

In Re: Universities

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Court : Authority for Advance Rulings

Decided On : Feb-25-2005

Reported in : (2005)194CTRAAR289

Judge : S S Quadri, K Singh

Appellant : In Re: Universities

Judgement :

Appellants: In Re: Universities Superannuation Scheme Ltd. as Trustees of Universities Superannuation Scheme Income Tax Act, 1961 - Sections 45(1), 48, 112, 112(1), 115I, 115O, 115AD, 115AD(3) and 245(1); Finance Act, 1999; Finance (No. 2) Act, 2004; Securities Contracts (Regulation) Act, 1956 - Section 2
Union of India v. A. Sanyasi Rao, Appeal (Tribunal)--PROCEDURE
Reversal of order of CIT(A) without assigning any reason
Without giving reasons the Tribunal reversed the order passed by the CIT(A). Held: While reversing the order passed by the appellate officer it is the duty of the Tribunal to provide detailed reasons particularly when the decision of the Tribunal is considered to be final on facts.

1. The applicant in this application under Section 245(1) of the IT Act, 1961 (for short the 'Act'), is a tax resident of the United Kingdom (the UK). It is registered in India as Foreign Institutional Investor (FII) with the Securities and Exchange Board of India (SEBI) on 3rd March, 1998 and accordingly it has been investing in securities in India. The universities of the UK, for the purpose of providing pension and other superannuation benefits to academic and senior administrative staff in the universities and other higher education and research institutions, founded

Universities Superannuation Scheme (USS). The applicant, the Universities Superannuation Scheme Limited (USSL), was established to undertake and discharge the office of the trustee of USECTION The applicant is thus the legal owner of the assets of USS and operates to meet the existing and prospective entitlement of the beneficiaries of USECTION The applicant was incorporated in the UK as a company limited not by shares but by guarantee.

For the asst. yrs. 1999-2000 to 2003-04, the applicant filed returns of its income from investment in India as a FII by applying provisions of Section 115AD of the Act. In the accounting year relevant to the asst.

yr. 2003-04, the applicant incurred long-term capital losses of INR 12,94,46,340. The case of the applicant is that had it the option of computation under the second proviso to Section 48 as against Section 115AD(3) of the Act, the capital loss would have worked out to INR 17,38,75,450 and thus the loss would have been more by INR 4,44,29,110.

On these facts, the applicant is seeking advance ruling of the Authority on the following questions : "(1) Whether, on the facts and in the circumstances of the case, the applicant, i.e., the Universities Superannuation Scheme Limited as trustee of Universities Superannuation Scheme, a Foreign Institutional Investor (hereinafter referred to as "the FII), will be entitled to opt out of the provisions of Section 115AD of the IT Act, 1961 (hereinafter referred to as 'the Act'), which deals with the taxability of the income earned by an FII, and apply the normal provisions of the Act viz., Section 48 r/w Section 112 which allow the benefit of indexation, for computing the capital gains/losses arising to it from its investment activities in India (2) Whether, on the facts and in the circumstances of the case, if it is held that the applicant has an option to be governed under the normal provisions of the Act in a particular year, and such option is exercised by the applicant, then is it precluded from taking a different position in subsequent assessment years (3) Without prejudice to the above, would the provisions of Section 115AD be applicable to an assessee who has suffered a capital loss on the transfer of securities ?" 2. The Director of IT, International Taxation, Mumbai (hereinafter referred to as the "CIT") submitted the following comments : It is

stated that taxation of a non-resident in India is determined in accordance with the provisions of the Act read with the concerned Double Taxation Avoidance Agreement. The Government of Republic of India and the Government of the United Kingdom of Great Britain and Northern Ireland concluded a Convention on Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and Capital gains on 26th Oct., 1993 (hereinafter referred to as "Treaty"). The applicant is taxable both under the Act as well as the Treaty. Section 115AD is a special provision in respect of "Tax on income of FIIs from securities or capital gains arising from their transfer" in Chapter XII which deals with "Determination of tax in certain special cases". Section 115AD being a special provision will override the general provisions. There are several decisions of the Hon'ble Supreme Court laying down the law on this aspect. The applicant has not shown that Section 115AD is ambiguous and not clear. On the alleged ground that it no longer provides any preferential treatment to the FIIs, it cannot be ignored. The judgment of the Hon'ble Supreme Court of India in Union of India v. A. Sanyasi Rao (1993) 202 ITR 584 (SC) would not apply since the constitutional validity of that provision is neither in issue nor can it be questioned before the Authority. Section 115AD applies to all FIIs and there is no cogent reason as to why the applicant should be treated differently in the assessment year in question.

Where the Parliament so intended it provided, as in Section 115-I, an option to be exercised by the assessee. Absence of such a provision in the scheme of 115AD indicates that no option is available to FIIs. For the reason that the applicant suffered capital loss in an assessment year, it cannot claim the option to opt out of Section 115AD of the Act. If an option as in Section 115-I, is read into Section 115AD, it would result in applying such provisions of the Act which the Parliament did not intend to apply to FIIs. It is well settled position in law that income includes both profit and loss. In any event Section 115AD does not cause any discrimination and Article 26 of the Treaty is not attracted.

3. Mr. P.J. Pardiwalla, the learned counsel for the applicant, has argued that Section 48 and 112 of the Act deal with capital gains and are applicable to all the assesseees whereas Section 115AD of the Act which provides for a concessional rate of tax on gains, applies to FIIs, therefore, it would not apply to a case where

loss is suffered by FIs as no levy of tax on loss is involved. As the intention of the Parliament was to provide certain incentives to FIs, they must be deemed to have an option to be governed either by the normal provisions (Section 48 and 112) or by Section 115AD whichever is beneficial to them. The further contention is that on transfer of securities, computation should be under Section 48 of the Act and if gains accrue or arise, only then, for the purpose of rate of tax, Section 115AD should be resorted to. Under Article 26 of the Treaty there can be no discrimination of a non-citizen; by making the option available to domestic companies and denying the same to the FIs, Article 26 is violated. It is pleaded that the same option which is available to the domestic companies should also be made available to FIs.

4. Mr. Srivastava (Addl. Director of IT) who has appeared for the CIT, argued that Section 48 and 112 are general provisions and are not applicable to FIs which are governed by special provisions of Section 115AD--a concessional tax regime. For residents, two alternatives are available under the Act; the first is indexation provision of Section 48 and the higher rate of tax @ 20 per cent and the second is computation without indexation provision but lower rate of tax @ 10 per cent as provided in the proviso to Section 112(1) of the Act. Where the Parliament intended to give the benefit of an option, it had so provided as under Section 115-I which is grouped in Chapter XII. For FIs, there is no option to elect to work out profit or loss with or without indexation under the scheme of Section 115AD which falls in Chapter XII-A. The domestic companies and FIs are not based on similar footing, and there is no discrimination between a domestic company and a FI, on the basis of nationality, so Article 26 of the Treaty will not be violated.

Inasmuch as the discussion in respect of questions (1) and (3) is common and question No. (2) is consequential, we shall proceed to discuss them together.

The general provisions dealing with capital gains, relevant to the present discussion, may be noticed here. They are Section 45, 48 and 112 of the Act. Section 45(1) declares that any profits and gains arising from the transfer of a capital asset shall be (i) deemed to be the income of the previous year in which the transfer took place, and (ii) chargeable to income-tax under the head 'Capital

gains'. Section 48 outlines the mode of computation of capital gains and is germane to the issue. It is in the following terms : 48. The income chargeable under the head "Capital gains" shall be computed, by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amount namely : (i) expenditure incurred wholly and exclusively in connection with such transfer; (ii) the cost of acquisition of the asset and the cost of any improvement thereto: Provided that in the case of an assessee, who is a non-resident, capital gains arising from the transfer of a capital asset being shares in, or debentures of, an Indian company shall be computed by converting the cost of acquisition, expenditure incurred wholly and exclusively, in connection with such transfer and the full value of the consideration received or accruing as a result of the transfer of the capital asset into the same foreign currency as was initially' utilized in the purchase of shares or debentures, and the capital gains so computed in such foreign currency shall be reconverted into Indian currency, so, however, that the aforesaid manner of computation of capital gains shall be applicable in respect of capital gains accruing or arising from every reinvestment thereafter in, and sale of, shares in, or debenture of, an Indian company : Provided further that where long-term capital gain arises from the transfer of a long-term capital asset, other than capital gain arising to a non-resident from the transfer of shares in, or debentures of, an Indian company referred to in the first proviso, the provisions of Clause (ii) shall have effect as if for the words "cost of acquisition" and "cost of any improvement", the words "indexed cost of acquisition" and "indexed cost of any improvement" had respectively been substituted : The provisions, extracted above, lay down that income chargeable under the" head "Capital gains" shall be computed by deducting from the full value of consideration, received or accrued on transfer of the capital asset, the amounts representing the cost of acquisition of the asset together with the cost of improvement thereto and the expenditure incurred wholly and exclusively in connection with such transfer. The first proviso deals with computation of capital gains in the case of a non-resident assessee who utilizes foreign currency for purchasing shares in or debentures of an Indian company. It says that in the case of a non-resident where the capital gains arise from the transfer of shares in or debentures of Indian companies, the computation shall be made by converting the

cost of acquisition and expenditure incurred wholly and exclusively in connection with such transfer and the full value of consideration received or accruing as a result of transfer of the capital assets is to be first converted into the same foreign currency as was initially utilized in the purchase of shares or debentures and then the capital gains so computed in such foreign currency shall be reconverted into Indian currency. It also provides that the same method would apply for every reinvestment thereafter in any sale of shares or debentures of an Indian company. The second proviso is pertinent to the point. It ordains that long-term capital gains arising from the transfer of a long-term capital asset (not being the capital asset referred to in the first proviso) shall be computed by substituting "indexed cost of acquisition" for the expression "cost of acquisition" and "indexed cost of any improvement" for the expression "cost of improvement" in Clause (ii) of the main section. It will be apposite to highlight here that having regard to Sub-section (3) of Section 115AD, in respect of a Fn, while computing capital gains arising from the transfer of short-term or long-term capital assets, being securities other than unit referred to in Section 115AB of the Act, the operation of the first and the second proviso, referred to above, has to be excluded. We shall delve into this aspect presently.

Now, we may advert to Section 112 of the Act which incorporates the method of computation of tax and the rates of tax payable by an assessee whose total income includes capital gains arising from the transfer of long-term capital assets. It needs to be mentioned here that the proviso to Sub-section (1) of Section 112 (inserted by the Finance Act, 1999 w.e.f. 1st April, 2000), extends the benefits of limiting the rate of tax to 10 per cent in respect of any income arising from the transfer of a long-term capital assets (whether listed securities or units) where the tax payable exceeds 10 per cent of the amount of capital gains before giving effect to the provisions of the second proviso to Section 48. It is enjoined that such excess tax over 10 per cent shall be ignored for the purpose of computing the tax payable by the assessee. The position summed up above applies to assessees in general.

Under the scheme for permitting FIIS in our capital market as is evident from the budget speech of the Hon'ble Minister of Finance, a special provision--Section

115AD--has been inserted by the Finance Act, 1993 w.e.f. 1st April, 1993. It deals with tax on income of FIIs from securities or capital gains arising from their transfer. It needs no elaboration to hold that Section 115AD, being a special provision for FIIs, overrides the general provisions, discussed above (*Generalibus specialia derogant*). [Special things derogate from general (Latin for Lawyers)]

115AD. Tax on income of Foreign Institutional Investors from securities or capital gains arising from their transfer.--(1) Where the total income of a Foreign Institutional Investor includes-- (a) Income [other than income by way of dividends referred to in Section 115-O] received in respect of securities (other than unit referred to in Section 115AB); or (b) Income by way of short-term or long-term capital gains arising from the transfer of such securities, (i) the amount of income-tax calculated on the income in respect of securities referred to in Clause (a), if any, included in the total income, at the rate of twenty per cent; (ii) the amount of income-tax calculated on the income by way of short-term capital gains referred to in Clause (b), if any, included in the total income, at the rate of thirty per cent; The following proviso shall be inserted in Clause (ii) of Sub-section (1) of Section 115AD by the Finance (No. 2) Act, 2004, w.e.f. 1st April, 2005 : Provided that the amount of income-tax calculated on the income by way of short-term capital gains referred to in Section 111A shall be at the rate of ten per cent; (iii) the amount of income-tax calculated on the income by way of long-term capital gains referred to in Clause (b), if any, included in the total income, at the rate of ten per cent; and (iv) the amount of income-tax with which the Foreign Institutional Investor would have been chargeable had its total income been reduced by the amount of income referred to in Clause (a) and Clause (b).

(2) Where the gross total income of the Foreign Institutional Investor-- (a) consists only of income in respect of securities referred to in Clause (a) of Sub-section (1), no deduction shall be allowed to it under Section 28 to 44C or Clause (i) or Clause (iii) of Section 57 or under Chapter VI-A; (b) includes any income referred to in Clause (a) or Clause (b) of Sub-section (1), the gross total income shall be reduced by the amount of such income and the deduction under Chapter VI-A shall be allowed as if the gross total income as so reduced, were the gross total income of the Foreign Institutional Investor.

(3) Nothing contained in the first and second provisos to Section 48 shall apply for computation of capital gains arising out of the transfer of securities referred to in Clause (b) of Sub-section (1).

(a) the expression "Foreign Institutional Investor" means such investor as the Central Government may, by notification in the Official Gazette, specify in this behalf; (b) the expression "securities" shall have the meaning assigned to it in Clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956)] Section 115AD--a comprehensive provision--occurs in Chapter XII which deals with determination of tax in certain special cases. It specifies securities covered under the beneficial scheme, treatment given to the gross total income of FIIs; the permissible deductions therefrom, the mode of computation of capital gains arising out of the transfer of such securities and prescribes concessional rates of tax chargeable thereon. Under the said scheme, it may be noted, the income of a FII from securities and the capital gain arising from their transfer are taxed at concessional rate as a special case. A glance at Sub-section (1), would show that it contains two Clauses (a) and (b). Clause (a) speaks of income (other than income by way of dividend referred to in Section 115-O) received in respect of securities (other than unit referred to in Section 115AB). Clause (a) is not material for our purpose. Clause (b) speaks of short-term and long-term capital gains arising from the transfer of such securities. The words 'such securities' in Clause (b) refer to securities whose income is dealt with in Clause (a). What Sub-section (1) provides is that where the total income of a FII includes income mentioned in Clause (a) and (b), the income-tax payable shall be the aggregate of the amounts of income-tax calculated at the rates specified in Sub-clauses (i) to (iv). The applicant has neatly tabled comparative rates of tax applicable under Section 112 and Section 115AD. The same may be quoted here for proper appreciation of the point-- Taxability of FII under the specific provisions of s. 115AD of the Act (surcharge not applicable to foreign companies) Taxability of other assesseees under the provisions of s. 112 of the Act (Tax rates mentioned are excluding surcharge) (iii) 30% for cases other than (i) and (ii) above, i.e. firm, AOP/BOI, etc.

From this table the concessional rates of tax applicable to FIIs under Section 115AD in comparison with the rates of tax applicable under Section 112, are evident. The position which emerges on the basis of the proviso to Sub-section (1) of Section 112, is not indicated in this table.

Sub-section (2) thereof provides that, where gross total income of a FII consists only of income falling under Clause (a) of Sub-section (1), no deduction shall be allowed under Section 28 to 44C or Clause (i) or Clause (iii) of Section 57 or under Chapter VI-A and where such total income includes income referred to in Clause (a) or (b) of Sub-section (1), then it (such gross total income) shall be reduced by the amount of such income and the amount of deduction under Chapter VI-A. The resultant amount thus arrived at shall be treated as the gross total income of a FII. The guidelines for computation of capital gains arising to FIIs from the transfer of securities, dealt with in Sub-section (1), is embodied in Sub-section (3) of Section 115AD which, in effect, applies Section 48 with the modification of excluding the first and second provisos thereof. It may be apt to recapitulate here that Section 48 which incorporates the mode of computation of capital gains, provides that the income chargeable under the head "Capital gains" shall be computed by deducting from the full value of consideration received or accruing as a result of the transfer of capital assets, the following amounts; (i) expenditure incurred wholly and exclusively in connection with such transfer, and (ii) the cost of acquisition of assets and the cost of any improvement thereto. We pass over the first proviso which provides for the computation of capital gains where foreign currency is utilized by a non-resident-assessee in purchasing shares in or debentures of an Indian company, referred to above, as it is not pertinent here. The second proviso excludes from its operation capital gain arising to a non-resident from the transfer of shares in or debentures of Indian company referred to in the first proviso and directs that where long-term capital gain arises from the transfer of a long-term capital asset, then in computing such gains for the words "cost of acquisition" and "cost of improvement" the words "indexed cost of acquisition" and "indexed cost of improvement" shall be substituted in Clause (ii) of Section 48. It may be seen that even in the case of FIIs, capital gains are computed under Section 48 but by excluding the first and second provisos thereof. In our view absence of a provision in Section 48, in regard to computation of capital gain under Section 115AD, would

not make any difference as Section 115AD is a self-contained code. It is true that the first and the second provisos to Section 48 are applicable to residents as well as non-residents and that FIIs are also non-residents. But there can be no gainsaying of the fact that all non-residents are not FIIs and that they form a different category and are given a special treatment under the aforementioned scheme by enacting Section 115AD which provides for a special method of computation (discussed above) and special rate of tax.

There can be no doubt that the legislative intent in inserting Section 115AD in Chapter XII of the Act, is an important guiding factor in interpreting the said provision. We proceed on the common ground that Section 115AD which is meant for FII is a beneficial provision and indeed in asst. yrs. 1999-2000 to 2002-03, the applicant derived benefit of the same. Merely because in the asst.

yr. 2003-04, the applicant suffered capital losses and in view of non application of indexation provision under Section 115AD(3), it cannot boost up the loss it will be pointless to contend that the object of legislature is getting defeated or an inequitable situation is being created.

There is no merit in the contention of the applicant that Section 115AD is applicable when computation results in capital gain and not when it results in capital loss to a FII on transfer of securities.

Section 115AD is an inclusive provision containing, inter alia, mode of computation of tax and concessional rate of tax. Its application does not depend upon the result of computation. Gain and loss are but two sides of the same coin and indeed a loss is nothing but a negative profit. It will be useful to refer to the following observation of the Hon'ble Supreme Court of India in CIT v. Harprasad & Co. (P) Ltd. (1975) 99 ITR 118 (SC) which is apposite here.

"From the charging provisions of the Act, it is discernible that the words "income" or "profits and gains" should be understood as including losses also, so that, in one sense "profits and gains" represent "plus income" whereas losses represent "minus income". In other words, loss is negative profit. Both positive and negative profits are of a revenue character. Both must enter into computation, wherever it

becomes material, in the same mode of the taxable income of the assessee." We find no substance in the plea canvassed for the applicant that a right to opt out of Section 115AD must be read therein as is contained in Section 115-I of the Act. We may notice here Section 115-I, which falls in Chapter XII-A contains special provisions relating to certain income of non-resident Indian. Section 115-I reads as follows : 115-I. A non-resident Indian may elect not to be governed by the provisions of this Chapter for any assessment year by furnishing (his return of income for that assessment year under Section 139 declaring therein) that the provisions of this Chapter shall not apply to him for that assessment year and if he does so, the provisions of this Chapter shall not apply to him for that assessment year and his total income for that assessment year shall be computed and tax on such total income shall be charged in accordance with the other provisions of this Act).

A plain reading of the provision extracted above shows that a non-resident may opt out of the provisions of the said Chapter for any assessment year indicating in his return of income filed under Section 139 his option not to be governed by that Chapter and on so doing, the provisions of Chapter XII-A would not apply to him. It is, thus, obvious that Section 115-I gives a right to a non-resident Indian to elect to be governed by the provisions of that Chapter or by the general provisions of the Act. Such an option is not contained in Chapter XII so the applicant cannot opt out of Section 115AD and by no principle of interpretation such an option can be read in Section 115AD. It is also futile to contend that not providing an option to FII in Chapter XII to opt out of it as it provided for non-resident Indian in Section 115-I of Chapter XII-A or to resident assesseees including domestic companies, is discriminative and violative of Article 26 of the Treaty.

Article 26(1) of the DTAA, on which the applicant bases its case, reads as follows :
1. The nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances are or may be subjected.

Para 1 of Article 26 of the Treaty provides discrimination of nationals of a Contracting State either in regard to taxation or any requirement connected therewith.

The aforementioned para provides that nationals of a Contracting State cannot be subjected to any taxation or any requirement connected therewith in the other Contracting State, which are different or more burdensome than the taxation and connected requirements to which nationals of that other State are subjected to, in the same circumstances. It is important to note here that Article 26 of the Treaty forbids discrimination on the ground of nationality and not different tax treatment on the basis of residential status. The applicant is a national of UK; it is stated that under this para, it cannot be subjected to any taxation or any requirement which is more burdensome than the taxation and connected requirements to which national of India are subjected to in the same circumstances. The grievance of the applicant is that the Indian nationals both resident-assessee as well as domestic companies are entitled to compute their capital gains on the basis of "indexed cost of acquisition" and "indexed cost of any improvement" and on the gains so determined, they are taxed @ 20 per cent and they are allowed an option to be taxed @ 10 per cent without indexation under the proviso to Sub-section (1) of Section 112 of the Act. We do not think that under proviso to Section 112(1), they have the option to apply the provisions of indexation for computing capital gains and paying tax @ 10 per cent on the gains so arrived at as contended by Mr. Pardiwalla, so the plea that the applicant has no such option and therefore, the applicant is discriminated, is misconceived. Even on its own saying (as could be seen from the table quoted above) a domestic company and a resident-assessee of India have to pay tax at the higher rate of 20 per cent on the gains arrived at by applying indexation provisions. The import of the proviso to Section 112(1), discussed above, is that, where the tax payable in respect of any income arising from the transfer of securities (as long-term capital assets) exceeds 10 per cent of the amount of capital gains before giving effect to the provisions of the second proviso to Section 48, then such excess has to be ignored. In other words, without taking away the right of computation under the second proviso to Section 48, FIIs have been extended the benefit of limiting the tax rate to 10 per cent on the capital gains arising from the transfer of long-term capital assets being securities. Under

the scheme of Section 115AD which applies to FIIs like the applicant, (which does not apply to domestic companies and resident assesseees), FIIs are taxed @ 10 per cent of the gains computed under Section 48 without indexation, therefore, the proviso puts them on par. Thus, there cannot be said to be any discrimination on that basis. Further, they cannot also be said to be operating in the same circumstances inasmuch as FIIs can undertake only delivery based transactions, they are not subjected to margin requirement; they have no restrictions on repatriation of profit out of the country and they have overall cap in taking equity possession. It may be pointed out that as defined in Section 2(22A), domestic companies are not necessarily Indian companies. Admittedly, FIIs are non-resident and domestic companies and other resident-assesseees are Indian residents. The different treatment, if any, is based not on the nationality but on the status as resident, which does not amount to discrimination under Article 26 of the Treaty.

Question No. 1 that, on the facts and in the circumstances of the case, the applicant, i.e., the Universities Superannuation Scheme Limited as trustee of Universities Superannuation Scheme, a Foreign Institutional Investor (hereinbefore referred to as "the FII") will not be entitled to opt out of the provisions of Section 115AD of the Act which deal with the taxability of the income earned by a FII, and cannot claim to be covered by Section 48 r/w Section 112 of the Act together with indexation provisions for computing capital gains/losses arising to it from its investment activities in India.

Question No. 2 that it is consequential to the ruling pronounced on the first question, so in view of our ruling on question No. 1, this question does not arise.

Question No. 3 that the provisions of Section 115AD of the Act would apply to an assessee who has suffered capital losses on the transfer of securities.

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