also publishes Technical Explanations with respect to its model convention. This could be viewed as its own 'commentaries' on its model convention.

Even though models exist, entering into Tax Treaties is simply guided by economic needs of the respective countries and their respective ability to negotiate the balance between the residence and source-based taxation approach propounded by the models. The two nations entering into Tax Treaty voluntarily enter into it, using whichever model that is suitable to them and negotiate the provisions as per their economic needs. The model conventions provide broad guidelines.

Tools of interpretation of international taxation

(1) The Relationship of Treaties and Domestic Law

The first and foremost principle is to read both domestic law and the DTAA, to establish what is intended by the two countries.

The Income Tax Act, 1961 (**"IT Act"**) includes section 90, which does the following :

(i) It permits the Central Government to enter into agreement with another country or territory to grant relief from double taxation to the residents of both countries, for exchange of information, prevention of tax avoidance and recovery of tax both in India and the other country.

(ii) It authorises the central government to notify such agreements in the Official Gazette as necessary for implementation of the agreements. Thus, each agreement is not needed to be placed before the Parliament.

(iii) It also provides that where such agreement exists, in case of a taxpayer who is eligible to the application of such agreement, the provisions of the IT Act shall apply to the extent they are more beneficial to such taxpayer. In other words, the Treaty overrides the provisions of the IT Act, unless the IT Act is more beneficial to the non-resident taxpayer.

When considering taxability of a person, Sections 4 and 5 of the IT Act are most relevant. The charging section, S. 4- clearly states that income tax shall be charged for any year, in accordance with and subject to the provisions of the IT Act.

Section 5, dealing with the scope of total income begins with the words "Subject to the provisions of this Act, the total income ....."

While section 9, laying down the deeming provisions for income deemed to arise in India does not mention 'subject to', clearly the deeming section cannot work in isolation of and overriding sections 4 and 5.

This means that the charge of tax and scope of income are both subject to the provisions of section 90 of the IT Act.



Accordingly, where a DTAA exists, if the person coming from such territory or country is eligible to the DTAA, then that person will be taxed in India as per the provisions of the DTAA, unless the provisions of the IT Act are more beneficial. The IT Act also provides that where a term used in the DTAA is not defined in it or in the IT Act, the meaning assigned to it in the notification issued by the Government in the Official Gazette in this behalf would apply.

On several occasions the courts in India have stated that Tax Treaties are negotiated and entered into by the diplomats after negotiations. They are the result of their assessment of what factor of mutual benefit is to be given more importance. As the drafters of DTAA language are not the drafters of law, the language in the DTAA needs to be interpreted giving credence to the intention rather than the exact meaning of the words used.



If in case of a term or language of the DTAA, there is no Official Gazette in that regard or where there is one but does not address the issue, then other tools of interpretation and application as part of International Law can be referred to. The articles of Vienna Convention on the Law of Treaties ("VCLT"), commentaries on the model conventions ("MCs"), the interpretation given by courts in India as well as other jurisdictions in similar circumstances and the intention of the parties, as established through practice are all drawn upon.

While applying the guidance by VCLT, Commentaries on MCs, the constitutional approach in the respective countries to incorporate the Treaties in domestic law has to be examined. This is essential since it is likely that some of the negotiated provisions may not be in line with the domestic law provisions, e.g. rate of tax for a particular category of income, characterisation of income, when is it deemed to accrue or arise in the source state, etc. The two approaches followed by nations are Monism and Dualism.

Monism vs. Dualism[1]

Monism: Under this approach, international law and domestic law are considered part of the same legal system. International treaties are automatically incorporated into domestic law upon ratification, and domestic courts can directly apply them.

- ***Examples of Monist Countries:*** Some countries that follow this approach in their legal systems include Argentina, Italy, the Netherlands, Belgium, Brazil.

Dualism: International law and domestic law are seen as separate systems. International treaties need to be transformed into domestic law through legislation before they can be applied in domestic courts.

- ***Examples of Dualistic Countries:*** Some of the countries following this approach are

1. *Taken from AI Generated note from the Internet.*

Australia, Austria, Norway, Germany, Sri Lanka, UK, US, India.

- ***Approach of the UK and the US – Dualist or Monist?***[2] It is interesting to note that both these countries have oscillated between being dualist and monist, which is evident while going through their approach to implement Customary International Law ("CIL") and the international treaties. Though treaties in the US have supremacy over domestic laws, in some instances, they took the stance of being dualist and did not implement them because the parliament had not incorporated it in the domestic law. However, they have adopted CIL without any such incorporation of the legislature. The same is the situation in the UK.

(2) Vienna Convention on the Law of Treaties ("VCLT")

Despite the fact that Tax Treaties are mutually negotiated, voluntarily entered, and are based on MCs, a need for developing some sort of law which enables the contracting nations to implement the Tax Treaties and their provisions, notwithstanding the Treaty provisions being at variance with domestic law was recognised. Customary International Law ("CIL") emerged to provide guidance on how bilateral Treaties should be performed by each contracting state. VCLT is essentially codification of Customary International Law.

Known as the "treaty of treaties", it entered into force on January 27, 1980, though first came out in 1969.

It defines a treaty as "an international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation".

The VCLT establishes comprehensive operational guidelines, rules, and procedures on how treaties are drafted, defined, amended, interpreted and applied. It is perceived and applied by courts even in India as the Master Treaty which does not have statutory force but provides binding obligations under International Law. Thus, it becomes one of the major tools of interpretation of international taxation.

VCLT is binding only on its signatories, and provides useful basis of interpretation to non-signatories such as India since it serves as a mediator. Indian courts in general have referred to the articles of VCLT for interpreting international treaties, especially Tax Treaties and their application.

The Supreme Court ("SC") in case of ***Ram Jethmalani vs. Union of India :[2011]***[3], while examining the application of Article 26 of the DTAA between India and Germany on exchange of Information, refers to Article 31 of the VCLT and upholds its applicability in interpreting the DTAA.

At para 60, it states as follows :

Article 31, *"General Rule of Interpretation", of the Vienna Convention on the Law of Treaties, 1969 provides that a "treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."* While India is not a party to the Vienna Convention, it contains many principles of customary international law, and the principle

2. *Reference : The RMLNLU Law Review Blog, authored by Kartik Agarwal on "Are the Indian Courts Still Following the Constitutional Principle of Dualism? Not quite So".*
3. *12 taxmann.com 27 (SC) dated 4 July 2011*

of interpretation, of Article 31 of the Vienna Convention, provides a broad guideline as to what could be an appropriate manner of interpreting a treaty in the Indian context also.

Further, laying down important principle of interpretation of a DTAA, the SC at para 61, stated as follows :

'a treaty is an indirect enactment, instead of a substantive legislation. Drafting of treaties is notoriously sloppy, whereby inconveniences obtain. The Court noted the dictum of Lord Widgery, C.J. that the words "are to be given their general meaning, general to lawyer and layman alike.... The meaning of the diplomat rather than the lawyer." The broad principle of interpretation, with respect to treaties, and provisions therein, would be that ordinary meanings of words be given effect to, unless the context requires otherwise. .....The Government cannot bind India in a manner that derogates from Constitutional provisions, values and imperatives.

(3) Commentaries on Model Conventions ("MC") by the OECD, the UN and the US

In addition to VCLT, both OECD and UN have drafted their commentaries on the

The Government cannot bind India in a manner that derogates from Constitutional provisions, values and imperatives.

articles in the MCs. They provide guidance on interpreting and applying the provisions of relevant Tax Treaty, subject to the legal basis in the sovereign nation for infusing the same in the domestic law. In general, the OECD Commentaries are used by the developed countries for the DTAA amongst them, UN Commentaries are used by the developing nations for Tax Treaties amongst them. A mix of OECD and UN commentaries are used when the DTAA to be interpreted is between developed and developing country, depending on the actual language of the provision in the treaty and the intention of the parties. For interpreting US DTAA, a mix of UN and US commentaries are used.

OECD commentaries are regarded 'dynamic' and used frequently having persuasive value for interpreting DTAAs. Even Indian courts have drawn upon these commentaries. E.g. in the landmark judgement of Visakhapatnam Port Trust[4].

On the issue of the taxpayer seeking benefit of the DTAA, the Court referred to how to apply the provisions of the DTAA vis-à-vis the provisions of the IT Act. While doing so, the court quoted as follows in respect of the DTAAs :

Lord Radcliffe in Ostime (Inspector of Taxes) vs. Australian Mutual Provident Society [1960] AC 459 (HL) had described the language employed in these agreements as the 'international tax language'

While applying and invoking the provisions of the DTAA, the HC case extensively referred to the OECD Commentaries. This decision is dated 1988. All courts (where there was a need to refer to OECD Commentaries) thereafter have relied on this judgement to refer to OECD commentaries, having persuasive value for resolving an interpretation issue.

4. [1988] 144 ITR 146

(4) Does India follow Monism or Dualism?– Ambivalence of approach is observed

- In Vellore Citizens Welfare Forum[5] case, the SC was considering application of certain environmental laws, which were accepted as CIL. Applying those principles, the SC held that the rules of CIL which are not contrary to the municipal law shall be deemed to have been incorporated in the domestic law and shall be followed by the Courts of Law. While this is settled position, in case of Tax Treaties India's position is ambivalent.

- The language of Article 253 of the Constitution of India signifies the Dualist approach. This Article requires enabling legislation by the parliament to infuse any international agreement in the domestic legal system. However, the SC, in case of *Azadi Bachao Andolan*[6] held that enabling legislation by the Parliament is only required when the treaty or convention affects the rights of the citizens. By implication, this means that the treaties, other than those which affect the rights of the people, can be directly incorporated into the domestic law.

- In ***Vishakha vs. State of Rajasthan***[7], the SC held that the international conventions and laws can be considered by the Court for construing domestic law if they are not inconsistent with domestic law. Several such decisions by the SC show that the international treaties and conventions can be referred to and relied upon by the court, even if they are not part of municipal law.

- It may be observed through various decisions of the Indian courts that the position of India vis-à-vis international law is not always in consonance with its Constitutional policy. This may be due to the intention to remain practically relevant and in comity with the international community.

- However, the decisions of the SC in recent times in relation to interpretation of international tax has gone back to upholding the Dualist approach as propounded by Article 253 of the Constitution. This is the case of ***M/S Nestle SA***[8], decided on 19 October 2023. The SC has thus laid down the law that dualist approach must be followed for giving effect to beneficial provisions in the DTAA, enabling incorporation of the DTAA provisions in the domestic law.

The SC was dealing with interpretation of the Most Favoured Nation (**"MFN"**) clause contained in various Indian treaties with countries that are members of the OECD. The MFN Clause provides for lowering of tax rate at source on dividends, interest, royalties or FTS as the case may be, or restriction of scope of royalty / FTS in the treaty, similar to concession given to another OECD country subsequently.

The SC dealt with the 2 bilateral treaties : with The Netherlands and Switzerland

Two issues arose :

(i) Whether there is any right to invoke the MFN clause when the third country with which India entered into the latter DTAA was not an OECD member when the said beneficial DTAA was entered into.

5. *[1996] Supp. (5) S.C.R. 241/ 1996 INSC 952*
6. *[2003] 132 Taxman 373 (SC)*
7. *AIR 1997 SC 3011*
8. *2023 INSC 928 CIVIL APPEAL NO(S). 1420 OF 2023*

(ii) Whether the MFN clause is to be given effect automatically or it is to come into effect only after a notification is issued.

The first question did not need to look into the constitutional position of DTAAs in India but needed to interpret the language of Article IV of the first protocol in the DTAA. The second question raised the issue of constitutional approval. Seeking the concession granted under the Protocol, the taxpayers (residents of The Netherlands) relied on the language of the preface of the Protocol which inter alia stated that the Protocol "*shall form an integral part of the Convention*"

The text of the MFN provision is contained in Paragraph 2 of Article IV of the first Protocol reads as follows :

*If after the signature of this convention under any Convention or Agreement between India and a third State which **is** a member of the OECD India should limit its taxation at source on dividends, interests, royalties, fees for technical services or payments for the use of equipment to a rate lower or a scope more restricted than the rate or scope provided for in this Convention on the said items of income, then as from the date on which the relevant Indian Convention or Agreement enters into force the same rate or scope as provided for in that Convention or Agreement on the said items of income shall also apply under this Convention.*

Pursuant to this, several parts of the Protocol were made applicable to the India-Netherlands DTAA when latter DTAAs with OECD countries granted benefits which were absent in the India-Netherlands DTAA. This was done by notifying their applicability through notifications in the *official gazette*.

To respond to the questions raised above, the first interpretation issue that arose was in interpreting and applying the word "IS" in the protocol:.

a) Did "IS" in this context mean that the third country, with which later DTAA was entered, should be a member of OECD when the resident of the earlier DTAA with the OECD Country seeks the beneficial provision of the latter DTAA?

OR

b) Did "IS" in this context mean that the third country with which the later beneficial DTAA was entered into should have been a member of the OECD at the time of entering into the said DTAA?

While Delhi HC favoured the first interpretation, the SC favoured the second interpretation.

The Delhi HC used the following explanation for its interpretation of the use of the word "IS":

Para 17.4 : The word 'is'- is both autological and heterological. An autological word is one that expresses the property that it possesses. Opposite of that is a heterological2 word, i.e., it does not describe itself. The examples of autological words are expressions such as "English", "Noun", or "Word". Heterological words as indicated above are those which do not describe themselves or have the potential of developing into several forms or supporting multiple interpretations. An example of a heterological word is the word "long". The word long does not describe itself because it is not a long word.

Para 17.5.: Therefore, bearing the aforesaid in mind, the best interpretative tool that can be employed to glean the intent of the Contracting States in framing Clause IV (2) of the protocol would be as to how the other contracting State [i.e., the Netherlands] has interpreted the provision.

The Delhi HC thus relied on the executive decree issued by The Netherlands, pursuant to the Protocol, as a method of interpretation of how the event, i.e. entry of another country into OECD, which had a previous DTAA with India (or where a country which was member of OECD and subsequently entered into DTAA with India) had to be dealt with.

The SC however, disagreed with the principle relied upon by the HC and said that such an interpretation would be contradictory to the entire language of the Article IV of the Protocol and render some of the language redundant.

Constitutional Authority for incorporating Protocol into domestic law

The issue of the Dualistic approach under Article 253 of the Constitution of India was not raised before the Delhi HC

Before the SC, the Additional Solicitor General (**"ASG"**) of India, objected to the manner of interpretation adopted by the Delhi HC, siting Article 253 of the Constitution of India, which reads as follows :

Legislation for giving effect to international agreements. *Notwithstanding anything in the foregoing provisions of this Chapter, Parliament has power to make any law for the whole or any part of the territory of India for implementing any treaty, agreement or convention with any other country or countries or any decision made at any international conference, association or other body.*

Based on this, the ASG argued that India follows the "Dualist" practice. This meant that international treaties and conventions are not, upon their ratification, automatically assimilated into municipal law (i.e. the national legal system) but would require enabling legislation. This is in contrast to those countries which are "Monist", wherein the treaty provisions are enforceable like municipal law, and are to be given equal weight by courts.

As we have noted above, The Netherlands adopts Monist approach which seems to be the basis of their decree. The question that arises is whether a decree issued by the other country is binding on India and therefore the means of incorporating the provision into Indian domestic law? Clearly, the SC has taken a view that it is not.

It is important to note that, in the course of reaching their decision, the SC referred to several aspects, including the practice followed by India in applying the beneficial provisions of the protocol of Tax Treaties and concluded that India did indeed follow the Dualist approach and wherever the beneficial provision in a DTAA or protocol were to be incorporated, the practice followed was to notify the same.

It is also important to refer to Article 29 of the India-Netherlands DTAA, dealing with Entry into Force reads as follows :



Each of the States shall notify to the other the completion of the procedures required by its law for the bringing into force of this Convention. This Convention shall enter into force on the thirtieth day after the latter of the dates on which the respective Governments have notified each other in writing that the formalities constitutionally required in their respective States have been complied with, and its provisions shall have effect in both countries.

The counsels of the claimants of MFN clause argued that there was no requirement in the subject MFN clause to issue any notification to bring into force the beneficial provisions from subsequent DTAAs or by way of a notified protocol or negotiation. Since the DTAA itself along with the protocol(which was integral to the DTAA) was notified for becoming effective, the requirement of Article 253 was fulfilled. No further notification was needed for the MFN protocol to become effective. However, the SC did not accept this.

The SC relied on their own decision in case of Maganbhai Ishwarbhai Patel & Ors. v. Union of India & Others

What do we see as trends in interpreting International Taxation?

The CBDT, in Finance (No. 2) Act, 1991, clarified with retrospective effect from 1-4-1972, vide Circular No. 333 dated 2-4-1982 that where a specific provision is made in the DTAA, the provisions of the DTAA will prevail over the general provisions contained in the IT Act and where there is no specific provision in the DTAA, it is the basic law i.e. the provisions of the IT Act, that will govern the taxation of such income. This position has been upheld in many judicial decisions in India. The prominent amongst them are ***CIT vs. Visakhapatnam Port Trust, (1983) 144 ITR 146 (AP); Union of India vs. Azadi Bachao Andolan, (2003) 263 ITR 706; CIT vs. Kulandagan Chettiar (P.V.A.L.), (2004) 267 ITR 654 (SC)***.

It was generally regarded that this principle applies in case of invocation of the protocol in a DTAA.

However, the decision of the SC in case of Nestle lays down a different law. The SC relied on their own decision in case of ***Maganbhai Ishwarbhai Patel & Ors. vs. Union of India & Others***[9]. They referred to the following observations of the Court in that judgement:

If the national executive, the Government of the day, decide to incur the obligations of a treaty which involve alteration of law they have to run the risk of obtaining the assent of Parliament to the necessary statute or statutes.... .Parliament, no doubt, ...has a Constitutional control over the executive : but it cannot be disputed that the creation of the obligations undertaken in treaties and the assent to their form and quality are the function of the executive alone. Once they are created, while they bind the State as against the other contracting parties, Parliament may refuse to perform them and so leave the State in default."

These observations are valid in the context of our Constitutional set up.

9. *1970 (3) SCR 53*



The above can be regarded as resulting in India being a defaulter for implementing the DTAA provisions, notwithstanding Articles 26 and 31 of VCLT. However, there is a saving grace. The authority given to the executive by the parliament under section 90 of the IT Act provides this saving grace. It permits the executive to enter into Treaties and section 90(1) empowers the executive to notify such Treaties and thereby incorporate them in the domestic law. While each change is not required to be placed before the parliament, the notification under S. 90(1) is required.

The SC then also clarifies on the interpretation of the terms in the Treaty, where the legislative enactment is needed to implement the Treaty. In this context, the Court said that if the terms of the legislative enactment do not suffer from any ambiguity or are clear, they must be given effect to even if they do not carry out the treaty obligations. But the Treaty becomes important if the expressions used by the Parliament are open to be construed in more than one way. In such a situation, the meanings which is consonant with Treaty obligations is to be preferred.

In conclusion, the fact that India followed dualist approach had somewhere drowned in applying DTAA provisions, relying on VCLT, MCs and judicial precedents. This has now become prominent. The taxpayers and advisers will need to read the provisions of the DTAA, protocol and other tools of interpretation carefully for interpreting and applying the provisions in DTAA and Protocols. Notification by the government in the official gazette would remain the overriding requirement, to apply any Treaty or Protocol.

Whether this decision would impact India's position on honouring DTAA commitments in the comity of nations remains to be seen. We know that Netherlands has withdrawn the decree it had issued, thus, denying the more beneficial treatment as per para 2 of Article IV of the Protocol to Indian residents.

■

FINANCE BILL 2025



CA Snehal Mayacharya

Analysis of further amendments to Finance Bill 2025 as passed by Lok Sabha and received Presidential Assent

Current landscape of Indian taxation law revolves around unearthing the impact of the new Income Tax Bill 2025, a piece of legislation that heralds public engagement and consultation. On 25th March 2025, the Lok Sabha passed Finance Bill 2025 with several amendments, bringing the Budget 2025 into the limelight. The Rajya Sabha approved these changes on 27th March 2025. The Bill received Presidential Assent on 29th March 2025 with changes in the Income-tax Act, 1961 (ITA). The article discusses the impact of key amendments by the Finance Act 2025 (FA 2025) in respect of direct taxes.

Withdrawal of 6% equalisation levy (EL 1.0) on advertisement services

FA 2025 has withdrawn the 6% equalisation levy on non-residents providing specified services with effect from 1st April 2025 by amending the Finance Act, 2016.

Background

- To recapitulate, on 1st June 2016, India was the first mover to introduce an equalisation levy, pursuant to the 2018 OECD BEPS Action Plan 1

recommendation. EL 1.0 was introduced under Chapter VIII of the Finance Act 2016 as a measure to tax income of non-residents not having a physical presence in India. Section 165 of the Finance Act, 2016 provided that gross consideration earned by certain non-residents on the provision of specified services like an online advertisement, provisio n of digital space and related services shall be subject to a 6% levy. The levy applied to a rendition of services to residents in India carrying on business or profession and non-residents having a permanent establishment (PE) in India (specified payers). It excluded small-value transactions up to Rs. 1 lakh.

- To ensure appropriate deduction and payment of EL to the Government exchequer, Section 40(a)(ib) of ITA disallowed base expenditure on specified services in the hands of specified payers if there was a failure to deduct EL and/or deposit of the EL.

- Apart from the obligation to deduct and pay, specified payers were also obligated to comply with various procedural requirements such as furnishing statements, etc.

- In the hands of non-residents, income (excluding royalty and fees for technical services) which suffered EL 1.0 was exempt from income tax by virtue of Section 10(50) of ITA.

Amendment and impact

- FA 2025 amends Section 165 of the Finance Act 2016 to provide that EL 1.0 is not applicable to the consideration received or receivable by non-residents on or after 1st April 2025 on the rendition of specified services. Consequently, the exemption under section 10(50) available to non-residents is withdrawn on or after 1st April 2025.

- On account of the withdrawal of EL 1.0, non-resident service providers providing specified services shall be subject to taxation under the general provisions of ITA, such as business connection, royalty, etc.

- Accordingly, non-residents providing online advertisement services to residents and involving the provision of the right to use software (for instance, digital space) can be impacted by Explanation 4 to Section 9(1)(i), which covers any right to use computer software. In such cases, royalty income may be taxed on a gross basis under Section 115A at 20% or applicable rates under the respective DTAA's. Non-residents from tax jurisdictions that have a narrower definition of royalty under an applicable tax treaty can claim non-taxability by applying the ratio of the Supreme Court in the case of Engineering Analysis Centre of Excellence (P.) Ltd vs. CIT (2021) (432 ITR 471) .

- Further, Explanation 2A to Section 9(1)(i), which defines significant economic presence, includes any transaction in respect of service provided by a non-resident to the person in India provided the revenue threshold of Rs. 2 Crs. or engaging with 3 lakh users is met. Hence, non-resident service providers can trigger business connections in the form of a significant economic presence in India. Non-residents from countries with which India has a tax treaty shall have a greater onus of establishing that such non-residents providing advertisement services do not have a PE in India. If non-residents are not eligible

for tax treaty benefits or are tax residents in jurisdictions with which India does not have a tax treaty, business connection in the form of significant economic presence shall trigger. In the absence of any attribution rules for significant economic presence, the difficulty in determining income in hands of non-residents is multiplied.

- For transactions undertaken post 1st April 2025, resident payers shall have to comply with withholding tax, if applicable and undertake related compliance.

- Finance (No.2) Act, 2024 withdrew the 2% equalisation levy on e-commerce supply or service w.e.f. 1st August 2024 in the wake of ongoing negotiations taking place at OECD on Pillar 1 for taxing the top 100 large MNE groups . With the embarkment of the Trump Government in the USA, on 20th January 2025, the President issued an Executive Order stating that any prior consent or commitment made by the US Government on the BEPS 2.0 project has no force and effect in the US in the absence of ratification of the same by the US Congress. Further, another Executive Order also instructed the US Treasury Department to investigate whether any foreign country subjects US citizens or corporations to discriminatory or extraterritorial taxes . Hence, it was speculated that the withdrawal of EL 1.0 was pursuant to changes in the global political environment.

- While answering the apprehension in the Rajya Sabha, Finance Minister in Rajya Sabha Debate explained the reason as: "So about the levies, withdrawing of the levies, is it a reaction to President Trump's tariff war and so on?..... there were two types of equalisation levies. A 6% levy imposed in the financial year 2016 and 2% levy imposed in 2020 which were applicable before July 2024 itself. The 2% levy was removed after stakeholder consultation Sir in July budget to ease the compliance burden and that was much before President Trump - even before he took his office and similarly several other steps have been taken. So the 6% levy which is being removed is a part of that process and that's what is going on".

Presumptive taxation scheme for non-residents providing services to electronic manufacturing facility (Section 44BBD)

Background:

- Finance Bill 2025 introduced a new presumptive tax regime under Section 44BBD for non-residents providing services or technology in India to set up an electronics manufacturing facility or in connection with manufacturing or producing electronic goods, articles or things to resident companies. Under the regime, 25% of the specified amount shall be deemed to be profits and gains from business. Such income is taxed at a rate of 35% in the hands of foreign companies falling under Section 44BBD leading to an effective tax rate of less than 10%.

- Considering the nature of services covered by Section 44BBD, it is possible that the income of non-residents can be characterised as fees for technical services (FTS) or royalties. If such FTS and royalty are connected with the PE of non-residents in India, Section 44DA applies for the computation of the business income of non-residents from such services. Also, if such FTS or royalty income earned by non-residents

is not connected to a PE in India, then the income of non-resident becomes taxable on gross basis under Section 115A (subject to any tax treaty benefit).

- At the proposal stage, the interplay of Section 44BBD, Section 44DA and Section 115A was ambiguous. In a situation where fees for technical services and royalty earned by non-residents rendering services to electronic manufacturing entities in India are connected to PE, section 44DA would have been triggered. Section 44DA requires the computation of income as per provisions of the ITA, which includes Section 44BBD. Section 44DA(2) would have required non-residents to maintain books of account as per section 44AA and undertake tax audit compliance under section 44AB.

- This would have led to an anomaly with the underlying intent of a presumptive taxation scheme for non-residents, i.e. paying tax in India without the requirement of maintaining books of accounts and undertaking tax audits.

Amendment and impact

- FA 2025 has inserted a proviso to section 44BBD, which states that provisions of section 44DA and section 115A do not apply to income earned by non-residents on account of providing services or technology. It is also reiterated in Q.2 of FAQ 2 issued by Supplementary FAQs to Finance Bill.

- On comparison with other presumptive tax provisions applicable to non-residents like Section 44BB (services provided in relation to oil and gas) and Section 44BBB (construction services in relation to turnkey project), there is a specific section that enables non-residents covered under said sections to declare lower profits than deemed presumptive profits. Such facility is not provided to non-resident service providers under Section 44BBD.

- There is no specific relaxation to non-residents covered under Section 44BBD from complying with provisions of tax audit under Section 44AB. Presently, tax audit is not applicable to non-residents covered by Section 44B (non-residents engaged in shipping business) and Section 44BBA (non-residents engaged in aircraft). The language of corresponding provisions in the new Income Tax Bill 2025 also does not provide any relaxation to non-residents covered by Section 44BBD from compliance with maintenance of books of account and tax audit under the proposed legislation.

- Also, the provision of minimum alternative tax under Section 115JB is not applicable to non-residents covered by presumptive tax regimes like Section 44B, 44BB, 44BBA, 44BBB. No such exclusion is provided for non-resident company covered under Section 44BBD.

Relaxation of ascertaining indirect participation by Indian residents in eligible offshore investment funds managed from India (Section 9A)

Background:

- Section 9A provides relaxation from the scope of business connection under Section 9(1) to an eligible offshore investment fund managed by an eligible investment manager in India. The section lays down conditions basis which such relaxation is granted. One of the conditions is that the direct or indirect participation by a person resident

in India, including the fund manager, should not exceed 5% of the corpus fund. Further, the investments made by eligible fund managers up to Rs. 25 Cr in the first 3 years of operation of the fund shall not be taken into account in the calculation of the 5% threshold.

- Rule 10V of Income-tax Rules, 1962 prescribed guidelines for applying safe harbour under Section 9A. Rule 10V(1) requires offshore investment funds to adopt a look-through approach where any investor is an institutional entity. Rule 10V(2) requires the offshore fund to undertake due diligence where a direct investor is not a natural person to ascertain the indirect participation of Indian residents and the extent thereof.

Amendment and impact

- FA 2025 has removed the condition of ascertaining indirect participation by Indian residents in eligible offshore investment funds. Q.2 of FAQ 1 to the Supplementary Finance Bill explains that the amendment will reduce the compliance burden and enable offshore fund managers to relocate to India.

- The said amendment is a welcome move as it alleviates the requirement on offshore investment funds to ascertain and monitor the indirect participation by Indian residents through overseas collective investment funds, institutional investors, etc. The offshore investment fund is no longer required to undertake due diligence and internal controls to identify the extent of indirect participation of Indian residents. Removing restrictions shall also encourage more investment in an eligible offshore investment fund.

- The amendment introduced by Finance Bill 2025 regarding the biannual evaluation of breaches of the 5% threshold shall apply to direct investment by Indian residents.

Restoration of power to the Central Government for relaxing condition of Section 9A for funds located in the International Financial Services Centre (IFSC)

Background

- Section 9A(8A) empowers the Central Government to relax the conditions for availing safe harbour of offshore investment funds, not creating business connections or residency under ITA if such fund manager is located in IFSC and has commenced business on or before 31st March 2024. Finance Bill 2025 had proposed an amendment to restrict the power of the Central Government to relax/modify one of the conditions, viz., aggregate of direct and indirect participation by Indian resident investors does not exceed 5% of the corpus in eligible investment fund located in IFSC.

- Amendment and impact: FA 2025 has restored the powers of the Central Government to exempt or, modify or relax the condition of the 5% threshold by Indian residents in offshore investment funds whose fund manager is located in IFSC. This gives flexibility to policy makes to tweak the conditions to encourage and promote fund managers located in IFSC in the future.

Change in definition of capital gains definition for investment made by Alternate Investment Funds (AIF) (Section 2(14))

Background

- Section 2(14) defines capital assets in a wide manner to include property of any kind, whether or not connected to business, with certain exclusions like stock in trade. In order to resolve the uncertainty revolving around the characterisation of income of Foreign Portfolio Investors (FPI), Section 2(14)(b) deems securities held by FII investing as per Securities Exchange Board of India (SEBI) Regulations as a capital asset. Hence, income from the transfer of such securities is always taxed as capital gains in the hands of FIIs.

- In order to alleviate similar difficulty encountered by AIF, Finance Bill 2025 proposed to extend the fiction of Section 2(14)(b) to Category 1 and 2 AIF as per Section 115UB that invests in compliance with SEBI Act, 1992. The Explanatory Memorandum explains that amendment is made to clear ambiguity in determining the characterisation of income earned from securities. This amendment did not cover AIF set-up and investment according to IFSC regulations.

Amendment and impact

- FA 2025 now extends the fiction under S.2(14)(b) to AIFs that make investments according to IFSC. There is prevailing controversy on the characterisation of income from securities, i.e. gain on sale of securities, whether taxable under business income or capital gains. Central Board of Direct Taxes (CBDT) has issued circulars from time to time to clarify factors to be considered for the characterisation of securities as stock in trade or capital assets.

- By virtue of deeming fiction under Section 2(14)(b), AIFs under Section 115UB are relieved from the onus of substantial intent of holding the investment and treating it as inventory or capital gains. The amendment takes effect on 1st April 2026 and applies to existing investments in securities held by investment funds. For past years in assessment or litigation, the amendment may act as a guide for characterising securities invested as per SEBI and IFSC regulations.

Removal of conditions prescribed under Rule 21AIA for claiming tax exemption by fund under Retail Schemes and Exchange Traded Funds (ETFs) in IFSC

Background

- Section 10(4D) exempts certain incomes earned by specified funds, which includes funds granted certification as a retail scheme or an ETF under IFSC regulations and which fulfil prescribed conditions under ITA. CBDT vide Notification No. 10/2025 amended Rule 21AIA(3) of Income-tax Rule, 1962, which enlisted conditions to be fulfilled by funds under the retail scheme and ETF to claim the said exemption. This created difficulty for such funds as they had to fulfil conditions under IFSC regulations and Rule 21AIA.

Amendment and impact

- FA 2025 has eliminated the requirement to fulfil any conditions under Rule 21AIA for specified funds under retail schemes and ETFs to claim an exemption under Section 10(4D). Hence, it is required to fulfil only the conditions laid down for such funds or schemes in the IFSCA regulations .

- This grants relaxation to such specified funds to fulfil conditions under different statutes. The amendment takes effect from 1st April 2025, which is aligned with the date from which the Finance (No.2) Act 2024 intended exemption to funds under retail schemes and ETFs.

- Correspondingly, Finance Bill 2025 granted an exemption under Section 47(viiiad) to shareholders/unit holders/interest holders of the original fund on the relocation of the offshore original fund and receipt of shares/units/interest in the resultant fund in lieu thereof. At the proposal stage, the exemption was extended to include the resultant fund being a retail scheme, and ETFs provided they fulfil conditions under Section 10(4D). On removal of conditions under Section 10(4D), the consequential amendment is also made to Section 47(viiiad). Now, any retail Scheme or ETF that has been granted IFSCA certification will be treated as a 'resultant fund' for the purposes of section 47(viiad). The offshore fund as well as its investors, can enjoy tax neutrality on relocation to IFSC.

Extending the exemption under Section 10(4E) to income distributed from OTC derivatives

Background

- Section 10(4E) of ITA provides an exemption to non-residents on income arising from the transfer of offshore derivate instruments (ODI), non-deliverable forward contracts (NDFC) and over-the-counter derivative (OTC) products, as well as distribution of income from ODI contract entered into with an IFSC Banking Unit (IBU).

- The Finance Bill 2025 extended the said exemption to ODI, NDFC, and OTC products entered into by non-residents with FPIs located in IFSC and the distribution of income from ODI contracts entered into with FPIs located in IFSC.

- Amendment: FA 2025 now extends the exemption to the distribution of income from OTC derivate products entered into by non-residents with IBU or FPI located in IFSC. The amendment is a policy measure to incentivise IFSC and attract foreign investors.

Adjustments to total income in the course of processing of returns under Section 143(1):

Background

- Section 143(1) deals with the processing of the return of income with certain adjustments for determining the total income of an assessee. The adjustments are arithmetical error, apparent incorrect claim in return, disallowance of loss claimed or denial of profit-linked deductions if return is not filed within the due date, disallowance of expense or increase in income due to mismatch in the audit report, etc.

Amendment and impact:

- FA 2025 introduced a new adjustment under Section 143(1)(iia), i.e. inconsistency in the return of the previous year, with respect to information in the return of any preceding previous year, as may be prescribed. Thus, while processing a return under Section 143(1), an adjustment can be made to total income if there is any inconsistency between information furnished in the earlier year's return and the current year's return. The CBDT shall prescribe the inconsistencies

basis on which adjustments shall be made.

- Q.3 of FAQ 9 of Supplementary FAQ to Finance Bill 2025 explains that the inconsistencies are yet to be prescribed. It gives an example of an adjustment, such as a taxpayer claiming any credit in a previous return, but the corresponding figures are not the same in the current return.

- A plain reading of the amendment suggests that the prescribed inconsistency in the current year's return of income should be in respect of information furnished in the return of earlier previous years. While CBDT has been given the discretion to define the scope of inconsistencies, as the new adjustment under Section 143(1)(iia) affects the total income of the taxpayer, it can cover inconsistencies like tax credits, MAT/AMT credit, carry forward and set-off of losses, variation in closing and opening written down value of asset, inventory etc. This widened scope of adjustment shall lead to an increase in litigation.

Changes to the scope of block assessment from total income to undisclosed total income

- With effect from 1st September 2024, the scheme of search assessment under Chapter XIV-B migrated from individual year to assessment for the block period. The said scheme primarily focussed on the assessment of the total income of an assessee, including undisclosed income arising from search conducted for a block period. It contemplated abatement of regular assessment, which is ongoing on the date of initiation of the search. There was ambiguity on scope and manner of computation of total income and likely treatment that may arise to additions made out of regular disclosed income besides assessment of undisclosed income.

- Finance Act 2025 has shifted the spotlight of block assessment from the determination of the "total income" of the assessee to "total undisclosed income" (UDI). Q.1. of FAQ 8 of the Supplementary FAQ to Finance Bill 2025 explains this as a paradigm shift and suggests that search assessment's main objective is to identify undisclosed income basis search action. The change focuses on assessing total undisclosed income and placing trust in taxpayers to disclose regular income in block income tax return.

- The amendment, besides defining what may constitute UDI of the block, it also proceeds to define which disclosed income will not to form part of block assessment. Section 158BB, as amended by FA 2025 explains scope of total income for block period and has laid a straight-forward method for determining total undisclosed income. It, inter alia, includes UDI, which is suo-moto declared by the assessee in search return and undisclosed income assessed by the Assessing Officer. It excludes income determined in assessment/reassessment proceedings, income declared earlier in return of income, income computed based on books of accounts, maintained in normal course, etc. FA 2025 has clarified that cases where assesses are not mandated to file return like Section 115A in case of specific incomes of non-residents, Section 115G taxing investment income and capital gains earned by non-resident Indians and S.194P for senior citizens earning pension income, where appropriate taxes has been deducted are treated as disclosed income.

- Section 158BA empowers the Assessing Officer for undertaking block assessment on or after 1st September 2024 qua undisclosed total income. Further, it abates any pending assessment proceedings undertaken by the Assessing Officer pertaining to any year falling in the block period. While FAQs clarify that focus is on the determination of undisclosed income. However, the literal reading of abatement provisions along with Supplementary FAQ suggests that the Assessing Officer can even assess regular income as part of total undisclosed income. This creates an anomaly on the rights of the Assessing Officer to conduct pending proceedings for a year falling in block assessment.

- It also clears the air that tax rate of 60% under Section 113 shall be applicable on total undisclosed income rather than total income as prevalent earlier.

- FA 2025 has also amended other provisions in block assessment, enabling filing of search return under Section 158BC with an extension of 30 days in certain circumstances. Correspondingly, in such cases, the limitation period for completing the search assessment under Section 158BE has also been extended. The assessing Officer has been allowed more time for passing order under search by extending the date from 12 months from the end of "month" to 12 months from the end of "quarter" in which the last authorisation is executed. Section 158BD has also been amended to provide a period for which assessment shall be made in respect of other person whose information is found in search of the assessee.

- Section 158BI, which stated that Chapter XIV-B does not apply to searches initiated or requisitions made before 1st September 2024, has been omitted.

- The Finance Act 2025 has introduced the amendment in block assessment with retrospective effect from 1st September 2024.

Concluding thoughts

The Finance Bill 2025 has been enacted with significant amendments with provisions relating to non-resident assessees, incentivising the IFSC sector, block assessment in search cases, computerised processing of return of income. Generally, enactment stage amendments are aimed to correct or address concerns arising from the language of provision deployed at the proposal stage of the Bill. However, introducing substantive amendments at the enactment stage is not novel as in past years as well, an equalisation levy on e-commerce supply or service was introduced at the enactment stage of the Finance Bill, 2020. Now, EL 1.0 has been withdrawn at the enactment stage.

The Government has also given a booster shot to the IFSC sector by enhancing various tax incentives and exemptions in an attempt to align with similar regimes in Dubai, Singapore, etc.

With substantive amendments made in block assessment in light of "trust first, scrutinise later" motto of the Government as announced in Finance Budget 2025, one has to wait and watch how the block assessment evolves.

It is expected that the enactment stage changes shall be replicated in corresponding provisions of Income Tax Bill 2025 in simplified language in upcoming Monsoon Session of the Parliament.

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SUPREME COURT



Keshav B. Bhujle
Advocate

1 PRINCIPAL CIT VS. JUPITER CAPITAL PVT. LTD.: [2025] 472 ITR 616 (SC): DATED 02/01/2025

Capital gains — Transfer — Definition — "Extinguishment of any right therein" — Shares — Reduction of share capital by company — As a result right of shareholder to share in distribution of net assets upon liquidation extinguished proportionately — High Court held, such a reduction of right in capital asset is transfer — Assessee entitled to claim long-term capital loss on reduction in share capital from sale of shares — Supreme Court dismissed the special leave petition filed by Revenue: Ss. 2(47) and 45 of ITA 1961: A. Y. 2014-15

The assessee company made an investment in A Ltd., an Indian company engaged in the business of telecasting news, purchasing 14,95,44,130 shares of face value of Rs. 10 each. Thereafter, the assessee purchased 38,06,758 shares from other parties, thereby increasing its shareholding to 15,33,40,900 shares which constituted 99.88 per cent. of the total number of shares of the company, i. e., 15,35,05,750. That company incurred losses, as a result of which the net worth of the company was eroded. The company filed a petition and the High Court ordered a reduction in the share capital of the company from 15,35,05,750 shares to 10,000 shares. Consequently, the shareholding of the assessee was reduced proportionately from 15,33,40,900 shares to 9,988 shares. However, the face value of the shares remained the same at Rs. 10 even after the reduction in the share capital. The High Court also directed the company to pay Rs. 3,17,83,474 to the assessee as consideration.

For the A. Y. 2014-15, the assessee claimed long-term capital loss accrued on the reduction in share capital from the sale of shares of A Ltd. The Assessing Officer took the view that the reduction in shares of the subsidiary company did not result in the transfer of a capital asset as envisaged in section 2(47) of the Income-tax Act, 1961 and disallowed the claim.

The Commissioner (Appeals) affirmed this. The Tribunal reversed the order passed by the Commissioner (Appeals) and allowed the appeal filed by the assessee.

The High Court dismissed the appeal filed by the Department and affirmed the order passed by the Tribunal. The High Court held that the Tribunal had rightly followed ***Karthikeya V. Sarabhai vs. CIT [1997] 228 ITR 163 (SC)***. (see Principal ***CIT vs. Jupiter Capital Pvt. Ltd. [2025] 472 ITR 561 (Karn)***).

The Supreme Court dismissed the special leave petition filed by the Revenue and held as under:

"i) The following principles are discernible from the decision of the court in ***Karthikeya V. Sarabhai vs. CIT [1997] 228 ITR 163 (SC)***: (i) Section 2(47) of the Income-tax Act, 1961 , which is an inclusive definition, inter alia, provides that relinquishment of an asset or extinguishment of any right therein amounts to a transfer of a capital asset. While the taxpayer continues to remain a shareholder of the company even with the reduction of share capital, it could not be accepted that there was no extinguishment of any part of his right as a shareholder qua the company. (ii) A company under section 66 of the Companies Act, 2013 has a right to reduce the share capital, and one of the modes which could be adopted is to reduce the face value of the preference share. (iii) When, as a result of the reduction of the face value of the share, the share capital is reduced, the right of the preference shareholder to the dividend or his share capital and the right to share in the distribution of the net assets upon liquidation is extinguished proportionately to the extent of reduction in the capital. Such a reduction of the right of the capital asset clearly amounts to a transfer within the meaning of section 2(47) of the Income-tax Act, 1961.

ii) The expression "extinguishment of any right therein" is of wide import. It covers every possible transaction which results in the destruction, annihilation, extinction, termination, cessation or cancellation, by satisfaction or otherwise, of all or any of the bundle of rights - qualitative or quantitative-which the assessee has in a capital asset, whether such asset is corporeal or incorporeal.

iii) Reduction of right in a capital asset would amount to "transfer" u/s. 2(47) of the Income-tax Act, 1961. Sale is only one of the modes of transfer envisaged by section 2(47) of the Act. Relinquishment of any rights in it, which may not amount to sale, can also be considered transfer and any profit or gain which arises from the transfer of such capital asset is taxable u/s. 45 of the Act. The reduction in the share capital of the subsidiary company and subsequent proportionate reduction in the shareholding of the assessee would be squarely covered within the ambit of the expression "sale, exchange or relinquishment of the asset" used in section 2(47) of the Income-tax Act, 1961.

iv) The face value per share remained the same before the reduction of share capital and after the reduction of share capital. However, as the total number of shares had been reduced from 15,35,05,750 to 10,000 and out of this, the assessee held 15,33,40,900 shares prior to reduction and 9,988 shares after reduction, it could be said that on account of reduction in the number of shares held by the assessee in the company, the assessee had extinguished its right of 15,33,40,900 shares, and in lieu thereof, the assessee received 9,988 shares at Rs. 10 each along with an amount of Rs. 3,17,83,474."

2 VINUBHAI MOHANLAL DOBARIA VS. CIT; [2025] 473 ITR 394 (SC) DATED 07/02/2025

A. Offences and prosecution — Composition of offences — Power of CBDT to issue orders, instructions, or directions concerning the proper composition of offences — Commissioner to follow guidelines issued by the board while exercising discretion in compounding offence: Ss. 119 and 279(2) of ITA, 1961: A. Y. 2013-14:

B. Offences and prosecution — Wilful failure to file returns in due time — Offence when committed — Offence complete on the day immediately following the due date prescribed for filing of return u/s. 139(1) — Commission of offence not contingent upon actual filing of belated return: Ss. 139(1), (4), (8) and 276CC of ITA, 1961:

C. Offences and prosecution — Composition of offences — Discretion whether or not to compound offence to be guided by factors including the conduct of assessee, nature and magnitude of offence and unique facts of each case — Guidelines do not exclude competent authority making an exception and allowing application on facts: Ss. 276CC and 279(2) of ITA, 1961: Guidelines for compounding of offences under direct tax laws, 2014[1], Paragraphs 4, 8, 12.:

D. Offences and prosecution — Composition of offences — Guidelines issued by board that offences falling under category B not generally compounded other than first offence — "First offence" — Definition — Offence committed prior to date of issuance of show-cause notice for prosecution in relation to offence or prior to any intimation relating to prosecution by Department to assessee or prior to launching of prosecution, whichever is earlier — Offence which is voluntarily disclosed by assessee before its detection by department also treated as "first offence": Ss. 276CC and 279(2) of ITA, 1961: Guidelines for compounding of offences under direct tax laws, 2014[1], Paragraphs 4, 8, 12.:

E. Offences and prosecution — Compounding of offences — Wilful failure to file returns in due time — Assessee failing to file returns for two assessment years within the due date prescribed in section 139(1) for those years — Due dates for filing of returns for both assessment years falling prior to the issue of show-cause notice — Held, offences committed prior to the date of issue of any show-cause notice for prosecution — Offence for latter year also covered by expression "first offence" as defined under guidelines and compounding application preferred by assessee for that year could not have been rejected: Ss. 276CC and 279(2) of ITA. 1961: Guidelines for compounding of offences under direct tax laws, 2014[1], Paragraphs 4, 8, 12.:

F. Offences and prosecution — Voluntary disclosure of commission of the offence by the assessee — Held, the assessee cannot be said to have intention of evading payment of taxes: ITA, 1961, Chapter XXII.:

The due date for filing the return of income for the A. Y. 2011-12 was September 30, 2011. The assessee filed his return on March 4, 2013.

A show-cause notice dated October 27, 2014, proposing prosecution u/s. 276CC of the Income-tax Act, 1961, was issued. In response to which on November 11, 2014, the assessee filed an application for compounding the offence. The application was allowed. For the A. Y. 2013-14, the due date for filing the return of income was October 31, 2013, whereas the assessee filed the return for this year on November 29, 2014. The assessee received a notice dated March 12, 2015, for prosecution u/s. 276CC of the Act and, on March 19, 2015, filed an application for compounding of the offence. The Chief Commissioner rejected it on the ground that it was not the "first offence" of the assessee, and the rejection was upheld by the High Court.

The Supreme Court allowed the appeal filed by the assessee and held as under:

"i) Section 276CC of the Income-tax Act, 1961 punishes the wilful failure by the assessee, inter alia, to furnish the return of income which he is required to furnish under sub-section (1) of section 139 or by notice given under clause (i) of sub-section (1) of section 142 or section 148 or section 153A. Section 139(1), inter alia, provides that every person shall, on or before the due date, furnish a return of his income during the previous year in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed. Sub-section (4) of section 139 provides that if a person has failed to furnish the return of income within due time prescribed under sub-section (1), then he may furnish the return for any previous year at any time before the end of the relevant assessment year or before the completion of the assessment, whichever is earlier. To fully understand the import of section 276CC of the Act, it is necessary to understand the meaning of the expressions "wilfully fails" and "in due time" used in the provision.

ii) An offence u/s. 276CC could be said to have been committed as soon as there is failure on the part of the assessee to furnish the return of income within the due time as prescribed u/s. 139(1) of the Act. Subsequent furnishing of the return of income by the assessee within the time limit prescribed under sub-section (4) of section 139 or before prosecution is initiated does not have any bearing upon the fact that an offence u/s. 276CC has been committed on the day immediately following the due date for furnishing the return of income. The point in time when the offence u/s. 276CC could be said to be committed is the day immediately following the due date prescribed for filing of return of income u/s. 139(1) of the Act, and the actual date of filing of the return of income at a belated stage would not affect in any manner the determination of the date on which the offence u/s. 276CC of the Act was committed. This can also be discerned from section 139(8) of the Act, which makes it clear that irrespective of whether the return of income is filed by an assessee after the specified date or is not furnished at all, the assessee shall be liable to pay simple interest at 15 per cent reckoned from the day immediately following the specified date notwithstanding the fact that the Assessing Officer has extended the date for furnishing of return.

iii) It could never have been the intention of the Legislature in enacting the provision that the commission of an offence u/s. 276CC is made contingent upon the filing of the actual belated return by an assessee as such a reading would mean that no assessee would file a return of

income after the due date has expired and, despite such failure, would be able to escape any liability u/s.276CC of the Act.

iv) The Explanation to section 279(2) (which allows compounding of offences by the Chief Commissioner) grants the CBDT the authority to issue orders, instructions, or directions concerning the proper composition of offences u/s. 279(2) and explicitly allows for directives requiring prior approval from the Board. When section 279(2) is read alongside the Explanation, it becomes clear that the Commissioner must follow the instructions given by the Board when exercising discretion under this section.

v) While paragraph 4 of the Guidelines for Compounding of Offences under Direct Tax Laws, 2014 [1] issued by the CBDT for the exercise of the power conferred by section 279(2) of the Act stipulates that the eligibility conditions prescribed in (paragraph 7) of the Guidelines are to be satisfied necessarily, the ultimate discretion whether or not to compound the offence or offences has to be guided by factors which include the conduct of the assessee, the nature and magnitude of the offence and the unique facts of each case.

vi) Paragraph 8 of the 2014 Guidelines1 prescribes offences which are generally not to be compounded under the compounding Guidelines. It provides that category B offences (the offence u/s. 276CC being one) will not be generally compounded other than the first offence as defined in the Guidelines. A "first offence" has been defined in paragraph 8 as any offence committed prior to the date of issuance of any show-cause notice for prosecution in relation to the said offence or prior to any intimation relating to prosecution by the Department to the person concerned or prior to the launching of any prosecution, whichever is earlier. The expression "first offence" is also defined to include any offence which has not been detected by the Department, but has been voluntarily disclosed by a person prior to the filing of an application for compounding of offence in the case under any Direct tax Acts. Clause 8 further clarifies that the first offence would be determined separately with reference to each section of the Act under which it is committed, and it would be relevant only if it is committed by the same entity.

vii) Paragraph 8 of the 2014 Guidelines [1] defines a "first offence" in two different manners: First, all those offences which are committed by the assessee prior to a formal intimation of his liability for being prosecuted by the Department are to be treated as "first offence", and it shall be open to the assessee to pray for the compounding of such offences subject to other requirements being fulfilled. Second, any offence which is voluntarily disclosed by the assessee before its detection by the Department would also be treated as a "first offence". The scheme that permeates paragraph 8 of the 2014 Guidelines1 allows only those offences to be treated as the "first offence" which are committed by the assessee either prior to a notice that he is liable to prosecution under the Act for the commission of such offences or those offences which are voluntarily disclosed by the assessee to the Department before they come to be detected. The latter part of the definition of the expression "first offence" is not to curtail the scope of the first half but to expand its ambit by

including those cases where the assessee comes forward on his own initiative and discloses the commission of the offence.

viii) Paragraph 12.4 of the 2014 Guidelines1 shows that the compounding fee is to be levied in the case of an offence u/s. 276CC is to be reckoned from the date immediately following the date on which the return was due. This is in consonance with section 139(8) of the Act and further fortifies the argument that it is not the date of actual filing of the belated return but the date immediately following the due date for filing of the return which is to be considered as the date of commission of the offence.

ix) Voluntary disclosure for the purpose of paragraph 8 of the 2014 Guidelines [1] has to be construed in a manner which ensures that such disclosure on the part of the assessee saves the Department from the trials and tribulations of having to detect the commission of offence by the assessee by setting in motion its own machinery of detection of offences. Neither the filing of a belated return of income by the assessee nor the making of an application for compounding of offence after a show-cause notice has already been issued to the assessee fulfils this underlying idea of saving the Department the inconvenience of detecting the offence. Even after a belated return of income is filed, the Department is still required to process the return, identify the cases wherein offences have been committed, issue show-cause notices to the defaulting assessees and thereafter prosecute the offenders to recover the dues and punish the offenders. A voluntary disclosure by the assessee before the stage of detection by the Department, besides being economically viable also saves time and effort on the part of the Department and also ensures that the dues are recovered promptly.

x) The primary purpose of the prosecution provisions enshrined in Chapter XXII of the Act is to ensure the penalisation of offenders adjudged guilty of tax evasion and other tax-related offences while simultaneously instilling a deterring effect in the minds of those who might contemplate circumventing the payment of lawful taxes. When an assessee voluntarily discloses the commission of an offence, he cannot be said to have the intention of evading payment of taxes.

xi) Paragraph 4 of the 2014 Guidelines [1] specifies that compounding is not a matter of right of the assessee, and the competent authority may allow the compounding application upon being satisfied that the applicant fulfils the eligibility conditions and keeping in mind the conduct of the applicant, the nature and magnitude of the offence and the facts and circumstances of each case. A plain reading of the 2014 Guidelines reveals that while it is mandatory that the eligibility conditions prescribed under paragraph 7 are to be satisfied, the restrictions laid down in paragraph 8 have to be read along with paragraph 4 of the Act, which provides that the exercise of discretion by the competent authority is to be guided by the facts and circumstances of each case, the conduct of the appellant and nature and magnitude of the offence. Seen thus, it becomes clear that although the restrictions laid down in paragraph 8 of the Guidelines are required to be

generally followed, the Guidelines do not exclude the possibility that in a peculiar case where the facts and circumstances so require, the competent authority cannot make an exception and allow the compounding application.

xii) In both the Guidelines of 2019 and 2022 [2] issued by the Board, the offence u/s. 276CC has been made a category A offence instead of a category B offence and is compoundable up to three occasions. Although this would not have any direct implication on cases covered by the 2014 Guidelines1, yet this indicates a clear shift in the policy of the Department when it comes to the compounding of offences u/s. 276CC in particular, and in making the compounding regime more flexible and liberal in particular.

xiii) The date of commission of both offences would be the day falling immediately next to the due date for filing of the return, that is, October 1, 2011, for the A. Y. 2011-12 and November 1, 2013 for the A. Y. 2013-14.

xiv) As the compounding application for the A. Y. 2013-14 was preferred by the assessee on March 19, 2015, it would be governed by the 2014 Guidelines. Since the offence u/s. 276CC of the Act could be said to have been committed on the dates immediately following the due date for furnishing the return of income for both these assessment years, respectively, the offence for the A. Y. 2011-12 could be said to have been committed on October 1, 2011, and the offence for the A. Y. 2013-14 could be said to have been committed on November 1, 2013. The show-cause notice for the initiation of prosecution for the A. Y. 2011-12 was issued to the assessee on October 27, 2014. Therefore, both offences u/s. 276CC of the Act were committed prior to the date of issue of any show-cause notice for prosecution. Therefore, the offence for the A. Y. 2013-14 was covered by the expression "first offence" as defined under the 2014 Guidelines, and thus the compounding application preferred by the assessee could not have been rejected.

xv) The orders passed by the High Court and the Chief Commissioner rejecting the compounding application of the assessee were to be set aside. The decision of the Gujarat High Court in ***Vinubhai Mohanbhai Dobaria vs. Chief CIT [2025] 473 ITR 387 (Guj)*** reversed."

[The assessee was directed to prefer a fresh application for compounding within two weeks, and it was to be adjudicated by the competent authority within four weeks from the date of application having regard to the conduct of the assessee, the nature of the offence and the facts and circumstances of the case. The proceedings pending before the trial court were to remain stayed pending the decision of the competent authority on the compounding application. In the event the fresh compounding application was accepted by the competent authority, the proceedings pending before the trial court would stand abated. If the compounding application was rejected by the competent authority, the trial was to continue and be brought to its logical conclusion.]

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HIGH COURT



Jitendra Singh
Advocate



Radha Halbe
Advocate



Harsh Shah
Advocate

1 PR. CIT VS. GANESH DEVELOPERS [2025] 172 TAXMANN.COM 542 (BOMBAY)

Unexplained expenditure - Bogus Purchases - Section 69C of the Income Tax Act 1961 – Assessee failed to furnish the bank details of the alleged suppliers - CIT(A) as well as Appellate Tribunal held that purchases were non genuine - ad-hoc estimation of profit element of such non genuine purchases are against the express provisions of section 69C of the Act - entire purchases from the said purchase parties is to be disallowed.

Facts:

The assessee before the Hon'ble Bombay High Court is a partnership firm carrying on the business of development of real estate. During the course of assessment proceedings, the AO observed that the assessee had made purchases from certain parties who are declared hawala dealers by the Sales Tax Authority. The AO, therefore, verified the purchases made from said parties by issuing the notices under section 133(6) of the Act. All the parties had duly replied to the notices and furnished their bank statements except the two parties. Thus, the AO could not verify the purchases from the bank statements from the said two parties. The AO made the additions of entire purchases from the parties declared as hawala dealer by the Sales Tax Authority. On appeal the first appellate authority restricted the disallowances to 12.5% of the purchases made from the said two parties who had not furnished their bank accounts. The department, challenged the order of the Ld. CIT(A) before the Income Tax Appellate Tribunal (ITAT). The ITAT upheld the order of the Ld. CIT(A) by restricting the disallowance at 12.5 percent of the alleged bogus purchases from the two Parties.

The department being aggrieved by the order of the ITAT challenged the order before the Hon'ble Bombay High Court under section 260A of the Act. The department challenged the deletion of addition proposed by AO on all purchases from identified parties. Further, the department also challenged ITAT's observation of restricting the disallowance from the two parties to the extent of 12.5 per cent.

Ruling of the High Court:

Hon'ble Bombay High Court upheld the order of ITAT in deleting the disallowance of the bogus purchases with respect to the purchase made from parties who had responded to the reply under section 133(6) and also furnished their bank statements. However, Hon'ble Bombay High Court reversed the order of Ld. CIT(A) and ITAT in estimating the disallowance at 12.5 percent with respect to the two parties who had not furnished their bank statement. The High ourt held that "It is also important to note that the respondent-assessee has accepted the addition of 12.5% of the purchases from these two parties. By accepting the said percentage, the respondent-assessee has impliedly accepted that the transactions with these two parties could not be proved and, therefore, the logical conclusion that both the Appellate Authorities ought to have adopted was to confirm the total additions of purchases from these two parties." The High Court observed that if the approach of the Appellate Authorities is accepted, then the provision of section 69C, which is an enabling provision, would become redundant. Section 69C provides that where an assessee has incurred any expenditure and offers no explanation about the source of expenditure or the explanation offered is not in the opinion of the AO satisfactory, then the amount of expenditure may be deemed to be the income of the assessee and such unexplained expenditure which is deemed to be the income of the assessee shall not be allowed as a deduction under any head of income. Thus, if the approach of the Ld. CIT(A) and the ITAT is accepted, then it would amount to endorsing outright conduct of illegality contrary to the express provisions of section 69C, which the Appellate Authorities have entirely ignored.

2 PR. CIT VS. BUNIYAD CHEMICALS LTD. [2025] 172 TAXMANN.COM 462 (BOMBAY)

Unexplained cash credit - Section 68 of the Income Tax Act 1961 - in the absence of any cogent explanation with respect to the credits in the bank accounts, AO is justified in treating the entire credits as unexplained cash credit under section 68 of the Act.

Facts:

The assessee before the Hon'ble Bombay High Court was engaged in providing accommodation entries, charging a commission of 0.15 percent. For AY 2009-10, the company filed its return of income declaring Nil income. During the assessment proceedings, the director of the assessee company admitted that the company was merely an accommodation entry provider, and the receipts and payments in the bank accounts were from customers for whom accommodation entries were provided. However, no details of these customers were provided to the AO. Therefore, the AO made an addition under Section 68 of the Income-tax Act, 1961, treating credits in the bank accounts as unexplained cash credits due to the lack of details regarding the identity, source, and genuineness of the deposits. On appeal, Ld. CIT(A) held that if the assessee identifies the beneficiaries, then the rate of commission adopted should 0.37 per cent of such identified beneficiaries and if the assessee fails to identify the beneficiaries, the amounts credited would be confirmed as unexplained cash credits under Section 68. The assessee being aggrieved by the order of the Ld. CIT(A) preferred an appeal before the

ITAT Mumbai. Hon'ble ITAT directed the AO to make addition of only 0.15 per cent of the total deposits (explained and unexplained) appearing in the bank accounts as income. The department revenue being aggrieved by the order of the ITAT challenged the same before the Hon'ble Bombay High Court under section 260A of the Act.

Ruling of High Court:

Hon'ble High Court upheld the addition as made by AO under Section 68, observing that the assessee failed to explain the identity, source, and genuineness of the credits. Hon'ble Court rejected the assessee's argument that bank statements do not constitute "books of an assessee" under Section 68, noting that the data extracted from the computer constitutes books of account. Hon'ble Court highlighted that the definition of "books or books of account" includes data stored in electronic form, and the data extracted from the computer of the assessee would constitute "books of an assessee" for the purpose of Section 68. However, the Hon'ble High Court upheld the ITAT's decision to adopt a commission rate of 0.15% for identified beneficiaries.

Hon'ble High Court further observed that as, the director admitted to engaging in fraudulent activities, abetting tax evasion, and money laundering. The Court directed further investigations by law enforcement agencies due to the admission of serious economic crimes by the assessee's director under the Indian Penal Code and the Prevention of Money Laundering Act, 2002.

3 MADHURI SAMEER GOKHALE VS. ADDL. JOINT/DEPUTY/ASST. COMMISSIONER OF INCOME-TAX/ INCOME-TAX OFFICER, NATIONAL FACELESS ASSESSMENT CENTRE [2025] 172 TAXMANN.COM 696 (BOMBAY)

Faceless Assessment - Section 144B of the Income Tax Act 1961 - AO failed to abide by procedure enumerated in the SOP issued under provisions of section 144B(6)(xi) – Assessment Order is in breach of principles of natural justice.

Facts:

For the AY 2014-15, the AO issued a reopening notice under section 148 of the Act on ground that the assessee had not filed her return of income for the relevant assessment year, inspite of having entered into financial transactions amounting to Rs. 11.61 crores, the source of which was not explained. The assessee vide letter dated 14.01.2022 requested the AO to grant an adjournment of 15 days to file her reply, in the light of the difficulties faced by her during the Covid pandemic period, coupled with the fact that the partner of her chartered accountant firm was recuperating after a serious surgery. The AO, however, without considering the request of the assessee, issued a show cause notice-cum-draft assessment order under Section 144 and proposed to make a best judgment assessment under Section 144 bringing to tax the entire amount which had escaped assessment for the A.Y. 2014-15. In response to the same, the assessee submitted that the entire amounts were in the nature of receipts from Trust and HUF on which tax had already been paid by the Trust and HUF for the earlier years. The assessee also furnished relevant documentary evidences in support of her contentions. The AO, however, proceeded to pass the final assessment order under section 144, holding that the amount of Rs. 11.61 crores invested by

the assessee for the assessment year 2014-15 had escaped assessment.

The assessee, being aggrieved, filed instant writ petition challenging the order passed under section 147 read with section 144 and 144B on the ground that the order was arbitrary, illegal, irrational in as much as it was passed without following the mandatory procedure under section 144B, in gross violation of the well settled principles of natural justice.

Ruling of the Hon'ble High Court:

Hon'ble High Court is pleased to allow the assessee's writ petition by observing that the Assessment Unit failed to adhere to the SOP issued by CBDT dated 03.08.2022 which provides for mandatory 7 day's time to the assessee's to file its response. In the present case the assessee was provided with only 3 day's time which is in contravention of SOP and therefore, impugned assessment order passed in undue haste and in gross violation of principles of natural justice and the same is quashed. Hon'ble High Court also quashed the reopening notice issued under section 148 of the Act by observing that the amount that formed part of re-opening of assessment was already brought to tax in earlier assessment year and there was no fresh tangible material brought on record by the AO to justify such re-opening.

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" We are responsible for what we are, and whatever we wish ourselves to be, we have the power to make ourselves. If what we are now has been the result of our own past actions, it certainly follows that whatever we wish to be in the future can be produced by our present actions; so we have to know how to act."

Swami Vivekananda

TRIBUNAL



CA Nikhil Mutha



CA Viraj Mehta



CA Kinjal Bhuta
Advocate

1 M/S. BALAJI DEVELOPERS VS. ITO [ITA NO.375/PUN/2024 DATED 24/03/2025] [AY 2016-17]

Section 10(37) – Section 96 of RFCTLAAR – Exemption on compulsory acquisition – Allowed even to a non-individual/non-HUF person and even if the land is held as stock in trade

Facts:

The assessee is a partnership firm engaged in the business of land development and trading in plots. The assessee filed nil return of income for AY 2016-17 on 03/02/2018. In the said return, the assessee claimed an exemption of INR 2.74 crores for compensation received from the National Highways Authority of India (NHAI) on the compulsory acquisition of land. The said exemption was claimed by relying upon section 96 of the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013 (RFCTLAAR) and CBDT Circular No. 36/2016 dated 25/10/2016. The Learned Assessing Officer (Ld. AO) passed an assessment order, disallowing the exemption claimed on the ground that the sum of INR 2.74 crores was received from the sale of stock in trade and is purely a business income. Moreover, section 10(37) of the Act applies only to individuals and Hindu Undivided Family (HUF) and, therefore, the assessee is not eligible for the exemption. Aggrieved by the said order passed by the Ld. AO, the assessee filed an appeal before the Ld. Commissioner of Income Tax (Appeals). The Ld. CIT(A) dismissed the assessee's appeal, stating that CBDT Circular No. 36/2016, issued in the context of Section 10(37) of the Act, exempts all acquisitions under the RFCTLAAR Act from income tax but applies only to individuals and HUFs. Aggrieved by the same, the assessee filed an appeal before the Hon'ble Income Tax Appellate Tribunal (ITAT). In the course of proceedings before the Hon'ble ITAT, the Department Representative ('DR') raised a new argument that compensation received from NHAI is not eligible for exemption under section 96 of RFCTLAAR.

Held:

The Hon'ble ITAT, relying on various judicial precedents, rejected the Ld DR's new argument stating the same was not raised by the Ld.AO or the Ld. CIT(A) and the DR can support the order of the AO on the grounds on which the addition has been made.

The Hon'ble ITAT held that when the lands of various land owners are acquired by the Government in the public interest even if the owners are not willing to sell the land, they have to abide by the law and are forced to offer their lands for compulsory

acquisition. Therefore, the amount received by the assessee of INR 2.74 crores, is exempt from income tax in terms of section 96 of the RFCTLAAR.

In this regard, the Hon'ble ITAT relied on the decision of Coordinate Bench in the case of Parasnath ***Vinimay Pvt. Ltd. vs. CPC (ITA No. 151/Kol/2023)*** which relied on the decision of the Hon'ble Mumbai Tribunal in case of ***DCIT vs. M/s Ganga Developers (ITA No. 2328/Mum/2021)*** wherein it has been held that according to section 96 of the RFCTLARR Act, compensation received through award agreements is exempt from income tax except as provided in section 46 of the said Act, even if it is not a case of individual or HUF. The Hon'ble ITAT further relied on the decision of the Hon'ble Calcutta High Court in the case of PCIT vs. Durgapur Projects Ltd. (ITA No. 282/2022), which held that no distinction is made between compensation for agricultural and non-agricultural land for income tax exemption. The CBDT clarified that compensation exempt under Section 96 of the RFCTLAAR, is not taxable under the Act, even without a specific exemption provision.

The Hon'ble ITAT also relied on the decision of the Hon'ble Karnataka High Court in ***BMRCL vs. Sri Balaji Corporate Services PCIT and Ors [Writ Petition No. 890/2022, dated 27.09.2023]***, granting exemption under Section 96 of the RFCTLAAR, even for acquisitions made under the Karnataka Industrial Area Development Act, 1966. In this case, the court citing the decision of the Hon'ble Supreme Court's judgment in ***Nagpur Improvement Trust vs. Vithal Rao and Others [(1973) 1 SCC 500]***, held that unequal treatment of landowners violates Article 14 of the Constitution, supporting the assessee's claim for exemption on compensation from NHAI.

Therefore, appeal filed by the assessee was allowed.

2 VINOD JAIN VS. ITO (ITA NO. 6156/MUM/2024 DATED 12.03.2025) (AY 15-16)

Section 45/147 –Assessee's brother is sole owner and beneficial owner of property – assessee's name merely appears out of natural love and affection - Assessee's brother enjoyed 100% possession and purchase consideration was paid by him – On sale of property, capital gain not taxable in the hands of the assessee

Facts:

The assessee earned income from salary and from capital gains on equity shares and mutual funds. On the basis of the information received that the assessee has sold immovable property, notice under section 148 of the Act was issued and proceedings under section 147 of the Act were initiated. During the re-assessment proceedings, the assessee submitted that the immovable property was originally purchased on 23.06.2004 by his brother, Shri Babulal Nihalchand Jain and the name of the assessee and his father was added to the property as joint owners out of natural love and affection. The Property was sold on 19.09.2014 for a consideration of Rs.54 Lakhs, which was entirely credited to the bank account of the assessee's brother. Thus, the assessee submitted that even though the property was purchased in the joint name, but the actual possession and the 100% right of the property belonged to his brother, as the whole consideration was paid by him at the time of purchase of the said property. The assessee also furnished the original purchase deed, bank statement of his brother highlighting

the receipt of consideration in his account, Form 26AS stating that the TDS on the property has been fully deducted on the PAN of his brother, sale agreement, and the ITR along with computation for the year under consideration of his brother. However, AO did not consider the submissions of the assessee and held that though the amount of sale consideration of the property was received in the account of the assessee's brother, however, half of the sale consideration, i.e., Rs.27 Lakhs, legally belonged to the assessee as he had not relinquished his rights on the property. Thereby adding Rs 27 lakhs as income under head LTCG. CIT(A) confirmed the assessment order. Hence, appeal was filed before Hon'ble ITAT.

Held:

Hon'ble ITAT held that the assessee's brother had paid the entire purchase consideration for the property, was in actual possession and had 100% rights over the said property. Even though the assessee's name was mentioned in the purchase deed as one of the joint owners, the consideration received on the sale of the said property cannot be added in the hands of the assessee once his brother has declared the entire consideration in his return of income. Hon'ble ITAT further held that we do not find any basis in making the addition on account of Long-Term Capital Gains in the hands of the assessee, when assessee's brother was the sole owner of the property for all practical purposes and the assessee's name appears to have been added only out of natural love and affection. On the above basis, addition made u/s 45 was directed to be deleted and appeal was thereby directed to be allowed.

3 ANIL DATTARAM PITALE VS. ITO [ITA NO. 465/MUM/2025 (MUMBAI TRIB.)] (AY:2018-19)

Section 56(2)(x) – Redevelopment of property - assessee received a new flat in lieu of old flat – AO added difference between stamp duty value of new flat and indexed cost of old flat as income of the assessee – held sec 56(2)(x) not applicable to such facts

Facts:

The assessee had purchased a flat in the financial year 1997-98. The society underwent redevelopment in accordance with the redevelopment agreement. Pursuant to the redevelopment agreement, the assessee received a new flat in lieu of the old flat surrendered by him. The stamp duty value of the new flat was Rs. 25,17,1700/- and indexed cost amounted to Rs.5,43,040/-. The AO added the difference between the stamp duty value and indexed cost amounting to Rs.19,74,660/- to the income of the assessee. Upon appeal, the CIT(A) confirmed the order. Against the said order, the assessee filed an appeal before the Hon'ble ITAT.

Held:

The Hon'ble ITAT held that the assessee received a new flat in the redeveloped property in lieu of old flat. Hence, it is a case of extinguishment of old flat and in lieu of the old flat, the assessee has received a new flat as per the redevelopment agreement. It is not a case of receipt of immovable property for inadequate consideration that would fall within the purview of the provisions of sec.56(2)(x) of the Act. Therefore, the provisions of Section 56(2)(x) will not be applicable to the assessee's case. The Hon'ble ITAT also stated that at the most, this transaction may attract the provisions relating to capital gains. The assessee should be entitled for deduction of cost of new flat

u/s. 54 of the Act. In that case also, there will be no tax liability upon the assessee on account of these transactions. The addition made u/s. 56(2)(x) was accordingly deleted.

4 NFAC, DELHI VS. NRB DEVELOPERS [172 TAXMANN.COM 385] (MUM ITAT) (AY:2018-19)

Section 56(2)(x) - Assessee purchased a property and allotment letter was issued on 30-3-2010 – AO made an addition u/s. 56(2)(x) being difference between agreed value and stamp duty value – CIT(A) restricted addition to DVO's valuation report– ITAT held increase in tolerance limit from 5% to 10% has retrospective effect - any incremental value above the tolerance limit of 10% to be added back.

Facts:

The assessee purchased a property for a total consideration of Rs. 8.19 crores. The assessee booked the property by paying Rs. 3.50 crores through banking channels, and a letter of allotment was issued in favour of the assessee on 30-3-2010. At the time of registration, there was a difference of Rs. 9.04 crores between the set forth value and the stamp duty value. The issue was referred to the DVO for valuation of the property; however, no valuation report was provided to the assessee during the assessment proceedings. Consequently, the assessment was completed with an addition of Rs. 9.04 crores made under section 56(2)(x). On appeal, the Commissioner (Appeals) received a valuation report and, in accordance with section 56(2)(x), the DVO valued the property as pertaining to the financial year 2009-10 since the property was allotted on 30-3-2010, and payment was made through banking channels. The difference between the DVO''s valuation and the set forth value, amounting to Rs. 81.19 lakhs, was considered for addition. The Commissioner (Appeals) restricted the addition to this amount, and the assessee's appeal was partially allowed. Both the revenue and the assessee, being aggrieved by the appeal order, filed appeals before the Hon'ble ITAT.

Held:

Before the Hon'ble ITAT, the Ld. DR contended that the Ld. CIT(A) erred in treating the allotment letter as an agreement for sale, and the value should not be deemed as at the financial year 2009-10. The Ld. AR argued that the Ld. CIT(A) correctly considered the valuation in relation to the allotment letter issued on 30/03/2010, and that the property should be valued as at that date. With respect to the valuation difference of Rs.81,19,625/-, since the difference is less than 10%, the assessee is entitled to the benefit under section 56(2)(x)(b)(B) of the Act, thereby necessitating the deletion of the differential value confirmed by the Ld. CIT(A). The AR relied on Mumbai Bench decision in the case of Balkrishna ***Venkappa Bhandary vs. DCIT [2024] 169 taxmann.com 76***. The point of consideration was that the application of the section in the impugned assessment year, whether it is treated as clarificatory/curative in nature having retrospective application or otherwise. It was argued that the issue is squarely covered by the order of the coordinate bench of ITAT-Mumbai in the case of ***Glory Ship management Private Limited vs. CIT (Appeals) ITA No.3149/MUM/2023***. It was held that the provision of section 56(2)(x)(b)(B) has retrospective effect and is applicable to the impugned assessment year. The Hon'ble ITAT upheld the view adopted by the Ld. CIT(A) in reducing the addition under section 56(2)(x). The matter

was remitted back to the file of the Ld. AO for allowing the assessee the incremental differences as per the said Act for the alleged properties. In one of the units, it was seen that the incremental difference was exceeding a little over 10% i.e. 10.01%, it was held that the excess over 10% shall be considered for addition. Consequently, the appeal of the assessee was allowed. The appeal filed by revenue was dismissed, however no specific reason of dismissal is given in the said order.

5 MANISH DEVENDRAKUMAR SHAH VS. ITO [172 TAXMANN.COM 466] (AHD ITAT) (AY:2014-15)

Section 68 r.w.s 10(38) – Assessee earned LTCG on sale of shares and claimed it exempt u/s. 10(38) – AO treated it as a bogus transaction – made addition u/s. 68 as unexplained cash credits – held that assessee acquired shares through direct preferential allotment– furnished substantial documentary evidence – all transactions through authorized banking channels – addition deleted.

Facts:

The assessee had claimed exemption u/s. 10(38) on long-term capital gain earned by him on the sale of shares of Looks Health Services Ltd. (LHSL). The return was processed under section 143(1). The assessment was reopened u/s. 147 based on information received from the Investigation Wing, which indicated that LHSL was a penny stock and the assessee was a beneficiary of a bogus LTCG scheme. The Ld. AO disallowed the LTCG claim and made an under section 68 on the following grounds –

1. LHSL was identified as a penny stock with no significant financial activity and weak fundamentals

2. Abnormal share price movement, with a sharp rise and fall without any corresponding business growth,

3. Investigation Wing's report indicated price manipulation and circular trading

4. The assessee could not explain why he invested in LHSL, a company with no business operations, absence of due diligence before investment.

On appeal, CIT(A) upheld the addition u/s. 68 on the grounds that the investment in the shares of LHSL is only a make-believe transaction intended to bring back his black money into his books in a circular route through manipulation of prices of penny stock. Aggrieved by Ld. CIT(A) order, the assessee appealed before the Hon'ble ITAT.

Held:

Before the Hon'ble ITAT, the Ld. AR argued that the shares were allotted by the company itself and not purchased off-market. Since the allotment was direct from the company, there was no question of any manipulative transaction or accommodation entry. The AR also stated that the shares were subject to a lock-in period as per the terms of preferential allotment and the AO's assumption that the market price movement must correlate with the financials of the company is incorrect, as market prices are influenced by multiple factors beyond earnings per share. He merely invested in shares of LHSL and sold them when the prices were favourable. Since he was neither a director nor an authorized person of the company, he had no control over its financials or operations. There was no cash involvement in these transactions, as all payments were made through banking channels using account

payee cheques and RTGS. The assessee had furnished all necessary documents, including bank statements, allotment letters, DEMAT account details, and sales invoices. Since these documents were not disputed by the AO, there was no valid basis to invoke Section 68 of the Act. It was also pointed out that the networth and EPS of LHSL was increasing over the years and the same should be considered as turnaround by the company.

The DR relied on the order of CIT(A) and pointed out that the assessee has dealt with only this share and very few shares of other companies which shows that the assessee is not a regular investor and has taken benefit the bogus shares.

It was held by the Hon'ble ITAT that, the issue of penny stock transactions and their taxability under section 68 of the Act requires a comprehensive and well-founded approach. The mere fact that a stock has exhibited significant price fluctuations or has been categorized as a penny stock does not by itself, render transactions in such shares non-genuine. The stock market operates under a regulatory framework where shares, irrespective of their financial fundamentals, are allowed to be traded on stock exchanges. Once such share is permitted to be listed and traded, any investor or trader - whether a regular market participant or a one-time investor- is free to take advantage of price movements and seek potential profits. Price volatility in shares can arise due to various market forces, including speculative trading, demand supply dynamics, market sentiments and external economic factors. The mere fact that a share has witnessed unusual price movements does not automatically lead to the conclusion that all transactions in that share are sham or that an assessee's trading activities lack genuineness. However, in cases where there is an allegation of share price manipulation, the AO must conduct a detailed investigation to establish whether the assessee was merely an investor availing market opportunities or an active participant in a scheme of manipulation designed to launder unaccounted income. If the revenue seeks to treat a transaction bogus, it must be supported by concrete evidence that the purchase or sale of share was a sham which would require proving that the transaction lacked actual transfer of ownership, that the contract notes, DEMAT entries were mere paper transactions, or that the corresponding money flow was circular in nature, involving accommodation entries. If the sale or purchase is alleged to be non-genuine, the revenue must demonstrate that the entire money trail, from the purchase to the final realization of sale proceeds, was a facade used to introduce unaccounted income. It is settled principle of law that the primary onus lies on the assessee to substantiate the genuineness of the transaction by furnishing documentary evidence. If the fundamental aspects are satisfied, the burden then shifts to the revenue to bring on record specific material evidence proving that the transactions were merely a colourable device aimed at tax evasion. The mere fact that a share has been subject to price manipulation does not automatically lead to addition under section 68 of the act unless it is conclusively demonstrated that the assessee was part of the scheme, and the transactions were structured to generate artificial gains or losses. In the present case such detailed investigation by AO is absent. There were several ITAT and HC decisions relied upon by the AR where such additions were deleted for lack of conclusive evidence. Further, the CIT(A) and DR's reliance on the decision in the Kol HC decision in case of Swati Bajaj (446 ITR 56) was considered by the Hon'ble ITAT as misplaced as in this case as the assessee was not provided with the investigation report neither given any opportunity of cross examination of such statements violating principles of natural justice. The addition therefore was deleted. The Tribunal even dealt with the alternate ground that the entire sale

consideration without giving effect to the cost of the shares cannot be added as undisclosed income. It was held that not allowing the cost was contrary to established judicial principles.

6 AARTI SONI VS. ITO (ITA NO. 3233/MUM/2024 DT. 21.02.2025) (AY 14-15)

Section 69 – Addition made only on the basis of statement of third party recorded during survey – No independent enquiry made by AO – Evidences submitted by the assessee not considered – Addition deleted

Facts:

The assessee had purchased a flat from M/s Shah Housecon Pvt. Ltd. vide agreement dated 15.02.2014 for a consideration of Rs. 1,27,30,000/-. A survey was conducted in the business premises of M/s Shah Housecon Pvt. Ltd. on 11.11.2024 and the statement of Shri Binesh Balkrishnan, Senior Accountant was recorded. Based on the documents received during the survey proceedings and the statement recorded, the Ld. AO called on the assessee to show-cause why the amount of Rs. 33,00,000/- allegedly paid to the M/s Shah Housecon Pvt. Ltd. as on-money over and above the agreement value should not be treated as unexplained investment. The assessee submitted before the AO that she did not pay any on-money and submitted the bank statements. The assessee also filed an affidavit dated 02.12.2016 stating that no on-money payments were made to M/s Shah Housecon Pvt. Ltd. The assessee further requested the AO to issue summons to the parties for cross-examination. However, submissions of the assessee were not considered, and additions were made for the reason that the parties to whom summons were issued did not appear before the AO. On further appeal, the CIT(A) confirmed the addition. Hence, appeal was filed before the Hon'ble ITAT.

Held:

The Hon'ble ITAT held that the AO has made an addition of Rs. 33,00,000/- as unexplained investments in the hands of the assessee based on the statement found during the course of survey and based on the statement recorded from the Senior Accountant of the Builder that the assessee has made on-money payments. The assessee before the AO denied having made any such payment and also filed an affidavit to this effect. The assessee further submitted before the AO that the Builder could be summoned and an opportunity to cross-examine may be given. The AO issued summons to the Builder and since there was no response, the AO treated the entire amount of Rs. 33,00,000/- as unexplained investment under section 69. The Hon'ble ITAT relied on the decision in the case of M/s Yash Synthetic Pvt. Ltd. [ITA No. 268/Mum/2024 dated 18.06.2024] wherein it has been held that no addition can be made based on the statement of Senior Accountant Shri Binesh Balakrishnan. It was further held that the AO has solely relied on the statement recorded during the course of survey and the AO has not conducted any independent enquiry to substantiate that the assessee has made the alleged on-money payments. Further, the AO has not considered the bank statements submitted by the assessee and also the affidavit filed stating that no on-money payment in cash is done by the assessee. It is a settled position that the assessee cannot be required to substantiate a negative fact and that the AO ought to have conducted necessary further enquiries in support of the alleged claim that the assessee has made on-money payments. On above basis, additions were deleted by the Hon'ble ITAT and appeal filed by the assessee was allowed.

7 ENRICH HAIR AND SKIN SOLUTION PVT. LTD. VS. ACIT (ITA NO. 6331/MUM/2024 DATED 26.03.2025) (AY 07-08)

Section 69/148 – Addition made only on the basis of information received from the Investigation Wing regarding cash payment – No independent enquiry made by AO – Evidences submitted by the assessee not considered – No addition can made

Facts:

Notice u/s 148 was issued on 29.03.2024 on the basis of information received from the Investigation Wing, Mumbai regarding a cash payment of Rs. 46,00,000/- by the assessee in FY 2006-07 to M/s Lake View Developers, belonging to Hiranandani Group, for the purchase of a shop at Ventura Building. The assessee denied having made any transaction for the purchase of shop with M/s Lake View of Developers. Ld. AO made the addition on the basis that in the backdrop of specific information received from the investigation wing, the onus lay upon the assessee to prove that it had not made any such transaction. On further appeal, the CIT(A) confirmed the addition. Hence, appeal was filed before Hon'ble ITAT.

Held:

Hon'ble ITAT held that perusal of the assessment order shows that the assessee was asked to explain the sources of cash payment amounting to Rs. 47,00,000/- during the year under consideration, on the basis of information received from the Investigation Wing, Mumbai. No documentary evidence or copy of the statement relied upon has been supplied to the assessee nor any such details are noted in the assessment order. Subsequently, during the course of appellate proceedings, Ld. CIT(A) sought a remand report from the Ld. AO. However, in the remand report, the main issue was not addressed.

It is thus clear that no documentary evidence regarding the payment made by the assessee for the purchase of any property from M/s. Lake View Developers has been brought on record by the Ld. AO. The assessee has been able to demonstrate that the only transaction with M/s. Lake View Developers was for taking a shop on rent for which a security deposit was paid and received back vide cheque of Rs. 4,14,000/-, that too in FY 2008-09. As no document and/or statement of a third party has been mentioned in the assessment order or in the remand report submitted by the Ld. AO, Hon'ble ITAT directed the additions to be deleted on the basis that there was no justification in making addition u/s 69. On above basis, additions were deleted by Hon'ble ITAT and appeal filed by the assessee was allowed.

8 SACHIN, HISAR VS. DCIT [ITA NOS. 2613 & 2614/DEL/2022, DATED 05/03/2025] [AY'S 2016-17 & 2017-18]

Section 292C – Presumption of ownership applies to searched person and does not apply to the third party

Facts:

The assessee is the proprietor of M/s Meru Jewels, carrying the wholesale business of gold bullion. He filed his return of income for AY 2016-17, declaring a total income of INR 17,37,170. A search and seizure operation under Section 132 of the Act was conducted in the case of Jindal Bullion Ltd. (JBL). During the search, digital data stored in a software called "Hajir Johri" was seized

from the residence of Mr. Kushagra Jindal (the promoter of JBL). This software however contained parallel books maintained by JBL, recording both bank and cash transactions with various other parties including the assessee. Upon examination of the seized data, a ledger account with the code "Pankaj kb" was found and Ld. AO allegedly held that such account was linked to the assessee. The AO relied heavily on third party statements (Mr. Parul Ahluwalia and employee of JBL) recorded during the search without any independent corroboration. The Ld. AO then drew conclusion on this data arguing that these entries reflected undisclosed transactions without providing further supporting evidence and subsequently made additions towards the total income of the assessee under the Act.

Held:

The Hon'ble ITAT observed that the Hazir Johri Software was found and seized from the premises of JBL and hence the presumption under section 292C of the Act would apply to JBL and not the assessee. The Hon'ble ITAT further held that no concrete material and corroborative evidence such as bills/vouchers, sales, stock ledgers, etc were found by Ld. AO which proves the alleged cash sales belonged to the assessee. The additions are based on conjecture and the statement of Mr. Parul Ahluwalia without any supportive evidence.

The Hon'ble ITAT relied on its decision in case of Anoop Kumar Soni vs. DCIT [ITA No. 1641/Del/2021] wherein it was held that ledger found during the search, contains the entries of parties other than assessee, then said ledger cannot be said to be belonging to the assessee and addition made on the basis of assumption was deleted.

The Hon'ble ITAT further relied on its decision in case of Surender Kumar Jain in [ITA No. 1314/Del/2023] wherein it was held that entries in the Hajir Johri ledger of M/s. JBL, supposedly involving M/s. S.K. Impex, do not prove actual transactions without corroborative evidence such as bills or invoices. The appeals of the revenue were dismissed.

Therefore, the additions made by Ld. AO for both assessment years (AY 2016-17 and 2017-18) were deleted.

9 ABIL REALTY PVT. LTD. VS. ITO [ITA NO. 446/PUN/2024 DATED 19/03/2025] [AY 2016-17]

CBDT Instruction on limited scrutiny – prior approval required for expanding the scope

Facts:

The assessee is a company engaged in the business of real estate. It filed its return of income on 16/10/2016 declaring the loss of INR 18,08,517. Subsequently, the assessee's case was picked up for limited scrutiny on account of the following reasons:

- Low income in comparison to high loans/advances/investment in shares appearing in balance sheet
- Low income in comparison very high investment appearing in balance sheet
- Large other expenses claimed in the Profit and Loss a/c
- Large current liability in comparison to total asset in balance sheet

The Ld. AO issued notices under section 143(2) and 142(1) of the Act. The assessee duly responded to these notices. The Ld. AO noted that the assessee received advances against the sale of land of INR 164 crores from ABIL Corporation Pvt. Ltd (INR 94 crores) and Shashbindu Constructions Pvt. Ltd (INR 70 crores) and are reflected under the head current liabilities in the balance sheet. The Ld. AO further noted that the assessee holds 51% of the stake in Shashbindu Constructions Pvt. Ltd whose reserves and surplus stood at INR 9.31 crores as on 31/03/2015 and therefore the provisions of section 2(22)(e) of the Act are applicable to the assessee. The Ld. AO passed the assessment order making addition of INR 9.31 crores to the total income of the assessee. Aggrieved by the said order passed by the Ld. AO, the assessee filed an appeal before the Ld Commissioner of Income Tax (Appeals). The Ld CIT(A) dismissed the appeal filed by the assessee. Aggrieved by the said order of Ld CIT(A), the assessee filed an appeal before the Hon'ble ITAT raising an additional ground that addition under section 2(22)(e) of the Act treating the amount as deemed dividend was outside the scope of reasons stated for selection of the case for limited scrutiny and the said addition was made without seeking requisite approval for conversion of the case from limited scrutiny to complete scrutiny and therefore, unsustainable in law.

Held:

The Hon'ble ITAT held that if during the course of assessment proceedings in limited scrutiny cases, it comes to the notice of the Ld. AO that there is potential escapement of income exceeding certain limit requiring substantial verification on any other issue(s), then, the case may be taken up for complete scrutiny with the approval of the PCCIT/ Pr. CIT/CIT concerned. Without obtaining prior approval of the PCCIT/Pr.CIT/CIT or Pr.DIT/DIT, the Ld. AO cannot expand the scope of limited scrutiny to complete scrutiny.

The Hon'ble ITAT relied on the decision of the Hon'ble Calcutta High Court in the case o***f PCIT vs. Weilburger Coatings (India) (P) Ltd. (supra) [(2024) 296 Taxman 205 (Cal))*** wherein it has been held that the AO making additions in respect of issues not mentioned in limited scrutiny were beyond jurisdiction of the AO as the scrutiny assessment was selected for limited scrutiny u/s 143(2) and not complete scrutiny.

The Hon'ble ITAT further relied on the decision of the Hon'ble Orissa High Court in the case of ***PCIT vs. Shark Mines and Minerals Pvt. Ltd. (supra) [ITA No. 1/2023 (Orissa High Court)]*** wherein it has been held that what persuades this Court to reach this conclusion is the requirement in law that if the Assessing Officer has to go beyond the scope of the issues for which limited scrutiny has to be undertaken by him, he has to seek prior permission of the superior officer in terms of the CBDT Instruction No.7/14 dated 26 September, 2014 and Instruction No.20/15 dated 19 December, 2015.

In view of the above, the appeal filed by the assessee was allowed. ■

CASE LAW UPDATE



Dr. CA Sunil Moti Lala
Advocate

A. SUPREME COURT

1 NEW DELHI TELEVISION LTD. VS. ACIT [2025] 172 TAXMANN.COM 384 (SC)

Where the AO made TP addition on account of alleged guarantee fee connected with issuance of bonds by subsidiary in assessee's hands by holding it to be an international transaction as per section 92B, and the matter was remanded to AO by the Tribunal with clarification that remit was to be confined to examining whether undertaking of obligation in question amounted to an international transaction and once same was affirmed, consider transmitting matter to TPO; SLP filed against the order of the Hon'ble HC (affirming the order of the Tribunal) was dismissed.

Facts

i. During assessment proceedings, inquiries were initiated by Investigating Wing in relation to certain Step-up Coupon Bonds issued by assessee's UK subsidiary, outside India to various investors.

ii. On receipt of investigation report, Assessing Officer made reference to TPO in respect of international transactions including issuance of those bonds alleging that assessee submitted corporate guarantee in support thereof.

iii. TPO, however, did not make any TP additions in respect of alleged corporate guarantee.

iv. Upon receipt of TP report, AO independently examined the issue and made addition on account of alleged guarantee fee connected with issuance of bonds by subsidiary in hands of assessee by holding it to be an international transaction as per section 92B.

v. Tribunal remitted matter to AO holding that under statutory scheme it was only TPO which could have undertaken that exercise and made consequential TP adjustments.

vi. The Hon'ble High Court by impugned order held that end of justice would merit that matter was remanded to AO with clarification that remit was to be confined to examining whether undertaking of obligation in question amounts to an international transaction, to be answered first and at outset and only once it came to conclusion that obligation amounts to an international

transaction, consider transmitting matter to TPO.

vii. Aggrieved, assessee filed SLP against impugned order of the Hon'ble High Court.

Decision

i. The Hon'ble Sc noted that the short question that fell for the consideration of the High Court while deciding the petition was whether the undertaking furnished by the petitioner - herein would amount to a corporate guarantee or a mere obligation and which could be viewed as an international transaction. This issue was kept open for the petitioner - assessee to be canvassed before the AO in accordance with law.

ii. The Hon'ble SC, thus dismissed the SLP holding that there was no reason to interfere with the impugned order passed by the Hon'ble High Court.

iii. It further clarified that, all other contentions available to the assessee were also kept open to be canvassed before the AO.

2 SOCIETE DE PARITICIPATIONS FINANCIERS VS. ACIT [2025] 171 TAXMANN.COM 393 (SC)

SLP was dismissed by the Hon'ble SC against order of High Court that a notification under section 90(1) would be a mandatory condition to give effect to a DTAA, or any protocol changing its terms or conditions, which would have effect of altering the existing provisions of law.

B. HIGH COURT

1 SFDC IRELAND LTD. VS. CIT [2025] 171 TAXMANN.COM 731 (DELHI)

Where assessee, a tax resident of Ireland, entered into a reseller agreement with an Indian company, SFDC India and appointed SFDC India as a non-exclusive reseller of its products, the Hon'ble HC held that since there was little indication at least at this stage, that amounts paid by SFDC India to assessee as consideration for sale of products would be chargeable to tax in India, assessee's application under section 197 for nil withholding tax was to be allowed

Facts

i. The assessee, a tax resident of Ireland, entered into a reseller agreement with an Indian company, SFDC India and appointed SFDC India as a non-exclusive reseller of its products.

ii. Assessee filed an application under section 197 for nil withholding tax rate on payments to be received from SFDC India.

iii. AO rejected assessee's application on ground that SFDC India was involved in price determination process and was empowered to enter into contracts with customers on its behalf, which indicated dependency of SFDC India on assessee.

iv. Aggrieved, the assessee filed writ petition before the Hon'ble HC.

Decision

i. The Hon'ble HC noted that the AO had not rendered any prima facie finding that assessee had a PE in India and that SFDC India habitually exercised authority to conclude contracts in name of assessee.

ii. Since there was little indication at least at this stage, that the said amounts paid by SFDC India to assessee as consideration for sale of products would be chargeable to tax in India, the Hon'ble HC held that assessee's application under section 197 for nil withholding tax was to be allowed.

iii. However, the Hon'ble HC further clarified that this order would not preclude the AO from examining and framing an assessment in accordance with law, uninfluenced by this order.

iv. Thus, the Hon'ble HC thus allowed the petition in the aforesaid terms.

2 CIT VS. EXPEDITORS INTERNATIONAL OF WASHINGTON INC* [2025] 171 TAXMANN.COM 576 (DELHI)

The assessee, US company, provided freight logistic support services to its Indian subsidiary by helping customers clear shipments through customs by apprising persons of various rules and regulations. The Hon'ble HC upheld the order of the Tribunal holding that, since rules and regulations pertaining to clearance of customs frontiers was clearly not specialized skill or knowledge acquired or possessed by assessee, it did not qualify "make available " condition and, thus, services rendered by assessee could not be treated as technical services under the India-US DTAA.

3 PR. CIT VS. DCM SHRIRAM LTD. [2025] 170 TAXMANN.COM 631 (DELHI)

Assessee had supplied power from its eligible units to its other units. The TPO made adjustment on account of ALP of power supplied by assessee's power plants to its other units on basis of rates of electricity quoted on Indian Energy Exchange (IEX). Since IEX was not a source for uninterrupted power and transactions of sale and purchase of power on IEX was not comparable to regular supply of power by State Electricity Board (SEB) or power distribution companies, the Hon'ble HC held that rates at which electricity was supplied by SEBs to industrial consumers was to be accepted as being market value of said supplies by assessee. Consequently, the impugned adjustment made by TPO was deleted. The Hon'ble HC followed the judgement of the Hon'ble SC in ***CIT vs. Jindal Steel and Power Limited [2024] 460 ITR 162*** wherein the rates at which electricity was supplied by the SEBs to industrial consumers was accepted as being the market value of the said supplies for the purposes of sub-section (8) of section 80-IA. Accordingly, the Hon'ble HC dismissed the Revenue's appeal.

4 PCIT-1, NEW DELHI VS. BEAM GLOBAL SPIRITS & WINE (INDIA) (P.) LTD. [2025] 172 TAXMANN.COM 292 (DELHI)

The Hon'ble HC held that where assessee incurred high AMP expenditure for marketing products using brands owned by and licensed to it by its AE, merely because of high level of expenditure, it could not be presumed that an international transaction had come into being before embarking upon a benchmarking analysis. Revenue needs to demonstrate on basis of tangible material or evidence that there exists an international transaction for provisions of brand building services between assessee and AE. Accordingly, the Hon'ble HC dismissed the Revenue's appeal and upheld the order of the Hon'ble Tribunal deleting the adjustment made on account of AMP expenditure.

5 PR. CIT VS. TEREX INDIA (P.) LTD. [2025] 172 TAXMANN.COM 291 (BOMBAY)

The Hon'ble HC dismissed the Revenue's appeal and upheld the order of the Hon'ble Tribunal holding that, while determining ALP of international transactions, benchmarking should be done only on associated enterprise or related party transactions and not with respect to the entire turnover.

6 AON CONSULTING (P.) LTD. VS. PR. CIT [2025] 171 TAXMANN.COM 336 (DELHI)

The assessee filed an application under MAP with competent authority of US under article 27 of India US-DTAA and settlement had been arrived at between competent authority of India with respect to adjustment on account of transfer pricing issues related to US transaction. The Hon'ble HC held that the Tribunal was not justified in directing the TPO to adopt same approach for non-US transactions as adopted in MAP for US transactions. It held that an agreement arrived at by competent authorities of two contracting states under MAP cannot substitute determination of ALP under Act and Rules in cases which are not covered under MAP.

C. TRIBUNAL

1 MITESH VIJAY GULATI VS. INCOME-TAX OFFICER [2025] 172 TAXMANN.COM 382 (MUMBAI- TRIB.)

Where the assessee who went to US partially for employment and partially in search of employment and stayed in India for a period less than 182 days in preceding year, the Hon'ble Tribunal held that he would be entitled to claim exemption qua income earned out of India being non-resident of India during that year, as per Explanation 1 to section 6.

Facts

i. Assessee filed his return claiming his status as non-resident. Assessee claimed that during year under consideration

he had remained out of India for a period of 210 days in total for purpose of employment and therefore remained in India for a period of 156 days.

ii. AO excluded stay of 28 days on ground that assessee had not shown salary receipt for period of 28 days and accepted remaining period of 182 days spent by assessee out of India for purpose of employment. He, thus, ultimately treated status of assessee as 'resident of India' having stayed in India more than 182 days in the relevant assessment year and made addition of salary income and NRE interest income and added same in his total taxable income.

iii. The CIT(A) upheld the order of AO.

iv. Aggrieved, assessee filed appeal before the Hon'ble Tribunal.

Decision

i. The Hon'ble Tribunal noted that assessee stayed in India for period of less than 182 days and was outside India for 210 days (182 days for employment and 28 days in search of employment).

ii. It was also not case of Revenue that assessee had visited foreign countries exclusively for other purposes such as tourists, medical treatment, studies.

iii. In absence of relevant contrary material, certificates issued by concerns at USA could not be sidelined and could not be construed that assessee visited foreign countries for specific and exclusive purposes other than employment.

iv. Thus, the Hon'ble tribunal concluded that the assessee was entitled to claim exemption for income earned outside India being non-resident of India during that year as per Explanation 1 to section 6.

2 PHILLIPS INDIA LTD. VS. DCIT [2025] 172 TAXMANN.COM 340 (KOLKATA- TRIB.)

The Hon'ble Tribunal held that delayed payment of receivables could not be considered as a separate international transaction and that therefore, TPO was not justified in making transfer pricing adjustment in respect of outstanding receivables in respect of trade creditors being Associated Enterprises (AEs) by using 6 months LIBOR rate and CUP as most appropriate method.

Note

A contrary view has been taken in ***Ariba Technologies India (P.) Ltd. vs. DCIT – [2025] 172 taxmann.com 304 (Bangalore – Trib)***

GST





CA Naresh Sheth *CA Jinesh Shah*

A. WRIT PETITIONS

1 B BRAUN MEDICAL INDIA (P.) LTD. V. UNION OF INDIA [2025] 172 TAXMANN.COM 534 – DELHI HIGH COURT

Facts and Issues involved

Petitioner is engaged in the sale of various pharmaceutical products and medical devices. Petitioner had purchased a large quantum of products from M/s. Ahlcon Parenterals (India) Limited (hereinafter 'Ahlcon") based on various purchase orders. The invoices for the said products were raised by Ahlcon on the Petitioner. however, the said invoices inadvertently reflected the Bombay address and Bombay GSTN of the Petitioner, instead of the Delhi GSTN number. This led to issuance of demand order of Rs. 5,65,91,691/- by GST authorities on the ground that the Petitioner has wrongly availed of excess Input Tax Credit (hereinafter ITC).

Discussions by and observations of High Court

The Petitioner is clearly a Delhi based company and incorrect reflection of Petitioner's Bombay GSTN on the invoices was merely an error by the supplier. The Petitioner's name is correctly mentioned in the invoices, however, the wrong GST number, i.e., of the Bombay office has been mentioned. Substantial loss would be caused to the Petitioner if the credit is not granted for such a small error on behalf of the supplier. Petitioner fairly admitted that no other entity has also claimed at the ITC on these purchases. Petitioner is permitted to avail ITC of Rs. 5,65,91,691 in respect of supplies received for the period 2017-18 to 2020-21.

Decision of High Court

Petition is allowed and impugned order rejecting the ITC is set aside.

2 HIGH TECH ECOGREEN CONTRACTORS LLP VS. JOINT DIRECTOR, DGGSTI [2025] 172 TAXMANN.COM 110 (GAUHATI) – GAUHATI HIGH COURT

Facts and issues involved

Petitioner is engaged in the business of rendering works contract Service. SCN dated 23.12.2021 was issued to the petitioner mainly alleging wrong availment of Input Tax Credit (ITC) which is not allowable under the provision of Rule 36(4) of the CGST Rules.

Additional Commissioner also passed an order dated 31.03.2023 confirming GST demand along

with interest and penalty. Petitioner appealed to the Commissioner (Appeals), CGST, but the appeal was dismissed on 12.02.2024, citing bar of limitation. Thus, petitioner has preferred the present writ.

Petitioner's Submissions

The only ground taken by the petitioner for assailing the validity of Rule 36(4) of the CGST

Rules is that the said Rule is enacted drawing power from Section 43A(4) of the CGST Act, which was inserted by the Central Goods and Services Act (Amendment) Act, 2018 and that the effective date of implementation of Section 43A was never notified. Further, since it is omitted w.e.f. 01.10.2022, vide notification dated 28.09.2022, it is clear that Rule 36(4) of the CGST Rules has no constitutional or legal validity before 01.01.2022 when Section 16(2)(aa) was inserted in the Act vide notification dated 21.12.2021 which came into effect from 01.01.2022.

Discussions by and Observations of High Court

Section 1(2) of the CGST (Amendment) Act, 2018, whereby Section 43A is enacted, provided that the provisions of the Amendment Act of 2018 shall come into force on such date the Central Government may, by Notification, in the Official Gazette, appoint. The proviso to Section 1(2) says that different dates may be appointed for different provisions of this Act and any reference in any such provision to the commencement of this Act shall be construed as reference to the coming into force of that provision.

Learned counsel for the Revenue has failed to satisfy that the Central Government, by Notification in the Official Gazette, has appointed a date from which Section 43A has been enforced till the date it was omitted by the Finance Act, 2022, i.e. from 01.10.2022.

Section 43A has never come into operation because the Central Government has never notified any date for its enforcement till it was omitted.

Section 16 of the CGST Act enables a registered person to take credit of input tax charged on any supply of goods or services or both which are used or intended to be used in the course or furtherance of his business. The eligibility and conditions for taking input tax credit by a registered person are enumerated in Section 16. Section 16 falls under Chapter V of the said Act under the heading "INPUT TAX CREDIT".

On the other hand, Section 43A, which was inserted by Act No.31 of 2018 vide Section 18 and later on omitted by Finance Act, 2022, i.e. from 01.10.2022, speaks about the procedure for furnishing return and availing tax credit for the registered person. Section 43A falls under Chapter IX of the CGST Act under the heading "RETURNS".

Rule 36 of the CGST Rules speaks about documentary requirements and conditions for claiming tax credit. It falls under Chapter V of the said Rules under the heading "INPUT TAX CREDIT". In our view Section 16 of the CGST Act and Rule 36 of CGST Rules are in relation to eligibility of a registered person who can avail input tax credit by furnishing required documents, whereas Section 43A of the CGST Act is defining procedure for furnishing returns for availing input tax credit.

From the above analysis, there is no doubt that Rule 36 of CGST Rules is relatable to Section 16 of the CGST Act and as such, sub-rule (4) of Rule 36 of the said Rules is also relatable to Section 16 of the CGST Act only. There is no doubt that Rule 36 or in particular sub-rule (4) of Rule 36 is framed as per the objects of the CGST Act and falls within the scope of general power conferred by sub-section (2) of Section 164 of the said Act.

Decision of High Court

Gauhati High Court upheld the validity of Rule 36(4) and dismissed the writ petition.

3 M/S ACULIFE HEALTHCARE PVT. LTD. AND ANR VS. UNION OF INDIA AND ORS [2025-TIOL-385-HC-AHM-GST] – GUJARAT HIGH COURT

Facts and issues involved

Petitioner is engaged in the business of manufacturing chemicals and pharmaceuticals products. During July 2017 to July 2022, the petitioner has deposited a total sum of Rs.45,14,300/- as tax on notice pay recovery, in lieu of various employees who left employment. This amount of tax has been deposited by the petitioner from its own pockets and the GST on the amount of notice pay recovery was deposited by the petitioner as and when such recovery was made. The amount deposited as GST, or any part thereof, has not been recovered by the Petitioner from any of the employees leaving employment.

The Union Government issued Circular No.178/10/2022-GST dated 03.08.2022 which clarified that such amount and such recovery was not chargeable to GST. At para 7.5 of this circular, the Government clarified that forfeiture of salary or payment of the bond amount in the event of an employee leaving employment before the minimum agreed period was not taxable. Hence, the amount of Rs. 45,14,300/- deposited by the petitioner as GST was therefore, not "tax".

In light of above clarification, since the petitioner had borne the entire burden of Rs. 45,14,300/- deposited as tax on recoveries made from outgoing employees, the petitioner filed for a refund for the same.

Notices proposing to reject the refund claim of the petitioner were issued by the GST Authorities. On subsequent adjudication, part of the refund claim was accepted and the balance was rejected by the GST Authorities solely on the ground of the same being time-barred as per Section 54 of the CGST Act, 2017.

Petitioner's Submissions

It is now a settled position that the petitioners were not liable to pay any tax in the present case. The collection and retention of the monies under the guise of tax is in violation of the mandate of Article 265 of the Constitution of India. Therefore, such actions of the GST Authorities and also the order of the Appellate Authority are liable to be quashed, set aside and consequent refunds must be directed to be paid to the petitioners.

It is inconceivable how any refund application could be filed before 03.08.2022 i.e. the date on which the clarification was issued vide Circular No. 178/10/2022-GST. Therefore, the limitation in respect of such refund applications could only be calculated from 03.08.2022

Therefore, the GST authorities have erred in rejecting the refund applications filed by the petitioners soon after the aforesaid Circular dated 03.08.2022.

Discussions by and Observations of High Court

On perusal of Circular No. 178/10/2022-GST dated 03.08.2022, it is clear that the forfeiture of salary or payment of bond amount in the event of an employee leaving employment before the minimum agreed period does not constitute a supply of service and hence, it is not taxable under GST Law.

Since the aforesaid Circular was issued on 03.08.2022, it has to be said that the petitioners could not have had the opportunity of filing the refund claims in respect of the GST deposited by it, till such date. Therefore, the period of two years for filing a claim, within the meaning of Section 54 of the CGST Act must be computed from the date of the Circular i.e. from 03.08.2022.

Hence, the refund claims filed by the petitioner promptly after the issuance of the Circular cannot be said to be time-barred.

The Hon'ble High Court has upheld a similar position in the case o***f Joshi Technologies Internation vs. Union of India [2016-TIOL-1240-HC-AHM-CX]***.

To sum up, just as citizens have to diligently pay tax which are legally due to the State, equally, as a corollary of the aforesaid statement, the State is not entitled to unjustly enrich itself with amounts collected from citizens which are not sanctioned as "Tax" within the meaning of Article 265 of the Constitution of India.

Decision of High Court

The impugned orders are quashed and set aside. GST Authorities were directed to sanction the refund of the balance amount to the petitioner along with Interest at the rate of 9% p.a. from the date of filing the refund application till the date of actual payment within a period of 12 weeks from the date of receipt of copy of the order.

B. RULINGS BY ADVANCE RULING AUTHORITY

1 A2MAC1 INDIA PVT LTD [2025-TIOL-02-AAR-GST] TAMIL NADU AAR

Facts and issue involved

Applicant is engaged in providing 'Collaborative Automobile Benchmarking services' to the customers as a subscription package through an online platform where the detailed analysis of software concept of structure, process and global benchmarking data is made available.

From the database, the subscribers of the Applicant will get 360 degree vehicle insights such as technology insights, cost insights, performance insights, market insights, sustainability insights, software insights, supply chain insights etc.

For vehicle benchmarking, the Applicant purchases brand new cars in the domestic market, disassembles them and adds research data to the corpus knowledge database for providing various insights to the customers. Motor vehicles bought by the Applicant are wholly and exclusively used for automotive research purpose carried out at the applicant's factory. Hence, these vehicles are temporarily registered with RTO (Regional Transport Office).

The cost of the vehicles bought and used for automotive benchmarking process are expensed out in the books.

Further, at the end of the vehicle retention period, they are sold and the Applicant is of the view that it qualifies as an activity of 'supply' in the course of its business and discharges applicable GST on such transactions.

Applicant has sought a ruling as to whether the input tax credit (ITC) on the purchase of vehicles / cars are claimable, in terms of 17 (5) (a) of the CGST Act, 2017.

Applicant's submissions

Applicant submitted that ITC is essentially the set-off of the amount of GST paid on

purchases from the amount of GST to be paid on the sales. It quoted Section 16(1) stating that Section 16(1) entitles a registered person to take ITC on supply of inputs as well as capital goods with conditions and restrictions. It also quoted Section 16(2) claiming that it has complied with all the conditions laid down in the said sub-section to be eligible to claim ITC.

It is submitted that for the Company's business, motor vehicles are indispensable tools for carrying out 'Automotive Research Study' which is in turn offered for subscription to the customers. It is a business requirement to buy the latest launched and popular vehicles, the cost of which is expensed out in the books as input cost and after a specific/retention period the cars are sold by paying the applicable taxes/GST.

Hence, it satisfies the conditions laid down in Section 17(5)(a)(A) of the Act and should be eligible to claim ITC on the Motor Cars purchased by it.

Discussion by and Observations of AAR

ITC on inputs and input services is a facility provided by the Government to avoid cascading effect of tax on tax. As a general rule, Input Tax Credit is not available on motor vehicles with an approved seating capacity of less than or equal to 13 persons (including the driver). The exception to the general rule is only applicable to:

(A) a person engaged in business as an authorized dealer of a manufacturer of motor vehicles who sells the motor vehicles after purchasing from manufacturers or any person acting as an agent to the manufacturer without buying it;

(B) a person engaged in providing service by way of transportation of passengers; and

(C) person engaged in imparting training on driving such motor vehicles

By providing an exception to the exclusion for availability of Input Tax Credit, the law is very clear and specific that except for the exceptions provided, the input tax credit on the purchase of vehicles irrespective of any kind of outward supplies shall not be eligible. Hence, it is clear that for a motor vehicle specified in 17(5)(a) of the Act, even if it is used for supplying goods or services, it is not eligible for availment of input tax credit, irrespective of whether or not it is used in providing taxable outward supply.

Further, on perusal of the sample invoices relating to supply of motor vehicles after retention period, it is seen that the applicant is not classifying the product after use as 'used or old motor vehicles' but is supplying it as scrap of Automobile part' paying GST at the rate of 18%. As the applicant is supplying the goods as 'Scrap', the activity will not fall within the scope of 'further supply of such motor vehicles'. Accordingly, the applicant cannot claim the exception and hence are not eligible to take ITC on the motor vehicles purchased by them.

Ruling of AAR

The input tax credit on the purchase of motor vehicles used for providing taxable outward supply of Automobile Bench Marking Service' and supplied as 'Scrap of Automobiles' is not available to the applicant as the applicant's activity would not fall within the exception to the exclusion provided under Section 17(5)(a) of CGST/TNGST Act, 2017.

2 MEGA FLEX PLASTICS LIMITED [2025-TIOL-06-AAR-GST] WEST BENGAL AAR

Facts and Issues involved

Applicant has taken a land on lease situated in the 'Howrah Poly Park' for a period of 99 years by a Deed of Lease executed with the West Bengal Industrial Development Corporation Limited (WBIDC) with a right to transfer or mortgage or assign its leasehold interest. Applicant has developed the said land and constructed factory building and warehouse over the said land. The applicant, in addition to the lease rent mentioned above, is also entitled to reimbursement for electricity charges on an actual basis as specified in the agreement.

Applicant has sought an advance ruling as to whether GST is liable to be paid on reimbursement of electricity charges on actual basis?

Applicant's submissions

The agreement entered by the applicant is towards supply of services i.e. renting of the premises to the sub-lessee. The applicant being the owner of the licensed premises receives the electricity bills in its name and pays the same to the concerned authorities.

The applicant determines the electricity charges attributable to the premises as per the sub-meter readings and collects the same from the sub-lessee as reimbursement of expenses incurred by it

The electricity is received and consumed by the sub-lessee directly. The applicant merely pays the amount and then recovers it from the sub-lessee. Accordingly, the reimbursement of expenses is not a supply to fall under section 7 (1) of the CGST Act, hence the electricity charges are not liable to GST.

Discussions by and observations of AAR

Applicant has contended that reimbursement of expenses of electricity charges should not be a part of consideration since the applicant is acting here as a pure agent. As per para (a) of explanation of rule 33, "pure agent" is a person who "enters into a contractual agreement with the recipient of supply to act as his pure agent to incur expenditure or costs in the course of supply of goods or services or both.

Circular No. 206/18/2023 - GST dated October 31, 2023 clarifies that where the Real Estate Owners, Resident Welfare Associations (RWAs), Real Estate Developers etc., charge for electricity on actual basis that is, they charge the same amount for electricity from their lessees or occupants as charged by the State Electricity Boards or DISCOMs from them, they will be deemed to be acting as pure agent for this supply.

The fact of the case involved in the instant case is identical to the clarification given in the Circular No. 206/18/2023-GST dated 31st October, 2023. We therefore hold that the applicant here will be deemed to be acting as pure agent in regard to supply of electricity to its sub-lessee and the reimbursement amount shall not be a part of his value of supply. In this impugned case, applicants separately invoice electricity charges based on actual consumption, making it a clear pure agent transaction.

Ruling of AAR

Applicant is not liable to pay GST on reimbursement of electricity charges on actual basis.

■

SERVICE TAX





CA Rajiv Luthia *CA Keval Shah*

1 SPAIN ELECTRONICS VS. CCE(APPEALS)-I 2025-3-TMI-507-CESTAT NEW DELHI

Backgrounds and facts of the case

- The appellant is registered with the service tax department for providing "erection, commissioning and installation services". The appellant was investigated by the anti-evasion wing of the service tax Commissionerate and it was found that the appellant had supplied 1000KVA DG sets to Indian Oil Corporation Limited (IOCL) on its Panipath-Jalandhar LPG pipelines which activity appeared to be chargeable to service tax. Therefore, it came to the conclusion that the appellant had also rendered the service of "supply of tangible goods" and SCN was issued.

- Another SCN dated 15.09.2015 was issued as it was found that the appellant had sold DG sets to its customers and also erected, commissioned and installed them. It was alleged that such contracts were composite contracts including the sale of the DG sets and rendering services of erection commissioning and installation which were, therefore, classifiable as a "works contract" on which service tax needs to be paid.

- The CCE(Appeals) upheld the Order in Original and hence the present appeal.

Arguments by the Appellant

- The supply of DG sets to IOCL is not covered under "supply of tangible goods" because the effective possession and control over the DG sets have been transferred to its client IOCL.

- As regards the 2nd SCN for works contract services, the appellant had sold DG sets to its buyers. As a part of the condition of such sale, the appellant had also installed and commissioned the DG sets. The appellant did not charge any amount towards erection or commissioning of the DG sets. What was done was essentially sale of DG sets and their installation at the buyers' premises. The Department had wrongly taken this contract for sale of goods as a "works contract service". Merely because some incidental service such as installation and commissioning were also taken upby the appellant, it does not automatically mean that the appellant had rendered "works contract services".

Decision of the Hon'ble Tribunal

- As regards the allegation under supply of tangible goods services, the Supreme Court in Bharat Sanchar Nigam Limited

has dealt in detail with what constitutes effective possession and control over the goods. The Supreme Court has laid down five criteria and if these are fulfilled the effective possession and control would have been transferred to the transferee and VAT can be charged. Otherwise, service tax can be charged under section 65(105)(zzzzd).

- In this regard, all the conditions, such as goods available for delivery, both the parties must be a consensus ad idem as to the identity of the goods, transferee should have a legal right to use and consequently all legal consequences of such use including permissions should be available to the transferee, During the period the appellant had transferred the DG set to IOCL, the appellant had no right to use them as well and it were under exclusive right of IOCL and last e appellant had no right to transfer the same goods to others as well , were satisfied.
- In view of the above, we find that only VAT could have been charged by the State Government on the DG sets supplied by the appellant to IOCL
- As far as the second show cause notice is concerned, no separate amount was charged by the appellant in installation or commission. that the pre-dominant nature of the contract is that of sale of DG set. When a large equipment such as DG set is purchased, the customer naturally wants the seller to install and commission it so to necessary to ensure that the DG sets were in working order. Merely because the goods were installed and commissioned after sale, the contract would not become a works contract services.
- Therefore, the demand of service tax on the sale of generators by treating them as "works contracts" merely because the generators were also installed and commissioned by the appellant cannot be sustained and is liable to be set aside.

2 ITC LTD VS. CST, KOLKATA 2025-3-TMI-626 CESTAT- KOLKATA

Backgrounds and facts of the case

- The appellant as owner of ITC Centre, Kolkata, and ITC Infotech Park, Bangalore, permitted certain entities to use portions of its said premises under leave and licence agreements. In terms of the said agreements, the licencees concerned were required to pay the monthly licence fee to the appellant for the use and enjoyment of the specified area in the property concerned. In addition to the licence fee, the licencees were to pay for the electricity consumed as well as charges on account of maintenance.
- A single bill for electricity, maintenance charges and telephone was raised by respective vendors on the appellant for the entire premises. Such bill was paid by the appellant at the first instance. The said expenses were then allocated pro rata basis with reference to the area occupied by licencees and identification of telephone number / account number, installed in the areas occupied by the licencees, the amount charged by the said service providers was recovered from by the licencees without any markup.

- SCN dated 20.04.2012 was issued to the appellant and demanding Service tax of ` 95,06,861, on the recoveries made by the appellant from the licensees, on the allegation that the appellant had recovered such service tax amount of ` 95,06,861/- from the licencees but had not deposited the same with the Government exchequer.

- Aggrieved against the confirmation of the demands, the appellant has filed this appeal.

Arguments by the appellant

- The Ld. Adjudicating authority on verification of invoices, found that no service tax was recovered by the appellant from the licencees in respect of the cost of electricity, telephone and maintenance, as alleged in SCN. Therefore, in view of the said finding, the Commissioner should have dropped the proceedings and could not have confirmed the demand as if service tax was "recovered from the client but not deposited to Govt. exchequer". After having found against the Department on the ground on which the show cause notice was issued, the Commissioner had no jurisdiction to confirm the demand on any other ground.

- Secondly, the appellant submits that they did not provide electricity or telephone or maintenance to the licensees. Accordingly, the payments received by them are the reimbursements and they were not expenditure or cost incurred by the appellant in the course of providing renting of immovable property service. The amounts reimbursed by the licencees for electricity, telephone and maintenance were not 'consideration' for any service provided by the appellant in the course of providing renting of immovable property service. Further they got the reimbursements of the actual cost without any mark up. Thus, they acted as 'pure agents' for collecting the charges and paying it to the concerned agencies.

Decision of the Hon'ble Tribunal

- We agree with that the Ld. Commissioner should not have confirmed the demand on any other ground. Accordingly, we hold that the demand confirmed in the impugned is not sustainable and the same is liable to be set aside on this ground alone.

- Regarding merits of the case, we observe that the amounts reimbursed by the licencees on account of electricity, telephone and maintenance cannot be included in the value of renting of immovable property service. The amounts reimbursed by the licencees for electricity, telephone and maintenance were not 'consideration 'for any service provided by the appellant in the course of providing renting of immovable property service. Further, we observe that the appellant got the reimbursements of the actual cost without any mark up.

- We set aside the demands of service tax along with interest confirmed in the impugned order. Since the demand of service tax is not sustained, the question of imposing penalty does not arise.

3 CCE, BELAPUR VS. SAPPHIRE CABLE AND SERVICES PVT LTD. 2024-167-TAXMANN.COM-48 BOMBAY HIGH COURT

Backgrounds and facts of the case

- The appeal was filed by the department challenging the appeal filed in Mumbai CESTAT against order dated 07.07.2023, wherein the respondent made pre-deposit made by debiting the Electronic Credit Ledger. The Pre-deposit was not considered as due compliance to Section 83 of the Finance Act, 1994 Section 35F of the Act. Under these legal provisions pre-deposit was a pre-condition for entertaining any appeal.

- This appeal therefore is against the decision taken by the CESTAT rejecting appellant's preliminary objections.

Arguments by the Respondent

- The appeal before CESTAT is still pending. The provisions of Section 35G of the Act is pari materia to Section 260 A of the Income Tax Act, 1961. The Division Bench of this court in ***Chem Amit vs. Asstt. CIT2004 SCC OnLine Bom 976/ [2005] 143 Taxman 348/272 ITR 397 (Bombay)*** held that the expression "an appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal" obviously refers to such order disposing the appeal. If the legislature intended to provide an appeal to the High Court from each and every order passed by the Tribunal, the legislature would have used the expression "an appeal shall lie to the High Court from every order passed by the Tribunal and not from every order passed in appeal by the appellate Tribunal". Therefore, on this ground alone the appeal is not maintainable.

- Secondly, the appellant has relied upon a Circular dated 28th October 2022 issued by the Central Board of Indirect Tax and Customs (CBIC) to submit that the pre-deposit made by respondent by utilizing credit ledger account (ITC) ledger maintained in the SNGST regime is not a valid payment in compliance of Section 35F of the Act, which would apply prospectively.

Decision of the Hon'ble High Court

- Preliminary objections by revenue were rejected because the CESTAT rightly concluded that the circular had come into force only on 28th October 2022 and the appeal had been filed much before the circular came into force.

- Relying upon the judgment of the Hon'ble Apex Court in ***CCE vs. Mysore Electricals Industries Ltd. 2007 taxmann.com 1555/[2006] 204 ELT 517 (SC)***, the CESTAT held that the circular would apply only prospectively.

- In fact, this court in ***Oasis Realty vs. Union of India (2023) 3 Centax 86/[2022] 143 taxmann.com 5/94 GST560/71 GSTL 158 (Bombay)*** decided on 16th September 2022 has held that assessee may utilize the amount available in the Electronic Credit Ledger to pay 10% of the amount of tax in dispute under Section 107(6) of the Maharashtra Goods and Services Tax Act, 2017.

- We should also note that the High Court of Karnataka in ***Union of India vs. Vkant Tyres Ltd. 1999taxmann.com 362 (Karnataka)*** while dealing with the pre-deposit under Section 35F of the Act has taken a similar view.

- Therefore, Appeal was dismissed. ■

CASE LAW UPDATE



CS Makarand Joshi

IBC

MURLIDHAR VINCOM PRIVATE LIMITED – APPELLANT VS. SKODA (INDIA) PRIVATE LIMITED RESPONDENT

In the matter of *Murlidhar Vincom Private Limited – Appellant vs. Skoda (India) Private Limited Respondent* at National Company Law Appellate Tribunal(NCLAT) New Delhi dated 26 November 2024

Facts of the case:

- During the financial years 2010-11 & 2011-12 sum of Rs. 1.32 Cr. was paid as share application money by the **Murlidhar Vincom Private Limited** – Appellant – financial creditor (FC) for allotment of equity shares as share application money.

- The shares were not allotted by the **Skoda (India) Private Limited** - Corporate Debtor (CD) Respondent however, the amount of Rs. 40 lakhs was refunded from the said share application money.

- The CD was not able to refund the balance amount of Rs. 92 lakhs. The Appellant thereafter provided additional funds of Rs 79.60 lakhs which were paid in several installments from 2012-14.

- Since neither the shares were allotted nor the share application money was refunded, the Appellant sent a Demand Notice on 07 July 2023 to the CD for repayment of the share application money with statutory interest of 12% in terms of Section 42(6) of the Companies Act, 2013(the Act).

- Since the CD failed to repay the amount, the Appellant filed a Section 7 application under the Insolvency and Bankruptcy Code, 2016 – (IBC) before the National Company Law Tribunal (NCLT) on 30 August 2023.

- The NCLT however held that share application money in respect of the shares not allotted cannot be deemed to be a financial debt. The order dated 22 March 2024 further held that the requirements of the Section 7 application under the IBC were not fulfilled and therefore rejected the Section 7 application.

- Aggrieved by the above order an appeal was filed by the Appellant at NCLAT.

Arguments of the Appellant:

- Section 42(6) of the Act states that shares are to be allotted within 60 days of receipt of share application money and that if shares are not allotted within such period, money is to be refunded within 15 days from the expiry of 60 days. Any delay in the refund of share application money beyond the period of 15 days attracts interest at the rate of 12% per annum.

- Furthermore, Rule 2 of the Companies (Acceptance of Deposit) Rules (CADR Rules) provides that if shares are not allotted within 60 days of receipt of share application money, the same amount is deemed to be treated as deposit money.

- The appellant stated that since in the present factual matrix, shares were not allotted within the time period as prescribed by the Act against the share application money, the share application money provided by the FC to the CD should have been deemed by the NCLT to be deposit money which would have come within the meaning of 'financial debt' under Section 5(8) of the IBC.

- Placing reliance on the judgment of NCLAT in the case of ***Kushan Mitra Vs Amit Goel and Ors. in CA(AT) (Ins) No. 128 of 2021*****,** it was submitted that the Tribunal in the said judgment clearly held that share application money in the event of non-allotment of share attracts interest under Section 42(6) of the Act falls within the ambit of financial debt under Section 5(8) of the IBC. Hence, the NCLT ought to have admitted the Section 7 application filed by the Appellant against the CD. It was, therefore, strenuously contended that the impugned order had been passed contrary to law and was liable to be set aside.

- The basic ingredients that are required to be met for a debt to become 'financial debt' are that there must be a disbursal against the consideration for the time value of money. Further sub-clauses (a) to (i) of Section 5(8) delineate the various transactions which are included in the ambit of 'financial debt'. Prima facie, amounts raised by way of share application money are not expressly covered in the transactions covered by sub-clauses (a) to (i) of Section 5(8) of the IBC. It is however the contention of the Appellant that in the present case when share application money was advanced by the Appellant but shares were neither allotted nor the share application money refunded, based on the statutory provisions of the Act and CADR Rules, 2014, the share application money had assumed the colour of deposit money and acquired the character of financial debt under Section 5(8) of IBC.

- The NCLT had erred by relying upon the judgment of NCLT in the case of ***Promod Sharma Vs M/s Karanaya Heart Care Pvt. Ltd. in CA(AT)(Ins) No. 426 of 2022*** as it was based on distinguishable facts as in that case the principal amount had already been refunded, and Section 7 application was filed only on the outstanding interest amount.

- Further, it was also contended that since neither any share was allotted nor the share application money was returned, the sum advanced became a deposit. This deposit therefore assumed the character of financial debt and hence application under Section 7 was maintainable. It was further the contention of the Appellant that in terms of Kushan Mitra judgment supra, the share application money in case of non-allotment of shares attracts the provisions of the Act and CADR

Rules and therefore was under the ambit of financial debt in terms of Section 5(8) of the IBC.

Arguments of the Respondent:

- The CD needed the funds for working capital therefore the CD requested the financial creditor to provide long/short-term debt to defray the aforesaid costs. However, the FC refused to provide debt funds but agreed to provide funds against the allotment of equity shares. In the year 2009-2010, the CD further asked for the funds, therefore the financial creditor deposited Rs. 1.71 Crore approx., upon various dates during the period 2011-2014 towards the share application money for the allotment of equity shares but shares were not allotted as there was a dispute pertaining to the valuation of shares between the CD and FC. The management of FC was also participating in the business decisions of the CD and it was decided that the shares will be allotted at the valuation determined on the basis of audited financial statements for the Financial Year (FY) 2014-15.

- Due to certain business decisions, the CD could not sustain the turnover and profit margins in 2014-15 and the FC demanded the refund of its share application money however the share application money could not be refunded due to the liquidity crunch.

- Further, in the subsequent financial years, the CD could not do much business therefore the business operation was shut down in the year 2017-18. The management of CD could not revive the operations thereafter due to covid 19.

- The CD alleged that the purported understanding between the CD and FC pertaining to the share application money had not been substantiated with the requisite evidence.

- Further, the CD has alleged that the CD is not liable to service the debt i.e. the Share Application Money since the FC was involved in pivotal business decisions of CD during FY 2013-14 & 2014- 15.

- The application u/s 7 was filed by the FC seeking a refund of the Share Application Money issued to the CD. However, in the case of ***Mr. Promod Sharma vs. M/s Karanaya Heartcare Private Limited (Comp. App. (At) (Ins.) No. 426 of 2022),*** the Hon'ble NCLAT held that – *"We are of the view that the Adjudicating Authority rightly took the view that the amount which was given by the Appellant as Share Application Money cannot be treated to be a financial debt so as to enable the Appellant to trigger the Insolvency Process under Section 7 of the Code." the* FC's claim is barred, as the Share Application money cannot be deemed to be a Financial Debt.

Held:

- From the principal clause of Section 5(8) of the IBC, the basic requirement for a debt to qualify as a 'financial debt' is the existence of a disbursal against consideration for the time value of money. Furthermore, sub-clauses (a) to (i) of Section 5(8) outline the various transactions that fall within the scope of 'financial debt.'

- ***Prima facie*, amounts raised by way of share application money are not expressly covered in the transactions covered by sub-clauses (a) to (i) of Section 5(8) of the IBC.**

- From Rule 2(c)(vii) of the CADR Rules and the explanatory clause appended

thereto, it becomes clear that it refers to any amount received and held pursuant to an offer made in accordance with the provisions of the Act towards a subscription to any securities, including share application money. **It follows that for the CADR Rules to apply to share application money, there must be a clear nexus demonstrating that the share application money was advanced in accordance with the relevant provisions of the Act.**

- From Section 42 of the Act, several statutory compliances must be fulfilled before issuing shares on a private placement basis. Section 42(2) of the Act mandates the issuance of a private placement offer letter in such cases.

- From the records available on file, there is no evidence that the CD issued any private placement offer letter to the Appellant. Additionally, there is no proof of a valid and concluded agreement between the two parties regarding the allotment of shares. Therefore, the amount advanced by the Appellant cannot be considered as having been given in response to a private placement offer.

- Rule 2 of the CADR Rules stipulates that an amount qualifies as a deposit only if it is received pursuant to a private placement offer made in compliance with the Act, and no shares are allotted against it. In the absence of any evidence from the Appellant demonstrating that a private placement offer was made in accordance with the Act, the CADR Rules cannot be deemed applicable. Since the amount advanced cannot be linked to Section 42 of the Companies Act, the applicability of Section 42(6), as contended by the Appellant in the present case, cannot be sustained.

- The NCLAT did not find any infirmity in the NCLT's order rejecting the Appellant's Section 7 application.

- However, the Appellant retains the right to seek a refund or recovery of the share application money through appropriate proceedings before a competent forum, in accordance with the law.

- The appeal was dismissed.

Companies Act

SANTOSH KUMAR LAHOTI (PETITIONERS/APPELLANT) VS. REGISTRAR OF COMPANIES, WEST BENGAL (RESPONDENT)

In the matter of Santosh Kumar Lahoti (Petitioners/Appellant) vs Registrar of Companies, West Bengal (Respondent) High Court of Calcutta order dated April 2, 2024

Facts of the Case:

- Petitioner is the Company Secretary of Jayshree Chemicals Ltd. whose shares are listed on the BSE Ltd. (hereinafter referred to as the "company"), and appointed in terms of section 203 of the Act, and has been associated with company since February 9, 2016

- The petitioner has been arrayed as an accused person in a Complaint pending before the learned 2nd Special Court, Calcutta which was initiated on the

basis of a complaint filed by the opposite party under sections 447 and 448 of the Companies Act, 2013 (The Act) for alleged violation of section 233(1)(b) of the Act.

- The allegation was that the total number of shares of the company (M/s. Jayshree Chemicals Ltd.) on the cut-off date (August 14, 2018) for the general meeting was 2,93,26,457 while for 1,35,90,589 shares votes were given favouring the scheme. Therefore, in respect of less than 90 % of total shares votes were cast in favour of the scheme. But the company secretary Shri Santosh Kumar Lahoti gave a false declaration to get the application under section 233 of the Act approved, by suppressing real facts and thereby attracting the provision of section 448 of the Act.

- The scheme was approved by 80 shareholders of the transferee company holding 100% of the total number present and voting at the meeting of the shareholders of the transferee company held on August 21, 2018, wherein the shareholders were also given the option of e-voting from August 18, 2019 to August 20, 2019.

- Transferee company-M/s. Jayshree Chemicals Ltd. through its company secretary has filed the notice of approval of the scheme of merger in the prescribed form CAA 11 dated August 24, 2018 with the Central Government as required under section 233(2) of the Act read with rule 25(4) of the Companies (Compromises, Arrangement and Amalgamations) Rules, 2016. Therefore, the petitioner has been made an accused for acting in discharge of duties of the company.

- In the petition of complaint, all the allegations in respect of the offence alleged are in respect of the company, and acts done on behalf of the company. But the company and the persons responsible for the affairs of the company have not been made parties.

- The appellant had applied before the High Court of Calcutta for quashing aside the pending complaint before the learned 2nd Special Court under section 448 of the Act for alleged violation of section 233 of the Act.

Question of Law

- Whether a company secretary, acting in the discharge of official duties and making a declaration in Form CAA 11 regarding the approval of a Scheme of Amalgamation by the requisite majority of shareholders, can be personally held liable under Section 447 of the Act, in the absence of fraudulent intent (mens rea) or statutory provision specifically imposing such liability?

Contentions of the Appellant:

- The appellant contended that there was no misstatement in the declaration since Section 233(1)(b) does not require 90% of the members "entitled to vote" at the general meeting, unlike Section 101(1) proviso. The expression in Section 233(1)(b) refers to the "members at a general meeting," meaning approval is based on 90% of the members present, not 90% of those entitled to vote based on the total paid-up share capital.

- No objections or suggestions were raised by the Registrar of Companies or the official liquidator under Rule 25(5) of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016. Subsequently, the Regional

Director, by an order dated October 25, 2018, confirmed the scheme in Form CAA 12

- The Deputy Registrar of Companies after 5 (five) months issued the impugned show-cause notice dated March 25, 2019 for an alleged false declaration by the petitioner in form CAA 11

- Further stated that the essential ingredients of making a complaint under section 447 for violation of section 448 read with section 233(1)(b) are as follows:

  (a) There has to be a statement which is false;

  (b) Person making the false statement must know it to be false thus having "Mens rea".

- Further contended that, it is not a false statement as such declaration was given by the petitioner on the basis of the reasonable interpretation with respect to the provisions of section 233 (1)(b) of the Act.

- It is submitted that the petitioner/ transferee company has filed the above petition before this Hon'ble Tribunal under section 233(6) against the order of rejection of the scheme by the Regional Director (Southern Region). The Regional Director is of the view that the petition may be considered in terms of section 230(6) of the Act on merits, as there is approval of the scheme by the majority of members of the transferee company in the extraordinary general meeting held on December 9, 2020 and the transferee company being the holding company of the transferor companies 1 and 2, has also given its consent by way of affidavits and also submitted that the majority of the creditors of the transferor companies and the transferee company, who have attended the meetings have also given their consent approving the scheme of amalgamation.

- It is submitted that the undersigned has no objection, if the scheme is approved by this Hon'ble National Company Law Tribunal, Chennai under section 230(6) of the Act and prays for passing suitable orders as deemed fit and proper in the circumstances of the case…"

Contentions of the Respondent:

- It is submitted that at Sl. No. 6(a)(iv) of CAA-11 shows that approval of 13590589 equity shares who were present and voting but not 90 per cent of the total number of shares thus, there is mis-statement has been made by company secretary at Sl. No. (iii) of the declaration. Hence, the accused herein has made a false declaration in the form CAA 11 knowing it to be false, to get the application under section 233 of the Act approved, and therefore the statement made by the accused is a false statement within the meaning of section 448 of the Act, for which he is liable under section 447 the Companies Act, 2013

- The ROC argued that Section 233(1)(b) mandates that the scheme must be approved by members holding at least 90% of the total shares at a general meeting. The declaration was allegedly made with the intent to improperly facilitate the approval of the scheme.

Held:

- The High Court ruled that the trial judge had taken cognizance of the complaint without proper judicial consideration. The order to take cognizance was found to be a mere formality, and the High

Court concluded that the cognizance taken was prima facie bad in law.

- The Court further noted that there was no reason for the petitioner to commit fraud, as the petitioner had recourse to various provisions under Sections 233(5), (6), and 232 of the Companies Act. The company could have convened new meetings of the shareholders and creditors to comply with Section 233(1) (b) if necessary.

- The Court clarified that the petitioner, as the company secretary, was acting in the discharge of their duties.

- It is clear from the petition of complaint that neither the company nor the persons, who were in charge of the day affairs of the company, have been made parties in the case. Without the company and the persons responsible for the day-to-day affairs of the company, the prosecution of the petitioner alone, who acted on behalf of the company is bad in law and thus clearly an abuse of the process of law.

- In the petition of complaint, all the allegations in respect of the offence alleged are in respect of the company, and acts done on behalf of the company. But the company and the persons responsible for the affairs of the company have not been made parties.

- It was stated that when a corporate entity commits an offense, it is typically the officers or directors responsible for the company's affairs who can be held liable, provided that a statutory provision for vicarious liability exists.

- Citing various judgements, the Court emphasized that there is no vicarious liability for managing directors or directors of a company unless explicitly provided for by law.The Court held that vicarious liability could not be imposed on the petitioner in the absence of fraudulent intent.

- It also cited earlier judgments to clarify that an individual can only be personally liable if the statutory provisions explicitly provide for vicarious liability or there is a clear demonstration of intent (mens rea).

- Thus, in view of the findings above, the proceedings pending before the learned, 2nd Special Court, Calcutta at West Bengal under section 448 of the Companies Act, 2013 for alleged violation of section 233 of the Companies Act, 2013, is bad in law and thus liable to be set aside.

Particulars	***Decided Caselaws/ Judgements refered***
Cases relied upon by the petitioner	ACCEL IT Service Ltd., the NCLT, DB-II Chennai
	IDFC Ltd. vs. Regional Director, Southern Region, Chennai
	Apollo Hospitals Enterprise Ltd. (transferee company) sanctioned by the Regional Director, Southern Region on June 28, 2021

Cases relied upon by the defendant	Satva Jewellery and Design Ltd
Cases referred by the Court	*Dayle De'Souza vs. Government of India*
	Aneeta Hada vs. Godfather Travels and Tours P. Ltd
	Sunil Bharti Mittal vs. Central Bureau of Investigation
	Maksud Saiyed vs. State of Gujarat

SEBI

EMAMI REALTY LIMITED

Adjudication Order Securities Exchange Board of India in the matter of Emami Realty Limited

Facts of the Case

1. Emami Realty Limited. ("Noticee", "Company") had obtained unsecured loan from the promoter group companies of Noticee from time to time.

2. In order to enhance the permanent capital base of the Noticee and reduce the financial cost Noticee requested the Lenders, being promoter group companies, to convert the unsecured loan of an amount of Rs 700,00,00,028/- (Rupees Seven Hundred Crores and Twenty-Eight only) into Optionally Convertible Debentures ("OCDs"), convertible at the option of the Noticee into 8,53,65,854 number of equity share as per the pre-agreed conversion ratio and on such other terms and conditions.

3. Noticee vide postal ballot notice dated January 12, 2023, had obtained the approval of the shareholders of Noticee for conversion of the existing unsecured loan of Rs 700,00,00,028/- (Rupees Seven Hundred Crores and Twenty-Eight only) taken from promoter group companies of Noticee.

4. Securities and Exchange Board of India ("SEBI") received a complaint on January 19, 2023, in the matter of Noticee, regarding unreasonably favourable terms offered by the Noticee to promoter group companies for the issuance of OCDs.

5. Based on the findings of the examination by the National Stock Exchange ("NSE"), SEBI observed certain non-compliances, under of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 ("ICDR Regulations") and SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR Regulations") and initiated adjudication proceedings against Noticee.

Charge levied: Failure to obtain in-principle approval from the Stock Exchange for issuance of OCDs against conversion of unsecured loan. Alleged non-compliance with reg. 28(1) of the LODR Regulations. Further, it was alleged that issuance and allotment of OCDs by the Noticee was in violation of Regulation 160(f), 162 (1), 163, (1) (d), (f), (fa), (j), 163(2), 164, 167(1) of the ICDR Regulations.

Contentions by the Noticee

1. **OCDs issued do not fall within the meaning of Convertible Security** -Noticee issued OCDs pursuant to the

approval granted by the shareholders of the company by postal ballot. Noticee was under the understanding that OCD do not fall within the meaning of "Convertible Security.". As per the definition of convertible security, the option to convert into equity shares is with the investor and not with the issuer therefore, OCDs issued by the Noticee does not fall within the meaning of "Convertible Securities." Noticee has further submitted that NSE did not agree to the view of the Noticee and therefore, to avoid any confrontation, Noticee revoked the OCDs and converted the same to NCDs in discussion with NSE.

Contentions by SEBI

1. **OCDs issued do not fall within the meaning of Convertible Security: SEBI stated as follows:**

   a. **Noticee has not obtained in-principle approval from the stock exchange** -Noticee issued and allotted OCDs convertible at the option of the investor at a pre-agreed conversion ratio of one equity share. SEBI further stated that as the nature of securities is such that it is convertible into equity shares at a pre-agreed conversion ratio at a later date, it is a convertible security as defined in the ICDR. The words *"with or without the option of the holder"* used in the definition of convertible security was just to emphasize that any security which is convertible (with or without the option of the holder) into shares at a later date is a convertible security. Therefore, Noticee was required to comply with the provisions of ICDR Regulations for the issuance of OCDs. SEBI further highlighted that Noticee has failed to obtain in-principle approval from the stock exchange for issue of OCDs.

   b. **Tenure of OCD`s was against the mandate of Regulation 162 (1)** -Noticee kept the tenure of the OCD`s as 10 years as against the mandate of the sub-regulation (1) of Regulation 162 **of ICDR Regulations** which prescribes the tenure of the convertible securities of the Issuer shall not exceed 18 months from the date of allotment. The OCDs issued by the Noticee were in the nature of convertible securities, therefore, Noticee was required to comply with the provisions of ICDR Regulations with respect to pricing as provided under Regulation 164 and lock-in as provided under Regulation 167 of ICDR Regulation. The Noticee was also required to make the disclosures in terms of Regulation 163 of ICDR Regulations with respect to the issuance of OCDs. All these provisions of ICDR Regulations have not been complied with, by the Noticee.

Penalty: SEBI imposed a penalty of Rs 5 lakh on the Noticee for violations related to the issuance of OCD`s to its Promoter Group Companies without complying with relevant provisions of ICDR Regulations.

■

FEMA – UPDATES AND ANALYSIS





CA Hardik Mehta *CA Tanvi Vora*

A. Update through A.P. (DIR Series) Circulars

ASIAN CLEARING UNION (ACU) MECHANISM – INDO-MALDIVES TRADE

In this article, we have discussed recent amendments made in FEMA through Notifications, Circulars, Master Directions, Press Notes & Press Releases. We have also analysed recent case laws on Foreign Exchange Management Act, 1999.

At present, under Regulations 3 of Foreign Exchange Management (Manner of Receipt and Payment) Regulations, 2023, trade transactions between ACU member countries are to be routed through the ACU mechanism or as per the directions issued by the Reserve Bank of India (RBI).

In November 2024, the RBI and the Maldives Monetary Authority (MMA) signed a Memorandum of Understanding (MoU) for establishing a framework to promote the use of local currencies viz., the Indian Rupee (INR) and the Maldivian Rufiyaa (MVR) for a wide range of cross-border transactions. The MoU encourages the use of INR and MVR in current account transactions, permissible capital account transactions and any other economic and financial transactions as agreed upon by both countries.

In light of this MoU it has been decided that India's bilateral trade transactions with Maldives may also be settled in INR and / or MVR in addition to the ACU mechanism.

A.P. (DIR Series) Circular No. 22 dated March 17, 2025

(Comments: This step of the RBI would enable exporters and importers to invoice and settle in their respective domestic currencies, which in turn would enable the development of trading in INR-MVR in foreign exchange market. This will reduce dependency on other currencies. Use of local currencies would optimise costs and settlement time for transactions and will eventually contribute to promoting trade between India and Maldives as well as deepen financial integration and strengthen the economic relations between India and Maldives. The amendment could also help stabilize the Maldivian economy *by reducing foreign exchange fluctuations and* ***dependency on the US dollar.)***

B. Analysis of case law on FEMA, 1999

HIGH COURT OF DELHI – MARTIN JEBARATHNA DOSS ANTONISAMY VS. RESERVE BANK OF INDIA

Facts of the Case

Martin Jebarathna Doss Antonisamy, a U.S. citizen and an Overseas Citizen of India (OCI) cardholder, purchased agricultural land in Tamil Nadu.

As per Regulation 8 of Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2000 (as applicable at the time of transaction), agricultural land cannot be purchased by NRIs / OCIs without prior approval from RBI. Mr. Martin did not obtain the required approval prior to purchase.

As part of the compounding process under FEMA, violators are required to regularize their actions by first rectifying the contravention and paying a penalty.

RBI directed Mr. Martin to do the following:

(1) Transfer the agricultural land within a maximum period of 6 months to either of the following provided they are eligible under FEMA for acquisition of the property:

- a person resident in India; or
- a person who is a citizen of India

(2) Post this transfer, Mr. Martin may approach the RBI for compounding.

Mr. Martin complied by selling the properties and approached the RBI for compounding. Compounding proceedings were concluded and vide impugned order dated 19.08.2024, a sum of Rs. 41,04,675/- was levied as compounding fee in terms of Section 13 of the FEMA r.w. the relevant rules.

However, Mr. Martin filed a writ petition under Article 226 of the Indian Constitution on the basis of the following arguments:

1. Good Faith: He did not knowingly violate FEMA and had already sold the land to comply with the law

2. Excessive Fine: The imposed fine was disproportionately high

3. Due Process: He was not given an opportunity to contest the calculation of the penalty

Compounding Penalty Levied

The counsel for RBI explained that the amount of penalty was levied as per Master Direction – Compounding of Contravention (Compounding Master Direction) under the Foreign Exchange Management Act, 1999 (FEMA, 1999) and has referred to 'Guidance Note on Computation Matrix' at Sub-Clause [4] of Part I of Clause 7.4 of the Compounding Master Direction, which provides as under:

Fixed Amount: INR 50,000/- (applied once for each regulation/ rule contravened, in a compounding application) + plus

Variable Amount:

Period	% of amount of contravention
<1 year	0.50%
1-2 years	0.55%
2-3 years	0.60%
3-4 years	0.65%
4-5 years	0.70%
> 5 years	0.75%

Further the computation is subject to Part-II of Clause 7.4, which provides that the amount imposed should not exceed 300% of the amount of contravention. Accordingly, the following information was taken into consideration for computation:

- The period of contravention was considered from date of purchase till the date of sale of the property i.e. 18 years, 7 months and 12 days, which fell under more than 5 years bracket.

- Amount of contravention was taken as the value of agricultural property paid by the petitioner at the time of acquisition (Contravention A). Further, the mode of payment was also in contravention of extant FEMA guidelines (Contravention B).

- As per the Compounding Master Direction, while calculating penalty, the compounding authority also considered the amount of undue gain made as a result of the contravention. Mr. Martin sold the property for Rs. 1,62,00,000, while purchase price was Rs. 13,68,225.

Calculation:

For both contraventions, i.e., purchase of agricultural property (Contravention A) and mode of payment (Contravention B), penalty was calculated in terms of para 7.4(I), Guidelines Note on Computation Matrix, of Compounding Master Direction.

a. Penalty for Contravention A = Rs. 50,000 (Base penalty) + Rs. 10,261.69 (0.75% of the amount of contravention, i.e., Rs. 13,68,225/-)

b. Penalty for Contravention B = Rs. 50,000 (Base penalty) + Rs. 8,686.69 (0.75% of the amount of contravention, i.e., 11,58,225/-)

c. Undue gain = Rs. 1,48,31,775/-.

Total calculated penalty = Rs. 1,49,50,723.38/-

However, as per Para 7.4(II) of Compounding Master Direction, the amount imposed should not exceed 300% of the amount of contravention. Accordingly, the final penalty imposed on the petitioner was restricted to Rs. 41,04,675/- i.e. 300% of Contravention A. Thus, the penalty imposed on the petitioner was much less than the original penalty calculated in the case.

Held

The Delhi High Court held as follows:

1. No Procedural Violation: Mr. Martin was given a chance to present his case before the RBI. However, he knowingly opted out of a personal hearing.

2. Legitimate Fine Calculation: The fine was within the prescribed range under FEMA's compounding matrix provided in Compounding Master Direction .

3. Legal Compliance by RBI: The RBI followed the due process while deciding the fine.

The Court found no merit in Mr. Martin's challenge and dismissed the petition, upholding the RBI's decision.

[2024] 167 taxmann.com 353 (Delhi) dated 11th September 2024

(Comments: It is evident the RBI through FEMA strictly regulates foreign ownership of agricultural land in India. NRIs and OCIs must obtain prior RBI approval before purchasing such property. Compounding under FEMA allows violators to regularize their actions but involves significant monetary penalties. Courts would not likely interfere with RBI's penalty decisions if they are within the prescribed limits available in public domain and follow due process. While compounding orders do not hold precedence value, this case before the Delhi HC would serve as a precedent for how FEMA violations regarding property acquisition by foreign nationals are handled in India. Undue gains are recoverable by the RBI since the gains on sale of property which was not permitted to be purchased in the first place would provide unfair advantage to the NRI/ OCI. It is worthwhile to know that the penalty is capped at 300% of the amount of contravention i.e. the 300% limit on the penalty amount would include the amount of undue gains earned.)

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BEST OF THE REST





Rahul Hakani
Advocate

Niyati Mankad
Advocate

1 THE COSMOS CO. OPERATIVE BANK LTD. VS. CENTRAL BANK OF INDIA & ORS. – ORDER DATED 4TH FEBRUARY 2025 PASSED IN CIVIL APPEAL NO. 1565 OF 2025 [2025 INSC 243] [SUPREME COURT]

Section 100 of the Transfer of Property Act, 1882 – legal mortgage vs. equitable mortgage - An equitable mortgage or charge does not require registration to be valid, but it cannot bind subsequent transferees or creditors unless they had notice of such charge - Mere deposit of part-title deeds may create an equitable mortgage if intent is clear, but priority in enforcement depends on the presence of notice - A subsequent lender without notice of a prior unregistered charge will retain priority over recovery

Facts:

The dispute arose between Cosmos Co-operative Bank Ltd. (Appellant) and Central Bank of India (Respondent) concerning priority of rights over a mortgaged flat. The original borrowers availed two separate loans from both banks by depositing different unregistered agreements to sale and documents as security over the same flat. The Central Bank of India initiated recovery proceedings first, but Cosmos Bank also obtained a decree in its favour. A dispute then arose as to who had a prior charge over the property. The Debt Recovery Tribunal ruled in favour of Cosmos Bank. However, the Bombay High Court set aside the DRT order, accepting Central Bank's claim of a prior equitable mortgage. This led to the appeal before the Supreme Court.

Issues Involved:

i. Whether the Respondent Bank (Central Bank) had a valid and enforceable equitable mortgage in terms of Section 100 of the Transfer of Property Act, 1882?

ii. Whether the creation of a charge or equitable mortgage requires registration under Section 59 of the Act?

iii. Whether the absence of notice to the Appellant Bank (Cosmos Bank) disentitled the Respondent from enforcing the mortgage against the recovery proceeds?

iv. How priority of charges under equitable mortgage law is to be determined in cases of successive creditors?

Held:

The Supreme Court allowed the appeal and set aside the High Court's judgment. It held

that the Central Bank's claim of an equitable mortgage was unenforceable against Cosmos Bank since there was no proof of notice or intimation about such charge. Referring to Section 100 of the Transfer of Property Act, 1882, the Court reaffirmed that a charge or equitable mortgage, even if unregistered, may be enforceable in equity—but only against parties with notice. The Court relied on ***M. L. Abdul Jabbar Sahib vs. M.V. Venkata Sastri & Sons (1969) 1 SCC 573***, clarifying that charges do not require registration unless created as legal mortgages. It further held that equitable mortgages created without notice to subsequent creditors cannot defeat the latter's claim. Hence, the deposit of part-deeds or documents did not create a charge binding on Cosmos Bank, and the ` 51 lakhs lying in escrow must be disbursed in Cosmos Bank's favour.

2 A. RAJENDRA VS. GONUGUNTA MADHUSUDHAN RAO – ORDER DT 4-4-2025 PASSED IN CIVIL APPEAL NOS.11070 - 11071 OF 2024 – [2025 INSC 447] [SUPREME COURT]

Section 61(2) of the Insolvency and Bankruptcy Code, 2016 - an appeal must be filed within 30 days of the order's pronouncement, extendable by only 15 days upon showing sufficient cause - This limitation is strict and cannot be extended beyond 45 days - The benefit of Section 12(2) of the Limitation Act (excluding time for obtaining certified copies) is available only if such copies are applied for - A litigant's failure to seek certified copies or to disclose true facts disentitles them from relief.

Facts of the Case:

The Appellant, A. Rajendra, a suspended Managing Director of Dharti Dredging and Infrastructure Ltd. (Corporate Debtor), filed appeals before the NCLAT against NCLT orders dated 20.07.2023. The NCLT had dismissed his application under Section 60(5) of the IBC to place his resolution plan before the CoC and approved another resolution plan under Sections 30(6) and 31(1) of the IBC. The NCLAT dismissed the appeals solely on the ground of limitation, noting the appellant had failed to file the appeals within the statutorily prescribed 30 days and that the delay condonation applications were based on misstatements regarding certified copy requests.

Issues Involved:

i. Whether the appeals were barred by limitation under Section 61(2) of the IBC?

ii. Whether the benefit of Section 12(2) of the Limitation Act could be claimed without applying for a certified copy?

iii. Whether the NCLAT erred in refusing to condone the delay given the appellant's explanation and the statutory discretion to condone up to 15 days beyond the 30-day limit?

Held:

The Supreme Court upheld the NCLAT's decision and dismissed the appeals, holding that limitation under Section 61(2) of the IBC starts from the date of pronouncement of the order and not from the date of knowledge or uploading unless certified copies are sought. The Court stressed that the 30-day appeal period is extendable only by a further 15 days, strictly upon sufficient cause. It held that the Appellant neither applied for certified copies within time nor provided valid grounds for

condonation. Relying on ***V. Nagarajan vs. SKS Ispat [(2021) 14 SCR 736], Cethar Ltd. v. SKS Ispat [(2002) 2 SCC 244]***, and ***National Spot Exchange Ltd. vs. Anil Kohli [(2022) 11 SCC 761],*** the Court reaffirmed the strict timeline and ruled that the Appellant failed to satisfy the conditions for delay condonation under the proviso to Section 61(2) of the IBC.

3 NEW MANGALORE PORT TRUST & ANR. VS. CLIFFORD D SOUZA ETC. ETC. – ORDER DT 3RD APRIL, 2025 PASSED IN CIVIL APPEAL NOS. 1796-1828 OF 2024 [2025 INSC 440] [SUPREME COURT]

Section 7 of the Public Premises Act & Section 18 of the Limitation Act - Where a party acknowledges liability in writing before expiry of the limitation period, a fresh limitation begins from the date of such acknowledgment under Section 18 of the Limitation Act, 1963. Proceedings for recovery under Section 7 of the Public Premises Act are thus not barred by limitation if such acknowledgment exists.

Where a directly related matter is sub judice, courts should await its outcome before deciding dependent proceedings.

Facts:

The New Mangalore Port Trust (NMPT) had allotted plots to several licensees for port-related operations under agreements that allowed periodic revision of licence fees with the approval of the Tariff Authority for Major Ports (TAMP). In 2010, a notification revised fees retrospectively from February 2007. NMPT raised demands accordingly, which the licensees contested in writ petitions, challenging the retrospective application. The Single Judge of the Karnataka High Court dismissed these writs in 2013, upholding the validity of the retrospective revision. However, the licensees filed intra-court appeals, which are still pending. Meanwhile, NMPT initiated recovery proceedings under the Public Premises (Eviction of Unauthorised Occupants) Act, 1971 (PP Act), which were challenged and quashed as barred by limitation by the District Judge and upheld by the High Court.

Issues Involved:

i. Whether the recovery proceedings initiated by NMPT under Section 7 of the PP Act were barred by limitation?

ii. Whether limitation under Article 52 of the Limitation Act applied? Whether Section 18 of the Limitation Act could extend the limitation period due to acknowledgment of liability by the licensees.

iii. Whether the High Court should have awaited the outcome of the pending intra-court appeals which directly concerned the validity of the retrospective fee revision?

Held:

The Supreme Court held that proceedings under Section 7 of the PP Act are subject to limitation period of 3 years under Article 52 of the Limitation Act, as clarified in ***NDMC vs. Kalu Ram (AIR 1976 SC 1637).*** However, it held that the licensees' letters (particularly dated 04.02.2015) amounted to an acknowledgment of liability under Section 18 of the Limitation Act, thereby extending the limitation period. The Court further found that since the intra-court appeals challenging the retrospective revision were still pending, the High Court ought not to have quashed

NMPT's demand notices. Accordingly, the Court set aside the High Court's order and restored NMPT's writ petitions, to be decided after the intra-court appeals. The Respondents would be liable to pay revised tariff along with applicable interest only if they fail in their appeals.

4 RAKESH KUMAR VERMA VS. HDFC BANK LTD. AND HDFC BANK LTD. VS. DEEPTI BHATIA [2025 INSC 473]

Section 20 of the Code of Civil Procedure, 1908 ("CPC"), The Indian Contract Act, 1872 - An exclusive jurisdiction clause in a private employment contract is valid and binding if the chosen court has jurisdiction under Section 20 CPC, the clause does not contravene Section 28 of the Contract Act, and the parties have expressly or impliedly excluded other forums - The status of the contracting parties does not alter the enforceability of such clauses, and employment contracts are to be treated at par with other contracts for the purposes of jurisdiction.

Facts:

The two civil appeals arise from two separate suits filed by ex-employees of HDFC Bank challenging their termination. Rakesh Kumar Verma filed a civil suit in Patna, and Deepti Bhatia filed in Delhi. Both had appointment letters/employment agreements containing clauses conferring exclusive jurisdiction on courts in Mumbai. HDFC Bank sought rejection of the suits on jurisdictional grounds, citing the exclusive jurisdiction clauses. While the Patna High Court upheld HDFC's objection and allowed its revision, the Delhi High Court dismissed HDFC's plea, holding that the Delhi courts had jurisdiction based on where the termination effects were felt and served.

Issues Involved:

Whether the civil suits filed by Rakesh and Deepti could be maintained in Patna and Delhi, respectively, despite the exclusive jurisdiction clause in their contracts specifying Mumbai courts as the appropriate forum? Whether such clauses in private employment contracts are valid and enforceable, and if a distinction should be made between employment and commercial contracts when interpreting such jurisdiction clauses?

Held:

The Supreme Court upheld the validity of exclusive jurisdiction clauses in private employment contracts, holding them enforceable so long as (i) they don't bar legal remedies (Section 28, Contract Act), (ii) the chosen court has jurisdiction under Section 20 CPC, and (iii) the clause expressly or impliedly excludes other forums. Citing precedents such as ***Swastik Gases vs. Indian Oil [(2013) 9 SCC 32]***, ***Hakam Singh vs. Gammon India [(1971) 1 SCC 286]***, and ***ABC Laminart vs. A.P. Agencies [(1989) 2 SCC 163],*** the Court clarified that employment contracts are not to be treated differently from other contracts. It affirmed the Patna High Court's decision but corrected the relief to a return of the plaint under Order VII Rule 10 CPC (not rejection). The Delhi High Court's decision was reversed.

5 SOHOM SHIPPING PVT. LTD. VS. THE NEW INDIA ASSURANCE CO. LTD. & ANR. [2025 INSC 453] [SUPREME COURT]

An insurance clause requiring the voyage to "commence and complete before monsoon sets in" cannot be construed as a material or precedent condition when the insurer was aware that the voyage would occur during foul weather - A literal enforcement resulting in the denial of all claims would defeat the purpose of the insurance itself - Such clauses, if non-material and part of a standard form, are considered impliedly waived when the insurer enters into the contract with full knowledge of contrary facts.

Facts:

Sohom Shipping Pvt. Ltd., engaged in shipping operations, purchased a barge named Srijoy II and planned its maiden voyage from Mumbai to Kolkata. The company secured a single voyage permit and obtained an insurance policy for the period 16.05.2013 to 15.06.2013. The insurance contract included a special condition that the "voyage should commence and complete before monsoon sets in." The vessel set sail on 06.06.2013 but encountered engine failure and ran aground due to bad weather. The insured filed a claim with the insurer, which was repudiated on the grounds that the vessel breached the special condition by commencing its journey after the monsoon had begun. A consumer complaint was filed before the NCDRC, which dismissed the complaint for lack of good faith on the Appellant's part.

Issues Involved:

i. Whether the special condition (regarding commencement and completion of the voyage before the onset of the monsoon) stands breached justifying the de facto repudiation of the Appellant's claim by the Respondent.

ii. Whether the contra proferentem rule apply due to alleged ambiguity in the insurance terms?

iii. Whether there was a breach of the doctrine of uberrima fides (utmost good faith) by the appellant?

iv. Whether the special condition in the insurance contract was a material term and if it could be construed as a condition precedent?

Held:

The Supreme Court held that the phrase "before monsoon sets in" was not ambiguous and therefore contra proferentem did not apply. However, it found the special condition to be non-material and impliedly waived, given the insurer's knowledge that the voyage would take place during the foul weather period. Relying on precedents including Chandumull Jain (1966), New India Assurance (2016), and Ramji Karamsi (1951), the Court concluded that enforcing the condition as a strict prerequisite would lead to absurdity, rendering the insured without remedy even when insured against such risks. Thus, the NCDRC's order was set aside, and the matter remanded for assessment of the payable insurance sum. The Court emphasized that other allegations like forgery or further contractual breaches must be addressed independently on merits by the NCDRC. ■

THE CHAMBER NEWS



CA Mehul Sheth
Hon. Jt. Secretary



CA Neha Gada
Hon. Jt. Secretary

Important events and happenings that took place online/physical between **March 1, 2025 to March 31, 2025** are being reported as under:

I. ADMISSION OF NEW MEMBERS

The details of new members who were admitted in the Managing Council Meeting held on March 25, 2025 are as under:

Type of Membership

Life Member	Ordinary Member – Half Yearly	Student Member	Associate Member	Total Members
29	**–**	**1**	**–**	**30**

II. PAST PROGRAMMES

INTERNATIONAL TAXATION

1.3.2025

Topic: Gujarat International Finance Tec-City (GIFT CITY) – Demystifying Tax and Regulatory Insights

a Transforming IFSC - Chairman's vision
Speaker: ***Mr. Dipesh Shah, ED, IFSCA***

b Regulatory Framework for Diverse Entities in GIFT City: An In-Depth Overview
Speaker: ***CA Paresh P. Shah***

c Tax Implications for Entities Operating in GIFT City: A Comprehensive Guide
Speaker: ***CA Vishal Gada***

d Decoding Roadblocks: Practical Challenges in GIFT City's Tax and Regulatory Landscape
Moderator: CA Anish Thacker
Panelist: Mr. Jaiman Patel, Ms. Shefali Shah, CA Rinkesh Devnani

e Brainstorming Session – Exploring Practical Challenges and Subtleties in GIFT City Tax and Regulatory Framework
Moderator: Mr. Rajesh Gandhi
Panelist: Mr. Himanshu Jain, Ms. Parul Jain, Mr. Tushar Sachade

22.3.2025
Topic: Workshop on Wealth & Succession Planning and Estate Taxation

a Overview of Wealth and Succession Planning and its Rationale. The Circumstances leading to Provision of arrangement between the inheritors of the wealth and the Business Instruments for Succession, its use, limitations and impact on Laws affecting such instruments
Speaker: ***CA Gautam Doshi***

b The Legal and Regulatory aspects Governing Succession / Intestate Succession, Will and Probate Law of Will, Trust and Personal laws Governing the individuals and families and impact of taxation and Regulatory regime in India
Speaker: ***Adv. Ashish Ahuja***

c Taxation of Estate under Succession by Gift through trust or any other mode of Succession
Speaker: ***CA Yogesh Thar***

d FEMA – Wealth and Succession planning modes and Instruments, Provisions of FEMA applicable to transactions of Gift, Estate and succession through Trust
Speaker: ***CA Paresh Shah***

e Brain Trust Session – Panel Discussion
Moderator:CA Dinesh Kanabar
Panelists: CA Girish Vanwari, Mr. Girish Venkatraman

STUDENT

Topic: **Certificate course on GST Law and Litigation Jointly with Government Law College (*contd.*)**

1.3.2025

a Input Tax Credit – Eligibility, Conditions
Speaker: ***CA Sunil Gabhawala***

b Input Tax Credit – Reversals (Section 17, 18 & Corresponding Rules)
Speaker: ***CA Parth Shah***

8.3.2025

c Zero Rated Supplies, Deemed Exports and relevant refunds provisions
Speaker: ***CA Jinit Shah***

d Refund Provisions under GST (other than Refund related to Zero Rated supplies and Deemed Exports)
Speaker: ***Mr. Raj Khona,*** *Advocate*

15.3.2025

e Input Service Distributor, Job Work Procedure, Goods sent on

Approval Basis
Speaker: ***Mr. Rushil Shah,*** *Advocate*

f Documentation, Books of accounts, E-Way Bills and E-Invoicing
Speaker: ***CA Gaurav Save***

22.3.2025

g GST Returns (monthly and annual) and Invoice Matching System
Speaker: ***CA Umang Talati***

h Scrutiny, Assessment, Department Audit, Inspection, Search & Seizure
Speaker: ***CA Ashit Shah***

29.3.2025

i GST Implications on Real Estate Sector
Speaker: ***CA Naresh Sheth***

14.3.2025 & 15.3.2025

Topic: **8th Dastur National Debate Competition**

Topic: **Webinar Series on "CA Students' Orientation Course, 2025"**

10.3.2025

a Communication Skills
Speaker: ***CA Jayant Gokhale***

Mastering Income tax filings
Speaker: ***Adv. Ravi Sawana***

11.3.2025

b Valuation Overview and Methodologies'
Speaker: ***CA Sujal Shah***

12.3.2025

c FEMA Basics & Compliance : What every CA Article Student Must Know
Speaker: ***CA Hinesh Doshi, CA Aarti Karwande***

13.3.2025

d GST Landscape: Best Practices for Returns and Compliance
Speaker: ***CA Yash Parmar***

17.3.2025

e Audit Insights 2.0: Checklist, AI tools and Best practices
Speaker: ***CA Ankit Sanghavi***

STUDY CIRCLE – DIRECT TAXES

4.3.2025

Topic: **Overview of New Income Tax Bill**
Speaker: ***CA Anish Thacker***

RESIDENTIAL REFRESHER COURSE

6.3.2025 to 9.3.2025

Topic: **48th Residential Refresher Course on Direct Taxes – 6th – 9th March, 2025 – Mayfair Lake Resort – Raipur**

a Keynote address
Speaker: ***Shri Gnanvatsal Swami***, BAPS Swaminarayan Sanstha

b Case Studies in Direct Taxation (Covering Recent Amendments to Capital Gains and other Live Topics)
Speaker: ***CA Abhitan Mehta***

c Foundational Tax Concepts: A Focus on Sections 4, 5, 6 & 9 of the Income Tax Act, 1961
Speaker: ***CA H. Padamchand Khincha***

d Income - Tax Bill, 2025 – An Overview
Speaker: ***CA Anish Thacker***

e Tax Terrain of Real Estate: Direct and Indirect Dimensions in Panel Discussion Format
Panelists: Mr. Tushar Hemani Sr. Advocate, Mr. Bharat Raichandani, Advocate
Moderator: Mr. Dharan Gandhi, Advocate

f Compliance, Concessions, and Corrections: Inside Sections 139, 119 & 264
Speaker: ***CA Shailesh Bandi***

g Brains' Trust
Panelists: Mr. Saurabh Soparkar – Sr. Advocate, CA Yogesh Thar
Moderator: CA Ameya Kunte

MEMBERSHIP & P.R.

19.3.2025
Topic: **SAS Meeting on Etiquette and climbing the corporate ladder**
Speaker: ***Adv. Deepak Tralshawala***

29.3.2025
Topic: **Basera Yehin Hai... A CTC Musical Evening of Togetherness**

DIRECT TAXES

27.3.2025
Topic: **Intensive Study Group (ISG) – Direct Taxes Meeting on Recent Important Decisions Under Direct Tax**
Speaker: ***Ms. Dinkle Haria,*** *Advocate*

Topic: **Webinar on A New Tax Frontier – Deep Dive into the New Income Tax Bill, 2025**

29.3.2025

a Overview, Use of New Terms, Savings Clause Impact
Speaker: ***Sr. Adv. Arvind Datar***

PUNE STUDY GROUP

29.3.2025
Claiming Customs duty benefit under Free Trade Agreements (FTAs) & related complexities
Speaker: ***CS, LLB Amrendra Chaudhri***

48th Residential Refresher Course on Direct Taxes held on 6th – 9th March, 2025 – Mayfair Lake Resort – Raipur

Organised by ***Residential Refresher Course Committee***



Dignitaries at the Inaugural Session



CA Vijay Bhatt (President) giving his opening remarks.
Seen from L to R: CA Vishal Shah (Vice Chairman), Mr. Kishor Vanjara (Advisor), CA Ankit Sanghavi (Chairman) and CA Darshak Shah (Vice Chairman)

CA Ankit Sanghavi (Chairman) welcoming the speakers and the delegates





Shri Gnanvatsal Swamiji giving Keynote address,
Seen from L to R: CA Ankit Sanghavi (Chairmam), CA Vijay Bhatt (President, Mr. Kishor Vanjara (Advisor) & CA Hinesh Doshi (Past President)



*Session on "**Foundational Tax Concepts: A Focus on Sections 4, 5, 6 & 9 of the Income-tax Act, 1961"** -*
Seen from L to R: CA Bandish Hemani (Convenor), CA Vijay Bhatt (President) CA H. Padamchand Kincha (Speaker), CA Darshak Shah (Vice Chairman)



*Session on **"Case Studies in Direct Taxation (Covering Recent Amendments to Capital Gains and other Live Topics)"** - Seen from L to R: Adv. Prakash Sinha, CA Mehul Sheth (Hon. Jt. Secretary), CA Abhitan Mehta (Speaker), CA Vishal Shah (Vice Chairman) & CA Parth Sanghvi*

48th Residential Refresher Course on Direct Taxes held on 6th – 9th March, 2025 – Mayfair Lake Resort – Raipur

Organised by ***Residential Refresher Course Committee***



*Session on **"Compliance, Concessions, and Corrections Inside Sections 139, 119, & 264"** - Seen from L to R: CA Kalpesh Doshi, CA Jayant Gokhale (Vice President), CA Shailesh Bandi (Speaker), CA Ankit Nandu, & CA Ankit Kothari*



*Session on **"Income-Tax Bill, 2025 – An Overview"** - Seen from L to R: CA Charmi G. Shah, CA Neha Gada (Hon. Jt. Secretary), CA Anish Thacker (Speaker), CA Khyati Vasani.*



***Brain Trust Session** - Seen from L to R: CA Vitang Shah (Hon. Treasurer), CA Ameya Kunte (Moderator), Sr. Adv. Saurabh Soparkar (Panel Member), CA Yogesh Thar (Panel Member) & CA Neelesh Vithlani*



***Case Studies discussion on "Tax Terrain of Real Estate: Direct and Indirect Dimensions in Panel Discussion Format"** - Seen from L to R: Adv. Dharan Gandhi (Moderator), Sr. Adv. Tushar Hemani (Panel Member), Adv. Bharat Raichandani (Panel Member)*

RRC Team



View of the Audience





Group Photo

The Workshop on Wealth & Succession Planning and Estate Taxation held on 22nd March, 2025 at Hotel Sahara Star, Mumbai

Organised by ***International Taxation Committee***



Dignitaries at the Inaugural Session



CA Vijay Bhatt (President) giving his opening remarks.
Seen from L to R: CA Vishal Shah (Convenor), CA Karishma Phatarphekar (Chairperson), CA Gautam Doshi and CA Harsh Shah

CA Karishma Phatarphekar (Chairperson) welcoming the speakers and the delegates





Seen from L to R: CA Vishal Shah (Convenor), CA Karishma Phatarphekar (Chairperson), CA Vijay Bhatt (President) CA Gautam Doshi (Speaker) and CA Harsh Shah



Seen from L to R: CA Harsh Shah, CA Karishma Phatarphekar (Chairperson), Adv. Ashish Ahuja (Speaker) and CA Monika Wadhani (Convenor).

The Workshop on Wealth & Succession Planning and Estate Taxation held on 22nd March, 2025 at Hotel Sahara Star, Mumbai

Organised by ***International Taxation Committee***

Seen from L to R: CA Vishal Shah (Convenor), CA Hinesh Doshi (Past President) CA Yogesh Thar (Speaker) and CA Ujwal Thakrar





Seen from L to R: CA Kirit Dedhia, CA Shabbir Motorwala (Co-Chairman), CA Paresh Shah (Speaker), CA Chintan Shah

Panel Discussion

Seen from L to R: CA Girish Vanvari (Panel Member), Mr. Girish Venkataraman (Panel Member), CA Dinesh Kanabar (Moderator), CA Jayant Gokhale (Vice President), CA Shabbir Motorwala (Co-Chairman)





View of the Audience







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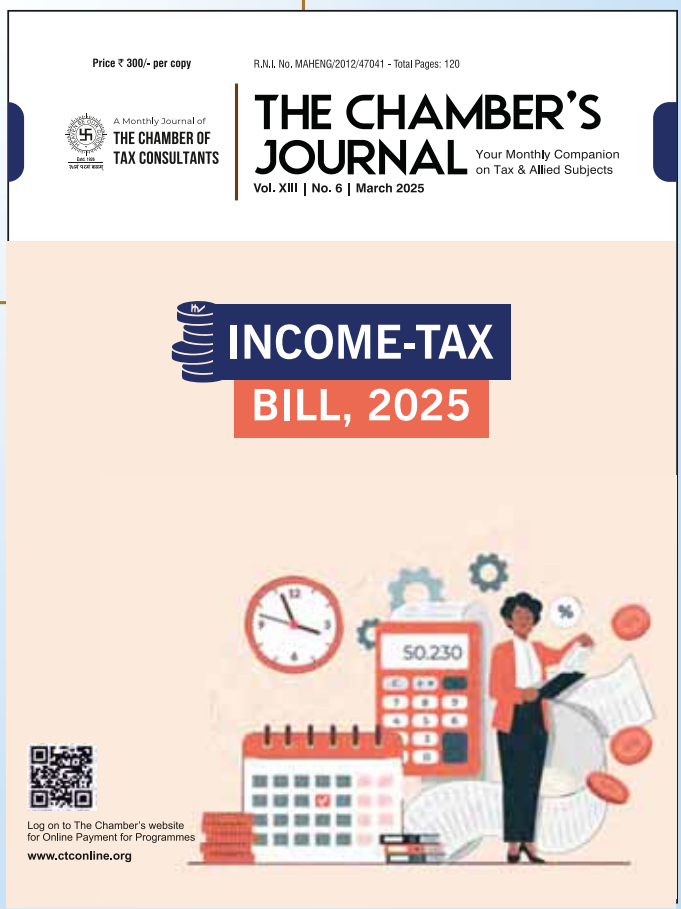

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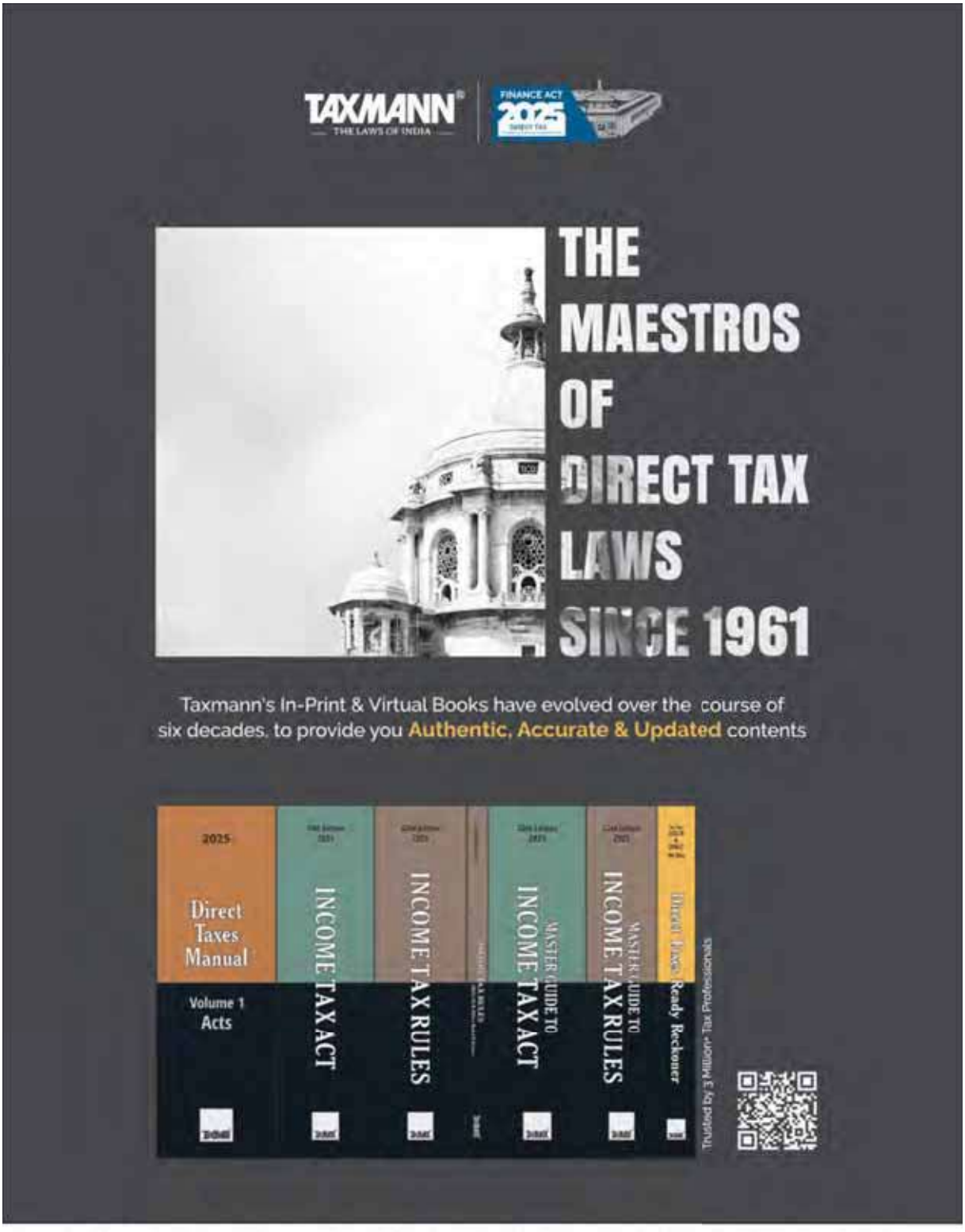

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