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SooperKanoon Citation : sooperkanoon.com/64776

Court : Income Tax Appellate Tribunal ITAT Delhi

Decided On : Oct-11-1991

Reported in : (1991)39ITD59(Delhi)

Judge : G Krishnamurthy, R Rattan, D Sharma

Appellant : inspecting Assistant

Respondent : Mitsui and Co. Ltd.

Judgement :

1. These two appeals by the Revenue arising out of the common order of the Commissioner of Income-tax (A)-X, New Delhi for the assessment years 1980-81 and 1981-82 involving identical grounds of appeal are being disposed of by a common order.

On the facts and in the circumstances of the case, the learned Commissioner of Income-tax (Appeals) erred in reducing the assessed income to Nil by holding :- (i) that the assessee company is not having a 'permanent establishment' in India and was, therefore, exempt under the provisions of Agreement for avoidance of double taxation between India and Japan, and (ii) that the assessee company is not liable to tax under Section 9(1) of the Income-tax Act because it is not having any business connection in India.

3. The assessee is a foreign non-resident company. It is one of the largest trading houses of Japan and its headquarters are in Tokyo and branches are all over the

world. Four branches of the company were also opened in India from 1954 onwards. These are at Calcutta, New Delhi, Madras and Bombay. It also has representative offices at Bangalore, Goa, Paradeep Port etc. The accounting period of the assessee is the financial year. For the assessment year 1980-81 the assessee company filed its return declaring loss of Rs. 3,97,014 during the current year and total loss of Rs. 01,81,61,084 after adjusting brought forward losses. Similarly for the assessment year 1981-82 it declared loss of Rs. 1,42,71,880 during the year and total loss of Rs. 3,24,32,864 after adjusting the brought forward losses. In the profit and loss account for the assessment year 1980-81, the assessee claimed expenses of Rs. 1,28,88,944 relating to the Indian Branches without showing any receipt on the receipts side. Similar is the manner for declaring loss for the assessment year 1981-82. An agreement for avoidance of double taxation between India and Japan was entered into on the 5th day of January, 1960.

4. Article III(1) of the Agreement provided that the Industrial or commercial profits (excluding the profits derived from the operation of ships or aircraft of an enterprise of one of the Contracting States) shall not be subjected to tax in the other Contracting State unless the enterprise has a permanent establishment situated in that other Contracting State. If it has such permanent establishment, the profits attributable thereto may be subjected to tax in that other Contracting State.

5. Sub-article (2) of Articles HI provided that where an enterprise of one of the Contracting States has a permanent establishment situated in the other Contracting State, there shall be attributed to such permanent establishment the industrial or commercial profits which it might be expected to derive in that other Contracting State, if it were an independent enterprise engaged in the same or similar activities under the same or similar conditions and dealing on an independent basis with the enterprise of which it is a permanent establishment.

6. Sub-article (3) further states that in determining the industrial or commercial profits of a permanent establishment, there shall be allowed as deductions all expenses wherever incurred, reasonably allocable to such permanent

establishment, including executive and general administrative expenses so allocable.

7. Sub-article (4) provides that in a case where the ascertainment of the correct amount of the industrial or commercial profits of a permanent establishment presents difficulties, such profits may be reasonably estimated with reference to the extent to which the activities of such permanent establishment have contributed to earning of profits.

8. Sub-article (5) is to the effect that, no profits shall be attributed to a permanent establishment of an enterprise of one of the Contracting States situated in the other Contracting State through or from operations which are confined merely to the purchase of goods for the purpose of export from such other Contracting State.

9. Article II assign certain meanings to certain words and terms used in the agreement. The term 'permanent establishment' has been defined in Clause (i) of Sub-article (1) of Article II to mean a fixed place of business in which the business of an enterprise is carried on and - (i) the term 'fixed place of business' shall include a branch, an office, a factory, a workshop, a warehouse and a mine, quarry or other place of extraction of natural resources...

(iii) the use of mere storage facilities of the maintenance of a place of business exclusively for the purchase of goods or merchandise and not for any of processing of such goods or merchandise in the country where such purchase takes place shall not constitute a permanent establishment....

(iiia) an enterprise of one of the Contracting States shall not be deemed to have a permanent establishment in the other Contracting State if it maintains a fixed place of business solely for the purpose of advertising, for the supply of information or the scientific research, being activities solely of a preparatory or auxiliary character in the trade or business of the enterprise.

10. According to the Revenue the words 'maintains a permanent establishment in India' meant maintaining branches and representative offices at various places in India. The assessee's contention was that its activities in India were purely of

liaison work and not of trading and is therefore covered by Clause (iii) quoted above. It was also stated on behalf of the assessee that the Reserve Bank of India under Section 29(2)(a) of the Foreign Exchange Regulation Act, 1973 had granted permission vide its letter No. EC.CO.PCs.

2361/747(Activity)-75, dated 4th September, 1975 to continue its branch offices at Calcutta, New Delhi, Bombay and Madras only as liaison offices. The condition imposed by the Reserve Bank of India on the Indian offices of M/s Mitsui and Company are that these will not undertake any activity of a trading, commercial or industrial nature in India and were allowed the permission for undertaking only the liaison work relating to export of iron ore, tobacco, food stuffs, textiles etc. and import of steel products, fertilizers, chemicals, machinery, etc. as referred to in the application under Section 29(2)(a) of the Foreign Exchange Regulation Act, 1973. It further imposed the following conditions : (a) the entire expenses of the Indian Office would be met exclusively out of the remittances received from abroad through normal banking channels; (b) No commission/fee would be charged or any other remuneration received for the liaison activities to be rendered by the Indian offices; (c) Excepting the said liaison work, the offices would not undertake any activity of a trading, commercial and industrial nature without the prior permission of the Reserve Bank of India; and (d) The liaison offices would furnish to us on yearly basis details of remittances received from abroad to meet their expenses in India together with the bank certificates showing receipt of funds and certified copy of the final accounts of the offices, quoting a reference to this letter.

11. The submission on behalf of the assessee, therefore, was that its branches and representative offices in India were permitted by the Competent Authority, namely, Reserve Bank of India to do only liaison work and were prohibited from undertaking any trading activity and, therefore, it did not maintain any permanent establishment in India and consequently its income was not taxable in India by virtue of the provisions in 'Avoidance of Double Taxation Agreement' between the Governments of India and Japan. This claim was also negated by the Assessing Officer holding that the activities of the assessee in India were much more than stated in Sub-article (iiia) referred to earlier.

According to the Assessing Officer the Indian Branch offices of the assessee company not merely collected and supplied to the Head Office information regarding the likely clients in India but they also played a wider role for the replacement of the contracts. He also relied upon the assessee's letter dated 30th November, 1990 filed during the course of assessment proceedings for the assessment year 1978-79 where the assessee had admitted that the negotiations which took place prior to entering into a contract were initiated by the branch offices. He further stated that an idea of the extensive and regular activities conducted by the assessee in India can be had from the fact that the assessee company was maintaining a huge establishment in its branch offices in India. Its expenses on salaries, wages and bonus of the Japanese and Indian staff kept in Indian branches amounted to Rs. 48,26,938 during the accounting period relevant to the assessment year 1980-81. These included expenses on travelling at Rs. 11,61,757, on traffic Rs. 13,57,654, on entertainment Rs. 3,15,819 and on telephone, telex, postage etc. at Rs. 19,59,836. He further noted that the assessee company's expenses on the establishment of branch offices in India did not decrease but further increased after 1975 when the assessee claimed that its branch offices were converted into liaison offices. From these facts, the Assessing Officer came to the conclusion that the assessee company through its offices in India, was maintain permanent establishment in India and was extensively helping the assessee company in carrying on its business activity of purchase and sale in India over a long period of time, thus, enabling it to earn profits out of trading in India. Therefore, the branch office in India clearly came within the definition of 'permanent establishment' notwithstanding the restrictions placed by the Reserve Bank of India under FERA. He further relied upon item (c) of Sub-clause (iv) of Clause (i) of Sub-article (1) of Article II to hold that the assessee company was habitually securing orders in India exclusively or almost exclusively for the enterprise itself or for such enterprise and other enterprises which were controlled by it or having controlling interest in it.

12. Referring to the provisions contained in Section 9(1) of the Income-tax Act, 1961 and negative the assessee's contention that it did not have any business connection in India, he held that the business income of the assessee-company in India arose from its sales operations in India and was taxable under Section 9(1)(i)

and Explanation (a) there below read with Rule 10 of the Income-tax Rules, 1962.

13. The Assessing Officer held that since the books of accounts of the Head Office were not available and, in any case income and expenses relating to selling operations in India were not available from these books of accounts maintained for world income, an estimate of taxable income in India had to be made as per the provisions of Section 9(1)(i), Explanation (a) of the Act and Rule 10 of the Income-tax Rules. He adopted the total sales from Japan into India at US \$ 10,73,03,516 and sales from Branches in other countries into India at US \$ 6,47,16,849. He thus worked out the total sales in India at US \$ 17,20,20,365. He then worked out net profits on sales in India @ 0.50 per cent which worked out to US \$ 860,100 out of which he estimated 50 per cent of the profits attributed to selling operations in India. He, therefore, estimated taxable profits in India at 4,30,050 US \$ and by converting the same to Indian rupees @ Rs. 9 per US \$, the taxable profits in India were adopted by him at Rs. 38,70,450 for the assessment year 1980-81. Similar exercise was done by him for the assessment year 1981-82.

14. It may be relevant to mention here that similar issue came up for consideration at the instance of the Revenue before Delhi Bench 'C' for the first time for the assessment year 1977-78 (I.T.A. No. 693/Del/83 dated 25-4-1984). The Appellate Tribunal dismissed the Departmental appeal for that year. It observed in paragraphs 9 and 10 of that order as under: 9. We have carefully considered the facts of the case and the rival arguments. As already noted above, there is an agreement between the Government of India and the Government of Japan for the Avoidance of Double Taxation in respect of taxes on income. As already pointed out wherever there is such an agreement with the foreign company, provisions of such agreement have precedence over the general principles or the provisions of the Income-tax Act. Article III(1) of the Agreement provides that the commercial profits of an enterprise of one country shall not be subjected to tax in the other country unless the enterprise has a permanent establishment situated in that other country. If it has such permanent establishment the profits attributable thereto may be subjected to tax in the other country. The other parts of that Article provide for the details as to how much profit is attributed to such permanent establishment.

The term 'permanent establishment' is also defined to include a branch which is used as a fixed place of business in which the business of an enterprise is carried on. It is not in dispute that the earlier branch in India was carrying on business activities and it was covered under the term 'permanent establishment'. However, the position underwent a significant change after 1973 when after the enactment of the Foreign Exchange Regulation Act the Reserve Bank of India laid down restrictions on the activities of such foreign establishments and the Indian branch of the assessee-company was permitted to continue only the liaison work. It was specifically prohibited from carrying on any activity of trading or commercial or industrial nature. The liaison office was to furnish to the Reserve Bank of India details of the remittances received from abroad to meet their expenses in India. According to this letter of the Reserve Bank of India details of the remittances received from abroad to meet their expenses in Indian branch had become illegal and the Indian branch was to continue only in respect of the liaison work or passing on the information from one country to the other.

Before this letter of the Reserve Bank of India sent to the assessee, the Double Taxation Avoidance Agreement had also undergone a modification and this modification was made in order to overcome difficulties which were being experienced and expanding the trading between the two countries. Clause (iii) was added in Article II. It is clarified that if the office or branch looks after only advertising or supply of information or for scientific research being activities of preparatory or auxiliary character in the trade and business of the foreign enterprise, the foreign enterprise cannot be held to have a permanent establishment in the other country. After this modification of the Agreement, all branches could not mean that they are permanent establishment of the foreign enterprise and it would depend on the activity which the branch carries on, it would thus depend on the actual nature of the activity of the branch. It has also to be borne in mind that if the branch is found to carry on any business activity or trading activity and not merely a liaison work it could be against the restrictions placed on the assessee by the Reserve Bank of India.

10. In view of the above position, we have perused the material on record and the facts mentioned in the order of the learned CIT (Appeals). We do not find any

material on the basis of which it could be held that the Indian branch of the assessee company was carrying on any business or trading activity itself and it was doing anything beyond what was contemplated in the directions of the Reserve Bank of India. The sale and purchases were being conducted by the head office of the company but the decisions were being communicated through the Indian branch. The delivery of the equipments was given outside India and the contract of sale was also executed by the head office in Japan. All operations like sale or delivery of goods took place outside India. It has not been shown that the Indian branch had accepted or rejected any offer of purchase of malonite sum. The concept of permanent establishment itself has undergone a change insofar as it relates to the modification made in 1973 and that could have been a permanent establishment earlier, has been specifically taken out from the classification. We have looked into some of the correspondence to which our attention was drawn by the Departmental Representative but in all these letters the Indian branch had not conducted any business and has merely passed on the decision taken by the head office to the Indian party or the decision of the Indian party to the head office. In our opinion, therefore, the Indian branch could not be considered to be a permanent establishment after the modification of the Double Taxation Avoidance Agreement and the restrictions placed by the Reserve Bank of India on the activities of the Indian branch. Once that position is ascertained the activity of the Indian branch cannot be said to generate any taxable income in India. We, therefore, agree with the conclusion of the learned CIT (Appeals).

15. The matter again came up before the Tribunal for the assessment years 1975-76 and 1976-77 before Delhi Bench 'C' (I.T.A. Nos. 1660 and 1661/Del/83 dated Nil January, 1985). This Bench also followed the earlier order dated 25-4-1984 of Delhi Bench 'C'.

16. For the assessment years 1980-81 and 1981-82 which are now under consideration, the Commissioner of Income-tax (Appeals) merely followed the orders of the Tribunal dated 25-4-1984 referred to above and allowed the appeals of the assessee against which the Revenue had preferred these appeals.

17. Another significant but relevant fact requiring mention here is that the similar matter had again come up for consideration before the Appellate Tribunal, Delhi Bench 'B' in respect of the assessment years 1978-79 and 1979-80. That Bench by its order in I.T.A. Nos. 1697 and 1698/Del/84 dated 30-4-1986 took a different view disagreeing with the views expressed by the earlier Bench referred to above. The view that prevailed with this Bench to depart from the views expressed by the earlier Benches was that the earlier Benches though observed that it examined the correspondence to which its attention was drawn and found from it nothing to conclude that the Indian Branch of the assessee company was carrying on any trading activity in India except to pass on the decisions taken by the Head Office to the Indian parties and vice versa. There was some other correspondence to which its attention was not drawn and which showed that the Indian branch was not only acting as a liaison office but was also negotiating and finalising sales contracts with the Indian counterparts and that this activity amounted to carrying on of trading in India, took the case outside the purview of Article III (A) of the Double Taxation Avoidance Agreement. This Bench then examined that correspondence according to which the Indian branch of the assessee company had finalised sales contracts and held that the assessee was maintaining a permanent establishment in India and, therefore, the profits attributable to that permanent establishment in India were taxable in India.

18. The appeals for the assessment years 1980-81 and 1981-82 had again come up before the Tribunal for consideration as a consequence of the directions given by the Bench. In view of the conflicting orders of the Benches of the Tribunal, the matter was referred to the President to constitute a Special Bench to dispose of these appeals. It was in that context that the Hon'ble President of the Tribunal constituted the Special Bench for resolving the following controversy: Whether, on the facts and in the circumstances of the case, it is correct to hold that the assessee company did have a permanent establishment in India and hence income was not exempt under the provisions of Agreement for Avoidance of Double Taxation between Japan and India for the assessment years 1980-81 and 1981-82

19. The learned senior Departmental Representative Smt. S.Bhattacharya, heavily relied upon the order of the Tribunal (Delhi Bench 'C') dated 30-4-1986 in I.T.A. Nos. 1697 and 1698/Del/84 relating to assessment years

1978-79 and 1979-80, where it was held that the assessee company was engaged in business in India through its branches and representative offices. She, in particular, highlighted the following aspects : (a) She referred to the correspondence between M.M.T.C., New Delhi and the Branches of the assessee-company in India, which has been referred to in the above order of the Tribunal for the assessment years 1978-79 and 1979-80 and stated that the correspondence clearly established that the Branches of the assessee company were engaged in business in India. She referred to Sub-clause (iii) of Clause (j) of Sub-article (1) of Article II of the Double Taxation Avoidance Agreement with Japan and pointed out that it authorised the branches in India for the following items of work only : According to her, these activities were solely of preparatory or auxiliary character in the trading or business of enterprise and if a branch of the foreign company could be shown to have limited itself to only the aforesaid three types of activities, it could be said that the branch was not a permanent establishment in India.

(b) She further stated that if, however, the scope of activities of the branches in India exceeded the aforesaid three categories, it would be wrong to hold the branches in question as not having a permanent establishment in India. According to her, the branches in Indian were carrying out much more than what was mentioned in Sub-clause (iii) aforesaid. According to her, the branches in India were locating customers in India, making offers to them, getting the terms of contract settled with them and ensuring the opening of Letters of Credit and nomination of vessels for shipment from abroad, forwarding performance guarantees to the customers etc. and these multifarious activities amounted neither to mere advertising, nor to mere supplying of information nor mere constituting scientific research. Therefore, the activities of the branches were intended to formulate and finalise contracts of supply of goods to the Indian parties in India. Such activities were clearly trading activities. She also referred to the enormous magnitude of the expenditure incurred by the branches in India to show that they were actively engaged in business activities and not merely doing liaison work as canvassed by the assessee.

(c) The prohibitions imposed by the Reserve Bank of India, in its letter dated 4-9-1975 on the assessee-company were not couched in the same language as was

used in Sub-clause (iiia) aforesaid and the branches of the company could do activities in India exceeding those mentioned in the said sub-clause and yet did not transgress the conditions imposed on the assessee-company in terms of FERA by the Reserve Bank of India.

(d) For the assessment year 1977-78 though some correspondence was placed in the paper book, but the Tribunal did not specifically refer to these letters placed in the paper book, which showed that the assessee company was doing not only liaison work but also activities of trade. These letters in the paper book were not specifically highlighted by the Departmental Representatives and therefore the Tribunal had no occasion to deal with them although they showed that the assessee company was engaged in business in India through its net work of branches and representative offices.

Further, for the assessment years 1978-79 and 1979-80, further correspondence was summoned by the Commissioner of Income-tax from the MMTC, which showed that the branches of the assessee company were actively engaged in business in India. She, therefore, urged that the Commissioner (Appeals) had wrongly followed the order of the Tribunal for the assessment year 1977-78, (e) Since the activities of the branches in India were incidental to the execution of the contracts, which might have taken place outside India, but for that reason the role of Section 9 was not ousted, if it could be shown that there were business connections. The profits which had not accrued and arisen in India in terms of Section 4, could nevertheless be deemed to have accrued and arisen in India in terms of Section 9.

20. Sh. Harihar Lal, the learned counsel for the assessee, on the other hand, stated that, for the assessment years 1980-81 and 1981-82 under consideration, the Revenue has not brought on record any specific correspondence to show that the branches in India were actively associated with business activities and not the liaison work. According to him, the Assessing Officer had made general statements without any supporting evidence and, therefore, no case was made out by the Revenue in that direction. He further pointed out that, while completing the assessments for the two years, the Assessing Officer had relied upon his order for

detailed discussion for the assessment year 1977-78, which had been reversed by the Tribunal. Therefore the Commissioner (Appeals) has rightly followed the order of the Tribunal for the assessment year 1977-78 and allowed the ground of appeal by the assessee. Referring to the correspondence placed before the Tribunal for the assessment years 1977-78, 1978-79 and 1979-80, he submitted that it only showed that the assessee was engaged in liaison work and the activities of the branches in India were incidental to such liaison work. He pointed out that the information received from the branches of the assessee company abroad were simply passed on to MMTC and other concerns. Similarly, the information gathered in relation to such liaison work in India was passed on to the Branches abroad. The same, according to him, could not be branded as the activities relating to carrying on of business by branches of the assessee company in India.

According to him, the nature of the correspondence referred to by the Tribunal in its order for the assessment years 1978-79 and 1979-80 was of the same nature as filed in the paper book for the assessment year 1977-78. He further pointed out that all the papers in the compilation for the assessment year 1977-78 were duly highlighted in those proceedings before the Bench and, therefore, it was incorrect to say that the same were not referred to. It was after careful consideration of all the correspondence placed before the Bench that it came to the conclusion that the branches in India were engaged only in liaison work. He further stated that simply because the Tribunal did not specifically quote these letters in its order for the assessment year 1977-78, but referred to their gist, it would not make any difference so long as the correspondence placed before it was considered by the Tribunal. It was only a method of writing orders. He, therefore, urged that it was not open to the Bench in proceedings for the assessment years 1978-79 and 1979-80 to have reviewed the earlier order of the Tribunal for the assessment year 1977-78 and come to a different conclusion on the same set of facts and material. According to him, no new material had come before the Tribunal for the assessment years 1978-79 and 1979-80 to come to a different conclusion. According to him, it was the reappraisal of the same evidence by a different Bench for a different assessment year, which was judicially deprecated by the High Courts and the Supreme Court. He, therefore, urged that the Tribunal's order for the assessment years 1978-79 and 1979-80 should not be followed in appeal.

proceedings for the assessment years 1980-81 and 1981-82.

21. Regarding import of urea from USA and Bank guarantees etc. as listed by the Bank of Tokyo, he stated that Indian Branches merely passed on the information to MMTC and other concerns which was nothing but process of supply of information only and not business activities.

He also referred to the application of the assessee company dated 28-6-1974 addressed to the Reserve Bank of India, Bombay under Section 29(2)(e) of the Foreign Exchange Regulation Act, 1973 seeking permission to continue branch offices of the assessee company in India and a note justifying the continuance. The nature of the activities of the branches in India has been listed therein, which, according to the learned counsel for the assessee was liaison work. This is placed at pages 51 to 54 of the paper book, Volume I available in the Tribunal's records for the assessment year 1977-78.

22. Shri Harihar Lal, the learned counsel for the assessee also pointed out that the assessee company has been submitting annual accounts to the Reserve Bank of India, Bombay, in terms of Bank's letter dated 4-9-1975, under which the assessee company was allowed to retain its Branch offices in India. He has placed in the paper book such reports sent to the bank for the years ending 31 -3-1980 and 31 -3-1981, relevant to the assessment years 1980-81 and 1981-82 and further stated that the bank had pointed out no irregularity in the accounts nor violation of any of the conditions imposed in its letter dated 4-9-1975. Referring to the volume of expenditure in India by the Branches, he pointed out that the increase in the volume of expenditure was marginal as compared to the earlier years in view of the rising prices and also increasing liaison work. He, therefore, urged that no adverse inference should be drawn from this fact as the expenditure incurred was quite reasonable, considering the levels of expenditure by Multi-Nationals.

Shri Harihar Lal then submitted that once it was held that the Double Taxation Avoidance Agreement between India and Japan held the field, it would have precedence over the provisions of Section 9(1).

In view of the above submissions, he urged that the Commissioner (Appeals) had rightly accepted the appeals by the assessee and no interference with his order was called for.

23. We have given our very careful thoughts to the rival submissions and gone through the records and the orders of the Tribunal expressing conflicting views. We have also gone through the orders of the authorities below. The Revenue has emphasised that the Branches of the assessee company in India were not merely doing the liaison work, but much more than that. At the outset, we would like to mention that the Revenue has not placed on record any paper book containing the correspondence between the branches of the assessee company in India and other parties in India to show that it was engaged in business and not merely liaison work. The Assessing Officer has also not discussed specifically any documents in that direction. As a matter of fact, he has referred to in his order for the assessment year 1977-78, such material which was not approved by the Appellate Tribunal. The Commissioner (Appeals) has, therefore, rightly followed the order of the Tribunal for the assessment year 1977-78. It is settled law that each assessment year is a separate unit of assessment and there is no res judicata in the income-tax proceedings.

24. In the differing order of the Tribunal passed for the assessment year 1978-79, reference was made to certain letters, which were available in the compilation placed before the Tribunal for the assessment year 1977-78. Thus nothing new was found. Those letters, which according to the differing Bench made a difference were referred to in para 13.4 of its order as below:- 1. Two letter dated 25-1-1979 of Delhi Branch of the assessee company.

2. Letter dated 4-1-1979 of the Delhi Branch of the assessee company.

3. Letter dated 1-2-1979 from Delhi office of the assessee addressed to MMTC enclosing therewith the charter party.

It was by referring to these letters, that the Bench had drawn adverse inferences against the assessee, and held that a perusal of these letters showed that the assessee was engaged in the trading activities in India and not merely doing

liaison work. These letters were available in the paper book at pages 2,12,14 and 28. We shall refer to these letters specifically.

25. At page 28, is the copy of the letter dated 4-1 -1979 of Delhi Branch office of the assessee company addressed to MMTC, New Delhi.

This letter refers to a contract by MMTC bearing No. 558/78-FZ(96) dated 22-12-1979 for import of urea. With this letter, a letter of Guarantee dated 4-1 -1979 in original, as issued by the Bank of Tokyo Ltd., New Delhi was forwarded to the MMTC. It was further stated in this letter that their New York office was requested by them to increase the value of guarantee which would be enhanced accordingly.

The MMTC was, therefore, requested to establish Letter of Credit in favour of their New York office.

26. Letter dated 25-1-1979 at page 14 of the paper book was again to MMTC. This letter also referred to the import of urea against Contract No. 558/78-FZ(96) dated 22-12-1978. With this letter, a Bank of Tokyo letter was forwarded to the MMTC in original, whereunder they had increased the amount of Guarantee.

27. Another letter again dated 25-1-1979 at page 12 is addressed to MMTC. This letter also related to the same contract for import of Urea.

It conveyed that the assessee-company in USA quotes price on one port discharge basis at West Coast of India. It further stated that it was agreed that an extra charge of US cents 0.35 per MT would be payable to the supplier in case of discharge at one port on East Coast of India, if necessity arose. Request was to amend the contract accordingly and to confirm the port of discharge.

28. The other letter referred to was of 1-2-1979, which was available at page 2. By this letter, 12 copies of the charter party have been forwarded to MMTC, New Delhi.

29. A perusal of the letters, the contents of which have been referred to by us, would show that it was purely a liaison work i.e., passing on the information to MMTC on behalf of the USA counterparts of the assessee company. There are

several other letters in the compilation for the assessment year 1977-78 relating to import of Urea under Contract No. 558/78-FZ(96j dated 22-12-78. At page 8 is a letter dated 31 -1-1979 again addressed to MMTC, conveying the text of a telex message received from Mitsui & Co. New York. There are more than 20 letters placed in the compilation for the assessment year 1977-78, which are of the same nature relating to import of urea from the USA. One letter dated 22-12-78 on page 39 again addressed to MMTC, New Delhi, is in relation to information regarding shipment schedule of urea as received from the USA office. Again, there is a letter dated 4-1-1979 at page 33 to MMTC, New Delhi, conveying the acceptance of the request of MMTC for seven days free demurrage. There are other letters of the same nature. These are clearly relating to liaison work. In the order of the Tribunal for the assessment years 1978-79 and 1979-80 reference was made to letters mostly for import of urea from USA. We do not find from the correspondence anything which would show that the branches of the assessee company in India were engaged in trading activities. Shri Harihar Lal had stated that, for the assessment year 1977-78, all the letters in the compilation were specifically brought to the notice of the Bench and the Bench, instead of referring to individual letters considered them as a whole and came to the conclusion that the assessee company was engaged only in liaison work and there was no warrant for the Tribunal in the proceedings for the assessment years 1978-79 and 1979-80 to come to the conclusion that these letters were not specifically referred to by the Departmental Representative before the Bench. According to him, the Bench could not have known as to whether some of the letters were not specifically referred as the constitution of the Bench in the assessment year 1977-78 was altogether different. We are inclined to agree with the submissions made on behalf of the assessee on this point.

30. Here we would like to advert to Clause (iia) of the Double Taxation Avoidance Agreement which provided that supply of information which is preparatory or auxiliary to the formation of the contract between the contracting States does not amount to having a fixed place of business, and therefore, permanent establishment. What is important to note is that supply of information must only be preparatory or auxiliary to the formation of the ultimate contract. In contracts of this type which deal with the import-export policy of the country involving several public

institutions, supply of information can be on a variety of points which cannot be visualised. Supply of information is meant to clear the doubts in the minds of the contracting parties so that ad idem is established before a final contract is concluded. In International Trade and Commerce, there are several aspects on which information has to be gathered and supplied to the contracting parties.

It can start with negotiations from the very nascent stage to the final conclusion of the contract and also removal of doubts on various points relating to supply of material, transportation, payment schedule, mode of transport, freight and charges, bank guarantees, interest payable, commission payable etc. etc. It is difficult to specify the areas to which supply of information can be limited. That was why the Article (iiia) was so widely worded as to include extensively and intensively all areas of supply of information, the only limiting factor being that supply of information should be either preparatory or auxiliary to the formation of the final contract. Any information conveyed even after the conclusion of a contract say, for example, delay in the payment by the party in one contracting State to the party in another contracting State may also fall within the broad spectrum of supply of information.

Information can be elicited or gathered only by negotiations or questions and answers and communication of these answers to the questions raised cannot but be treated as supply of information. The Bench dealing with the assessment year 1977-78 had considered all these aspects and all these correspondence and came to the very right conclusion that all the correspondence showed that the Branches in India of the assessee company were engaged only in the work of supply of information and liaison work for which they were specifically permitted by the Reserve Bank of India and did not carry on any trade in India or any activity leading to trading activity. If a trading activity had been carried on by the Indian Officers of the assessee company then that would have amounted to violation and then it was the Reserve Bank of India that would be more concerned with such violation and would have withdrawn the permission for these Indian Branches to exist in India under the Foreign Exchange Regulation Act. No such violation was ever found by the Reserve Bank of India even though the Reserve Bank of India was put in the knowledge of these activities carried on by the Indian Branches of

the assessee company by submitting the annual returns to it as per the conditions imposed by it. Thus it cannot be said that the interpretation sought to be placed upon the correspondence by the Revenue is more authentic and correct than the interpretation placed by the very concerned authority namely the Reserve bank of India. The subsequent Bench dealing with the assessment years 1978-79 and 1979-80 had dealt with the same correspondence but came to a different conclusion. That apart from being incorrect, did not reflect the correct appreciation of the facts and the material on record. One is not to be led away by the enormity of the expenditure incurred in running an office in India. That would depend upon the level of the country to which the office belongs. We have to judge the expenditure incurred from that angle and not from our angle. It is not the case of the Revenue that the expenditure incurred was so camouflaged as to cover the expenditure incurred in a trading activity to show it as expenditure incurred on liaison activity. Nor is it the case of the Revenue that the work carried on by the assessee in India which according to them amounted to trading activity produced income in India or anywhere else. This expenditure incurred in India was met out of the remittances received by the Indian Branches again through the Reserve Bank of India. There was no evidence brought on record at any stage that the Indian Branches had exceeded the limits prescribed for it by the Reserve Bank of India. As long as the Indian Officers were conducting the operations within the restricted area and so long as those activities were not considered by the Reserve Bank of India, which is the concerned authority as amounting to anything other than carrying on of liaison work no inference adverse to the assessee can be drawn or is possible to draw. To repeat what all that was done by the assessee fell within the parameters of supplying of information which is preparatory to and auxiliary to the formation of the final contracts.

31. We are of the opinion that the activities of the Branches of the assessee company in India were within the ambit of sub -clause (iiia) of Clause (i) of Sub-article (1) of Article II of the Double Taxation Avoidance Agreement between India and Japan.

32. We are also in agreement with the learned counsel for the assessee that the increase in the expenditure of the Branches of the assessee company in India as

compared to the earlier years was marginal and quite reasonable in view of the general increase in prices as also increase in the liaison work.

33. In view of the above discussions we hold the activities of the Branches of the assessee company in India to be merely pertaining to liaison work. We are also of the opinion that provisions of Section 9(1) are not applicable and, therefore, no part of the income of the assessee is assessable in India. No interference with the order of the Commissioner of Income-tax (Appeals) for both the assessment years is, therefore, called for.

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